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WORLD INVESTMENT REPORT **2015**

REFORMING INTERNATIONAL INVESTMENT GOVERNANCE



UNITED NATIONS CONFERENCE ON TRADE AND DEVELOPMENT

UNCTAD



WORLD INVESTMENT REPORT 2015

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UNITED NATIONS
New York and Geneva, 2015

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PREFACE

This year's *World Investment Report*, the 25th in the series, aims to inform global debates on the future of the international policy environment for cross-border investment.

Following recent lackluster growth in the global economy, this year's Report shows that Foreign Direct Investment (FDI) inflows in 2014 declined 16 per cent to \$1.2 trillion. However, recovery is in sight in 2015 and beyond. FDI flows today account for more than 40 per cent of external development finance to developing and transition economies.

This *Report* is particularly timely in light of the Third International Conference on Financing for Development in Addis Ababa – and the many vital discussions underscoring the importance of FDI, international investment policy making and fiscal regimes to the implementation of the new development agenda and progress towards the future sustainable development goals.

The *World Investment Report* tackles the key challenges in international investment protection and promotion, including the right to regulate, investor-state dispute settlement, and investor responsibility. Furthermore, it examines the fiscal treatment of international investment, including contributions of multinational corporations in developing countries, fiscal leakage through tax avoidance, and the role of offshore investment links.

The *Report* offers a menu of options for the reform of the international investment treaties regime, together with a roadmap to guide policymakers at the national, bilateral, regional and multilateral levels. It also proposes a set of principles and guidelines to ensure coherence between international tax and investment policies.

I commend this publication as an important tool for the international investment community in this crucial year for sustainable development.



BAN Ki-moon
Secretary-General of the United Nations

ACKNOWLEDGEMENTS

The *World Investment Report 2015 (WIR15)* was prepared by a team led by James X. Zhan. The team members included Richard Bolwijn, Kwangouck Byun, Bruno Casella, Joseph Clements, Hamed El Kady, Kumi Endo, Masataka Fujita, Noelia Garcia Nebra, Axèle Giroud, Joachim Karl, Ventzislav Kotetzov, Guoyong Liang, Hafiz Mirza, Shin Ohinata, Sergey Ripinsky, Diana Rosert, William Speller, Astrit Sulstarova, Claudia Trentini, Elisabeth Tuerk, Joerg Weber and Kee Hwee Wee.

WIR15 benefited from the advice of Jeffrey Owens, Senior Tax Advisor.

Research and statistical assistance was provided by Bradley Boicourt, Mohamed Chiraz Baly and Lizanne Martinez. Contributions were also made by Bekele Amare, Ana Conover Blancas, Hasinah Essop, Charalampos Giannakopoulos, Thomas van Giffen, Natalia Guerra, Rhea Hoffmann, Mathabo Le Roux, Kendra Magraw, Abraham Negash, Chloe Reis, Davide Rigo, Julia Salasky, John Sasuya, Carmen Saugar Koster, Catharine Titi, as well as interns Anna Mouw and Elizabeth Zorrilla.

The manuscript was copy-edited with the assistance of Lise Lingo, and typeset by Laurence Duchemin and Teresita Ventura.

Sophie Combette and Nadege Hadjemian designed the cover, and Pablo Cortizo designed the figures and maps.

Production and dissemination of *WIR15* was supported by Elisabeth Anodeau-Mareschal, Anne Bouchet, Nathalie Eulaerts, Rosalina Goyena, Tadelle Taye and Katia Vieu.

At various stages of preparation, in particular during the experts meetings organized to discuss drafts of *WIR15*, the team benefited from comments and inputs received from external experts: Wolfgang Alschner, Carlo Altomonte, Douglas van den Berghe, Nathalie Bernasconi, Yvonne Bol, David Bradbury, Irene Burgers, Jansen Calamita, Krit Carlier, Manjiao Chi, Steve Clark, Alex Cobham, Aaron Cosbey, Lorrain Eden, Maikel Evers, Uche Ewelukwa, Michael Ewing-Chow, Alessio Farcomeni, Michael Hanni, Martin Hearson, Steffen Hindelang, Lise Johnson, Michael Keen, Eric Kemmeren, Jan Kleinheisterkamp, Victor van Kommer, Markus Krajewski, Federico Lavopa, Michael Lennard, Jan Loeprick, Ricardo Martner, Makane Mbengue, Nara Monkam, Hans Mooij, Ruud de Mooij, Peter Muchlinski, Alexandre Munoz, Thomas Neubig, Andrew Packman, Joost Pauwelyn, Facundo Perez Aznar, Raffaella Piccarreta, Andrea Saldarriaga, Mavluda Sattorova, Ilan Strauss, Lauge Skovgaard Poulsen, Christian Tietje, Jan van den Tooren, Gerben Weistra and Paul Wessendorp. MEED provided assistance in obtaining data for the West Asia region.

Also acknowledged are comments received from other UNCTAD divisions, including from the Division for Africa, Least Developed Countries and Special Programmes, the Division on Globalization and Development Strategies, and the Division on Technology and Logistics, as part of the internal peer review process, as well as comments from the Office of the Secretary-General as part of the review and clearance process. The United Nations Cartographic Section provided advice for the regional maps.

Numerous officials of central banks, government agencies, international organizations and non-governmental organizations also contributed to *WIR15*. The financial support of the Governments of Finland, Norway, Sweden and Switzerland is gratefully acknowledged.

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SUPPORTING ANNEXES AVAILABLE ONLINE

(<http://www.unctad.org/wir>)

Chapters I and II

- Detailed FDI, M&A, greenfield projects data tables

Chapter III

- List of IIAs as of end 2014 (see also UNCTAD's Investment Policy Hub)

Chapter V

- Annex I. Establishing the baseline: estimating the fiscal contribution of multinational enterprises
- Annex II. An FDI-driven approach to measuring the scale and economic impact of BEPS
- Annex III. Policy action against tax avoidance by multinational enterprises: existing measures and ongoing discussions

ABBREVIATIONS

ADR	alternative dispute resolution
AGOA	African Growth and Opportunity Act
APEC	Asia-Pacific Economic Cooperation
ASEAN	Association of Southeast Asian Nations
BEPS	base erosion and profit shifting
BIT	bilateral investment treaty
BOT	build, operate, transfer
BRICS	Brazil, Russian Federation, India, China, South Africa
CETA	Comprehensive Economic and Trade Agreement
CFIA	Cooperative and Facilitation Investment Agreement
CIL	customary international law
CIS	Commonwealth of Independent States
CLMV	Cambodia, Laos People's Democratic Republic, Myanmar, Viet Nam
COMESA	Common Market for Eastern and Southern Africa
CSR	corporate social responsibility
DTT	double-taxation treaty
EPZ	export processing zone
ETR	effective tax rate
FDI	foreign direct investment
FET	fair and equitable treatment
FTA	free trade agreement
GATS	General Agreement on Trade in Services
GCC	Gulf Cooperation Council
GFCF	gross fixed capital formation
GVC	global value chain
IIA	international investment agreement
IPA	investment promotion agency
IPFSD	Investment Policy Framework for Sustainable Development
ISDS	investor-State dispute settlement
LDC	least developed countries
LLDC	landlocked developing countries
M&As	mergers and acquisitions
MFN	most favoured nation
MNE	multinational enterprise
NAFTA	North American Free Trade Agreement
NEM	non-equity mode
ODA	official development assistance
PPP	public-private partnership
RCEP	Regional Comprehensive Economic Partnership
SEZ	special economic zone
SDT	special and differential treatment
SIDS	small island developing States
SME	small and medium-sized enterprise
SOE	State-owned enterprise
SPE	special purpose entity
SWF	sovereign wealth fund
TPO	trade promotion organization
TPP	Trans-Pacific Partnership Agreement
TRIMs	Trade-Related Investment Measures
TTIP	Transatlantic Trade and Investment Partnership
UNCITRAL	United Nations Commission on International Trade Law
WIPS	World Investment Prospects Survey
WTO	World Trade Organization

KEY MESSAGES

GLOBAL INVESTMENT TRENDS

Global FDI inflows declined in 2014. Global foreign direct investment (FDI) inflows fell by 16 per cent to \$1.23 trillion in 2014, mostly because of the fragility of the global economy, policy uncertainty for investors and elevated geopolitical risks. New investments were also offset by some large divestments.

Inward FDI flows to developing economies reached their highest level at \$681 billion with a 2 per cent rise. Developing economies thus extended their lead in global inflows. China became the world's largest recipient of FDI. Among the top 10 FDI recipients in the world, 5 are developing economies.

The low level of flows to developed countries persisted in 2014. Despite a revival in cross-border mergers and acquisitions (M&As), overall FDI flows to this group of economies declined by 28 per cent to \$499 billion. They were significantly affected by a single large-scale divestment from the United States.

Investments by developing-country multinational enterprises (MNEs) also reached a record level: developing Asia now invests abroad more than any other region. Nine of the 20 largest investor countries were from developing or transition economies. These MNEs continued to acquire developed-country foreign affiliates in the developing world.

Most regional groupings and initiatives experienced a fall in inflows in 2014. The groups of countries negotiating the Transatlantic Trade and Investment Partnership (TTIP) and Trans-Pacific Partnership (TPP) saw their combined share of global FDI inflows decline. ASEAN (up 5 per cent to \$133 billion) and the RCEP (up 4 per cent to \$363 billion) bucked the trend.

By sector, the shift towards services FDI has continued over the past 10 years in response to increasing liberalization in the sector, the increasing tradability of services and the growth of global value chains in which services play an important role. In 2012, services accounted for 63 per cent of global FDI stock, more than twice the share of manufacturing. The primary sector represented less than 10 per cent of the total.

Cross-border M&As in 2014 rebounded strongly to \$399 billion. The number of MNE deals with values larger than \$1 billion increased to 223 – the highest number since 2008 – from 168 in 2013. At the same time, MNEs made divestments equivalent to half of the value of acquisitions.

Announced greenfield investment declined by 2 per cent to \$696 billion. Developing countries continued to attract two thirds of announced greenfield investment. Greenfield investment by both developed- and developing-country MNEs remained unchanged.

FDI by special investors varied. The significance of *private equity funds* in the global M&A market, with \$200 billion in acquisitions in 2014, was reflected mainly in transactions involving large companies. *Sovereign wealth funds*, which invested \$16 billion in FDI in 2014, are increasingly targeting infrastructure internationally. *State-owned MNEs'* international expansion has decelerated; in particular, their cross-border M&As declined by 39 per cent to \$69 billion.

International production by MNEs is expanding. International production rose in 2014, generating value added of approximately \$7.9 trillion. The sales and assets of MNEs' foreign affiliates grew faster than their domestic counterparts. Foreign affiliates of MNEs employed about 75 million people.

FDI recovery is in sight. Global FDI inflows are projected to grow by 11 per cent to \$1.4 trillion in 2015. Expectations are for further rises to \$1.5 trillion in 2016 and to \$1.7 trillion in 2017. Both UNCTAD's FDI forecast model and its business survey of large MNEs signal a rise of FDI flows in the coming years. The share of MNEs intending to increase FDI expenditures over the next three years (2015–2017) rose from 24 to 32 per cent. Trends in cross-border M&As also point to a return to growth in 2015. However, a number of economic and political risks, including ongoing uncertainties in the Eurozone, potential spillovers from conflicts, and persistent vulnerabilities in emerging economies, may disrupt the projected recovery.

REGIONAL INVESTMENT TRENDS

FDI inflows to Africa remained flat at \$54 billion. Although the services share in Africa FDI is still lower than the global and the developing-country averages, in 2012, services accounted for 48 per cent of the total FDI stock in the region, more than twice the share of manufacturing (21 per cent). FDI stock in the primary sector was 31 per cent of the total.

Developing Asia (up 9 per cent) saw FDI inflows grow to historically high levels. They reached nearly half a trillion dollars in 2014, further consolidating the region's position as the largest recipient in the world. FDI inflows to *East and South-East Asia* increased by 10 per cent to \$381 billion. In recent years, MNEs have become a major force in enhancing regional connectivity in the subregion, through cross-border investment in infrastructure. The security situation in *West Asia* has led to a six-year continuous decline of FDI flows (down 4 per cent to \$43 billion in 2014); weakening private investment in parts of the region is compensated by increased public investment. In *South Asia* (up 16 per cent to \$41 billion), FDI has increased in manufacturing, including in the automotive industry.

FDI flows to Latin America and the Caribbean (down 14 per cent) decreased to \$159 billion in 2014, after four years of consecutive increases. This is mainly due to a decline in cross-border M&As in Central America and the Caribbean and to lower commodity prices, which dampened FDI to South America. The FDI slowdown, after a period of strong inflows driven by high commodity prices, may be an opportunity for Latin American countries to re-evaluate FDI strategies for the post-2015 development agenda. *FDI in transition economies decreased by 52 per cent to \$48 billion in 2014.* Regional conflict coupled with falling oil prices and international sanctions have damaged economic growth prospects and shrunk investor interest in the region.

FDI inflows to developed countries fell by 28 per cent to \$499 billion. Divestment and large swings in intracompany loans reduced inflows to the lowest level since 2004. Outflows held steady at \$823 billion. Cross-border M&A activities gathered momentum in 2014. Burgeoning FDI income is providing a counterbalance to trade deficits, particularly in the United States and more recently in Japan.

FDI flows to structurally weak, vulnerable and small economies varied. FDI to the least developed countries (LDCs) increased by 4 per cent. Landlocked developing countries (LLDCs) experienced a fall of 3 per cent in FDI inflows, mostly in those in Asia and Latin America. By contrast, FDI inflows to small island developing States (SIDS) increased by 22 per cent, due to a rise in cross-border M&A sales. The relative importance of FDI, its greater stability and its more diverse development impact compared with other sources of finance means that it remains an important component of external development finance to these economies. Over the past decade (2004–2014), FDI stock tripled in LDCs and SIDS, and quadrupled in LLDCs. With a concerted effort by the international investment-development community, it would be possible to have FDI stock in structurally weak economies quadruple again by 2030. More important, further efforts are needed to harness financing for economic diversification to foster greater resilience and sustainability in these countries.

INVESTMENT POLICY TRENDS

Countries' investment policy measures continue to be geared predominantly towards investment liberalization, promotion and facilitation. In 2014, more than 80 per cent of investment policy measures aimed to improve entry conditions and reduce restrictions. A focus was investment facilitation and sector-specific liberalization (e.g. in infrastructure and services). New investment restrictions related mostly to national security concerns and strategic industries (such as transport, energy and defence).

Measures geared towards investment in sectors important for sustainable development are still relatively few. Only 8 per cent of measures between 2010 and 2014 were specifically targeted at private sector participation in key sustainable development sectors (infrastructure, health, education, climate-change mitigation). In light of the SDG investment gap (WIR14), greater focus on channeling investment into key sectors for sustainable development would be warranted.

Countries and regions continue their search for reform of the international investment agreements (IIAs) regime. Thirty-one new IIAs were concluded in 2014, most with provisions related to sustainable development. Canada was the most active country (with seven new treaties). The IIA universe grew to 3,271 treaties. At the same time, countries and regions considered new approaches to investment policymaking. Reacting to the growing unease with the current functioning of the global IIA regime, together with today's sustainable development imperative and the evolution of the investment landscape, at least 50 countries and regions were engaged in reviewing and revising their IIA models. Brazil, India, Norway and the European Union (EU) published novel approaches. South Africa and Indonesia continued their treaty terminations, while formulating new IIA strategies.

Pre-establishment commitments are included in a relatively small but growing number of IIAs. Some 228 treaties now provide national treatment for the "acquisition" or "establishment" of investments. Most involve the United States, Canada, Finland, Japan, and the EU, but a few developing countries (Chile, Costa Rica, the Republic of Korea, Peru and Singapore) also follow this path.

There were 42 new investor-State dispute settlement (ISDS) cases in 2014, bringing the total number of known treaty-based claims to 608. Developing countries continue to bear the brunt of these claims, but the share of developed countries is on the rise. Most claimants come from developed countries. Forty-three decisions were rendered in 2014, bringing the overall number of concluded cases to 405. Of these, States won 36 per cent, investors 27 per cent. The remainder was either settled or discontinued.

REFORMING THE INTERNATIONAL INVESTMENT REGIME: AN ACTION MENU

There is a pressing need for systematic reform of the global IIA regime. As is evident from the heated public debate and parliamentary hearing processes in many countries and regions, a shared view is emerging on the need for reform of the IIA regime to ensure that it works for all stakeholders. The question is not about *whether* or not to reform, but about the *what, how* and *extent* of such reform. *This report offers an action menu for such reform.*

IIA reform can build on lessons learned from 60 years of IIA rule making: (i) IIAs "bite" and may have unforeseen risks, and safeguards need to be put in place; (ii) IIAs have limitations as an investment promotion tool, but also underused potential; and (iii) IIAs have wider implications for policy and systemic coherence, as well as capacity-building.

IIA reform should address five main challenges. IIA reform should aim at (i) *safeguarding the right to regulate in the public interest* so as to ensure that IIAs' limits on the sovereignty of States do not unduly constrain public policymaking; (ii) *reforming investment dispute settlement* to address the legitimacy crisis of the current

system; (iii) *promoting and facilitating investment* by effectively expanding this dimension in IIAs; (iv) *ensuring responsible investment* to maximize the positive impact of foreign investment and minimize its potential negative effects; and (v) *enhancing the systemic consistency of the IIA regime* so as to overcome the gaps, overlaps and inconsistencies of the current system and establish coherence in investment relationships.

UNCTAD presents policy options for meeting these challenges. This report sets out options for addressing the standard elements found in an IIA. Some of these reform options can be combined and tailored to meet several reform objectives:

- *Safeguarding the right to regulate*: Options include clarifying or circumscribing provisions such as most-favoured-nation (MFN) treatment, fair and equitable treatment (FET), and indirect expropriation, as well as including exceptions, e.g. for public policies or national security.
- *Reforming investment dispute settlement*: Options include (i) reforming the existing mechanism of ad hoc arbitration for ISDS while keeping its basic structure and (ii) replacing existing ISDS arbitration systems. The former can be done by fixing the existing mechanism (e.g. improving the arbitral process, limiting investors' access, using filters, introducing local litigation requirements) and by adding new elements (e.g. building in effective alternative dispute resolution or introducing an appeals facility). Should countries wish to replace the current ISDS system, they can do so by creating a standing international investment court, or by relying on State-State and/or domestic dispute resolution.
- *Promoting and facilitating investment*: Options include adding inward and outward investment promotion provisions (i.e. host- and home-country measures), and joint and regional investment promotion provisions, including an ombudsperson for investment facilitation.
- *Ensuring responsible investment*: Options include adding not lowering of standards clauses and establishing provisions on investor responsibilities, such as clauses on compliance with domestic laws and on corporate social responsibility.
- *Enhancing systemic consistency of the IIA regime*: Options include improving the coherence of the IIA regime, consolidating and streamlining the IIA network, managing the interaction between IIAs and other bodies of international law, and linking IIA reform to the domestic policy agenda.

When implementing IIA reform, policymakers have to determine the most effective means to safeguard the right to regulate while providing for the protection and facilitation of investment. In so doing, they need to consider the compound effect of options. Some combinations of reform options may “overshoot” and result in a treaty that is largely deprived of its traditional investment protection rationale.

In terms of process, IIA reform actions should be synchronized at the national, bilateral, regional and multilateral levels. In each case, the reform process includes (i) taking stock and identifying the problems, (ii) developing a strategic approach and an action plan for reform, and (iii) implementing actions and achieving the outcomes.

All of this should be guided by the goal of harnessing IIAs for sustainable and inclusive development, focusing on the key reform areas and following a multilevel, systematic and inclusive approach. In the absence of a multilateral system, given the huge number of existing IIAs, the best way to make the IIA regime work for sustainable development is to collectively reform the regime with a global support structure. Such a structure can provide the necessary backstopping for IIA reform, through policy analysis, coordination among various processes at different levels and dimensions, management of the interaction with other bodies of law, technical assistance and consensus-building. UNCTAD plays a key role in this regard. Only a common approach will deliver an IIA regime in which stability, clarity and predictability help achieve the objectives of all stakeholders: effectively harnessing international investment relations for the pursuit of sustainable development.

INTERNATIONAL TAX AND INVESTMENT POLICY COHERENCE

Intense debate and concrete policy work is ongoing in the international community on the fiscal contribution of MNEs. The focus is predominantly on tax avoidance – notably in the G20 project on base erosion and profit shifting (BEPS). At the same time, sustained investment is needed in global economic growth and development, especially in light of financing needs for the Sustainable Development Goals (SDGs). *The policy imperative is to take action against tax avoidance to support domestic resource mobilization and continue to facilitate productive investment for sustainable development.*

UNCTAD estimates the contribution of MNE foreign affiliates to government budgets in developing countries at approximately \$730 billion annually. This represents, on average, some 23 per cent of total corporate contributions and 10 per cent of total government revenues. The relative size (and composition) of this contribution varies by country and region. It is higher in developing countries than in developed countries, underlining the exposure and dependence of developing countries on corporate contributions. (On average, the government budgets of African countries depend on foreign corporate payments for 14 per cent of their funding.)

Furthermore, the lower a country is on the development ladder, the greater is its dependence on non-tax revenue streams contributed by firms. *In developing countries, foreign affiliates, on average, contribute more than twice as much to government revenues through royalties on natural resources, tariffs, payroll taxes and social contributions, and other types of taxes and levies, than through corporate income taxes.*

MNEs build their corporate structures through cross-border investment. They do so in the most tax-efficient manner possible, within the constraints of their business and operational needs. *The size and direction of FDI flows are thus often influenced by MNE tax considerations, because the structure and modality of investments enable opportunities to avoid tax on subsequent investment income.*

An investment perspective on tax avoidance puts the spotlight on the role of offshore investment hubs (tax havens and special purpose entities in other countries) as major players in global investment. *Some 30 per cent of cross-border corporate investment stocks have been routed through offshore hubs before reaching their destination as productive assets.* (UNCTAD's FDI database removes the associated double-counting effect.)

The outsized role of offshore hubs in global corporate investments is largely due to tax planning, although other factors can play a supporting role. MNEs employ a range of tax avoidance levers, enabled by tax rate differentials between jurisdictions, legislative mismatches, and tax treaties. MNE tax planning involves complex multilayered corporate structures. Two archetypal categories stand out: (i) intangibles-based transfer pricing schemes and (ii) financing schemes. Both schemes, which are representative of a relevant part of tax avoidance practices, make use of investment structures involving entities in offshore investment hubs – financing schemes especially rely on direct investment links through hubs.

Tax avoidance practices by MNEs are a global issue relevant to all countries: the exposure to investments from offshore hubs is broadly similar for developing and developed countries. However, profit shifting out of developing countries can have a significant negative impact on their prospects for sustainable development. Developing countries are often less equipped to deal with highly complex tax avoidance practices because of resource constraints or lack of technical expertise.

Tax avoidance practices are responsible for a significant leakage of development financing resources. *An estimated \$100 billion of annual tax revenue losses for developing countries is related to inward investment stocks directly linked to offshore hubs.* There is a clear relationship between the share of offshore-hub investment in host countries' inward FDI stock and the reported (taxable) rate of return on FDI. The more investment is routed through offshore hubs, the less taxable profits accrue. On average, across developing economies, every 10 percentage points of offshore investment is associated with a 1 percentage point lower rate of return. These averages disguise country-specific impacts.

Tax avoidance practices by MNEs lead to a substantial loss of government revenue in developing countries. The basic issues of fairness in the distribution of tax revenues between jurisdictions that this implies must be addressed. *At a particular disadvantage are countries with limited tax collection capabilities, greater reliance on tax revenues from corporate investors, and growing exposure to offshore investments.*

Therefore, action must be taken to tackle tax avoidance, carefully considering the effects on international investment. Currently, offshore investment hubs play a systemic role in international investment flows: they are part of the global FDI financing infrastructure. Any measures at the international level that might affect the investment facilitation function of these hubs, or key investment facilitation levers (such as tax treaties), must include an investment policy perspective.

Ongoing anti-avoidance discussions in the international community pay limited attention to investment policy. The role of investment in building the corporate structures that enable tax avoidance is fundamental. Therefore, *investment policy should form an integral part of any solution to tax avoidance.*

A set of guidelines for *coherent international tax and investment policies* may help realize the synergies between investment policy and initiatives to counter tax avoidance. Key objectives include removing aggressive tax planning opportunities as investment promotion levers; considering the potential impact on investment of anti-avoidance measures; taking a partnership approach in recognition of shared responsibilities between host, home and conduit countries; managing the interaction between international investment and tax agreements; and strengthening the role of both investment and fiscal revenues in sustainable development as well as the capabilities of developing countries to address tax avoidance issues.

WIR14 showed the massive worldwide financing needs for sustainable development and the important role that FDI can play in bridging the investment gap, especially in developing countries. In this light, strengthening the global investment policy environment, including both the IIA and the international tax regimes, must be a priority. The two regimes, each made up of a “spaghetti bowl” of over 3,000 bilateral agreements, are *interrelated*, and they face similar *challenges*. And *both are the object of reform* efforts. Even though each regime has its own specific reform priorities, there is merit in considering a joint agenda. This could aim for more inclusiveness, better governance and greater coherence to manage the interaction between international tax and investment policies, not only avoiding conflict between the regimes but also making them mutually supportive. The international investment and development community should, and can, eventually build a common framework for global investment cooperation for the benefit of all.

15

Global Investment Trends

C H A P T E R I

VIEW



A. CURRENT TRENDS

Global foreign direct investment (FDI) inflows fell by 16 per cent in 2014 to \$1.23 trillion, down from \$1.47 trillion in 2013.¹ The decline in FDI flows was influenced mainly by the fragility of the global economy, policy uncertainty for investors and elevated geopolitical risks. New investments were also offset by some large divestments. The decline in FDI flows was in contrast to growth in GDP, trade, gross fixed capital formation and employment (table I.1).

UNCTAD forecasts an upturn in FDI flows to \$1.4 trillion in 2015 and beyond (\$1.5 trillion in 2016 and \$1.7 trillion in 2017) due to growth prospects in the United States, the demand-stimulating effects of lower oil prices and accommodating monetary policy, and continued investment liberalization and promotion measures. Forecasts for macroeconomic fundamentals and continued high levels of profitability and cash reserves among multinational enterprises (MNEs) support the expectation of higher FDI flows. However, a number of economic and political risks, including ongoing uncertainties in the Eurozone, potential spillovers from geopolitical tensions, and persistent vulnerabilities in emerging economies, may disrupt the projected recovery.

1. FDI by geography

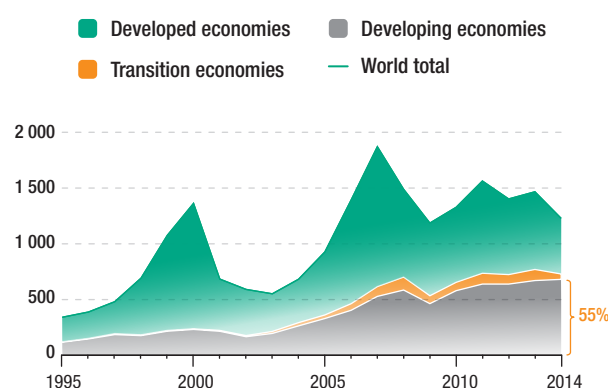
a. FDI inflows

The global FDI decline masks regional variations. While developed countries and economies in transition saw a significant decrease, inflows to developing economies remained at historically high levels.

FDI flows to the latter now account for 55 per cent of the global total (figure I.1). Developing Asia drove the increase while flows to Latin America declined and those to Africa remained flat.

FDI flows to *developed countries* dropped by 28 per cent to \$499 billion. Inflows to the United States fell to \$92 billion (40 per cent of their 2013 level), mainly due to Vodafone's divestment of Verizon, without which flows into the United States would have remained stable. FDI flows to Europe also fell by 11 per cent to \$289 billion. Among European economies, inflows decreased in Ireland, Belgium, France and Spain while they increased in the United Kingdom, Switzerland and Finland.

Figure I.1. FDI inflows, global and by group of economies, 1995–2014 (Billions of dollars)



Source: UNCTAD, FDI/MNE database (www.unctad.org/fdistatistics).

Table I.1.

Growth rates of global GDP, GFCF, trade, employment and FDI, 2008–2016 (Per cent.)

Variable	2008	2009	2010	2011	2012	2013	2014	2015 ^a	2016 ^a
GDP	1.5	-2.0	4.1	2.9	2.4	2.5	2.6	2.8	3.1
Trade	3.0	-10.6	12.6	6.8	2.8	3.5	3.4	3.7	4.7
GFCF	3.0	-3.5	5.7	5.5	3.9	3.2	2.9	3.0	4.7
Employment	1.2	1.1	1.2	1.4	1.4	1.4	1.3	1.3	1.2
FDI	-20.4	-20.4	11.9	17.7	-10.3	4.6	-16.3	11.4	8.4
Memorandum									
FDI value (in \$ trillions)	1.49	1.19	1.33	1.56	1.40	1.47	1.23	1.37	1.48

Source: UNCTAD, FDI/MNE database for FDI in 2008–2014; United Nations (2015) for GDP; IMF (2015) for GFCF and trade; ILO for employment; and UNCTAD estimates for FDI in 2015–2016.

^a Projections.

Note: FDI excludes Caribbean offshore financial centres. GFCF = gross fixed capital formation.

Methodological changes in FDI data compilation

In 2014, many countries adopted new guidelines for the compilation of FDI data, on the basis of the sixth edition of the International Monetary Fund's *Balance of Payments and International Investment Position Manual* (BPM6) and the fourth edition of the Organization for Economic Cooperation and Development's *Benchmark Definition of Foreign Direct Investment* (BD4). Two important aspects should be kept in mind in interpreting FDI statistics in this Report.

1. FDI statistics on an asset/liability basis vs the directional basis. On an *asset/liability basis*, direct investment statistics are organized according to whether the investment relates to an asset or a liability for the reporting country. On a *directional basis*, the direct investment flows and positions are organized according to the direction of the investment for the reporting economy – either inward or outward. The two presentations differ in their treatment of reverse investment (e.g. when an affiliate provides a loan to its parent).

Although presentation on an asset/liability basis is appropriate for macroeconomic analysis (i.e. the impact on the balance of payments), the directional basis is more useful in formulating investment policies because they capture the source or destination countries of direct investment and access to specific markets by direct investors. *UNCTAD will continue to report FDI data on the basis of the directional principle.*

2. Indirect or transit investment flows. BD4 recommends that countries compile FDI statistics in two ways, both including and excluding resident SPEs.² This recommendation provides a more meaningful measure of the FDI of an economy by removing FDI that involves funds passing through an SPE on their way to another destination (outward FDI) and those coming to the country through another economy's SPE (inward FDI). To avoid double counting, *UNCTAD removes SPE flows from its statistics where possible.* For similar reasons, FDI flows through offshore financial centres are excluded from analyses where possible.

Source: UNCTAD.

Note: Full details on methodological changes in UNCTAD's FDI data series are available online.

Inflows to *transition economies* declined by 52 per cent to \$48 billion, as regional conflict and sanctions deterred new foreign investors. FDI flows to the Russian Federation fell by 70 per cent to \$21 billion, in part an adjustment from the level reached in 2013 as a result of the Rosneft-BP mega-transaction (see *WIR14*).

FDI flows to *developing economies* increased by 2 per cent to a historically high level in 2014, reaching \$681 billion. *Developing Asia* drove the increase while flows to Latin America and the Caribbean declined and those to Africa remained flat (figure I.2). FDI flows to Asia grew by 9 per cent to \$465 billion in 2014. East Asia, South-East Asia and South Asia all saw increased inflows. FDI in China amounted to \$129 billion, up 4 per cent from 2013, mainly because of an increase in FDI in the services sector. FDI inflows also rose in Hong Kong (China) and Singapore. India experienced a significant increase of 22 per cent to \$34 billion. However, FDI flows to West Asia continued their downward trend in 2014 for the sixth consecutive year, decreasing by 4 per cent to \$43 billion, owing to the security situation in the region.

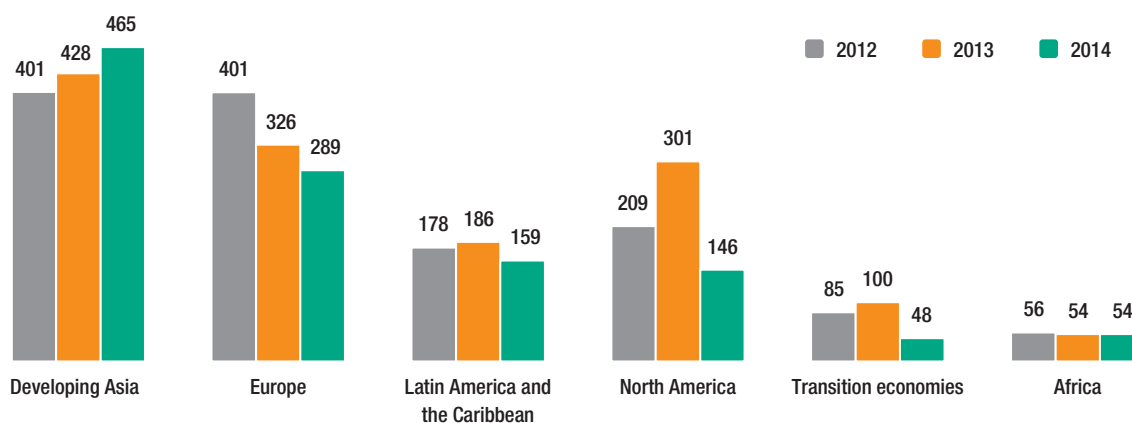
FDI flows to *Latin America and the Caribbean* – excluding the Caribbean offshore financial centres –

decreased by 14 per cent to \$159 billion in 2014, after four years of consecutive increases. This decrease was mainly the consequence of a 72 per cent decline in cross-border mergers and acquisitions (M&As) in Central America and the Caribbean, and of lower commodity prices, which reduced investment in the extractive industries in South America. While FDI flows to Mexico, the Bolivarian Republic of Venezuela, Argentina, Colombia and Peru declined, flows to Chile increased, owing to high levels of cross-border M&A sales. In Brazil, the sharp fall of FDI in the primary sector was compensated by an increase in FDI in manufacturing and services, keeping total flows similar to 2013 levels.

Inflows to *Africa* remained stable at \$54 billion. North Africa saw its FDI flows decline by 15 per cent to \$12 billion, while flows to Sub-Saharan Africa increase by 5 per cent to \$42 billion. In Sub-Saharan Africa, FDI flows to *West Africa* declined by 10 per cent to \$13 billion, as Ebola, regional conflicts and falling commodity prices negatively affected several countries. Flows to *Southern Africa* also fell by 2 per cent to \$11 billion. By contrast, *Central Africa* and *East Africa* saw their FDI flows increase by 33 per cent and 11 per cent, to \$12 billion and \$7 billion, respectively.

Figure I.2.

FDI inflows, by region, 2012–2014 (Billions of dollars)



Source: UNCTAD, FDI/MNE database (www.unctad.org/fdistatistics).

Structurally weak, vulnerable and small economies witnessed divergent trends in FDI flows in 2014. FDI to least developed countries (LDCs) increased by 4 per cent to \$23 billion, led by greenfield investment projects. Landlocked developing countries (LLDCs) experienced a fall of 3 per cent in FDI inflows to \$29 billion, mainly in Asia and Latin America. FDI inflows to small island developing States (SIDS) increased by 22 per cent to \$7 billion, boosted by a strong rise in cross-border M&As sales.

Overall, China became the largest FDI recipient in the world in 2014 (figure I.3), while the United States dropped to the third largest host country, primarily because of the large Verizon divestment by Vodafone (United Kingdom). Of the top 10 FDI recipients in the world, five are developing economies.

Most major regional groupings and groups of economies engaged in regional integration initiatives experienced a fall in inflows in 2014.

The global and regional declines in FDI inflows in 2014 affected the performance of FDI to regional groupings and initiatives. The groups of countries discussing the Transatlantic Trade and Investment Partnership (TTIP) and the Trans-Pacific Partnership (TPP), saw their combined share in global FDI flows decline. Two Asian groups bucked the trend – the Association of Southeast Asian Nations (ASEAN), with a 5 per cent increase in inflows, and the Regional Comprehensive Economic Partnership (RCEP), with a 4 per cent increase (figure I.4).

FDI trends in regional groups were largely determined by wider global trends, economic performance and geopolitical factors. Longer-term cooperation efforts will, for the most part, lead to increased FDI in regional groups, by opening sectors to investment and aligning policies for the treatment of investors. Intra-regional FDI may increase as a result of fewer investment restrictions (e.g. liberalizing investment in particular industries) or reduced transaction costs and converging policy regimes. Extraregional FDI (i.e. inflows by investors from outside a region) may increase as a result of enlarged market size (especially important for regional groups of smaller economies). Investment from outside a region may also increase as a result of coordinated efforts to promote regional investment.

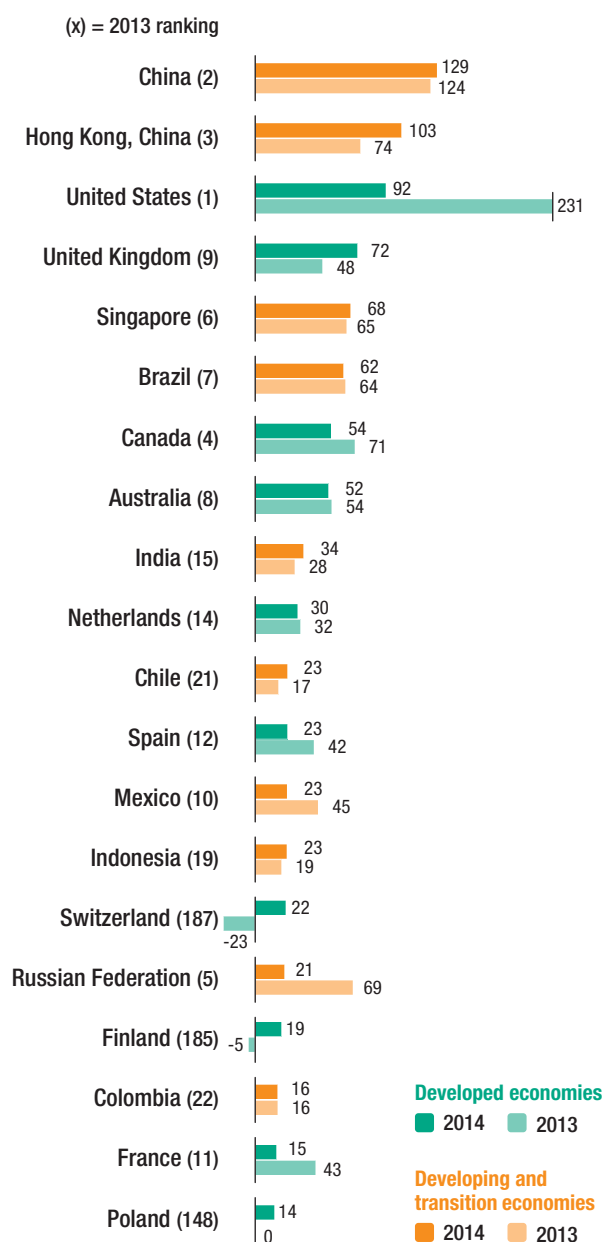
The impact of regional integration on intraregional and extraregional FDI varies considerably by region. The share of intraregional FDI among some regional groupings of developing economies in total inward FDI is still very low.³ In contrast, regional integration in Asia, e.g. through ASEAN, has had a significant impact on FDI. FDI inflows into the APEC economies reached \$652 billion in 2014, accounting for more than half of global FDI flows. Intra-APEC FDI flows and stocks are significant, at about 40 per cent of inward stock in 2009–2011.

b. FDI outflows

Investment by MNEs from developing and transition economies continued to grow.

Figure I.3.

FDI inflows: top 20 host economies, 2013 and 2014 (Billions of dollars)



Source: UNCTAD, FDI/MNE database (www.unctad.org/fdistatistics).

Note: Excludes Caribbean offshore financial centres.

Developing Asia became the world's largest investor region.

In 2014, MNEs from developing economies alone invested \$468 billion abroad, a 23 per cent increase from the previous year. Their share in global FDI reached a record 35 per cent, up from 13 per cent in 2007 (figure I.5).

Developing-country MNEs have expanded foreign operations through greenfield investments as well as cross-border M&As.

More than half of FDI outflows by developing-economy MNEs were in equity, while developed-country MNEs continued to rely on reinvested earnings, the share of which increased to a record 81 per cent of their FDI outflows (figure I.6). Equity-financed flows are more likely to result in new investments and capital expenditures than are reinvested earnings, which may translate into further accumulation of cash reserves in foreign affiliates.

Among developing economies, MNEs from Asia increased their investment abroad, while outflows from Latin America and the Caribbean, and Africa fell. For the first time, MNEs from developing Asia became the world's largest investing group, accounting for almost one third of the total (figure I.7). Nine of the 20 largest home economies were developing or transition economies, namely Hong Kong (China), China, the Russian Federation, Singapore, the Republic of Korea, Malaysia, Kuwait, Chile and Taiwan Province of China (figure I.8).

Outward investments by MNEs based in *developing Asia* increased by 29 per cent to \$432 billion in 2014. The growth was widespread, including all the major Asian economies and subregions. In East Asia, investment by MNEs from Hong Kong (China) jumped to a historic high of \$143 billion, making the economy the second largest investor after the United States. The remarkable growth was mainly due to booming cross-border M&A activity. Investment by Chinese MNEs grew faster than inflows into the country, reaching a new high of \$116 billion. In South-East Asia, the increase was principally the result of growing outflows from Singapore, to \$41 billion in 2014. In South Asia, FDI outflows from India reversed the slide of 2013, increasing fivefold to \$10 billion in 2014, as large Indian MNEs resumed their international expansion. Investments by West Asian MNEs declined by 6 per cent in 2014, owing to decreased flows from Kuwait, the region's largest overseas investor, with flows of \$13 billion. Investments by Turkish MNEs almost doubled to \$7 billion.

MNEs from *Latin America and the Caribbean*, excluding offshore financial centres, decreased their investment in 2014 by 18 per cent to \$23 billion.

Figure I.4.

FDI inflows to selected regional and interregional groups, 2013 and 2014

(Billions of dollars and per cent)

Regional/ interregional groups	2013		2014	
	FDI inflows (Billions of dollars)	Share in world (%)	FDI inflows (Billions of dollars)	Share in world (%)
APEC	837	57	652	53
G20	894	61	635	52
RCEP	349	24	363	30
TTIP	564	38	350	28
TPP	517	35	345	28
BRICS	294	20	252	21
NAFTA	346	24	169	14
ASEAN	126	9	133	11
MERCOSUR	83	6	73	6

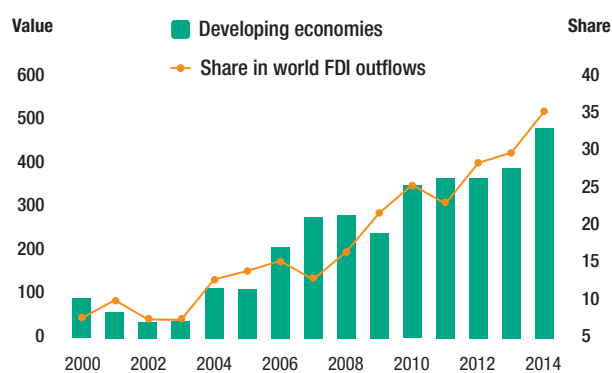
Source: UNCTAD, FDI/MNE database (www.unctad.org/fdistatistics).

Note: Ranked in descending order of 2014 FDI flows. G20 = only the 19 member countries of the G20 (excludes the European Union); APEC = Asia-Pacific Economic Cooperation; TTIP = Transatlantic Trade and Investment Partnership; TPP = Trans-Pacific Partnership; RCEP = Regional Comprehensive Economic Partnership; BRICS = Brazil, Russian Federation, India, China and South Africa; NAFTA = North American Free Trade Agreement; ASEAN = Association of Southeast Asian Nations; MERCOSUR = Common Market of the South.

Figure I.5.

Developing economies: FDI outflows and their share in total world outflows, 2000–2014

(Billions of dollars and per cent)



Source: UNCTAD, FDI/MNE database (www.unctad.org/fdistatistics).

Note: Excludes Caribbean offshore financial centres.

Outward flows from Mexican and Colombian MNEs fell by almost half to \$5 billion and \$4 billion, respectively. In contrast, investment by Chilean MNEs – the region's main direct investors abroad for the year – increased by 71 per cent to \$13 billion, boosted by a strong increase

in intracompany loans. Brazilian MNEs continued to receive repayments of loans or to borrow from their foreign affiliates, resulting in negative FDI outflows from that country for the fourth consecutive year.

Outward investments by MNEs in *Africa* decreased by 18 per cent in 2014 to \$13 billion. South African MNEs invested in telecommunications, mining and retail, while those from Nigeria focused largely on financial services. These two largest investors from Africa increased their investments abroad in 2014. Intra-African investments rose significantly during the year.

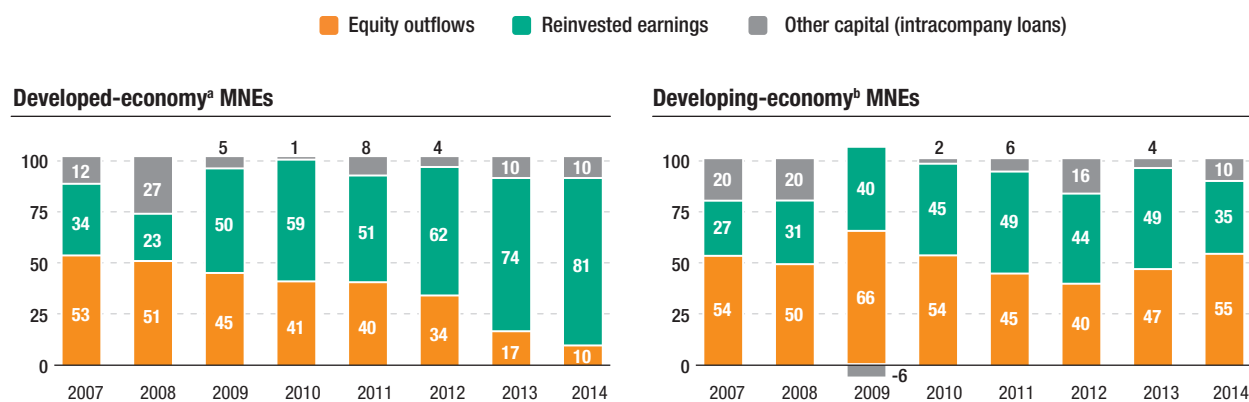
MNEs from *transition economies* decreased their investments abroad by 31 per cent to \$63 billion. Natural-resource-based MNEs, mainly from the Russian Federation, reduced investments in response to constraints in international financial markets, low commodity prices and the depreciation of the rouble.

Investments from MNEs based in *developed economies* were almost steady at \$823 billion at the aggregate level, but this figure hides a large number of new investments and divestments that cancelled each other out.

Outflows from *European* MNEs remained flat. A robust rise in investments by German and French MNEs

Figure I.6.

FDI outflows by component, by group of economies, 2007–2014
(Per cent)



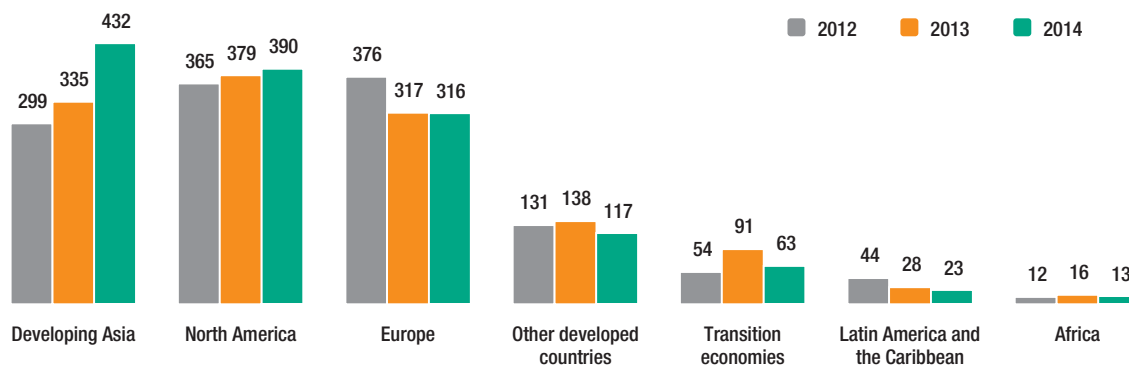
Source: UNCTAD, FDI/MNE database (www.unctad.org/fdistatistics).

^a Economies included are Australia, Belgium, Bulgaria, Canada, Croatia, Cyprus, the Czech Republic, Denmark, Estonia, Finland, Germany, Greece, Hungary, Iceland, Ireland, Israel, Latvia, Lithuania, Luxembourg, Malta, the Netherlands, Norway, Portugal, Slovakia, Slovenia, Spain, Sweden, Switzerland, the United Kingdom and the United States.

^b Economies included are Algeria, Anguilla, Antigua and Barbuda, Aruba, the Bahamas, Bahrain, Bangladesh, Barbados, Belize, the Plurinational State of Bolivia, Botswana, Brazil, Cambodia, Cabo Verde, Chile, Costa Rica, Curaçao, Dominica, El Salvador, Fiji, Grenada, Guatemala, Honduras, Hong Kong (China), India, Indonesia, the Republic of Korea, Kuwait, Lesotho, Malawi, Mexico, Mongolia, Montserrat, Morocco, Namibia, Nicaragua, Nigeria, Pakistan, Panama, the Philippines, Saint Kitts and Nevis, Saint Lucia, Saint Vincent and the Grenadines, Samoa, Sao Tome and Principe, Seychelles, Singapore, Sint Maarten, South Africa, Sri Lanka, the State of Palestine, Suriname, Swaziland, Taiwan Province of China, Thailand, Trinidad and Tobago, Turkey, Uganda, Uruguay, the Bolivarian Republic of Venezuela and Viet Nam.

Figure I.7.

FDI outflows, by group of economies and region, 2012–2014
(Billions of dollars)



Source: UNCTAD, FDI/MNE database (www.unctad.org/fdistatistics).

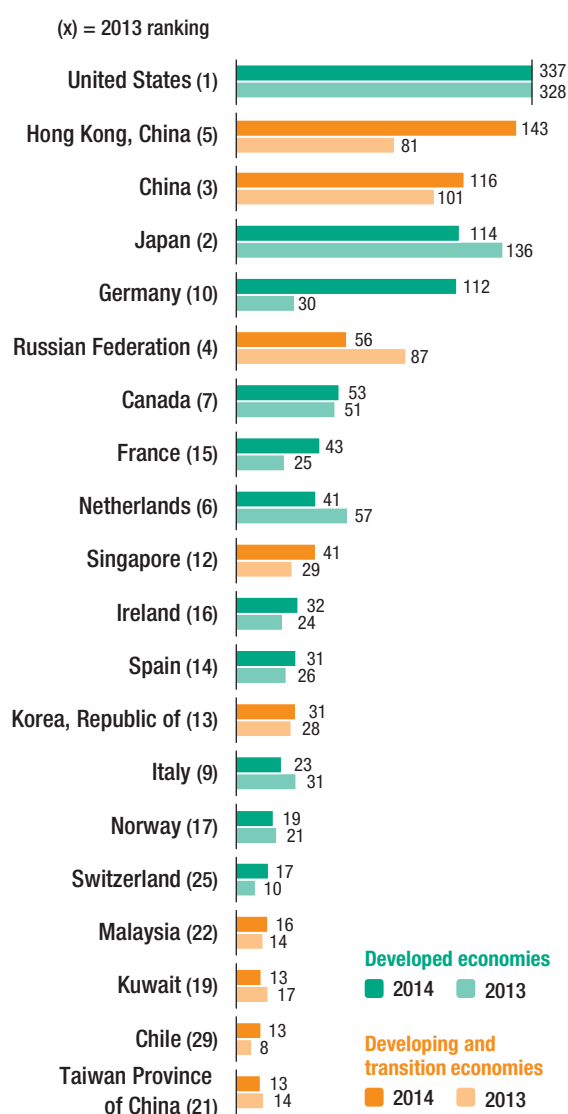
Note: Excludes Caribbean offshore financial centres.

was offset by the negative flows from MNEs in the United Kingdom and Luxembourg. Germany became the largest investing country in Europe. Vodafone's divestment of its stake in Verizon Wireless heavily dented outflows from the United Kingdom (down \$45 billion to -\$60 billion). Outflows from Luxembourg fell sharply (down from \$35 billion to -\$4 billion), primarily due to changes in intracompany loans.

In *North America*, active acquisitions of assets by Canadian MNEs increased Canada's outflows by 4 per

cent to \$53 billion. FDI from the United States rose by 3 per cent to \$337 billion. Investment in and divestment from equity, and the withdrawal of intracompany loans cancelled each other out, so that United States outward investment in 2014 effectively consisted only of reinvested earnings. FDI from *Japan* declined by 16 per cent, ending a three-year expansion. Although Japanese MNEs' investments into North America remained stable, they declined sharply in major recipient economies in Asia and Europe.

Figure I.8. FDI outflows: top 20 home economies, 2013 and 2014
(Billions of dollars)



Source: UNCTAD, FDI/MNE database (www.unctad.org/fdistatistics).
Note: Excludes Caribbean offshore financial centres.

c. Intensity index and South–South FDI

South–South FDI flows, including intraregional flows, have intensified in recent years. FDI from developing economies has grown significantly over the last decade and now constitutes over a third of global flows. The largest outward investing economies include Brazil, China, Hong Kong (China), India, the Republic of Korea, Malaysia, Mexico, Singapore, South Africa and Taiwan Province of China. FDI outward stock from

developing economies to other developing economies, excluding Caribbean offshore financial centres, grew by two-thirds from \$1.7 trillion in 2009 to \$2.9 trillion in 2013. East Asia and South-East Asia were the largest recipient developing regions by FDI stock in 2013 (figure I.9). The share of the poorest developing regions in South-South FDI is still low, but it is growing.

Most developing-economy investment tends to occur within each economy's immediate geographic region. Familiarity eases a company's early internationalization drive, and regional markets and value chains are a key driver. The strong regional links of South African FDI are a particular case in point, as shown by the country's high bilateral FDI intensities with neighbouring countries (table I.2).

Beyond the familiarity of immediate regions, factors determining the specific patterns of South-South FDI include MNE investment motives, home government policies and historical connections (*WIR06*). In terms of motives, for example, MNEs from the Republic of Korea investing for efficiency-seeking reasons especially target East and South East Asia, whereas South Asia is also a destination for those looking for markets. In a similar vein, the geography of natural resources determines FDI in extractive industries to a high degree; hence, for instance, the high bilateral FDI intensities between China and a number of African countries.

Home government policies can also strongly influence patterns of FDI internationalization. The narrow geographic dispersal of Singapore MNEs has been influenced by the country's strategic policy encouraging enterprise internationalization into nearby Asian countries.

Finally historical connections, such as diaspora, also affect the location of investments, which partly explains the high FDI intensity between India and countries such as Kenya, Gabon and the United Arab Emirates.

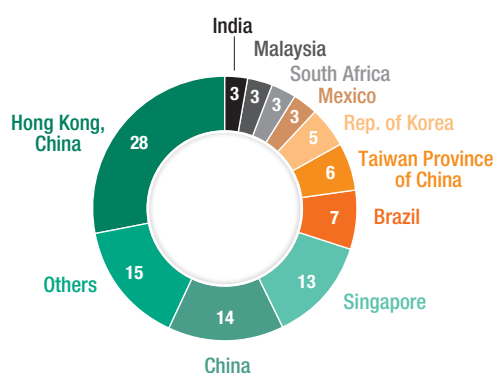
2. FDI by mode of entry

Significant momentum for cross-border M&As, decline in greenfield FDI projects.⁴ After two consecutive years of decline, M&A activity resumed growth in 2014 (figure I.10). In net terms,⁵ the value of cross-border M&As increased by 28 per cent over 2013, reaching almost \$400 billion. MNEs have gradually regained the confidence to go back on the acquisition trail.

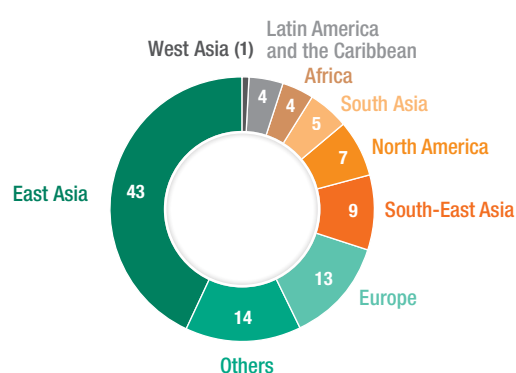
Figure I.9.

FDI stock by developing economies: major source economies and destination regions, 2013 (Per cent)

Major developing-economy sources of FDI



Developing-economy FDI by major destination regions



Source: UNCTAD, FDI/MNE database (www.unctad.org/fdistatistics).

The value of cross-border M&As in developed economies increased by 16 per cent and those in developing and transition economies by 66 per cent.

Investors' appetite for new greenfield investment projects is less buoyant. After a first rebound in 2013, the total value of announced greenfield investment declined slightly by 2 per cent, remaining close to the \$700 billion level of 2013. In particular, in 2014 the value of greenfield projects in developed and developing economies was substantially unchanged compared with 2013 (annual growth rates of –1 per cent in both groupings), while transition economies saw a considerable fall (–13 per cent).

MNEs back on the acquisition trail. The gross value of cross-border M&A deals increased in 2014 by 34 per cent, hitting \$900 billion, considerably above the recent annual average (\$775 billion during the period 2010–2014). The acquisition wave involved both manufacturing (up 77 per cent in the gross value of cross-border M&As) and services (up 36 per cent). Although growth occurred across all industries in the two sectors, the chemicals and pharmaceutical industries and the telecommunications industry were particularly active, as evidenced by some large deals.

The return of large deals. The re-emergence of large deals was one key factor in the increased cross-border deal activity. The largest MNEs were more willing to use their significant cash reserves to engage in large cross-border operations. In 2014, the number of M&A deals with values larger than \$1 billion expanded, from 168

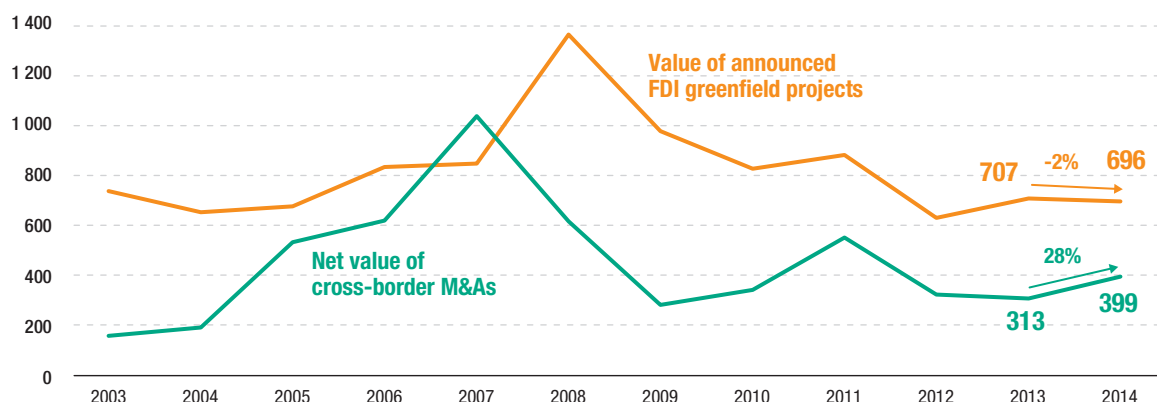
to 223 – the highest number since 2008. The average value of these deals was almost \$3.4 billion, compared with \$2.9 billion in 2013. Of the 223 largest deals, 173 took place in developed economies, with a value of \$598 billion or some 77 per cent of the total value of large deals (\$762 billion).

United States companies represented an attractive target, absorbing more than one third of the largest M&A acquisitions globally. European MNEs targeted the United States market, in particular pharmaceutical firms but also other industries. For example, Germany-based Bayer purchased the consumer care business of Merck for \$14.2 billion, and Swiss Roche Holding acquired Intermune for \$8.3 billion. In January 2014, Italian automaker Fiat completed its acquisition of Chrysler for \$3.65 billion, gaining full ownership.

Large M&A deals in Europe occurred predominantly in the telecommunications industry. Of the five largest acquisitions in Europe, three were in telecommunications, and all were led by other European MNEs. The largest deal was the acquisition of SFR SA (France) by Altice SA (Luxembourg) for \$23 billion.

Divestments: the other side of MNEs' cross-border M&A activity. MNEs resorted to strategic transactions not only to expand but also to downsize their international assets. The value of sales of MNEs' stakes in foreign entities (divestments,⁶ including sales to domestic firms or to other MNEs) reached a record high in 2014, at \$511 billion, a 56 per cent increase over 2013

Figure I.10. Value of cross-border M&As and announced greenfield projects, 2003–2014
(Billions of dollars)



Source: UNCTAD, cross-border M&A database for M&As (www.unctad.org/fdistatistics); Financial Times Ltd, fDi Markets (www.fDimarkets.com) for greenfield projects.

(figure I.11) and the highest value since 2008. This value was split almost equally in transactions between sales to other MNEs (52 per cent) and transfers from MNEs to domestic companies (48 per cent).

The wave of divestments reflects an increase in overall cross-border M&A activity, rather than signalling ongoing “de-internationalization” through M&As. In fact, the ratios in figure I.11 show that the share of divestments (*divested deals*) relative to acquisitions (*gross M&A deals*) is on par with the recent historical average, after removing the impact of the Vodafone divestment in Verizon.

Developing-economy MNEs continued “shopping” for developed-country MNE assets in developing economies. MNEs from developing and transition economies are consolidating their role as investors in cross-border M&A operations. The share of these MNEs in the total (net) value of cross-border M&As rose from about 10 per cent in 2003 to almost 40 per cent in 2012 and has remained stable since then.

The bulk of acquisitions by MNEs from developing economies (about 70 per cent) are in other developing economies (including intraregional transactions). A sizable share (about 50 per cent) of their M&A activity in developing economies represents the acquisition of assets from developed-economy MNEs (*WIR14*). In 2014, MNEs continued to acquire firms and other assets owned by developed-country MNEs in host developing economies. For example, MMG South America Management Co Ltd (Hong Kong, China) acquired Xstrata Peru – a foreign affiliate of Glencore/Xstrata (Switzerland)

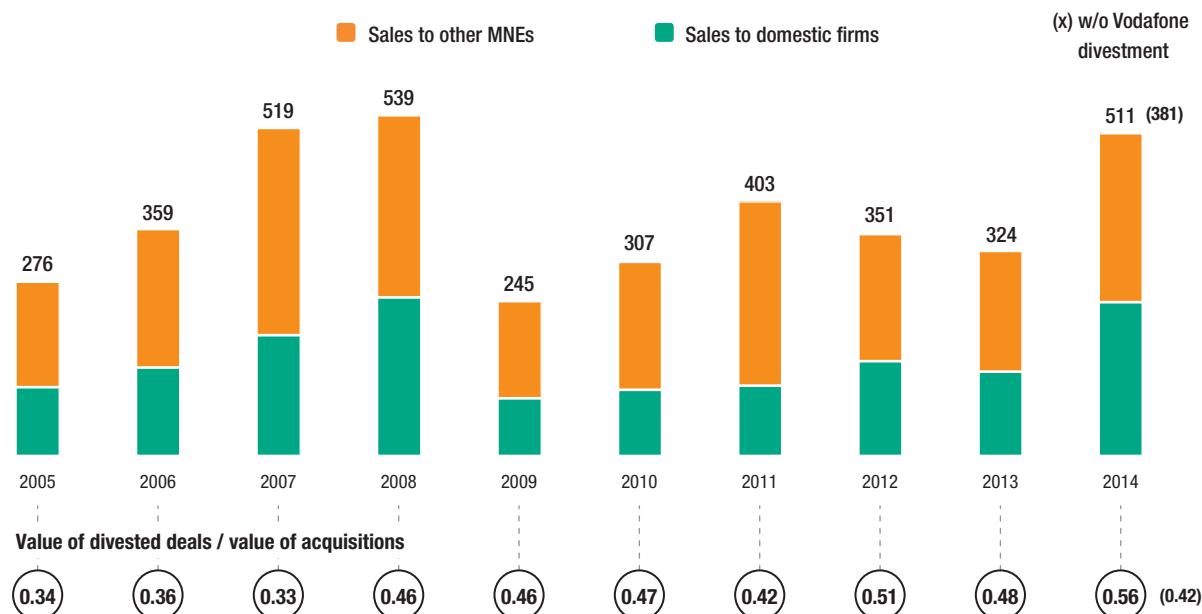
– for \$7 billion, and Emirates Telecommunications Corp (United Arab Emirates) bought a 53 per cent stake of Itissalat Al Maghrib SA – a foreign affiliate of Vivendi (France) – for \$5.7 billion.

MNEs from developing economies are becoming more active directly in developed economies as well. In 2014, some 32 per cent of M&A acquisitions by these MNEs targeted developed economies, more than in 2013 (at 28 per cent); in the first three months of 2015, acquisitions by these MNEs in developed economies rose to 47 per cent of their total M&A purchases. A number of sizable deals involved MNEs from China, Hong Kong (China) and Singapore, targeting companies in the United States and the United Kingdom in particular. For example GIC, Singapore’s sovereign wealth fund, acquired IndCor Properties (United States) for \$8.1 billion.

In greenfield projects, developing economies dominate. At the global level, announced greenfield FDI projects declined slightly in 2014. This decline is similar in both developed and developing economies (figure I.12). Greenfield projects in developing economies increased in 2013 and remained high in 2014, while the trend in developed economies remained stable.

A similar trend is observable on the investor side. Over the last 10 years, the announced value of greenfield projects from developed-economy MNEs has been essentially flat, with a compound annual growth rate (CAGR) of –1 per cent, while the same value for developing economies has increased steadily despite the financial crisis (at a CAGR of 5 per cent).

Figure I.11. Divested M&A deals, value, 2005–2014 (Billions of dollars)



Source: UNCTAD, cross-border M&A database (www.unctad.org/fdistatistics).

As a consequence, developing economies have gained 10 percentage points in the global value of announced greenfield FDI projects, from 20 per cent in 2005 to 30 per cent in 2014.

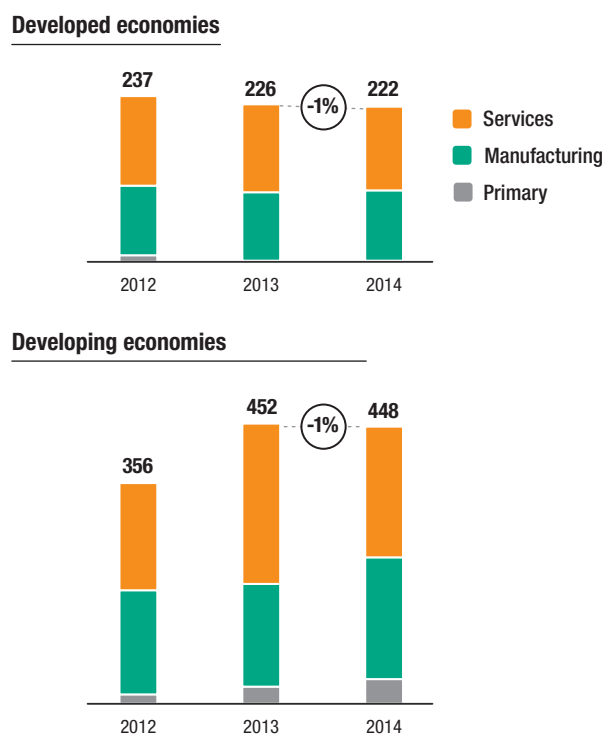
3. FDI by sector and industry

FDI stock data by sector highlight the prominent role of services in global FDI. In 2012, the latest year for which sectoral data are available, *services* accounted for 63 per cent of global FDI stock, more than twice the share of *manufacturing*, at 26 per cent. The *primary sector* contributed less than 10 per cent to global FDI stock (figure I.13).

The importance of services in the international investment landscape is the result of a long-term structural trend. In the period 2001–2012, the share of services in global FDI increased by 5 per cent (to 63 per cent), offset by a comparable decrease in the share of manufacturing. Overall, since 1990, the share of services in world FDI stock has gained 14 percentage points (from 49 per cent to 63 per cent) with a corresponding decrease in manufacturing (from 41 per cent to 26 per cent), while the share of the primary sector has been stable (at about 7 per cent). The ongoing shift in the sectoral composition of FDI from manufacturing to services

Figure I.12.

Value of announced greenfield FDI projects, by sector and economic grouping, 2012–2014 (Billions of dollars)



Source: UNCTAD, information from the Financial Times Ltd, fDi Markets (www.fdimarkets.com).

reflects an analogous trend in the distribution of global GDP, but it is also the result of increasing liberalization in the sector, enabling large FDI inflows, particularly in industries traditionally closed to foreign investment such as finance and telecommunications. This shift has occurred in both developed and developing economies. Among developing regions, Asia and Oceania has been the growth engine for services FDI, with services stock in the region increasing from about \$800 billion in 2001 to \$3.5 trillion in 2012, corresponding to roughly 80 per cent of the total growth of services FDI in the developing economies. This sector is also the largest in Africa (chapter II.A.1). Between developing regions, pronounced differences emerge in terms of industry distribution.

Recent trends in FDI by sector and industry. The most recent data on announced greenfield FDI projects and cross-border M&As reveal various sectoral trends (figure I.14). Globally in 2014, the primary sector recorded high growth in the value of greenfield projects (up 42 per cent from 2013), in the face of a decrease in the value of cross-border M&As (-2 per cent). The pattern ran the other way in the services sector, with a decrease in the value of greenfield projects (-15 per cent) and a strong increase in cross-border M&As (37 per cent). In manufacturing, the picture is consistent across the two modes of entry, with an increase of 14 per cent in greenfield projects and 25 per cent in cross-border M&As.

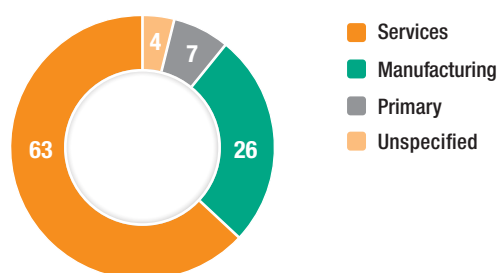
FDI in the *primary sector* is driven mostly by the extractive industry in developing economies. In 2014,

the value of greenfield FDI projects in *mining, quarrying and petroleum* in developing economies increased 60 per cent, from \$25 billion to \$40 billion. The bulk of the growth took place in Africa, where the total value of greenfield projects increased almost six-fold (from \$4 billion to \$22 billion). The increase in cross-border M&As in the extractive industry in developing economies, in contrast, was moderate, from -\$2 billion in 2013 to \$3 billion in 2014.

Manufacturing greenfield FDI projects rose from \$275 billion in 2013 to \$312 billion in 2014 (14 per cent). The fastest-growing industries were coke, petroleum products and nuclear fuels (60 per cent), machinery and equipment (29 per cent), and motor vehicles and other transports (32 per cent).

Unlike in developing economies (18 per cent), the value of greenfield FDI projects in developed economies was stable, levelling off for a third consecutive year between \$90 billion and \$100 billion, with no major trends discernible in individual manufacturing industries.

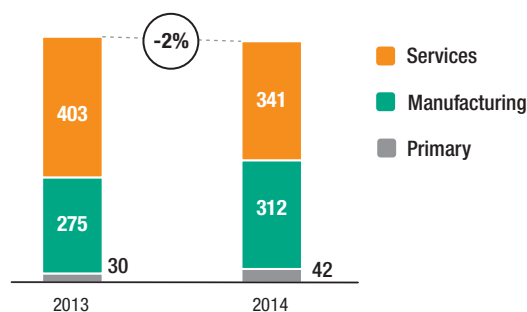
Figure I.13. Global inward FDI stock, by sector, 2012
(Per cent of total value)



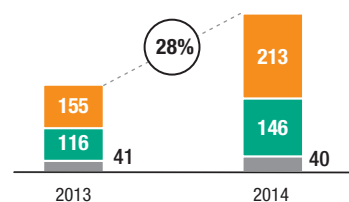
Source: UNCTAD FDI/MNE database (www.unctad.org/fdistatistics).

Figure I.14. FDI projects, by sector, 2013–2014 (Billions of dollars)

Value of FDI announced greenfield projects, 2013–2014



Value of cross-border M&A, 2013–2014



Source: UNCTAD, cross-border M&A database for M&As and information from the Financial Times Ltd, fDI Markets (www.fDimarkets.com) for greenfield projects.

Developed and developing economies display opposite trends in M&A activity in manufacturing. In 2014, there was a considerable increase in M&As in developed economies, with the total net value of deals rising from \$85 billion to \$152 billion (79 per cent). The growth was most marked in electrical and electronic equipment (125 per cent) and in food, beverages and tobacco (55 per cent). There was a sharp decrease in M&As in developing economies (from \$45 billion to \$16 billion); the decline occurred across most industries, particularly in food, beverages and tobacco, where the value of cross-border M&As plummeted to \$4 billion after peaking in 2013 at a historically high \$32 billion.

Services saw contrasting trends in greenfield FDI projects and cross-border M&As. While the total value of greenfield projects decreased (–15 per cent compared with 2013), the value of cross-border M&As registered a significant increase, from \$155 billion to \$213 billion (37 per cent).

The value of greenfield projects in developing economies decreased (from \$259 billion in 2013 to \$211 billion in 2014), but with differentiated dynamics at the industry level. *Construction* jumped from \$22 billion to \$42 billion and became the second largest service industry in developing economies, overtaking industries that traditionally receive large amounts of FDI, such as *finance* and *business services*. By contrast, both *business services* and *electricity, gas and water* – after strong expansion in 2013 (at \$76 billion and \$63 billion) – fell by 52 per cent and 27 per cent, respectively. Contraction in *business services* was particularly critical in Latin America and the Caribbean (–88 per cent), while *electricity, gas and water* declined in both Latin America and the Caribbean (–22 per cent) and West Asia (–77 per cent).

In developing economies, the growth engine of cross-border M&As in services was the increase in *finance* (from \$18 billion to \$61 billion), in particular in East and South-East Asia. For developed economies, the picture is multifaceted. While the traditionally largest FDI industries, *business services* and *finance*, saw a considerable increase, from \$36 billion to \$66 billion and from \$9 billion to \$30 billion respectively, the value of *information and communication* took a sharp downturn to a negative value (–\$73 billion against \$29 billion in 2013) because of the Vodafone divestment.

4. FDI by selected types of special investors

a. Private equity firms

Cross-border M&As by private equity funds rose.

The total value of cross-border M&As undertaken by private equity funds rose to \$200 billion in 2014 (table I.3), accounting for about 17 per cent of the global total. This share declined by 6 percentage points from 2013 and was 13 percentage points lower than in 2007 and 2008. In 2014 alone, global private equity funds cashed in about \$115 billion from previous overseas M&A deals, bringing the value of net cross-border M&As to \$85 billion. As the amount of cash and commitments from investors is at a very high level (estimated at about \$360 billion) and interest rates in developed countries remain low, prospects for private equity funds' leveraged international transactions are promising. Furthermore, more active global financial markets are expected to generate more cross-border investment opportunities.

The largest funds have played an increasingly important role in the global private equity market. In terms of fund raising, nine mega-funds attracted more than \$5 billion each, amounting to nearly half of the total capital raised by private equity funds in 2013. This contributed to an overall 21 per cent increase in global fund raising.⁷ As these mega-funds tend to invest in megadeals, the significance of private equity funds in the global picture of cross-border M&As is reflected in transactions involving large companies from large host-country economies. For example, 3G Capital (Brazil and the United States) was behind the merger of Tim Hortons (Canada) and Burger King Worldwide (United States) in 2014 which, at \$12.5 billion, was the largest international buyout of the year.

North America and Europe continued to be the major regions targeted for cross-border M&As by private equity funds in 2014. In Canada, for example, Blackstone (United States) acquired Gates Corporation – a manufacturer of power transmission belts and fluid power products – for \$5.4 billion, and TPG Capital Management LP (United States) bought Warranty Group – a provider of extended warranty contracts from the local Onex Corp for \$1.5 billion. These two large private equity funds have been important players in M&A markets not only in North America, but also

Table I.3.

Cross-border M&As by private equity firms, 1996–2014
 (Number of deals and value)

Year	Number of deals		Gross M&As		Net M&As	
	Number	Share in total (%)	Value (\$ billion)	Share in total (%)	Value (\$ billion)	Share in total (%)
1996	970	16	43	16	18	12
1997	1 057	15	58	15	18	10
1998	1 228	15	62	9	28	8
1999	1 451	15	80	9	27	5
2000	1 457	14	82	6	30	3
2001	1 435	17	82	11	34	8
2002	1 281	19	71	14	13	5
2003	1 555	23	91	23	31	19
2004	1 675	22	134	25	62	31
2005	1 842	20	202	22	103	19
2006	1 859	18	259	23	115	18
2007	2 046	17	528	30	279	27
2008	1 946	18	437	31	103	17
2009	2 083	24	105	17	62	22
2010	2 195	22	144	19	66	19
2011	1 953	19	155	15	66	12
2012	2 209	23	188	23	63	19
2013	1 964	23	169	23	82	26
2014	2 358	24	200	17	85	21

Source: UNCTAD, cross-border M&A database (www.unctad.org/fdistatistics).

Note: Value on a net basis takes into account divestments by private equity funds. Thus it is calculated as follows: Purchases of companies abroad by private equity funds (-) Sales of foreign affiliates owned by private equity funds. The table includes M&As by hedge and other funds (but not sovereign wealth funds). Private equity firms and hedge funds refer to acquirers as "investors not elsewhere classified". This classification is based on the Thomson Finance database on M&As.

in other developed regions and in developing ones. With \$67 billion under management, for instance, TPG Capital has established significant operations in Asia and Europe since the mid-1990s.

Asia has become increasingly attractive. In 2014, both the amount of transactions and their share in total private equity deals reached historically high levels (figure I.15). In East Asia, both China and the Republic of Korea experienced more deal making activities. In China, a number of megadeals were implemented, including pre-IPO deals related to Alibaba and JD.com, the country's leading e-commerce companies. In the Republic of Korea, Carlyle Group undertook a \$2 billion carve-out of the Korean unit of ADT, owned by Tyco (Switzerland). In South-East Asia, strong inflows of foreign private equity funds drove up the value of transactions but also led to fierce competition between funds.

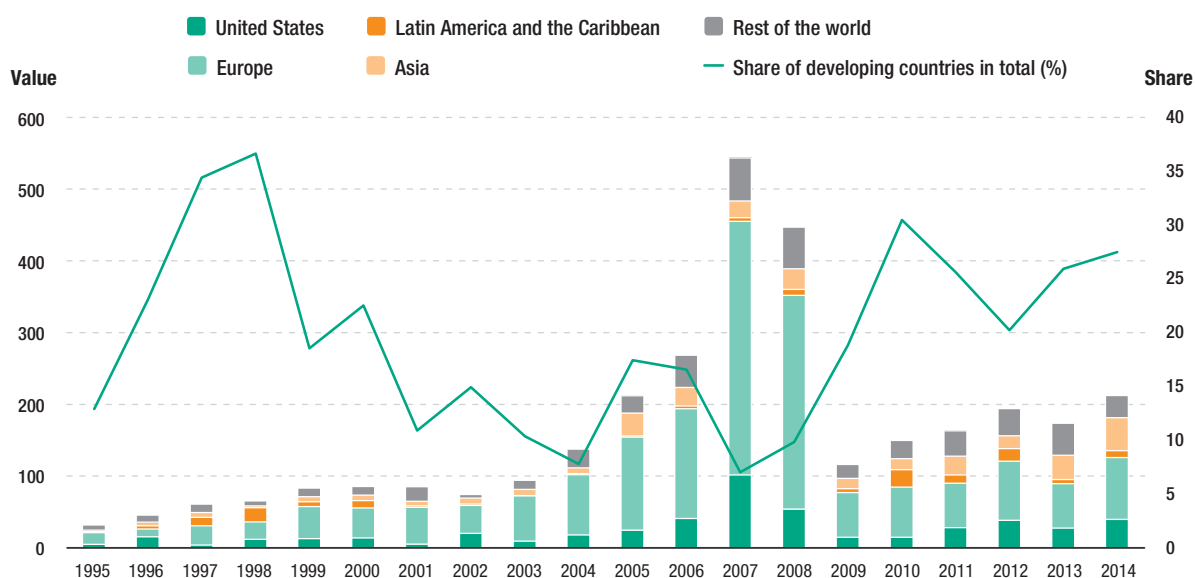
b. SWFs

FDI by SWFs more than doubled in 2014. There are more than 100 sovereign wealth funds (SWFs), managing more than \$7 trillion of assets in 2014 and

accounting for about one tenth of the world's total assets under management. These funds are in a strong position to influence global financial and capital markets, but are much less active in FDI. The value of their FDI has been marginal compared with the value of assets under management. During the period 2011–2013, the value of their FDI dropped continuously, but the downward trend has reversed (figure I.16). In 2014, the amount of FDI by SWFs more than doubled to reach \$16 billion, the highest level in five years. It was driven by large cross-border M&As undertaken by SWFs of a limited number of countries, in particular Singapore. There, Temasek Holdings acquired a 25 per cent stake in AS Watson Holdings (Hong Kong, China) for \$5.7 billion, while GIC Pte bought an 11 per cent stake in Emperor Inc. (Philippines) for \$390 million.

Many SWFs whose sources of finance rely on oil revenues (approximately 60 per cent of all SWFs) have had to face lower oil prices since mid-2014. This may affect their sources of funds in the near future, as well as their scale of investment. For a number of Asian SWFs, decelerated export growth may have similar effects.

Figure I.15. FDI by private equity funds, by major host region, 1995–2014
(Billions of dollars and per cent)

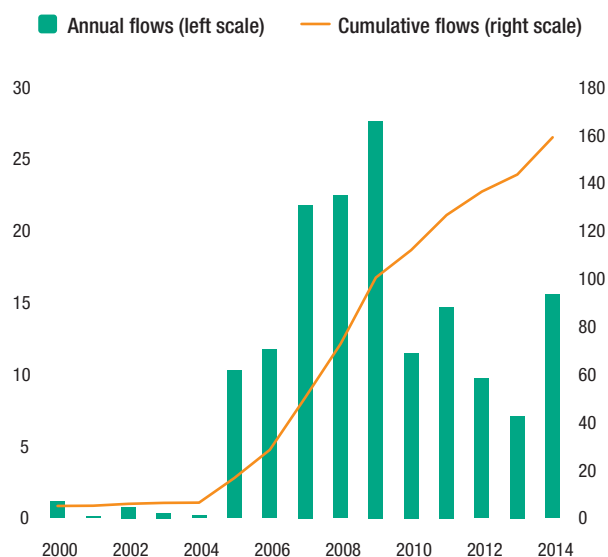


Source: UNCTAD, cross-border M&A database (www.unctad.org/fdistatistics).
Note: Data refer to gross values of M&As by private equity firms; they are not adjusted to exclude FDI by SWFs.

Some SWFs have engaged in long-term investments; they are increasingly involved in FDI projects, including through cross-border corporate acquisitions and overseas real estate purchases. For example, the Norwegian SWF, the world's largest in terms of assets under management, will increase the number of companies in which it can own more than 5 per cent equity to 100; its long-term investment in venture capital, private equity funds and real estate assets is on the rise.

As an increasingly important asset class, infrastructure offers SWFs some specific advantages for their portfolio management, including, for instance large-scale investment opportunities, and relatively stable returns. Consequently, more than half of SWFs have already started to invest in infrastructure. For example, GIC of Singapore has been an important investor in the sector in both developed countries and emerging markets, aiming at operating infrastructure assets.⁸ CIC (China) has included infrastructure projects in its investment strategy under the overall category of long-term assets, which account for 28 per cent of its total assets. In late 2014, GIC planned to participate in a \$1.6 billion co-investment in three airports in the United Kingdom. The company already owns a part of Heathrow Airport Holdings, together with other SWFs, including CIC, Qatar Holding and Caisse de Dépôt et Placement du Québec.

Figure I.16. Annual and cumulative value of FDI by SWFs, 2000–2014
(Billions of dollars)



Source: UNCTAD, cross-border M&A database for M&As (www.unctad.org/fdistatistics) and information from the Financial Times Ltd, fDi Markets (www.fDimarkets.com) for greenfield projects.

Note: Data should be considered approximate, as they include the value of flows for both cross-border M&As and announced greenfield FDI projects (for limitations of announced greenfield projects data, see the note in the section on modes of entry) and only investments in which SWFs are the sole and immediate investors. Data do not include investments made by entities established by SWFs or those made jointly with other investors. In 2003–2014, cross-border M&As accounted for about 60 per cent of the total.

c. State-owned MNEs

Internationalization of SO-MNEs continued in 2014 but it is slowing down.

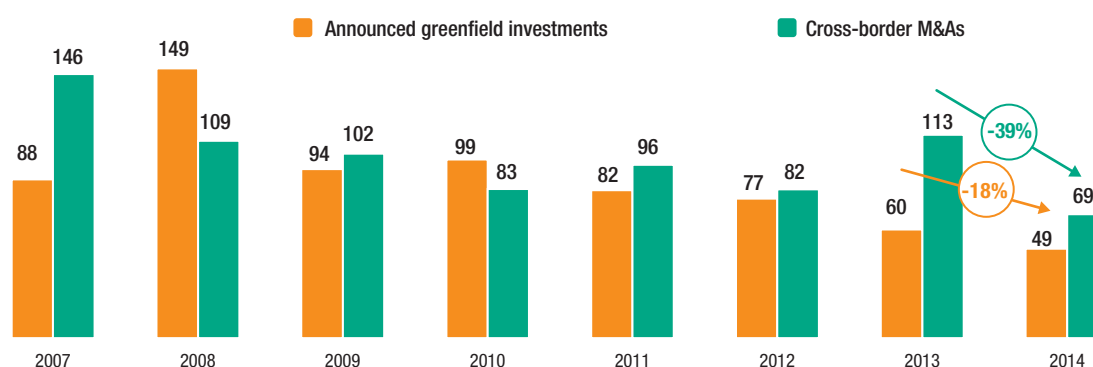
The amount of cross-border M&As and greenfield projects in 2014 dropped by 39 per cent to \$69 billion and 18 per cent to \$49 billion, respectively, to their lowest levels since the outbreak of the global financial crisis. In particular, the amount of announced greenfield investment by SO-MNEs has declined for four consecutive years – to only one third of the 2008 peak (figure I.17).

A number of SO-MNEs continued to consolidate their global activities. For instance, GDF Suez (France), the fifth largest SO-MNE in terms of foreign activities

(foreign sales, assets and employment; see table I.4), initiated a three-year, \$11 billion divestment programme in 2012, leading to significant sales of assets in Belgium, Italy and other countries. A number of other large SO-MNEs from developed countries undertook similar divestment programmes. Policy factors have also negatively affected the internationalization of SO-MNEs. For instance, stricter control of foreign ownership in extractive industries has reduced the access of SO-MNEs to mineral assets in a number of countries, for example in Latin America. From the home-country perspective, some government policy measures have also affected the degree of international investment of SO-MNEs.

Figure I.17.

Value of recorded cross-border M&As and announced greenfield investments undertaken by SO-MNEs, 2007–2014 (Billions of dollars)



Source: UNCTAD, cross-border M&A database for M&As (www.unctad.org/fdistatistics) and information from the Financial Times Ltd, fDi Markets (www.fDimarkets.com) for greenfield projects.

Table I.4.

The top 10 non-financial State-owned MNEs, ranked by foreign assets, 2013 (Millions of dollars and number of employees)

SO-MNE	Home economy	Industry	Assets		Sales		Employment		Transnationality Index ^a
			Foreign	Total	Foreign	Total	Foreign	Total	
Volkswagen Group	Germany	Motor vehicles	176 656	446 555	72 133	118 561	73 000	147 199	50
Eni SpA	Italy	Petroleum	141 021	190 125	211 488	261 560	317 800	572 800	70
Enel SpA	Italy	Utilities (electricity, gas and water)	140 396	226 006	109 886	152 313	56 509	83 887	67
EDF SA	France	Utilities (electricity, gas and water)	130 161	353 574	61 867	106 924	37 125	71 394	49
GDF Suez	France	Utilities (electricity, gas and water)	121 402	219 759	46 978	100 364	28 975	158 467	40
Deutsche Telekom AG	Germany	Telecommunications	120 350	162 671	50 049	79 835	111 953	228 596	62
CITIC Group	China	Diversified	97 739	703 666	11 127	60 586	25 285	125 215	17
Statoil ASA	Norway	Petroleum	78 185	144 741	23 953	105 446	3 077	23 413	30
Airbus Group NV	France	Aircraft	77 614	128 474	72 525	78 672	89 551	144 061	72
General Motors Co	United States	Motor vehicles	70 074	166 344	56 900	155 427	104 000	219 000	42

Source: UNCTAD, cross-border M&A database for M&As and information from the Financial Times Ltd, fDi Markets (www.fDimarkets.com) for greenfield projects.

^a The Transnationality Index is calculated as the average of the following three ratios: foreign assets to total assets, foreign sales to total sales, and foreign employment to total employment.

Note: These MNEs are at least 10 per cent owned by the State or public entities, or the State/public entity is the largest shareholder.

B. INTERNATIONAL PRODUCTION

Despite the uncertainty of global economic recovery, international production continued to strengthen in 2014, with all indicators of foreign affiliate activity rising. Indicators of international production – production of MNE foreign affiliates (table I.5) – show a rise in sales by 7.6 per cent, while employment of foreign affiliates reached 75 million. Exports of foreign affiliates remained relatively stable, registering a 1.5 per cent rise. Value added increased by 4.2 per cent. Assets of foreign affiliates rose by 7.2 per cent over the previous year. The financial performance of foreign affiliates in host economies improved, with the rate of return on inward FDI rising from 6.1 per cent in 2013 to 6.4 per cent in 2014. However, this level is still lower than that in the pre-crisis average (2005–2007).

In 2014, the top 100 MNEs again increased their degree of internationalization (table I.6) after some years of decline. A series of big deals and mergers that were concluded during the year contributed to growth in foreign assets, while sales of domestic non-core assets led to decreases in total assets (e.g. Deutsche Telekom's sale of the German e-commerce company 24Scout for roughly \$2 billion). A similar pattern is found for sales and employment, confirming MNEs' expansion of operations abroad. For developing- and transition-economy MNEs, growth rates of assets, sales and employment, both domestic and foreign, are higher than for their developed-country counterparts.

Table I.5.

Selected indicators of FDI and international production, 2014 and selected years

Item	Value at current prices (Billions of dollars)				
	1990	2005–2007 (pre-crisis average)	2012	2013	2014
FDI inflows	205	1 397	1 403	1 467	1 228
FDI outflows	244	1 423	1 284	1 306	1 354
FDI inward stock	2 198	13 894	22 073	26 035	26 039
FDI outward stock	2 254	14 883	22 527	25 975	25 875
Income on inward FDI ^a	82	1 024	1 467	1 517	1 575
Rate of return on inward FDI ^b	4.4	7.6	7.0	6.1	6.4
Income on outward FDI ^a	128	1 105	1 445	1 453	1 486
Rate of return on outward FDI ^b	5.9	7.6	6.6	5.8	5.9
Cross-border M&As	98	729	328	313	399
Sales of foreign affiliates	4 723	21 469	31 687	33 775 ^c	36 356 ^c
Value-added (product) of foreign affiliates	881	4 878	7 105	7 562 ^c	7 882 ^c
Total assets of foreign affiliates	3 893	42 179	88 536	95 230 ^c	102 040 ^c
Exports of foreign affiliates	1 444	4 976	7 469	7 688 ^d	7 803 ^d
Employment by foreign affiliates (thousands)	20 625	53 306	69 359	71 297 ^c	75 075 ^c
Memorandum					
GDP ^e	22 327	51 799	73 457	75 453	77 283
Gross fixed capital formation ^e	5 592	12 219	17 650	18 279	18 784
Royalties and licence fee receipts	31	172	277	298	310
Exports of goods and services ^e	4 332	14 927	22 407	23 063	23 409

Source: UNCTAD.

^a Based on data from 174 countries for income on inward FDI and 143 countries for income on outward FDI in 2014, in both cases representing more than 90 per cent of global inward and outward stocks.

^b Calculated only for countries with both FDI income and stock data.

^c Data for 2013 and 2014 are estimated based on a fixed effects panel regression of each variable against outward stock and a lagged dependent variable for the period 1980–2012.

^d For 1998–2014, the share of exports of foreign affiliates in world exports in 1998 (33.3%) was applied to obtain values. Data for 1995–1997 are based on a linear regression of exports of foreign affiliates against inward FDI stock for the period 1982–1994.

^e Data from IMF (2015).

Note: Not included in this table are the value of worldwide sales by foreign affiliates associated with their parent firms through non-equity relationships and of the sales of the parent firms themselves. Worldwide sales, gross product, total assets, exports and employment of foreign affiliates are estimated by extrapolating the worldwide data of foreign affiliates of MNEs from Australia, Austria, Belgium, Canada, the Czech Republic, Finland, France, Germany, Greece, Israel, Italy, Japan, Latvia, Lithuania, Luxembourg, Portugal, Slovenia, Sweden, and the United States for sales; those from the Czech Republic, France, Israel, Japan, Portugal, Slovenia, Sweden, and the United States for value added (product); those from Austria, Germany, Japan and the United States for assets; those from the Czech Republic, Japan, Portugal, Slovenia, Sweden, and the United States for exports; and those from Australia, Austria, Belgium, Canada, the Czech Republic, Finland, France, Germany, Italy, Japan, Latvia, Lithuania, Luxembourg, Macao (China), Portugal, Slovenia, Sweden, Switzerland, and the United States for employment, on the basis of three years average shares of those countries in worldwide outward FDI stock.

The largest MNEs maintained high cash balances.

The 100 largest MNEs registered a marginal decrease in the value of their cash balances in 2014, as these companies started to spend on new investments, especially through M&As, buy-backs of their own shares and dividend payments (figure I.18). For example, Ford Motors (United States) reduced its cash reserves by about 25 per cent to finance an increase in capital expenditures (13 per cent), and to finance significant share buy-backs and increased dividend payments. However, cash holdings of the top 100 remained exceptionally high as a share of their total assets as MNEs also undertook restructurings, including shedding non-core assets.

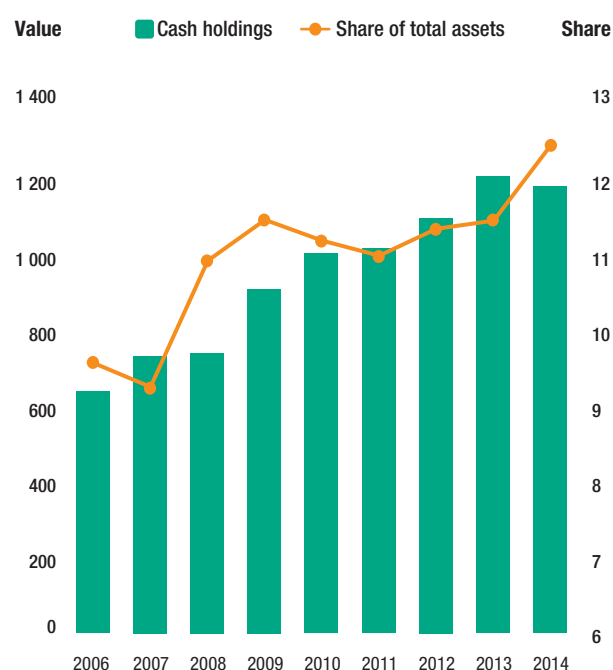
Looking at a far larger sample of 5,000 MNEs, the cash reserve picture is consistent. At the end of 2014, these MNEs had an estimated \$4.4 trillion of cash holdings, nearly double the level before the global financial crisis. These holdings have been accumulated in an effort to lessen their reliance on debt and to secure refinancing while interest rates are low, creating a buffer against financial turmoil.

However, in the last two years, MNEs in some industries have started to use their cash holdings for

Figure I.18.

Cash holdings of the largest 100 MNEs and their share of total assets, 2006–2014

(Billions of dollars and per cent)



Source: UNCTAD, based on data from Thomson ONE.

Table I.6.

Internationalization statistics of the 100 largest non-financial MNEs worldwide and from developing and transition economies

(Billions of dollars, thousands of employees and per cent)

Variable	100 largest MNEs worldwide					100 largest MNEs from developing and transition economies		
	2012	2013 ^a	2012–2013 % change	2014 ^b	2013–2014 % change	2012	2013	% change
Assets								
Foreign	7 942	8 249	3.9	8 266	0.2	1 506	1 632	8.4
Domestic	5 421	5 759	6.2	5 581	-3.1	4 025	4 403	9.4
Total	13 363	14 008	4.8	13 847	-1.1	5 531	6 034	9.1
Foreign as % of total	59	59	-0.5 ^c	60	0.8 ^c	27	27	-0.2 ^c
Sales								
Foreign	5 885	6 053	2.9	6 132	1.3	1 690	1 806	6.8
Domestic	3 072	3 263	6.2	3 101	-5.0	2 172	2 415	11.1
Total	8 957	9 316	4.0	9 233	-0.9	3 863	4 221	9.3
Foreign as % of total	66	65	-0.7 ^c	66	1.4 ^c	44	43	-1.0 ^c
Employment								
Foreign	9 831	9 562	-2.7	9 599	0.4	4 103	4 226	3.0
Domestic	7 106	7 135	0.4	7 211	1.1	6 493	6 688	3.0
Total	16 937	16 697	-1.4	16 810	0.7	10 596	10 914	3.0
Foreign as % of total	58	57	-0.8 ^c	57	-0.2 ^c	39	39	0.0 ^c

Source: UNCTAD.

^a Revised results.

^b Preliminary results.

^c In percentage points.

Note: Data refer to fiscal year results reported between 1 April of the base year to 31 March of the following year. Complete 2014 data for the 100 largest MNEs from developing and transition economies are not yet available.

Figure I.19.

Cash holdings and capital expenditures of the top 5,000 MNEs, by sector, 2008–2012 average and 2014 (Billions of dollars)



Source: UNCTAD, based on data from Thomson ONE.

capital expenditures and acquisitions. Taking average annual expenditures between 2008 and 2012 as a benchmark, for example, the oil and gas industry and the utilities industry more than doubled their capital expenditure, reaching \$582 billion and \$138 billion, respectively, in 2014 (figure I.19) (although capital expenditures in the oil and gas industry are expected to be cut back again in response to lower oil prices). Important increases in expenditure also took place in the telecommunications industry, where operators invested heavily in their networks, and in the food production and transport equipment industries.

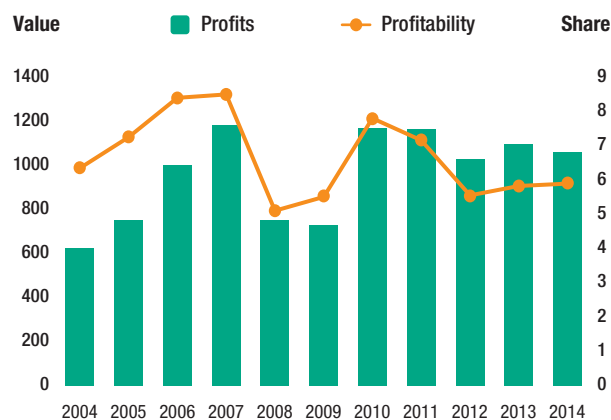
The lower levels of cash holdings do not necessarily mean higher levels of capital expenditure, as cash holdings can be used for buying back a company's own shares and paying dividends to shareholders. Furthermore, the observed increases in capital expenditures are limited to a selected group of MNEs and changes in behaviour are not as yet broad-based. However, as the UNCTAD business survey shows, companies are more optimistic about capital spending in 2015 and beyond (see next section).

Firm-level factors support prospects for growing capital expenditures. Annual MNE profits in 2014 remained

at a high level (figure I.20), adding to existing cash reserves at about the same rate as increased capital expenditures, implying further room for expansion.

Figure I.20.

Profitability and profit levels of MNEs, 2004–2014 (Billions of dollars and per cent)



Source: UNCTAD, based on data from Thomson ONE.

C. PROSPECTS

Global FDI flows are expected to reach \$1.4 trillion in 2015 – an 11 per cent rise. Flows are expected to increase further to \$1.5 trillion and \$1.7 trillion in 2016 and 2017, respectively. These expectations are based on current forecasts for a number of macroeconomic indicators, the findings of an UNCTAD business survey carried out jointly with McKinsey & Company, UNCTAD's econometric forecasting model for FDI inflows, and data for the first four months of 2015 for cross-border M&As and greenfield investment projects.

Macroeconomic factors and firm-level factors are expected to influence flows positively. Indeed, the gradual improvement of macroeconomic conditions, especially in North America, and accommodating monetary policy, coupled with increased investment liberalization and promotion measures, are likely to improve the investment appetite of MNEs in 2015 and beyond. Global economic

growth and gross fixed capital formation are expected to grow faster in 2015 and 2016 than in 2014 (table I.7).

However, the FDI growth scenario could be upended by a multitude of economic and political risks, including ongoing uncertainties in the Eurozone, potential spillovers from geopolitical tensions, and persistent vulnerabilities in emerging economies.

1. UNCTAD's econometric forecasting model

UNCTAD's econometric model projects that FDI flows will increase by 11 per cent in 2015 (table I.8). Developed countries should see a large increase in flows in 2015 (up by more than 20 per cent), reflecting stronger economic activity.

Table I.7.

Real growth rates of GDP and gross fixed capital formation (GFCF), 2014–2016 (Per cent)

Variable	Region	2014	2015	2016
GDP growth rate	World	2.6	2.8	3.1
	Developed economies	1.6	2.2	2.2
	Developing economies	4.4	4.9	4.8
	Transition economies	0.7	-2.0	0.9
GFCF growth rate	World	2.9	3.0	4.7
	Advanced economies ^a	2.7	3.3	3.9
	Emerging and developing economies ^a	3.2	2.9	5.3

Source: UNCTAD, based on United Nations (2015) for GDP and IMF (2015) for GFCF.

^a IMF's classifications of advanced, emerging and developing economies are not the same as the United Nations' classifications of developed and developing economies.

Table I.8.

Projections of FDI flows, by group of economies (Billions of dollars and per cent)

	Averages		2013	2014	Projections		
	2005–2007	2009–2011			2015	2016	2017
Global FDI flows	1 397	1 359	1 467	1 228	1 368	1 484	1 724
Developed economies	917	718	697	499	634	722	843
Developing economies	421	561	671	681	707	734	850
Transition economies	60	81	100	48	45	47	53
Memorandum	Average growth rates		Growth rates		Growth rate projections		
	2005–2007	2009–2011	2013	2014	2015	2016	2017
Global FDI flows	40.1	3.1	4.6	-16.3	11.4	8.4	16.2
Developed economies	48.2	3.0	2.7	-28.4	23.8	13.9	16.7
Developing economies	26.1	4.8	5.0	1.6	3.3	3.9	15.8
Transition economies	48.0	-1.1	17.0	-51.7	-2.3	5.3	12.3

Source: UNCTAD.

Note: Excludes Caribbean offshore financial centres.

FDI inflows to developing countries will continue to be high, rising by an average of 3 per cent over the next two years. They will, however, remain the major host group for FDI flows. Negative GDP growth rates in transition economies, due to continued economic recession, sanctions and low oil prices, imply that flows to those economies could decline further in 2015.

A jump in cross-border M&A activity in the beginning of 2015. An increase in FDI inflows and the rise of developed countries as FDI hosts are reflected in the value of cross-border M&As in early 2015. Between January and April 2015, (net) cross-border M&As increased almost four times compared with those in 2014, to reach their highest level since 2007 (figure I.21). MNEs from developing and transition economies continued to acquire assets in developed economies, consolidating their position as investors in cross-border M&As.

2. UNCTAD business survey

Global FDI activity outlook. According to UNCTAD's survey, carried out in collaboration with McKinsey & Company, of over 1,000 top managers in companies based in 89 countries, most executives expect an increase in global FDI activity in the coming years. This positive outlook is explained by relatively good economic prospects in North America, the BRICS and other

emerging economies, as well as regional integration processes and driven by corporate factors such as the expected continued offshoring of manufacturing and services functions.

Risk factors to the overall positive outlook listed by respondents include the risks of sovereign debt defaults, austerity policies and the state of the EU economy (figure I.22). They also include countertrends to the offshoring factors driving increased FDI, in the form of expected increases in the reshoring of business functions.

CEO investment sentiments vary by region.

Executives from Africa and the Middle East⁹ are the most optimistic about FDI prospects: 67 per cent expect global FDI activity to increase in the next few years (figure I.23); they are closely followed by respondents based in developing Asia.

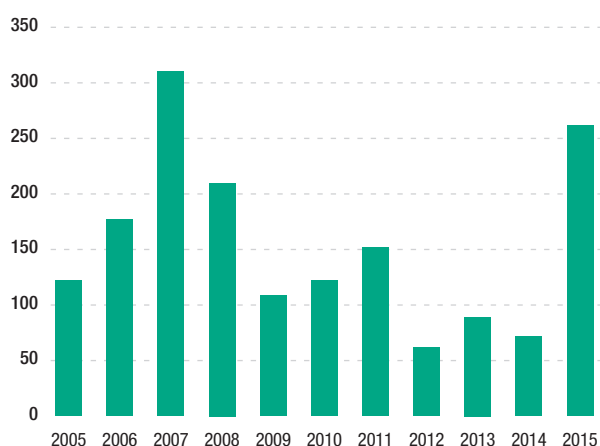
Among developed economies, European MNEs are the most upbeat about global FDI prospects (see figure I.24), despite continuing concern about the EU regional economy. These expectations arise from factors such as the quantitative easing programme launched by the European Central Bank; the considerable cash holdings accumulated by major MNEs in the region; the attractiveness for foreign investors of firms, in particular SMEs, based in weaker EU economies;¹⁰ and MNEs' consolidation strategies in industries such as pharmaceuticals and telecommunications. In contrast, executives from Latin America, North America and other developed economies (Australia, Japan, New Zealand, etc.) are less optimistic about global FDI prospects.

FDI spending intentions. MNEs' overall positive expectations of high global FDI translate only partly into their organizations' investment plans. About a quarter of executives plan to increase FDI expenditures in 2015; this share is set to grow to almost a third by 2017 (figure I.24). By corollary, the share of executives expecting to hold budgets constant or decrease them over the years from 2015 to 2017 shrank from 49 per cent to 34 per cent and from 10 per cent to 6 per cent, respectively.

By sector, firms in the financial and business services industries report the highest prospects for FDI expansion in 2015 (figure I.25), while a higher share of corporations active in the high-tech, telecommunications, pharmaceuticals and other manufacturing industries expect FDI to increase for 2016 and 2017.

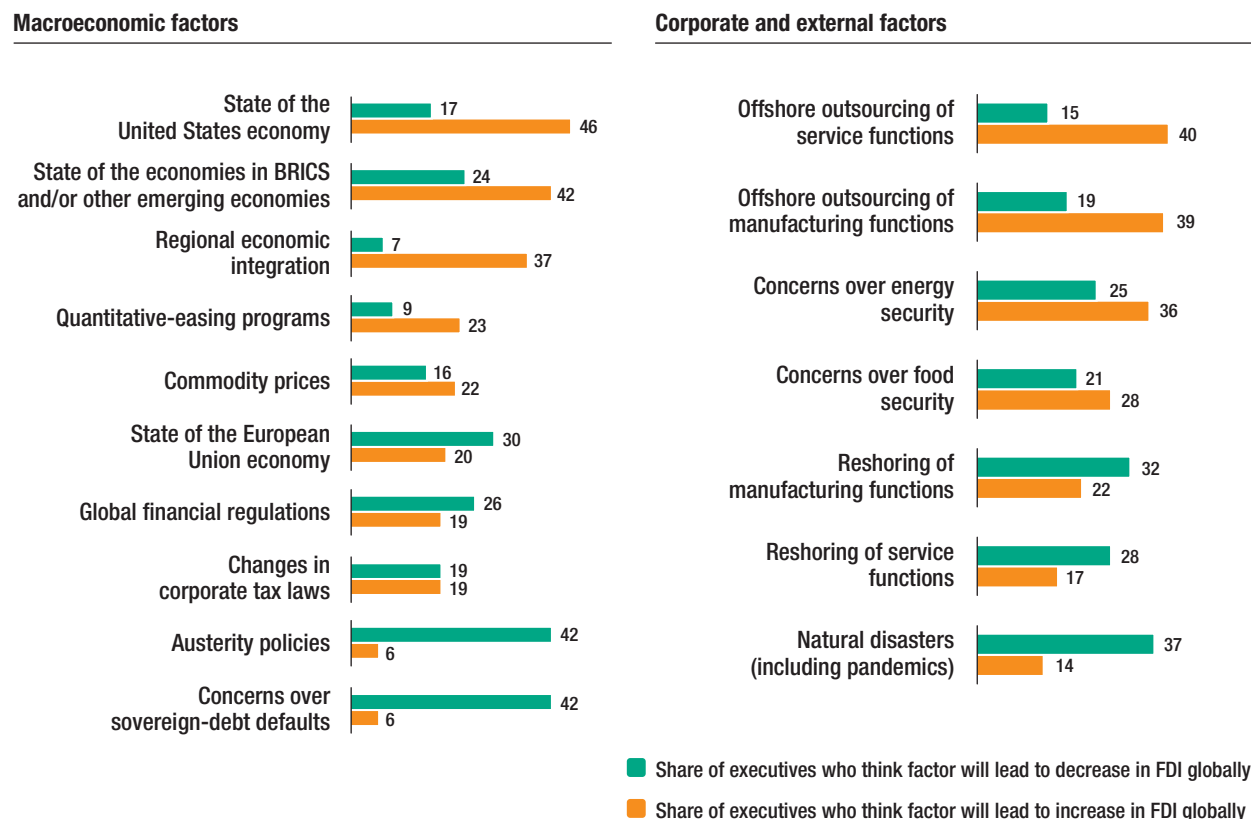
Figure I.21.

**Cross-border M&As,
January–April of each year,
2005–2015** (Billions of dollars)



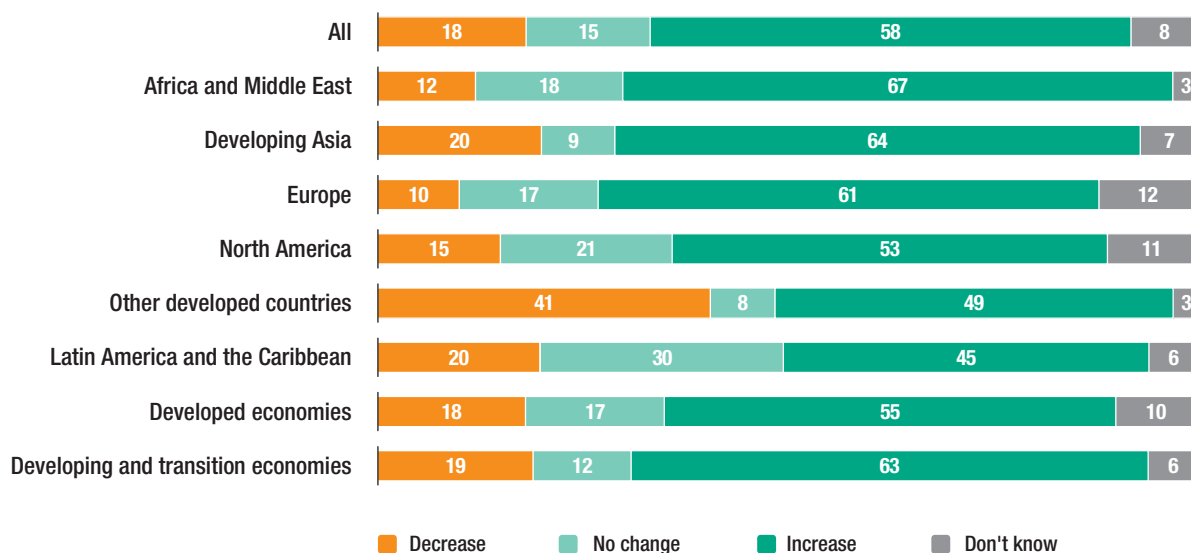
Source: UNCTAD, cross-border M&A database (www.unctad.org/fdistatistics).

Figure I.22. Factors influencing future global FDI activity (Per cent of all executives)



Source: UNCTAD business survey.
 Note: BRICS = Brazil, the Russian Federation, India, China and South Africa.

Figure I.23. Expectations for global FDI activity level from beginning 2015 until 2017 (Per cent of executives based in each region)



Source: UNCTAD business survey.

Large MNEs (those with more than \$1 billion of revenues) and those already well internationalized (with more than 21 company locations and/or with more than 50 per cent of revenue from outside the company's home market) have the most positive

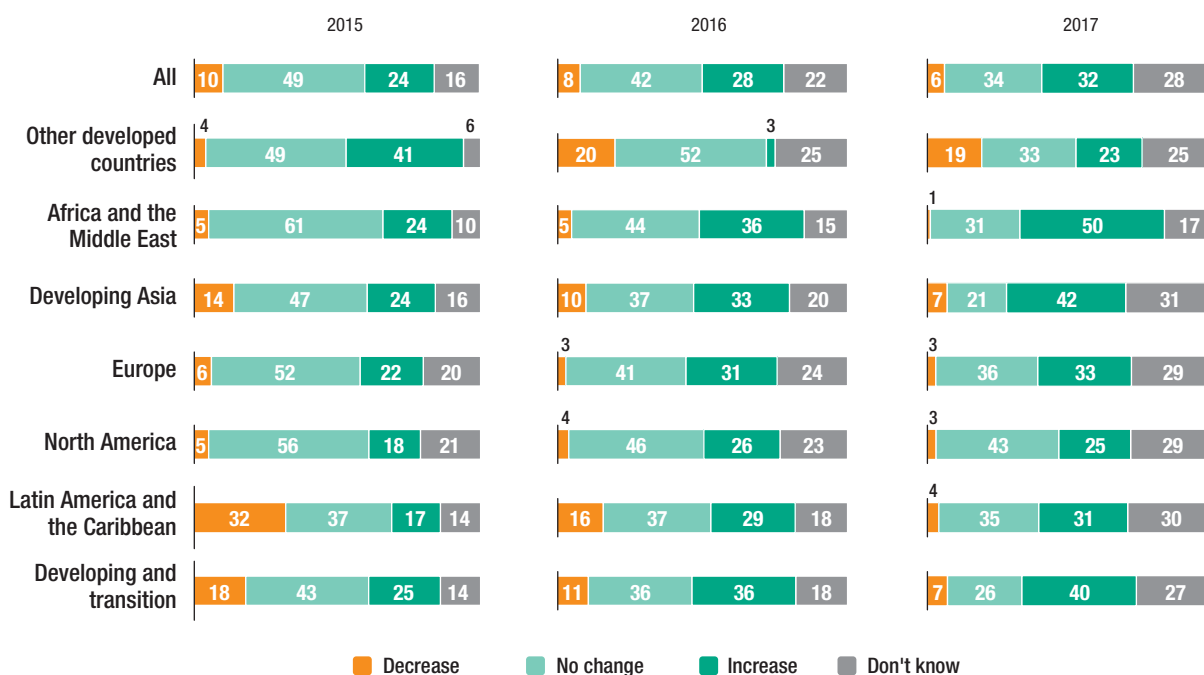
spending plans: about 45 per cent of them indicate intentions to increase FDI spending in 2017.

UNCTAD's survey of investment promotion agencies (IPAs)¹¹ indicates which industries are more likely to witness an increase in FDI activity. IPAs in developed

Figure I.24.

Global FDI spending intentions with respect to 2014 levels, by headquarters region, 2015–2017

(Per cent of executives based in each region)

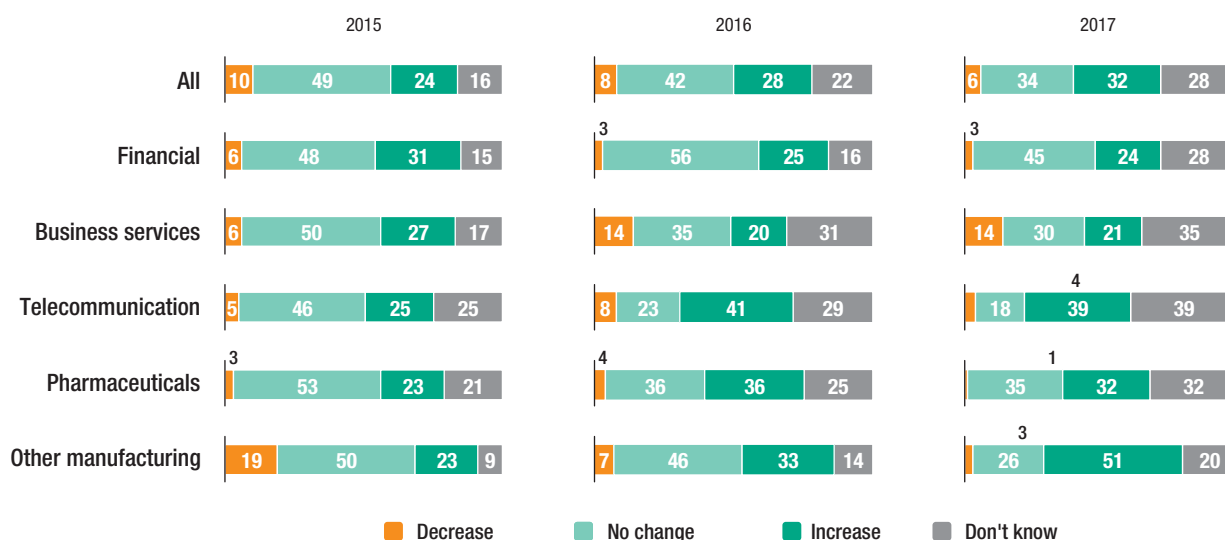


Source: UNCTAD business survey.

Figure I.25.

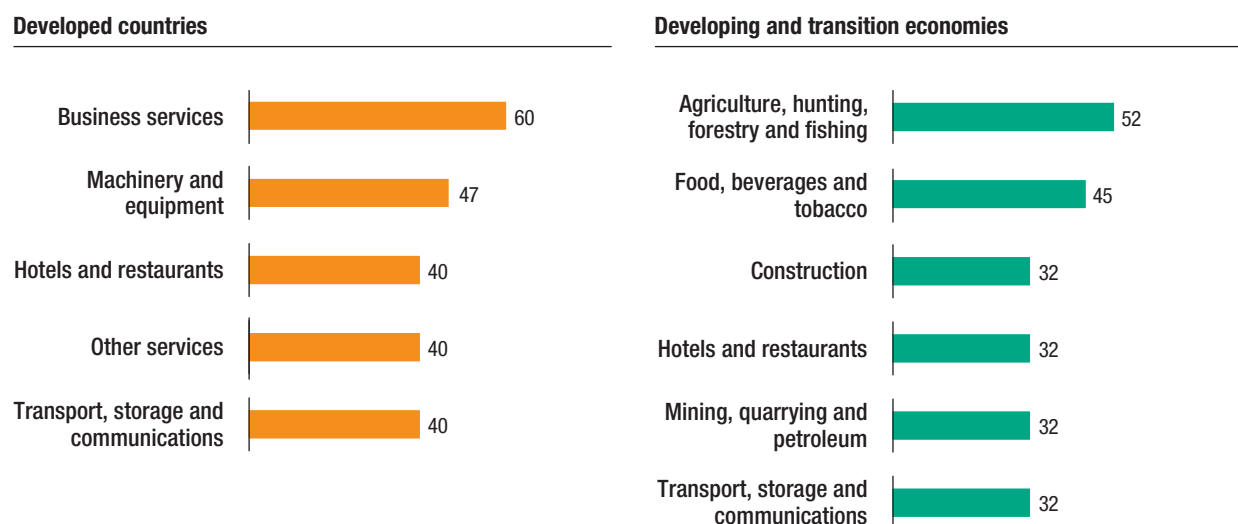
FDI spending intentions with respect to 2014 levels, by selected industries, 2015–2017

(Per cent of all executives)



Source: UNCTAD business survey.

Figure I.26. IPAs' selection of most promising industries for attracting FDI in their own country
(Per cent of all IPA respondents)



Source: UNCTAD IPA survey.

countries expect foreign inflows to target business services, machinery, transport and telecommunications, hotels and restaurants, and other services. Agencies in developing and transition economies consider the best targets in their countries to be in the agricultural and agribusiness industry, along with the transport and telecommunications, hotels and restaurants, construction and extractive industries (figure I.26).

Prospective top investing countries. Results from this year's IPAs survey point to developed countries as top global investing countries; of developing economies, only China, India, the United Arab Emirates, and the Republic of Korea appear in the top 12 positions (figure I.27). Domestic economic woes probably influenced expectations about some emerging economies, such as Brazil (ranked 10th in 2013) and the Russian Federation (ranked 13th) that do not figure in the results this year. The United Kingdom matched China in the rankings (2nd), and Italy and Spain gained several positions.

Prospective top destinations. Global corporate executives view China and the United States as the best investment locations worldwide: 28 per cent chose China and 24 per cent chose the United States (figure I.28). India, Brazil and Singapore make up the remainder of the top 5 destinations; interestingly,

developing-country economies constitute 6 of the top 10. Only the United Kingdom, Germany and Australia feature in this group, apart from the United States.

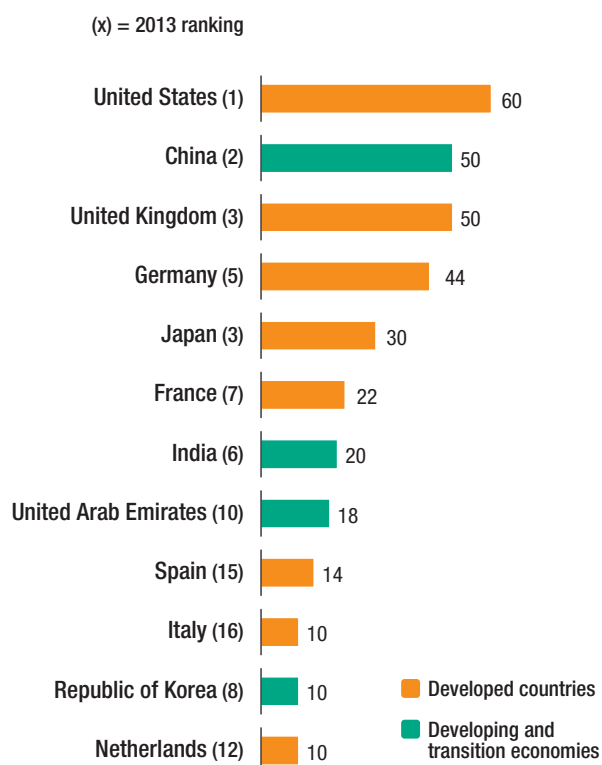
The rankings are influenced by the views of executives in various industries. For example, businesses linked to the information technology industry are more likely to have investment plans favouring the United States or India. Similarly, the United States maintains its leadership in rankings on the basis of their strength in the high-tech and telecommunication industries.

The overall global FDI trend in 2014 was negative. Cross-border investment flows remain significantly (about one third) below their 2007 peak. However, regional trends varied, with the developing-country group showing marginal positive growth. In addition, prospects for global FDI flows to 2017 are somewhat more positive. Nevertheless, in light of the important role that FDI is expected to play in financing for development – the subject of discussion during the third International Conference on Financing for Development in Addis Ababa mid-July 2015 – the current subdued trend is of concern. Policymakers may wish to consider concerted action to push increased productive investment for sustainable development.

Figure I.27.

IPAs' selection of the most promising investor home economies for FDI in 2014–2016

(Per cent of IPA respondents selecting economy as a top source of FDI)

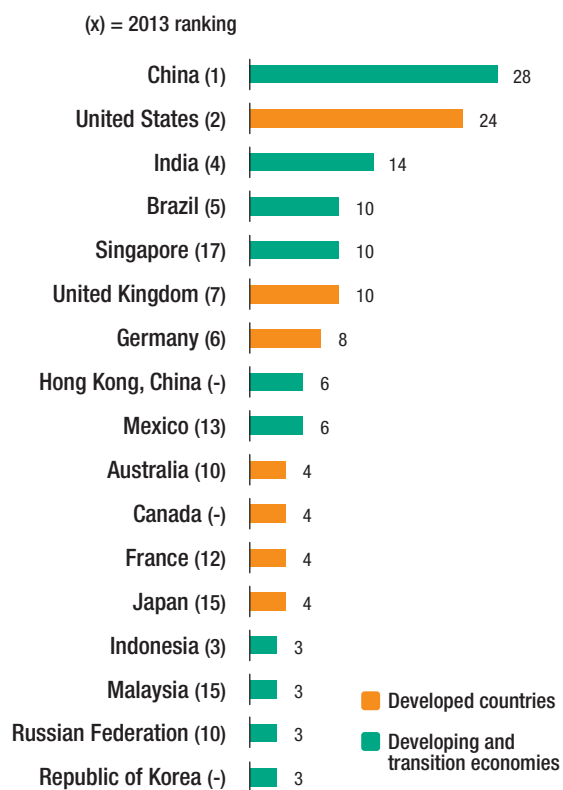


Source: UNCTAD IPA survey.

Figure I.28.

MNEs top prospective host economies for 2015–2017

(Per cent)



Source: UNCTAD business survey.

Note: Previous survey ranking appears in parentheses. The absence of a number in parentheses means the economy was not in the top 20.

Notes

- ¹ There are some differences in value between global FDI inflows and global FDI outflows, and these flows do not necessarily move in parallel. This is mainly because home and host countries may use different methods to collect data and different times for recording FDI transactions. This year is one of transition from directional-based FDI data to asset/liability-based FDI data. Although UNCTAD made efforts to use the data based on the directional principle, as explained in the methodological box in section A.1.a, many large countries already report data on the basis of the asset/liability principle. This is not the first year in which inflows and outflows did not move in parallel. The most recent years in which this data mismatch occurred were 2003 and 2005.
- ² SPEs are legal entities that have little or no employment or operations or physical presence in the jurisdiction in which they are created by their parent enterprises, which are typically located in other jurisdictions (in other economies). SPEs are often used as vehicles to raise capital or to hold assets and liabilities, and usually do not undertake significant production (BD4).
- ³ UNCTAD, "Regional integration and FDI in developing and transition economies", Multi-Year Expert Meeting on Investment, Innovation and Entrepreneurship for Productive Capacity-building and Sustainable Development, Geneva, 28–30 January 2013.
- ⁴ Greenfield investment projects data refer to *announced* projects. The value of such a project indicates the capital expenditure planned by the investor at the time of the announcement. Data can differ substantially from the official FDI data as companies can raise capital locally and phase their investments over time, and a project may be cancelled or may not start in the year when it is announced.
- ⁵ The net value of cross-border M&As is computed as the difference between M&A gross sales (all MNE cross-border acquisitions) and divestment of sales (sales from MNEs to domestic entities or to other MNEs). It reflects the M&A component of FDI flows.
- ⁶ In this context, the term "divestment" refers to the sale of MNEs to domestic companies or to other MNEs. It does not include liquidation and capital impairment.
- ⁷ Data from Bain Capital.
- ⁸ GIC Annual Report 2013/2014.
- ⁹ Because of low numbers of responses from Africa and the Middle East, the two regions are combined to enhance statistical credibility. This action hides subregional differences within Africa and regional differences between Africa and West Asia.
- ¹⁰ For example, see "Chinese go on spending spree and double investment in Europe", *Financial Times*, 10 February 2015.
- ¹¹ This survey obtained responses from 54 IPAs in 51 countries.

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15

Regional Investment Trends

C H A P T E R II

15



INTRODUCTION

Global foreign direct investment (FDI) inflows fell by 16 per cent overall in 2014 to \$1.23 trillion, down from \$1.47 trillion in 2013, but with considerable variance between country groups and regions.

FDI flows to developing economies increased by 2 per cent to reach their highest level at \$681 billion in 2014, accounting for 55 per cent of global FDI inflows (table II.1). Five of the top 10 host economies now are developing ones. However, the increase in developing-country inflows is, overall, primarily a developing Asia story. FDI inflows to that region grew by 9 per cent to \$465 billion, constituting the lion's share of total FDI in developing economies. Africa's overall inflows remained flat at \$54 billion, while those to Latin America and the Caribbean saw a 14 per cent decline to \$159

billion, after four years of consecutive increases. FDI to *transition economies* dropped by more than half to \$48 billion. Inflows to developed economies as a whole fell by 28 per cent to \$499 billion, decreasing both in Europe and North America. Flows to Europe fell by 11 per cent to \$289 billion, one third of their 2007 peak, while in North America FDI dropped 51 per cent to \$146 billion.

Outward FDI from developing economies increased by 23 per cent in 2014, to \$468 billion. In contrast, net investment by *developed countries* was flat, primarily because a large expansion in cross-border mergers and acquisitions (M&As) by some developed-country multinational enterprises (MNEs) was offset by large divestments by others. FDI outflows from

Table II.1. FDI flows, by region, 2012–2014 (Billions of dollars and per cent)

Region	FDI inflows			FDI outflows		
	2012	2013	2014	2012	2013	2014
World	1 403	1 467	1 228	1 284	1 306	1 354
Developed economies	679	697	499	873	834	823
Europe	401	326	289	376	317	316
North America	209	301	146	365	379	390
Developing economies	639	671	681	357	381	468
Africa	56	54	54	12	16	13
Asia	401	428	465	299	335	432
East and South-East Asia	321	348	381	266	292	383
South Asia	32	36	41	10	2	11
West Asia	48	45	43	23	41	38
Latin America and the Caribbean	178	186	159	44	28	23
Oceania	4	3	3	2	1	0
Transition economies	85	100	48	54	91	63
Structurally weak, vulnerable and small economies^a	58	51	52	10	13	10
LDCs	24	22	23	5	7	3
LLDCs	34	30	29	2	4	6
SIDS	7	6	7	2	1	1
Memorandum: percentage share in world FDI flows						
Developed economies	48.4	47.5	40.6	68.0	63.8	60.8
Europe	28.6	22.2	23.5	29.3	24.3	23.3
North America	14.9	20.5	11.9	28.5	29.0	28.8
Developing economies	45.6	45.7	55.5	27.8	29.2	34.6
Africa	4.0	3.7	4.4	1.0	1.2	1.0
Asia	28.6	29.2	37.9	23.3	25.7	31.9
East and South-East Asia	22.9	23.7	31.0	20.7	22.4	28.3
South Asia	2.3	2.4	3.4	0.8	0.2	0.8
West Asia	3.4	3.0	3.5	1.8	3.1	2.8
Latin America and the Caribbean	12.7	12.7	13.0	3.4	2.2	1.7
Oceania	0.3	0.2	0.2	0.1	0.1	0.0
Transition economies	6.1	6.8	3.9	4.2	7.0	4.7
Structurally weak, vulnerable and small economies^a	4.1	3.5	4.3	0.7	1.0	0.8
LDCs	1.7	1.5	1.9	0.4	0.6	0.2
LLDCs	2.5	2.0	2.4	0.2	0.3	0.4
SIDS	0.5	0.4	0.6	0.2	0.1	0.1

Source: UNCTAD, FDI/MNE database (www.unctad.org/fdistatistics).

^a Without double counting countries that are part of multiple groups.

Note: LDCs = least developed countries, LLDCs = landlocked developing countries, SIDS = small island developing States.

transition economies fell by 31 per cent to \$63 billion as natural-resources-based MNEs, mainly from the Russian Federation, reduced their investment abroad. Developing economies now account for more than one third of global FDI outflows, up from about just one tenth in 2000.

FDI flows to *structurally weak, vulnerable and small economies* increased by 3 per cent to \$52 billion, but with divergent trends: flows to least developed countries (LDCs) and small island developing States (SIDS) rose by 4.1 per cent and 22 per cent, respectively; landlocked developing countries (LLDCs) saw a decrease of 2.8 per cent.

The outcome of the first Conference on Financing for Development, the Monterrey Consensus of 2002, was a pledge by participants to mobilize financial assistance for developing economies in six principal areas, which include mobilizing international financial resources, such as FDI.¹ Both then and since, particular concern has focused on mobilizing financing and investment for the structurally weak, vulnerable and

small economies, in order to ensure robust, resilient growth and sustainable development. Over the past decade (2004–2014), FDI stock tripled in LDCs and SIDS, and quadrupled in LLDCs. With a concerted effort by the international investment-development community, it would be possible to have FDI stock in these structurally weak economies quadruple by 2030 from today's level. And more important, further efforts are needed to harness financing for economic diversification to foster greater resilience and sustainability in these countries.

At the third Conference on Financing for Development on 13–16 July 2015 in Addis Ababa, and at the global summit on the Sustainable Development Goals in New York on 25–27 September 2015, external financing for development will come again under the spotlight, as will the performance of FDI in developing economies since the Monterrey conference. In light of this background, section B of this chapter includes a stocktaking of FDI trends in LDCs, LLDCs and SIDS since 2002, in addition to analysis of last year's trends.

A. REGIONAL TRENDS

AFRICA

FDI inflows, top 5 host economies, 2014

(Value and change)

2014 Inflows

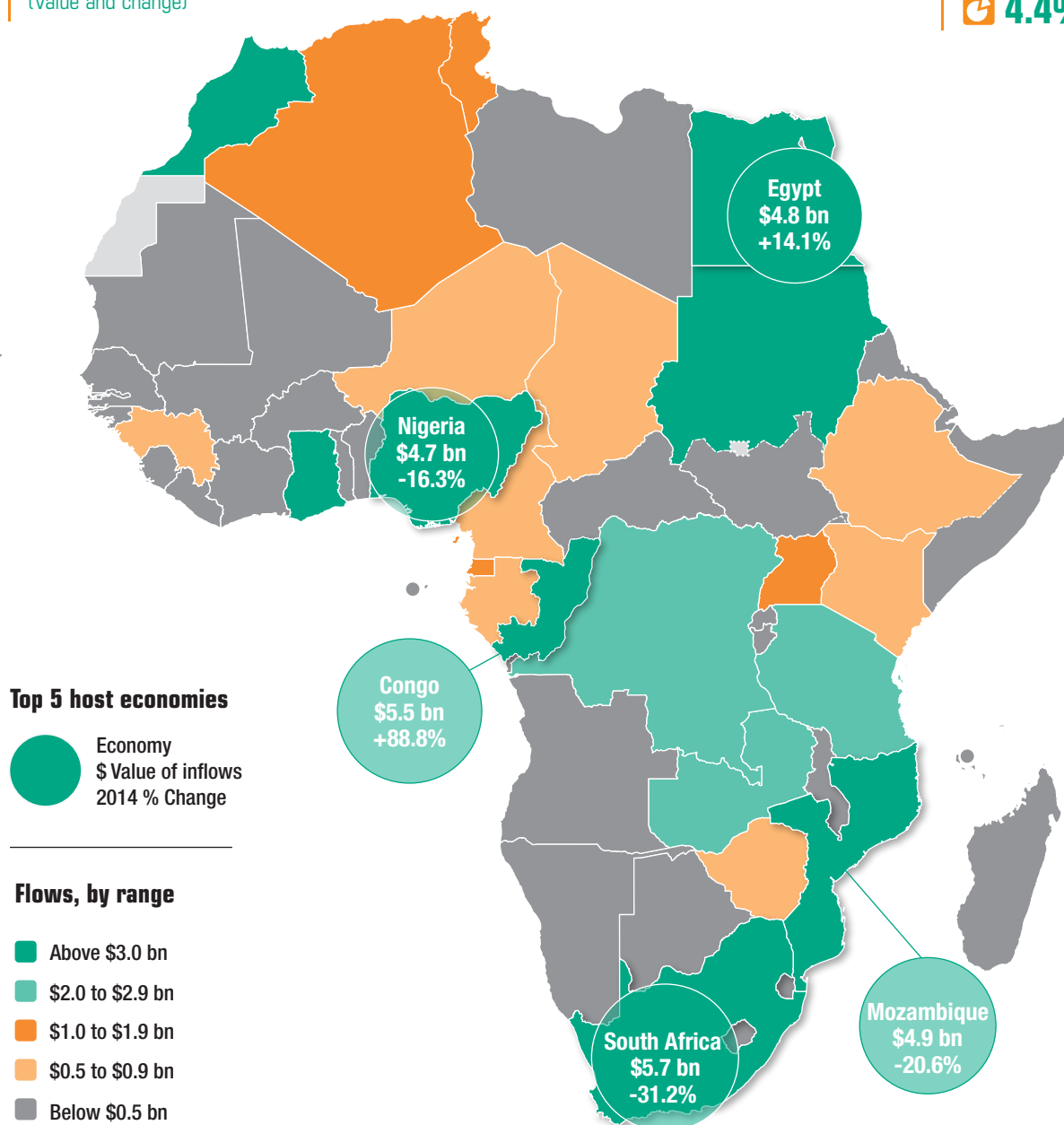
\$ 54 bn

2014 Decrease

-0.1%

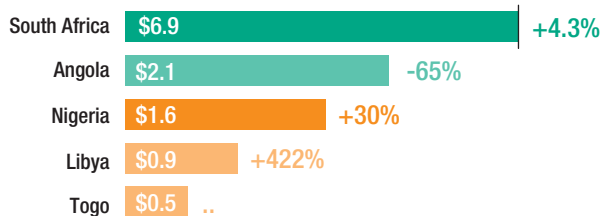
Share in world

4.4%



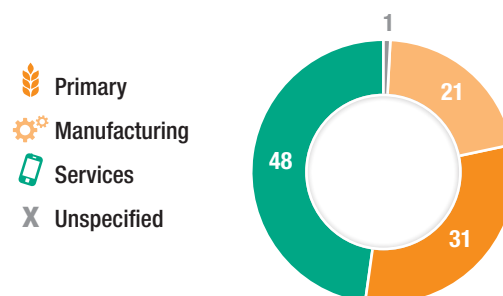
Outflows: top 5 home economies

(Billions of dollars, and 2014 growth)



Inward FDI stock by sector

(Percentage of the total inward FDI stock in Africa)



Source: UNCTAD.

Note: The boundaries and names shown and the designations used on this map do not imply official endorsement or acceptance by the United Nations. Final boundary between the Republic of Sudan and the Republic of South Sudan has not yet been determined. Final status of the Abyei area is not yet determined.

HIGHLIGHTS

- Increasing investment by developing-economy MNEs
- Services: largest sector in Africa's stock of FDI
- FDI in services concentrated in a few countries

Figure A.

FDI inflows, 2008–2014 (Billions of dollars)

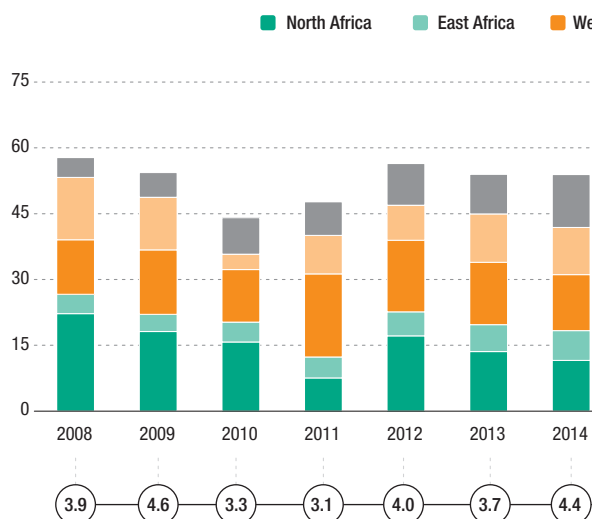


Figure B.

FDI outflows, 2008–2014 (Billions of dollars)

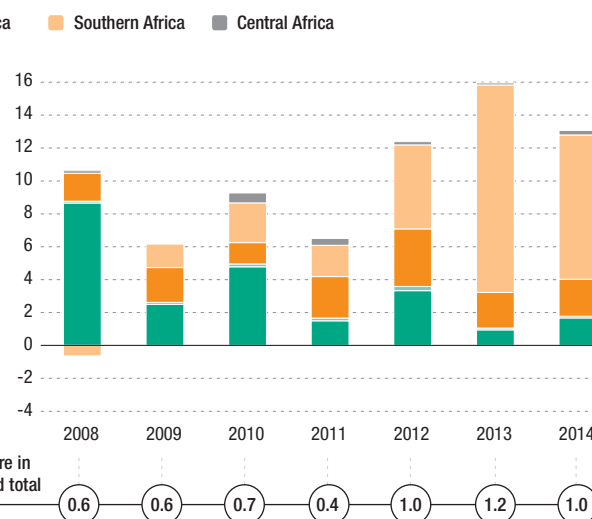


Table A.

Announced greenfield FDI projects by industry, 2013–2014 (Millions of dollars)

Sector/industry	Africa as destination		Africa as investors	
	2013	2014	2013	2014
Total	55 124	88 295	17 402	13 386
Primary	6 114	21 974	7	48
Mining, quarrying and petroleum	3 750	21 974	7	48
Manufacturing	14 722	28 787	8 013	3 848
Food, beverages and tobacco	1 437	2 099	535	1 214
Textiles, clothing and leather	1 744	2 091	126	23
Non-metallic mineral products	3 921	2 213	2 805	1 918
Motor vehicles and other transport equipment	1 642	1 585	98	15
Services	34 287	37 534	9 382	9 490
Electricity, gas and water	11 537	10 648	-	125
Construction	3 536	9 229	1 005	462
Transport, storage and communications	7 774	5 909	2 919	2 305
Business services	7 099	6 323	2 656	4 949

Table B.

Announced greenfield FDI projects by region/country, 2013–2014 (Millions of dollars)

Partner region/economy	Africa as destination		Africa as investors	
	2013	2014	2013	2014
World	55 124	88 295	17 402	13 386
Developed economies	28 010	63 024	2 742	1 112
European Union	16 939	46 957	1 575	939
France	2 070	18 931	297	127
United States	2 559	8 014	1 121	39
Developing economies	27 013	25 180	14 587	12 274
Africa	13 082	10 209	13 082	10 209
Nigeria	2 260	545	2 784	1 321
South Africa	5 379	4 789	343	176
Asia	13 735	14 886	1 421	1 769
China	289	6 132	454	92
India	5 311	1 122	83	107
Transition economies	101	90	74	-

Table C.

Cross-border M&As by industry, 2013–2014 (Millions of dollars)

Sector/industry	Sales		Purchases	
	2013	2014	2013	2014
Total	3 829	5 058	3 019	5 446
Primary	135	2 566	289	1 595
Mining, quarrying and petroleum	135	2 566	289	1 595
Manufacturing	3 326	326	1 632	209
Food, beverages and tobacco	1 023	22	244	35
Paper and paper products	-5	-101	-	-101
Pharmaceuticals, medicinal chemicals and botanical products	567	51	1 310	-51
Basic metal and metal products	-	301	-	-
Services	368	2 166	1 098	3 642
Electricity, gas, water and waste management	250	58	-	1 176
Transportation and storage	27	425	27	74
Financial and insurance activities	222	1 419	653	228
Business activities	104	12	135	129

Table D.

Cross-border M&As by region/country, 2013–2014 (Millions of dollars)

Region/country	Sales		Purchases	
	2013	2014	2013	2014
World	3 829	5 058	3 019	5 446
Developed economies	-8 953	-8 317	2 288	1 670
European Union	-4 831	-6 886	1 641	154
France	-2 310	-5 648	147	246
United States	-4 751	-1 801	-15	21
Developing economies	12 769	13 331	731	3 783
Africa	130	2 424	130	2 424
Latin America and the Caribbean	-430	400	-	1 094
Asia	13 069	10 507	596	265
India	419	2 730	233	137
Qatar	2 529	729	-	-
United Arab Emirates	538	5 677	29	-
Transition economies	-	-	-	-6

FDI inflows to Africa remained flat at \$54 billion, decreasing in North Africa and rising in Sub-Saharan Africa.

North Africa saw its FDI flows decline by 15 per cent to \$11.5 billion, while flows to Sub-Saharan Africa rose by 5 per cent to \$42.4 billion. As a percentage of global FDI flows, though, Africa's share increased to 4.4 per cent, from 3.7 per cent in 2013. Slow global economic growth may make the faster-growing African economies relatively more attractive, especially to emerging-market investors; at the same time, future growth prospects in key markets such as Nigeria and Zambia are weakening, as commodity prices fall. Important drivers that shape FDI trends to Africa include rising intra-African FDI; expansion by emerging-market firms (increasingly from West Asia) and non-traditional actors (private equity); and growing consumer markets, with the food and beverages industry having another standout year.

In *North Africa*, the decline in flows to Algeria, Libya, the Sudan, South Sudan and Tunisia was larger than the rise of flows in Egypt and Morocco. FDI flows to Egypt grew by 14 per cent to \$4.8 billion, driven by investments in oil and construction projects. Morocco also saw increased FDI flows, growing 8.6 per cent to \$3.6 billion. In 2014, Algeria saw its FDI flows almost halved from the level in the previous year, due to a 87 per cent fall in announced greenfield investment. The continuing unrest in Libya negatively influenced investors' perception of the region's potential as an FDI host.

FDI flows to *West Africa* declined by 10 per cent to \$12.8 billion, as Ebola, regional conflicts and falling commodity prices affected several countries. In those affected by Ebola, several companies either closed or suspended their expansion; e.g. in Sierra Leone, Africa Minerals (25 per cent Chinese owned) closed its flagship mine Tonkolili, and in Liberia, ArcelorMittal (Luxembourg) suspended an iron ore expansion project after contractors moved staff out of the country. Nigeria – the largest host country in the continent – saw its FDI flows fall by 16 per cent, as it moves away from overdependence on oil and diversifies into non-oil sectors.

East Africa saw its FDI flows increasing by 11 per cent, to \$6.8 billion. The gas sector in the United Republic of Tanzania, which has enormous potential, drew FDI despite political wrangling over its future. In Ethiopia,

the expanding textiles sector continued to attract FDI with its low wages and cheap power.²

Central Africa received \$12.1 billion, up 33 per cent from 2013. FDI flows in the Republic of the Congo almost doubled to \$5.5 billion as foreign investors continued investing in the oil refinery, despite falling commodity prices (for example Berven Group International Development (United States) signed an agreement with the government to build the country's second oil refinery for \$1.6 billion). The Democratic Republic of the Congo continued to attract notable flows, despite falling copper prices. Glencore significantly upgraded the Democratic Republic of the Congo's main hydroelectric plant as mining companies looked to overcome bottlenecks in power supplies.

Flows to *Southern Africa* fell by 2 per cent to \$10.8 billion. Mozambique saw its flows decline by 21 per cent to \$4.9 billion, despite a significant rise in cross-border M&As in the oil and gas industry (for example, ONGC Videsh Ltd (India) acquired a 10 per cent stake in Rovuma Offshore Area 1 for \$2.6 billion). South Africa – the largest host country in the subregion – received \$5.7 billion, down 31 per cent from 2013.

MNEs from developing economies continue to invest in Africa, targeting assets relinquished by developed-country MNEs. Although developed countries continue to account for the largest share of FDI stock, the investment of developing-country MNEs is increasing, as reflected in cross-border M&As and announced greenfield FDI projects. MNEs from developed economies (in particular, France and the United Kingdom) continued to divest from Africa. Demand from developing-economy investors for these divested assets was significant; for instance, Emirates Telecommunications Corp (United Arab Emirates) bought a 53 per cent stake in Itissalat Al Maghrib SA – a foreign affiliate of Vivendi (France) – for \$5.7 billion.

Chinese and Indian firms continue to be notable investors in Africa, with Tata investing in Algeria in 2014 and Chinese firms investing in South Africa's solar panel industry. The rise of non-traditional investors, especially from the United Arab Emirates, particularly Dubai, has been a new factor underpinning FDI flows into Africa in recent years. The country accounted for 6 per cent of total capital expenditure related to greenfield FDI projects into Africa in 2014, targeting consumer industries, infrastructure and services.³ Other major deals from this region include one by

Qatar National Bank, the Gulf's largest lender, which paid \$500 million to become the largest stakeholder in pan-African lender Ecobank.

Private equity drove many of the largest investments into Africa in 2014. Private equity group KKR (United States) made its first direct investment in Africa in 2014, investing \$200 million in Ethiopian rose producer Afriflora. Carlyle secured nearly \$700 million for its first Sub-Saharan African fund in early 2014, which it began to use by investing in TiAuto, a vehicle retailer in South Africa, as well as taking an 18 per cent stake (\$50 million) in Nigerian lender Diamond Bank. Private equity firm Blackstone entered into a partnership with Nigerian businessman Aliko Dangote to invest across the region, and Edmond de Rothschild opened its first private equity fund focused on Africa.

Sectoral investment trends in 2014 reflect the continued importance of services and manufacturing investments. Some 38 per cent of announced greenfield FDI projects and 33 per cent of related capital expenditure were in manufacturing in 2014. The services sector recorded 60 per cent of projects and 43 per cent of capital expenditures. Unusually high planned capital expenditures in services FDI were due to a notable pickup in announced construction projects. Noteworthy investments took place in manufacturing in Africa, mainly in electronic equipment, motor vehicles and food. In Nigeria, Nissan, Peugeot and Hyundai all began auto assembly in 2014. Nigeria's Automotive Industry Plan (introduced in 2012) has been important in the industry's expansion, positioning itself within the emerging automotive regional value chains. Food and beverages FDI is another beneficiary of growing consumer markets in Africa, with several large deals in 2014; e.g. Danone (France) bought a 40 per cent stake in Brookside Dairy, East Africa's largest milk processor, based in Kenya.

FDI outflows from Africa decreased by 18 per cent, from \$16 billion in 2013 to \$13 billion in 2014. Services continued to be the focus of African firms' outward FDI. In cross-border M&As, South Africa's Woolworths announced plans to acquire David Jones, the Australian department store, in a deal valued at \$2.14 billion.

Intra-African FDI remained preponderant in 2014. The share of intraregional greenfield investments by African firms in total announced greenfield investments

in Africa remained similar to the 2013 figures, at 76 per cent in terms of value and 68 per cent in the number of projects. Intra-African M&As accounted for 45 per cent of total cross-border M&A purchases by African firms, with Nigeria accounting for a large portion of sales and purchases. South African firms remained important investors: Nedbank agreed to purchase a 20 per cent stake in Togo's Ecobank for \$0.5 billion, while Shoprite will open 30 new stores on the continent by June 2015.

The potential of FDI into Africa's services sector

Services is the largest sector in Africa's stock of FDI. Available data show that Africa's services FDI stock increased four-fold between 2001 and 2012. The share of services FDI stock in the continent is still lower than the corresponding global and developing-country shares. In 2012 (the latest year for which data are available), although concentrated in a few countries, services FDI nonetheless accounted for 48 per cent of Africa's total stock of FDI, more than twice the share of manufacturing (21 per cent) and significantly more than the primary sector (31 per cent) (figure II.1).

Confirmation of the importance of FDI in services can be seen in announced greenfield investment data:⁴ the sector accounted for the majority of greenfield FDI projects into Africa and the largest single portion of related planned capital expenditure in 2014. For the 2003–2014 period, including the period when the commodity boom was in full swing, 38 per cent of planned capital expenditure (and 55 per cent of projects) related to announced greenfield FDI projects were in the services sector, more than in either the manufacturing sector or the primary sector.

The stock of services FDI in Africa is concentrated. In North Africa, where the services sector accounts for more than 60 per cent of the subregion's total FDI stock, Morocco has grown as a services hub in the subregion, through its efforts to position itself as a gateway to the continent. The array of incentives offered by Casablanca's "Finance City" have helped attract major MNEs such as BNP Paribas, AIG, Boston Consulting Group, Microsoft and Ford to move their regional headquarters there. Factors such as substantial investment in infrastructure (especially in information and communication technology (ICT)), a strong skills base, political stability and proximity to Europe make Morocco well placed to attract services FDI.

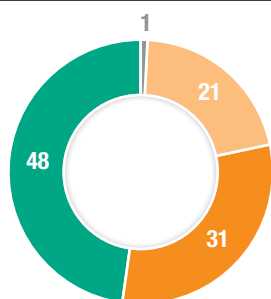
Figure II.1

Africa's inward FDI stock by sector and by subregion, 2012

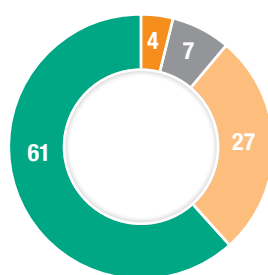
(Percentage of total inward FDI stock in region and subregion)

Primary Manufacturing Services Unspecified

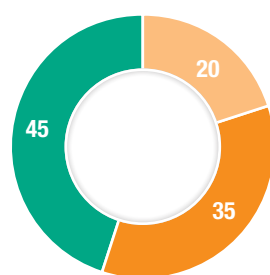
Africa as a whole



North Africa



Sub-Saharan Africa



Source: UNCTAD, FDI/MNE database (www.unctad.org/fdistatistics).

Note: Where 2012 numbers are unavailable, 2011 data are used. Data used here account for 20 per cent and 68 per cent, respectively, of total stock in North Africa and Sub-Saharan Africa.

Services FDI, at 61 per cent of Morocco's inward FDI stock (\$45 billion), is the largest component of the country's FDI and has been consistently so over the past decade. In 2012, some 29 per cent of Morocco's stock of services FDI was held in transport, storage and communications (with more than half in telecommunications), followed by real estate (27 per cent) and finance (15 per cent).

In *Sub-Saharan Africa*, South Africa predominates in the services sector. Over the past decade, South Africa's stock of manufacturing FDI has shrunk relative to services FDI. By 2012 finance and business services alone accounted for the major portion of its inward FDI stock at 36 per cent. When other industries are included, such as transport and retail, the services

sector accounted for 51 per cent, the primary sector (mining) for 31 per cent, and manufacturing for 18 per cent of the country's inward FDI stock. Two financial industry investments that considerably increased South Africa's – and Africa's – services FDI stock were the purchase by Barclays Bank of over 50 per cent of Absa Bank for R33 billion in 2005 (\$2.7 billion in current prices); and the purchase by China's largest bank, the Industrial and Commercial Bank of China (ICBC), of a 20 per cent stake in Standard Bank for R36.7 billion in 2007 (\$3 billion).⁵

Growth in the rest of Africa has been a primary reason why South Africa's services sector has received strong inflows, as companies look to use that country as a base from which to expand regionally. Notable non-financial examples are MNEs setting up Africa-oriented information technology services and call centres in the country (e.g. Wipro of India's establishment of a software company in 2014) and investments in hospitality (e.g. Marriott's acquisition of the 116-hotel Protea Hotel Group, completed in 2014).

In contrast to South Africa, Nigeria's services sector has attracted FDI oriented mostly to the local market. At \$30 billion, services FDI accounted for 39 per cent of Nigeria's inward stock in 2012. Finance accounted for the largest portion, at 63 per cent (indicating the importance of foreign – and especially African – banks in advancing into Nigeria's retail banking market), followed by transport, storage and communications (26 per cent), and construction (9 per cent).

Finance accounts for the major portion of Africa's stock of services FDI.

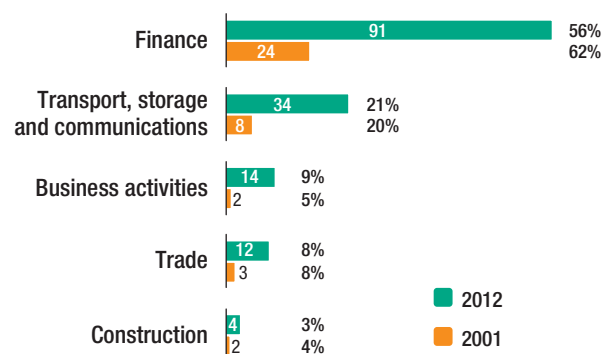
By 2012 more than half of Africa's services FDI stock was held in finance (56 per cent), followed by transport, storage and communications (21 per cent) and business activities (9 per cent) (figure II.2). FDI in tourism, though significant, is spread across a number of service industries. FDI in service industries is demonstrating. For instance, financial FDI inflows amounted to 11 per cent of total FDI inflows into Africa in 2010–2012. In absolute terms, inflows in this industry expanded from 30 per cent (\$0.9 billion) to 35 per cent (\$3.4 billion) of services FDI between 2001–2003 and 2010–2012.

Infrastructure and other services, including telecommunications, are becoming increasingly salient.

The stock of FDI into the transport, storage and communications industry grew more than four-fold between 2001 and 2012, from \$8 billion to

Figure II.2.

Africa: Services FDI stock, by industry, 2001 and 2012
(Billions of dollars and per cent of Africa's inward FDI stock in services)



Source: UNCTAD, FDI/MNE database (www.unctad.org/fdistatistics).
Note: Where 2012 numbers are unavailable, 2011 data are used.

\$34 billion. Although FDI accounts for a small portion of total infrastructure financing and development in Africa because of the wide use of non-equity modes (NEMs) of operation by MNEs, FDI is increasingly visible in, for instance, the growing ICT network as investors look to capture expanding consumer markets.

The rise of telecommunications FDI into the continent reflects increased consumer spending, unsaturated markets with first-mover advantages, greater affordability of smartphones and a push to expand broadband, 4G and fibre optics in order to take advantage of these trends. Another important aspect has been the disposal of cell phone towers by telecommunications companies (box II.1).

As an example of this push to advance connectivity, India's Bharti group undertook 11 greenfield investment

projects in Nigeria and Uganda in 2014 alone, adding to its existing investment in 13 other African countries (Burkina Faso, Chad, the Democratic Republic of Congo, Ghana, Kenya, Madagascar, Malawi, the Republic of Congo, Seychelles, Sierra Leone, the United Republic of Tanzania, Zambia and Uganda), in order to establish a Wi-Fi network across Africa.

African investors accounted for 31 per cent of global planned capital expenditure in announced greenfield FDI projects on the continent in 2014. Some 21 per cent of all such projects in transport, storage, and communications were led by Africa-based investors. South Africa's MTN is one major investor, establishing data centres, sales offices and 4G projects in Côte d'Ivoire, Ghana, Swaziland and Uganda in 2013. Mauritian companies are also prominent: in 2013, Smile Telecoms and Liquid Telecom established several greenfield FDI projects across Sub-Saharan Africa in order to construct a cross-country 4G and fibre-optic network.

The electricity, gas and water industry has seen strong inflows in recent years too, accounting for 9 per cent of FDI inflows into Africa's services sector in 2010–2012, though this has not yet translated into significant FDI stock holding. Inflows into the subsector reflect a growing willingness on the part of African governments to move public service provision into the sphere of public-private partnerships (PPPs), and a greater readiness by development financial institutions to help finance such projects through blending and leveraging arrangements.

African services MNEs are investing regionally. The dispersal of affiliates of African service MNEs confirms the intraregional dimension in a number of industries, including finance, infrastructure and

Box II.1.

Disposal of cell phone towers in Africa

MTN, Bharti Airtel, and Orange SA have all sold off large portions of their tower networks in Africa in recent years to reduce exposure arising from ownership and maintenance. Towers and the infrastructure that accompanies them can account for more than 60 per cent of the expense to build a cell phone network in the continent.⁶ The towers are especially costly to run due to electricity shortages, which means that backup generators and the employment of security personnel are required. Also, revenue per user in Africa is generally lower. Selling the towers to third parties allows for the hosting of multiple tenants—mobile operators and Internet providers—on the same tower. HIS Holding, partially owned by a Goldman Sachs-led consortium and now Africa's largest mobile telecommunications infrastructure provider, has purchased nearly 3,000 towers from MTN in Rwanda, Zambia, Cameroon and Côte d'Ivoire since 2012. Airtel has also agreed to sell and lease back over 1,100 towers from HIS in Zambia and Rwanda under a 10-year renewable contract. As a result, HIS now manages over 21,000 towers in Africa.

Source: UNCTAD, based on media sources.

trade. UNCTAD⁷ identified more than 500 African service MNEs, with some 2,700 overseas affiliates, half of them in other African countries. In industries other than finance, more than 60 African MNEs in both infrastructure and trade have expanded abroad, reflecting demand for these services. In trade, three quarters of 265 foreign affiliates are located within Africa, while in infrastructure two fifths are intraregional. Similarly, MNEs in the financial services sector have both a domestic and regional focus. Africa's growing consumer markets, financial deregulation and the regional orientation of financial firms are factors in intra-African investment flows (box II.2).

The potential for services FDI to develop Africa's economy is significant. FDI in services is important in supporting the participation of African economies in global value chains, as an increasing part of value added in trade consists of services. It is also important in the context of financing progress towards the sustainable development goals. As shown in *WIR14*, the principal investment gaps are in infrastructure industries and vital public services. Increasing attractiveness for services FDI therefore constitutes an opportunity for policymakers. At the same time, it is important to ensure continued affordability and accessibility of services provision for all.

Box II.2.

The contribution of intra-African services FDI to development of Africa's financial industry

Intra-African FDI has played a vital role in driving Africa's burgeoning financial industry, especially in retail banking services (Krüger and Strauss, 2015). Financial services accounted for about 50 per cent of intra-Africa greenfield investment projects between 2003 and the start of 2014, with about 38 per cent of these projects in retail banking, and 5 per cent in insurance.

Intra-African FDI into the financial industry has been led by banks from Kenya (Kenya Commercial Bank and Guaranty Trust Bank/Fina Bank), Nigeria (United Bank for Africa) and South Africa (FirstRand and Standard Bank). The geographical spread of these services has been impressive: South Africa's Standard Bank operates in 20 countries in Africa; Ecobank, a Togo-based pan-African bank in 36; and Nigeria's United Bank for Africa in 19. There has also been strong regional expansion by banks from North Africa – especially Banque Marocaine du Commerce Extérieur and Libya Foreign Arab Bank. Much of this expansion has occurred since the 2008 financial crisis. For example, in response to the crisis, South Africa's Standard Bank sold off its global operations and focused on becoming an African bank.

UNCTAD's database on foreign affiliates, which is based on data from Bureau van Dijk's Orbis database, reports 114 financial companies headquartered in Africa that have established 465 affiliates in other countries, three quarters of them located in the continent.

Source: UNCTAD, based on various sources.

EAST & SOUTH-EAST ASIA

FDI inflows, top 5 host economies, 2014

(Value and change)

2014 Inflows

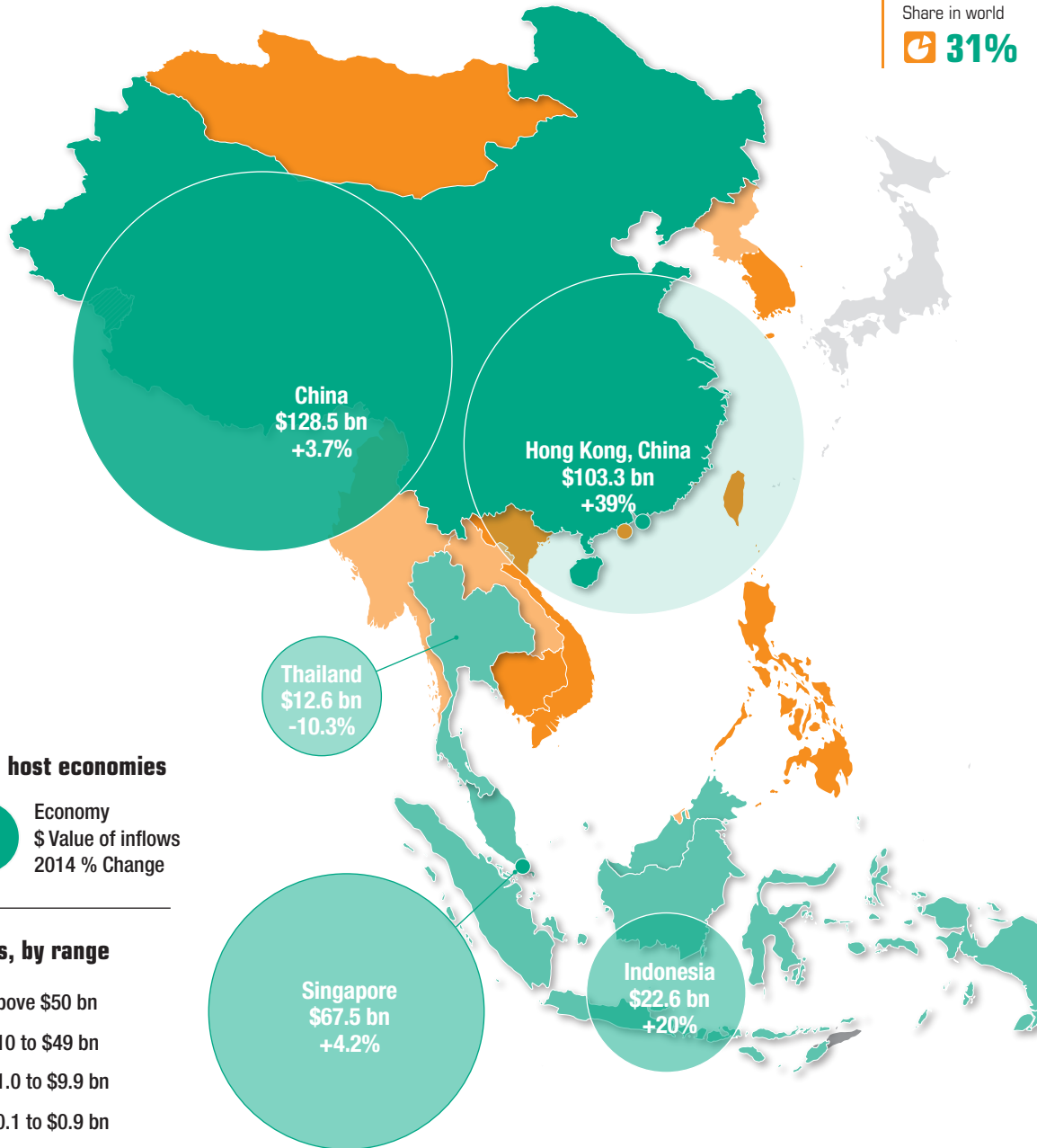
\$ 381 bn

2014 Increase

+9.6%

Share in world

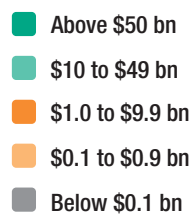
31%



Top 5 host economies

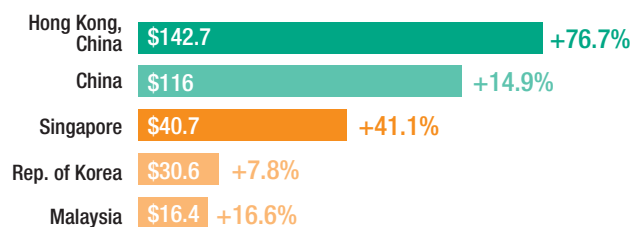


Flows, by range



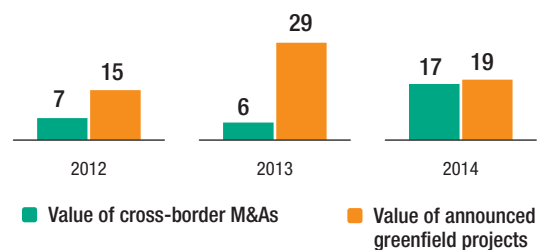
Outflows: top 5 home economies

(Billions of dollars, and 2014 growth)



East and South-East Asia: Cross-border M&As and announced greenfield investments in infrastructure industries, 2012–2014

(Billions of dollars)



Source: UNCTAD.

Note: The boundaries and names shown and the designations used on this map do not imply official endorsement or acceptance by the United Nations.

HIGHLIGHTS

- East and South-East Asia: largest recipient subregions
- China: largest FDI recipient
- Infrastructural connectivity intensifies

Figure A.

FDI inflows, 2008–2014 (Billions of dollars)

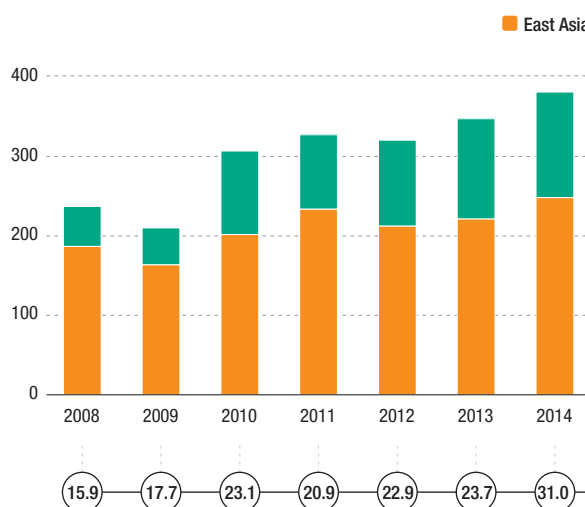


Figure B.

FDI outflows, 2008–2014 (Billions of dollars)

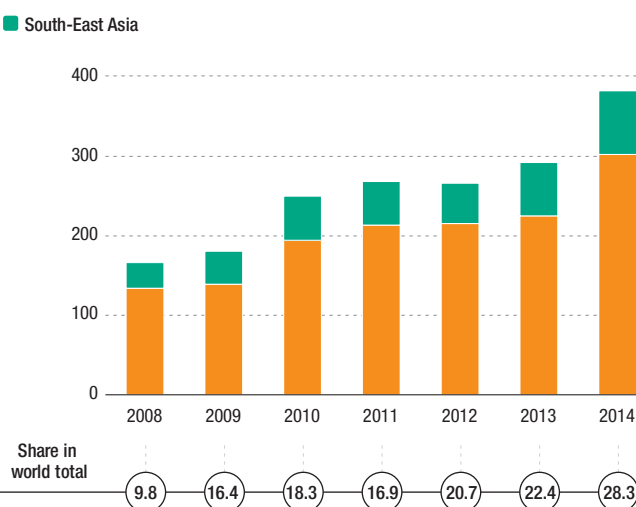


Table A.

Announced greenfield FDI projects by industry, 2013–2014 (Millions of dollars)

Sector/industry	East and South-East Asia as destination		East and South-East Asia as investors	
	2013	2014	2013	2014
Total	158 851	192 612	117 002	145 108
Primary	1 045	4 056	2 180	5 513
Mining, quarrying and petroleum	823	4 056	2 180	5 491
Manufacturing	81 779	106 402	24 241	69 877
Textiles, clothing and leather	5 591	6 519	1 367	4 276
Chemicals and chemical products	13 903	13 097	3 719	5 209
Electrical and electronic equipment	9 132	20 158	6 612	17 654
Motor vehicles and other transport equipment	18 155	28 896	3 157	19 098
Services	76 028	82 154	90 581	69 718
Electricity, gas and water	17 946	10 521	8 375	14 289
Construction	11 317	24 593	13 569	26 231
Finance	11 466	11 149	6 322	5 418
Business services	10 148	15 494	42 912	9 462

Table B.

Announced greenfield FDI projects by region/country, 2013–2014 (Millions of dollars)

Partner region/economy	East and South-East Asia as destination		East and South-East Asia as investors	
	2013	2014	2013	2014
World	158 851	192 612	117 002	145 108
Developed economies	107 844	114 729	17 999	28 369
European Union	42 975	41 227	9 150	9 938
Germany	13 340	14 982	398	388
United Kingdom	8 668	6 286	4 503	5 503
United States	25 142	30 794	5 133	12 024
Japan	29 540	29 201	1 785	2 553
Developing economies	50 457	77 093	97 361	107 058
Africa	483	111	2 411	7 587
Asia and Oceania	49 107	76 530	43 651	88 413
China	3 724	14 073	20 541	28 499
Latin America and the Caribbean	867	451	51 299	11 058
Transition economies	550	789	1 643	9 681

Table C.

Cross-border M&As by industry, 2013–2014 (Millions of dollars)

Sector/industry	Sales		Purchases	
	2013	2014	2013	2014
Total	33 344	80 653	91 009	125 250
Primary	-3 489	496	10 902	7 361
Mining, quarrying and petroleum	-3 492	172	10 845	7 657
Manufacturing	11 679	7 497	6 427	47 954
Food, beverages and tobacco	6 070	1 969	5 701	-1 879
Chemicals and chemical products	637	1 843	892	1 057
Basic metal and metal products	919	480	-2 339	42 161
Computer, electronic, optical products and electrical equipment	1 269	1 323	1 696	4 021
Services	25 154	72 660	73 680	69 935
Electricity, gas, water and waste management	1 216	899	4 873	5 955
Trade	-4 630	6 213	792	2 373
Financial and insurance activities	15 010	53 781	59 246	54 103
Business activities	10 149	7 453	3 714	5 418

Table D.

Cross-border M&As by region/country, 2013–2014 (Millions of dollars)

Partner region/economy	Sales		Purchases	
	2013	2014	2013	2014
World	33 344	80 653	91 009	125 250
Developed economies	6 065	8 720	50 834	44 887
European Union	-5 814	9 682	8 927	18 063
United Kingdom	721	1 767	3 033	5 673
United States	5 038	-3 269	11 279	12 597
Australia	-270	-1 065	6 861	7 737
Japan	9 005	4 894	1 676	2 801
Developing economies	24 836	70 869	38 015	79 225
Africa	334	119	9 456	1 358
Asia and Oceania	23 723	70 750	25 713	72 855
China	2 330	10 148	19 018	49 601
Latin America and the Caribbean	779	-	2 846	5 012
Transition economies	597	447	2 160	1 138

Despite the slowdown in economic growth in East and South-East Asia, FDI inflows to the region remained resilient. Combined inflows grew by 10 per cent to a historical high of \$381 billion in 2014. As a result, East and South-East Asia together continues to be the largest recipient region in the world. Both subregions saw growth: inflows to East Asia rose by 12 per cent to \$248 billion, while those to South-East Asia rose 5 per cent, to \$133 billion. Infrastructural connectivity is intensifying, with MNEs providing much of the investment; in particular, their contributions through NEMs are significant.

China has surpassed the United States to become the largest FDI recipient in the world. FDI inflows to China reached \$129 billion in 2014, an increase of about 4 per cent. This was driven mainly by an increase in FDI to the services sector, particularly in retail, transport and finance, while FDI fell in manufacturing, especially in industries that are sensitive to rising labour costs. FDI inflows in services surpassed the share of manufacturing for the first time in 2011. In 2014, the share of services climbed to 55 per cent, while that of manufacturing dropped to 33 per cent. Among major investing countries, the Republic of Korea's investment in China rose by nearly 30 per cent in 2014, and the European Union (EU) experienced a slight increase. By contrast, FDI flows from Japan and the United States declined by 39 per cent and 21 per cent, respectively.

FDI outflows from China reached \$116 billion. They continued to grow faster than inflows. FDI outflows from China grew by 15 per cent to a record-high \$116 billion; increasing faster than inflows into the country. Overseas acquisitions have become an increasingly important means of international expansion by some Chinese financial institutions. For instance, through six cross-border M&As during a short period between October 2014 and February 2015, China's Anbang Insurance Group took over Waldorf Astoria Hotel in New York in the United States at \$1.95 billion, FIDEA Assurances (cost undisclosed) and Delta Lloyd Bank (€219 million) in Belgium, Vivant Verzekeringen in the Netherlands at \$171 million, Tong Yang Life in the Republic of Korea at \$1 billion, and a 26-story office tower in New York from Blackstone Group. The rapid growth of Chinese outward FDI is likely to continue, particularly in services, as well as in infrastructure-related industries, as the country's "One Belt, One Road" strategy (referring to the Silk Road Economic Belt and the 21st Century Maritime Silk Road) starts to be implemented.

Inflows to Hong Kong (China) and Singapore rose at different paces. Inflows to Hong Kong (China) rose by 39 per cent to \$103 billion. This strong growth was driven by a surge in equity investment associated with some large cross-border M&As, such as the purchase of a 25 per cent stake in A.S. Watson Co. by Singapore's Temasek Holdings at \$5.7 billion, and the \$4.8 billion acquisition of Wing Hang Bank by OCBC Bank (also from Singapore). Investors from mainland China contributed considerably to growth as well. Companies from the mainland were important players in the M&A market in Hong Kong (China) in 2014. For example, COFCO Corporation acquired a 51 per cent stake in Noble Agri Limited, paying \$4 billion to its parent Novel Group, a global supply chain manager of agricultural and mineral products based in Hong Kong (China). In terms of greenfield projects, Chinese companies accounted for about one fifth of all projects recorded by InvestHK in 2014.⁸ FDI inflows to Singapore, another financial centre in the region, by contrast, rose by only 4 per cent to \$68 billion.

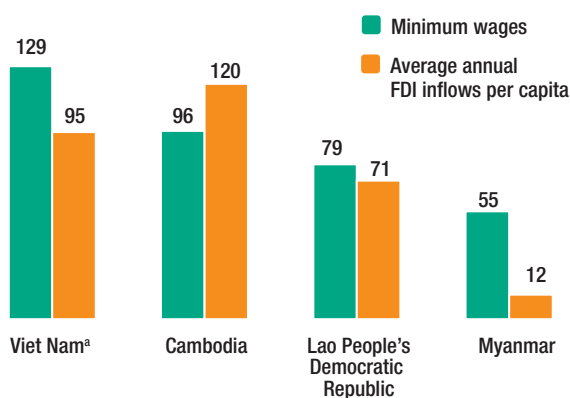
Performance of South-East Asian economies differed significantly. Singapore remained the dominant recipient of FDI in South-East Asia. FDI growth also increased in other South-East Asian economies. Inflows to Indonesia rose by 20 per cent to about \$23 billion. The increase was driven by a significant increase in equity investment, particularly in the third quarter of the year. According to recent data from the Indonesia Investment Coordinating Board, the most important targeted industries were mining; food; transportation and telecommunications; metal, machinery and electronics; and chemical and pharmaceutical. The largest investing countries were Singapore, Japan, Malaysia, the Netherlands and the United Kingdom, in that order.

Viet Nam saw its inflows increase 3 per cent in 2014. In November, the government decided to raise the minimum wage by about 15 per cent in 2015. Compared with 15 years ago, the nominal minimum wage at the national level had already increased 17-fold. Viet Nam still enjoys a labour cost advantage over China, but rapidly rising wages have reduced the difference, which may affect relatively small investors in labour-intensive industries.⁹

Neighbouring low-income countries in South-East Asia have significant labour cost advantages over Viet Nam. As a result, efficiency-seeking FDI in manufacturing to

Figure II.3.

CLMV countries: Minimum monthly wages, 2014, and annual FDI inflows per capita, 2012–2014 (Dollars)



Source: UNCTAD, based on information from the government of Viet Nam and Asia Briefing Ltd.

^a Viet Nam refers to only suburban areas.

Note: CLMV = Cambodia, the Lao People's Democratic Republic, Myanmar and Viet Nam.

those countries increased, including for large projects. In November 2014, for instance, the Taekwang and Huchems Group (Republic of Korea) announced an investment of \$600 million for producing chemical and related products in the Thilawa Special Economic Zone in Myanmar. However, labour costs are clearly not the only factor driving FDI, as witnessed by the FDI inflows per capita in the Lao People's Democratic Republic and Myanmar, which are still considerably lower than in Viet Nam (figure II.3).

Enhancing regional connectivity in East and South-East Asia through international investment

Connectivity between countries and economies of East and South-East Asia is intensifying across infrastructure, business connections and institutions. This has contributed to reduced transaction costs and easier movement of goods, services, information and people, both within and outside the region. There are strong links between international investment and the intensification of regional connectivity in East and South-East Asia.

Infrastructural connectivity intensifies, but more investment is needed. This trend is being driven by

policy efforts to deepen regional integration, and by business and economic imperatives in pursuit of more interlinked regional value chains. Investment in infrastructure industries has helped improve the investment climate and enhanced the region's attractiveness for efficiency-seeking manufacturing FDI, in particular.

Regional cooperation has helped improve infrastructural connectivity within the region and especially that between East Asia and South-East Asia. For example, the Greater Mekong Subregion initiative has brought together Cambodia, the Lao People's Democratic Republic, Myanmar, Thailand and Viet Nam, together with Yunnan Province in China. The initiative also has contributed to infrastructure connectivity between the CLMV (Cambodia, the Lao People's Democratic Republic, Myanmar and Viet Nam) countries and other parts of the region. Driven by regional integration initiatives, cross-border infrastructure projects are further strengthening regional connectivity in the electricity, highway and railway industries. For example, regional cooperation has led to the transmission of electricity supply from the CLMV countries to China, and to the development of the Singapore-Kunming railway link.

Cooperation on various growth triangles, corridors or areas in ASEAN (e.g. Indonesia-Malaysia and Thailand Growth Triangle) has also contributed to strengthening connectivity among contiguous areas. A number of new initiatives introduced recently at the national (e.g. China's "One Belt, One Road" initiative, Korea's Eurasia initiative), regional and international (e.g. Asian Infrastructure Investment Bank, AIIB) levels will further boost regional integration and connectivity. Japan pledged \$110 billion over the next five years to top up investment fund for infrastructure development in the Asian Development Bank. The planned AIIB is expected to have initial capital of about \$100 billion, to be contributed by more than 50 participating countries. The AIIB has the specific objective of boosting infrastructure investment and connectivity across Asia.

Nevertheless, uneven development in infrastructural connectivity between countries, subregions and sectors persists. In transport, for example, the quality of the intraregional road network remains much lower than in the industrialized economies, and the region as a whole has a much lower road density than the OECD average (World Bank, 2014). One reason is that

among countries within the region, there are significant gaps in the level of infrastructural development. For instance, in terms of infrastructure quality, a number of South-East Asian countries rank high globally – Singapore is second – but others rank low: Viet Nam and the Philippines, for instance, rank 82nd and 96th, respectively (WEF, 2013). For some low-income countries in the region, poor infrastructural connectivity has long been a major obstacle to attracting efficiency-seeking FDI and linking to global value chains.

In consequence, there are very large investment needs for infrastructure development in the region. According to estimates by the Asian Development Bank, total investment in infrastructure in Asia as a whole (including for connectivity) is expected to exceed \$8 trillion between 2010 and 2020 (ADB and ADBI, 2009). Lacking the necessary capital or capacity to meet these needs, both countries and the region need to mobilize sources of funding, in which private investors, both domestic and foreign, can play an important role (*WIR14*).

International investment in infrastructure by MNEs has been on the rise. For example, Metro Pacific Investments Corporation, an affiliate of First Pacific (listed in Hong Kong, China), is one of the leading infrastructure investment firms in the Philippines. With businesses in electricity, rail, road and water, its total assets amounted to \$4.5 billion in 2013. In the electricity industry in Thailand, Glow Energy – an affiliate of GDF Suez (France) – is an important player, with total assets and sales at \$3.8 billion and \$2.1 billion, respectively. In mobile telecommunications, subsidiaries of international operators from within and outside of the region account for significant market shares in South-East Asian countries such as Indonesia and Thailand. Asian companies, such as China Mobile and Singapore Telecommunications Ltd., have become important regional players in the industry.

In East Asia, FDI stock in transport, storage and telecommunications had reached \$33 billion in Hong Kong (China) by 2012. In South-East Asia, FDI stock in the same sectors stood at \$37 billion in Singapore and \$15 billion in Thailand, in the same year. More recently, FDI inflows to some infrastructure industries have been rising rapidly. In ASEAN, FDI inflows in electricity and gas utilities had reached \$1.2 billion in 2013, a five-fold rise over the year before. In China, inflows in transport, storage and postal services rose from \$3.4 billion in 2012 to \$4.2 billion in 2013, and this growth has been continuing.

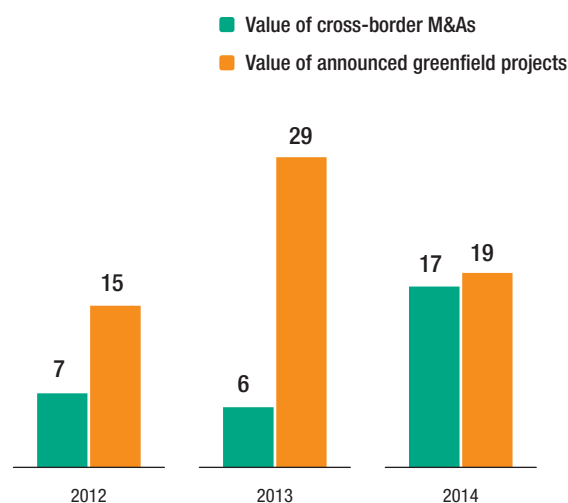
In 2014, the value of cross-border M&As in infrastructure industries nearly tripled to \$17 billion, but that of announced greenfield projects declined by 37 per cent to \$19 billion (figure II.4).

Major cross-border M&As included the purchase of companies in China, Hong Kong (China) and the Republic of Korea in East Asia, as well as in Indonesia, the Philippines, Singapore and Thailand in South-East Asia. In the latter subregion, electricity generation and mobile telecommunications have become important objects of cross-border M&As. In the Philippines, for example, Angat Hydropower Corporation, a subsidiary of Korea Water Resources Corp., took over a hydroelectric plant in Bulacan for \$440 million in October 2014. In June, China Mobile, the world's largest mobile operator by subscribers, bought an 18 per cent stake in True Corp., the third largest mobile operator in Thailand, for \$880 million.

MNEs also invested in infrastructure industries in South-East Asia by implementing new projects. In electricity, Japanese MNEs have been particularly active in the subregion: after investing in large power

Figure II.4.

**East and South-East Asia:
Cross-border M&As and
announced greenfield
investments in infrastructure
industries, 2012–2014**
(Billions of dollars)



Source: UNCTAD cross-border M&A database for M&As and information from the Financial Times Ltd, fDi Markets (www.fDimarkets.com) for greenfield investment projects.

generation projects in Myanmar and Viet Nam in 2013, they announced big investment plans in Malaysia, the Philippines and Thailand in 2014. For instance, Mitsui & Co. Ltd. (Japan), in cooperation with Gulf Energy Development Company Limited (United Arab Emirates), plans to invest approximately \$2.4 billion in a series of cogeneration plants in Thailand. The project aims to build, own and operate 12 gas-fired power plants with a total capacity of 1,470 MW in several industrial estates.

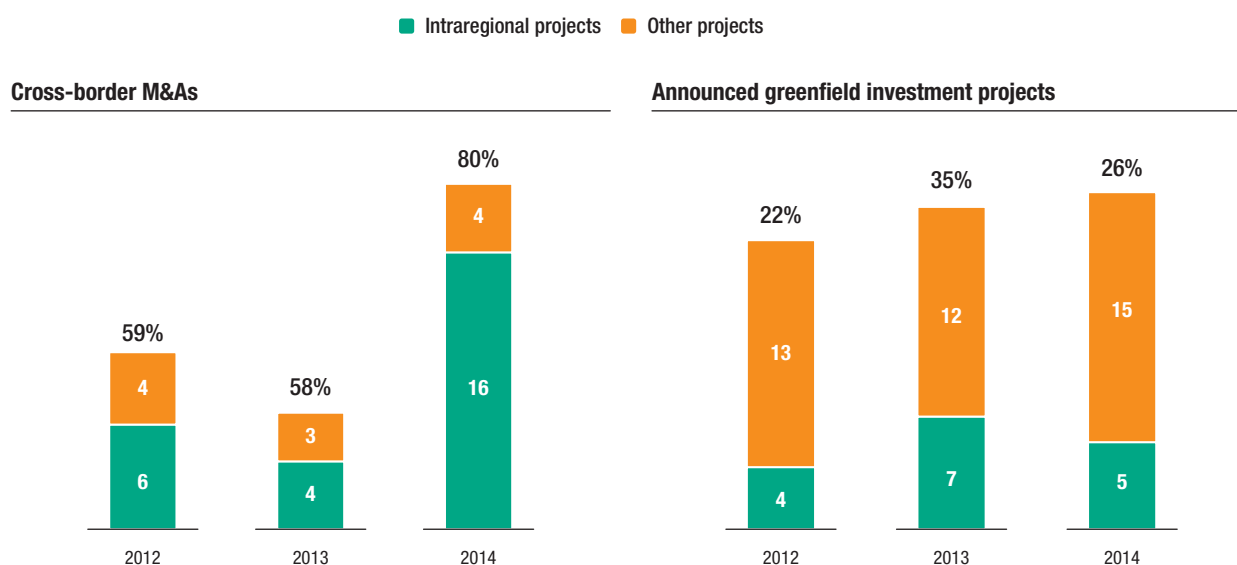
Intraregional FDI is a major driving force for infrastructure investment. A growing part of investment in infrastructure originates from within the region, with Hong Kong (China), China, Japan, Malaysia and Singapore among the most important sources of both investment and operations. There are, however, considerable differences in industry focus by country.

Outward investment in infrastructure industries from East and South-East Asia through cross-border M&As jumped by about 200 per cent to \$20.1 billion while the value of overseas greenfield investment announcements increased slightly in 2014 (figure II.5). The growth in M&As was mainly a result of an increase

in large deals in energy, telecommunications, transport and water. Major acquirers from China, Hong Kong (China) and Singapore were responsible for the largest 10 deals in 2014.

An estimated 45 per cent of outward investment by Asian MNEs in infrastructure industries targeted the region. Intraregional projects accounted for a much higher share in cross-border M&As than in greenfield projects (figure II.5). Traditionally, MNEs from Hong Kong (China) and Singapore have been the important investors in infrastructure industries. During the past few years, Chinese companies have also invested heavily in transport and energy (including electricity generation and transmission, pipelines, and so on) in countries such as Indonesia, Myanmar, the Philippines and Viet Nam. In transport, Chinese investment is expected to increase in railways, including in the Lao People's Democratic Republic and Myanmar. China and Thailand recently signed an agreement for the development of a high-speed rail line in Thailand with an estimated investment of \$23 billion – part of a planned regional network of high-speed railways linking Kunming, China and Singapore. A major part of the region's largest cross-border M&As in infrastructure

Figure II.5. International investment projects in infrastructure by investors from East and South-East Asia, value of projects and share of intraregional projects, 2012–2014
(Billions of dollars and per cent)



Source: UNCTAD cross-border M&A database for M&As and information from the Financial Times Ltd, fDi Markets (www.fDimarkets.com) for greenfield investment projects.
Note: Figures in percentages refer to the share of intraregional projects in the total.

in 2014 were intraregional, including the largest deal, the acquisition of electric utility company Castle Peak Power (Hong Kong (China)) by China Southern Power Grid and CLP Power Hong Kong from ExxonMobil Energy for \$3 billion.

For low-income countries in the region, intraregional flows account for a major share of FDI inflows, contributing to the build-up of infrastructure and productive capacities. For instance, with improving transport and energy infrastructure, Myanmar is emerging as an investment location for labour-intensive industries, including textiles, garments and footwear.

MNE participation through non-equity and mixed modalities increased as well. MNE contributions in the region through NEMs and mixed forms such as build, operate and transfer (BOT) are significant. In many cases, a PPP is developed, with governments providing subsidies while the private sector builds, finances and operates projects. Data from the World Bank's PPI database show that accumulated investment in infrastructure industries in East and South-East Asia through concessions and through management and lease contracts amounts to about \$50 billion. Among major infrastructure industries, water and transport are the most targeted for non-equity and mixed mode participation by MNEs. The two industries accounted for 46 per cent and 31 per cent of the total amount of such activities.

Some projects with BOT and other concession structures have leveraged significant foreign capital and contributed to infrastructure build-up in industries such as electricity and transport. For example, AES Corp (United States) partnered with POSCO Power Corp (Republic of Korea) and China Investment Corporation (a major Chinese sovereign wealth fund)

in developing the Mong Duong II power plant in Viet Nam. Through a BOT-type agreement with the government, the project will involve a total investment of \$1.4 billion and is likely to set an example for PPP-based power projects in the country.

In transport, a number of large projects have been signed or are being planned on a PPP/concession basis. Indonesia, for instance, has recorded a number of such projects in transport infrastructure with a total investment greater than \$1 billion. Examples are the West Coast Expressway concession and the Soekarno-Hatta Railway Project.¹⁰

Prospects for regional infrastructure and connectivity – and beyond. Further infrastructure expansion is necessary to boost regional connectivity in support of value chain development, trade facilitation and the development prospects of distant or isolated areas and communities. New and existing initiatives at national, regional and international levels are increasing the prospects for expansion of infrastructure investment and connectivity across the region – and beyond. In addition to initiatives by the Asian Development Bank, which has a long history of providing infrastructure loans to the region, a number of regional initiatives underpin regional integration development and connectivity.

A number of ASEAN member states have begun to open some transport industries to foreign participation, which may lead to more intraregional FDI. For example, Indonesia has recently allowed foreign investment in service industries such as port management as part of government efforts to enable Indonesia to become a strong maritime country. As more countries in South-East Asia announce ambitious long-term plans, total investment in infrastructure in this subregion is expected to grow further.

SOUTH ASIA

FDI inflows, top 5 host economies, 2014

(Value and change)

2014 Inflows

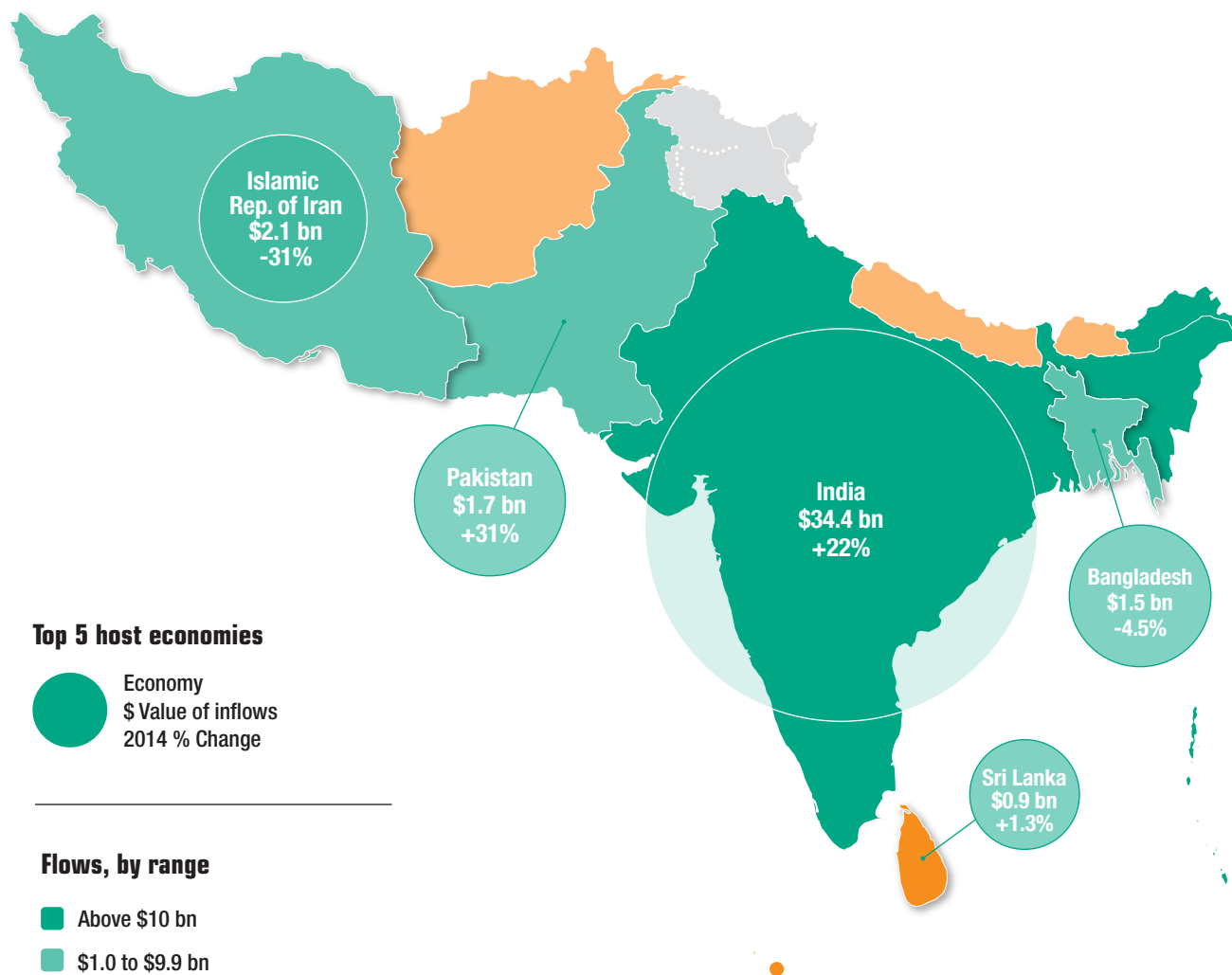
\$ 41.2 bn

2014 Increase

+16%

Share in world

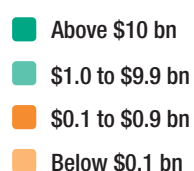
3.4%



Top 5 host economies

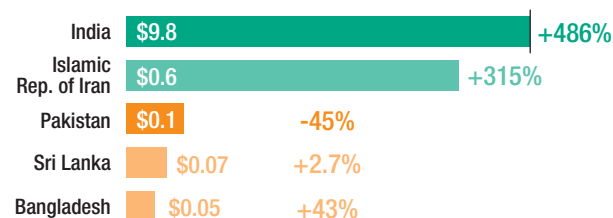


Flows, by range



Outflows: top 5 home economies

(Billions of dollars, and 2014 growth)



Five largest announced greenfield projects, Bangladesh, 2014 (Millions of dollars)

Industry	Capital expenditures	Investor	Home country
Oil and natural gas	1 048	Chevron Bangladesh	United States
Communications	107	SEA-ME-WE 5	Singapore
Communications	107	Verizon Communications	United States
Paper, printing and packaging	107	Britannia Garment Packaging	United Kingdom
Chemicals, paints, coatings, additives and adhesives	81	Asian Paints	India

Source: UNCTAD.

Note: The boundaries and names shown and the designations used on this map do not imply official endorsement or acceptance by the United Nations. Dotted line represents approximately the Line of Control in Jammu and Kashmir agreed upon by India and Pakistan. The final status of Jammu and Kashmir has not yet been agreed upon by the parties.

HIGHLIGHTS

- FDI inflows to India gained strength
- More FDI from China to the region
- FDI boosts automotive industry, particularly in India

Figure A.

FDI inflows, 2008–2014 (Billions of dollars)

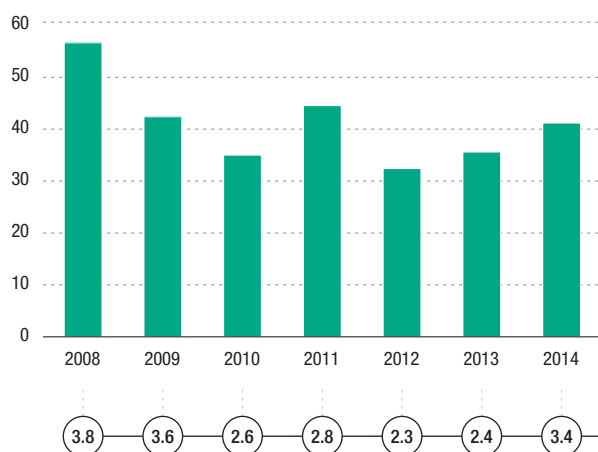


Figure B.

FDI outflows, 2008–2014 (Billions of dollars)

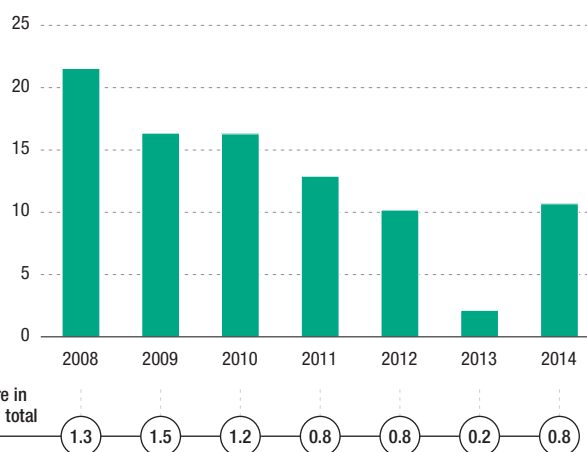


Table A.

Announced greenfield FDI projects by industry, 2013–2014 (Millions of dollars)

Sector/industry	South Asia as destination		South Asia as investors	
	2013	2014	2013	2014
Total	26 368	38 957	15 955	14 220
Primary	22	311	43	11
Mining, quarrying and petroleum	22	311	43	11
Manufacturing	10 919	14 223	7 085	6 879
Textiles, clothing and leather	397	431	104	1 037
Coke, petroleum products and nuclear fuel	44	1 057	81	2 645
Metals and metal products	589	1 364	885	369
Motor vehicles and other transport equipment	1 971	4 270	2 791	933
Services	15 427	24 423	8 827	7 331
Electricity, gas and water	2 044	6 701	2 756	250
Transport, storage and communications	3 644	5 936	2 185	784
Finance	3 378	5 216	861	793
Business services	2 710	3 389	2 079	1 179

Table B.

Announced greenfield FDI projects by region/country, 2013–2014 (Millions of dollars)

Partner region/economy	South Asia as destination		South Asia as investors	
	2013	2014	2013	2014
World	26 368	38 957	15 955	14 220
Developed economies	19 282	23 129	4 134	2 856
European Union	7 384	7 358	2 587	1 503
Germany	2 061	2 074	491	31
United Kingdom	2 470	1 146	1 718	530
United States	5 405	8 489	1 314	744
Japan	2 997	3 129	45	13
Developing economies	7 011	15 724	10 952	11 079
Africa	637	107	5 482	1 366
Asia and Oceania	6 355	15 586	4 755	9 202
China	884	6 079	506	137
Latin America and the Caribbean	20	30	715	510
Transition economies	74	104	870	285

Table C.

Cross-border M&As by industry, 2013–2014 (Millions of dollars)

Sector/industry	Sales		Purchases	
	2013	2014	2013	2014
Total	4 784	5 955	1 621	1 105
Primary	28	-40	1 482	2 934
Mining, quarrying and petroleum	2	-40	1 482	2 924
Manufacturing	4 608	4 170	920	-3 670
Food, beverages and tobacco	1 173	2 026	-34	-727
Chemicals and chemical products	3 620	28	246	19
Pharmaceuticals, medicinal chemicals and botanical products	3 148	1 757	551	55
Basic metal and metal products	-4 068	-1	65	-586
Services	148	1 824	-781	1 841
Trade	42	240	-80	-
Information and communication	-209	546	85	49
Financial and insurance activities	-298	89	-691	2 469
Business activities	621	314	350	-533

Table D.

Cross-border M&As by region/country, 2013–2014 (Millions of dollars)

Region/country	Sales		Purchases	
	2013	2014	2013	2014
World	4 784	5 955	1 621	1 105
Developed economies	3 367	5 361	1 883	-880
European Union	1 518	3 324	1 734	-551
United Kingdom	1 110	3 346	510	-657
United States	1 368	1 591	387	-422
Japan	382	250	-	-
Developing economies	1 212	556	-262	1 900
Africa	233	147	419	2 730
Asia and Oceania	979	409	-1 240	-771
India	-	24	-	32
Singapore	540	265	-771	-808
Latin America and the Caribbean	-	-	559	-59
Transition economies	-	-	-	85

Inflows to South Asia rose to \$41 billion in 2014, primarily owing to growth in India, the dominant FDI recipient in the region. Both announced greenfield investments and cross-border M&As increased across the region: the value of the former jumped by 48 per cent to \$39 billion, while that of the latter rose by about one quarter to \$6 billion. At the regional level, FDI in manufacturing has risen, as illustrated by the automotive industry. In the recently launched “Make in India” initiative, the country’s government has identified automotive as a key industry in which India has the potential to become a world leader.

Inflows to India increased by 22 per cent to \$34 billion. As an expected economic recovery gains ground, FDI inflows are likely to maintain an upward trend in 2015. In terms of sectoral composition, manufacturing is gaining strength, as policy efforts to revitalize the sector are sustained, including for instance the launch of the “Make in India” Initiative in mid-2014.

FDI outflows from South Asia originate mainly from India. In 2014, Indian outflows saw a five-fold jump to \$10 billion, recovering from a sharp decline in 2013. As the performance of the Indian economy has improved, large Indian MNEs have stopped large-scale divestments and some have resumed international expansion, including announcements of some intraregional investments in manufacturing (such as in the automotive and chemical products industries) in neighbouring countries.

A number of South Asian countries saw rising FDI from China. FDI inflows to Pakistan increased by 31 per cent to \$1.7 billion as a result of rising Chinese FDI flows in services, in particular a large investment made by China Mobile in telecommunications. In addition, Pakistan will benefit significantly from the China-Pakistan Industrial Corridor (WIR14, box II.3) and the associated Chinese investment in infrastructure and manufacturing in the overall context of implementing China’s “One Belt, One Road” strategy. According to agreements signed between the two governments in April 2015, Chinese companies will invest about \$45.6 billion in Pakistan over the next few years, including \$33.8 billion in electricity and \$11.8 billion in transport infrastructure.

In Sri Lanka, FDI flows from China rose as well. China has become the largest source of FDI to Sri Lanka in recent years.¹¹ For instance, a joint venture between two local companies and China Merchants Holdings (International) Company has invested \$500 million in Colombo International Container Terminals, the country’s largest foreign investment project. After two years of construction, the port started operation in August 2014. A China–Sri Lanka FTA will be signed in June 2015. If the implementation of the 21st Century “Maritime Silk Road” gains ground, an increasing amount of Chinese investment will flow to Sri Lanka, particularly in large infrastructure projects, including another port planned in Hambantota, as well as highways and an airport. Large projects with

Table II.2.

Ten largest announced greenfield projects in Bangladesh, 2014

Industry	Estimated capital expenditures (Millions of dollars)	Investor	Home country
Oil and natural gas	1 048	Chevron Bangladesh	United States
Communications	107	SEA-ME-WE 5	Singapore
Communications	107	Verizon Communications	United States
Paper, printing and packaging, converted paper products	107	Britannia Garment Packaging	United Kingdom
Chemicals, paints, coatings, additives and adhesives	81	Asian Paints	India
Transportation, freight/distribution services	70	Pacific International Lines	Singapore
Transportation, air transportation	70	Emirates SkyCargo	United Arab Emirates
Building and construction materials	64	Holcim	Switzerland
Medical devices	63	Telstar	Japan
Transportation, freight/distribution services	61	TNT Express	Netherlands

Source: UNCTAD, based on information from the Financial Times Ltd, FDI Markets (www.fDimarkets.com)

investment from India and United States were also recorded in Sri Lanka in 2014.¹²

Greenfield investment to Bangladesh increased.

FDI inflows to Bangladesh remained relatively high at \$1.5 billion, thanks to large greenfield investments in a range of industries (table II.2). As one of the most important foreign investors and the largest producer of natural gas in Bangladesh, Chevron (United States) invested \$500 million in the Bibiyana Expansion Project and prepared to invest another \$650 million to Petrobangla, the local State-owned oil company. Fully operational in 2015, the project in Bibiyana is the largest foreign investment project in the country in value. Other significant projects announced in 2014 were in manufacturing industries such as chemicals, construction materials and medical devices, as well as services industries such as telecommunications and transportation. In April, for example, a joint venture subsidiary of Azbil Telstar (Japan) in Dhaka was inaugurated with a local partner, SAKA International, aiming to serve the fast-growing pharmaceutical industry in the host country.

Nepal began to attract attention from MNEs. The country started to attract some FDI in manufacturing, services and infrastructure industries. For instance, Global Auto Tech (Republic of Korea) reached an agreement with a local company to invest in a truck production plant in Nepal. The announced investment is worth about \$200 million, twice the value of current annual FDI inflows. There is some expectation that Chinese and Indian investments may help boost

foreign investment to Nepal in the coming years. In recent years, hydropower has been the main attraction in Nepal, bringing in investors from electricity-hungry neighbouring countries.¹³ However, the earthquake in April 2015 has raised a major challenge to the economy and to foreign investment.

FDI helped develop the automotive industry in South Asia

Facing constraints such as weak productive capacities and poor infrastructure, South Asian countries have generally lagged behind East and South-East Asian countries in attracting FDI in manufacturing. However, some success stories have emerged at country, industry and local levels, partly because of higher growth rates in recent years and efforts to improve infrastructure and communication. The automotive industry shows how FDI inflows can reshape the trajectory of industrial progress.

India is the dominant recipient of FDI in the automotive industry in South Asia. The country accounted for the preponderance of greenfield investment projects announced by global automakers and first-tier part suppliers in South Asia during 2013–2014, including 12 projects larger than \$100 million (table II.3).

The automotive industry accounts for about 20 per cent of India's manufacturing value added. With annual production of 18 million vehicles, India is the seventh largest automotive producer and, with its large population and growing economy, is likely to ascend in the global ranking.¹⁴

Table II.3.

India: Announced greenfield investments in automotive industry greater than \$100 million, 2013

Industry	Estimated capital expenditures (Millions of dollars)	Investor	Home country
Automobiles	456	Fiat	Italy
Automobiles	320	Renault-Nissan Motor	Japan
Automobiles	249	Volkswagen	Germany
Heavy-duty trucks	235	Scania	Germany
Heavy-duty trucks	235	VE Commercial Vehicles	Sweden
Automobiles	233	Renault-Nissan Motor	Japan
Heavy-duty trucks	233	Wrightbus	United Kingdom
Automotive component	220	Bosch	Germany
Automobiles	207	Ford India	United States
Automobiles	206	Fiat-Tata	Italy
Automobiles	164	Honda Cars India	Japan
Automobiles	127	Mercedes-Benz	Germany

Source: UNCTAD, based on information from the Financial Times Ltd, fDi Markets (www.fDimarkets.com).

In the “Make in India” initiative, the government identified 25 industries in which India has the potential to become a world leader, including the automotive, chemicals, pharmaceuticals and textiles industries. The government has also prioritized environmentally friendly vehicles and launched a new scheme to provide financial incentives for hybrid and electric cars.

The development of the Indian automotive industry has been built on domestic efforts, supplemented and supported by foreign investors and technology. Since the formal opening of the industry to foreign investment in the early 1990s, FDI has flowed in and delivered impacts across different industries, products and value chain segments – from original equipment manufacturing to components and services.¹⁵ According to data from the country’s Department of Industrial Policy and Promotion, accumulated FDI inflows to the automotive industry from April 2000 to November 2014 amounted to \$11.4 billion. As MNEs have entered the Indian market, domestic companies (e.g. Tata Motors, Mahindra and Mahindra) have also started collaborations with MNEs to upgrade their own product offerings.¹⁶

The major sources of FDI in the automotive industry are Japan, United States and the Republic of Korea. MNEs from these countries entered the Indian market through either joint ventures or wholly owned subsidiaries. For example, Suzuki (Japan) was one of the earliest foreign investors in the Indian automotive industry through a joint venture with Maruti, a local company; the investment was aimed at the local market and has so far enjoyed an enduring first-mover advantage. In the early 2010s, Maruti Suzuki still

accounted for nearly 40 per cent of India’s passenger vehicle market. Other major global automakers, including Hyundai (Republic of Korea) and GM (United States), are also investing significantly in India.

An examination of the geographical distribution of automotive production within India shows that inward FDI has led to the emergence of a number of industrial clusters in the country, including those in the National Capital Region (Delhi–Gurgaon–Faridabad), Maharashtra (Mumbai–Nasik–Aurangabad), and Tamil Nadu (Chennai–Bangalore–Hosur) (figure II.6). Though considerable differences exist in the patterns of formation of these clusters,¹⁷ it is clear that FDI can play an important catalytic role. For example, the early entry of Suzuki has contributed to the development of an industrial cluster in the National Capital Region. The presence of six foreign companies, two domestic companies and more than 100 local suppliers has produced a strong automotive cluster in Tamil Nadu (Bapat et al., 2012).

Spillover effects may appear in other South Asian countries. During 2013–2014, Bangladesh, Nepal, Pakistan and Sri Lanka each recorded one greenfield investment project by foreign companies (table II.4). These projects are relatively large investments with a significant number of jobs created. In 2013, for instance, Mahindra & Mahindra (India) invested more than \$200 million in a plant to produce light trucks and utility vehicles in Bangladesh. Investment from the growing automotive industry in India shows the potential of a positive spillover effect to productive capacity-building in South Asia as a whole.

Table II.4.

South Asian countries other than India: Announced greenfield investments in automotive industry, 2013–2014

Host country	Industry	Estimated capital expenditures (Millions of dollars)	Investor	Home country	Year
Bangladesh	Light trucks and utility vehicles	227	Mahindra & Mahindra	India	2013
Nepal	Heavy-duty trucks	200	Global Autotech	Korea, Republic of	2014
Pakistan	Automobiles	200	Honda Atlas Cars Pakistan	Japan	2013
Sri Lanka	Automobiles	3	Toyota Lanka	Japan	2013

Source: UNCTAD, based on information from the Financial Times Ltd, fDi Markets (www.fDimarkets.com).

Figure II.6. India: Major industrial clusters in the automotive industry



Source: UNCTAD, based on the Automotive Component Manufacturers Association of India.

Note: Companies listed in the boxes are major manufacturers in each cluster; companies marked with an asterisk are Indian domestic companies; companies marked with two asterisks are joint ventures between Indian and foreign companies.

The boundaries and names shown and the designations used on this map do not imply official endorsement or acceptance by the United Nations.

WEST ASIA

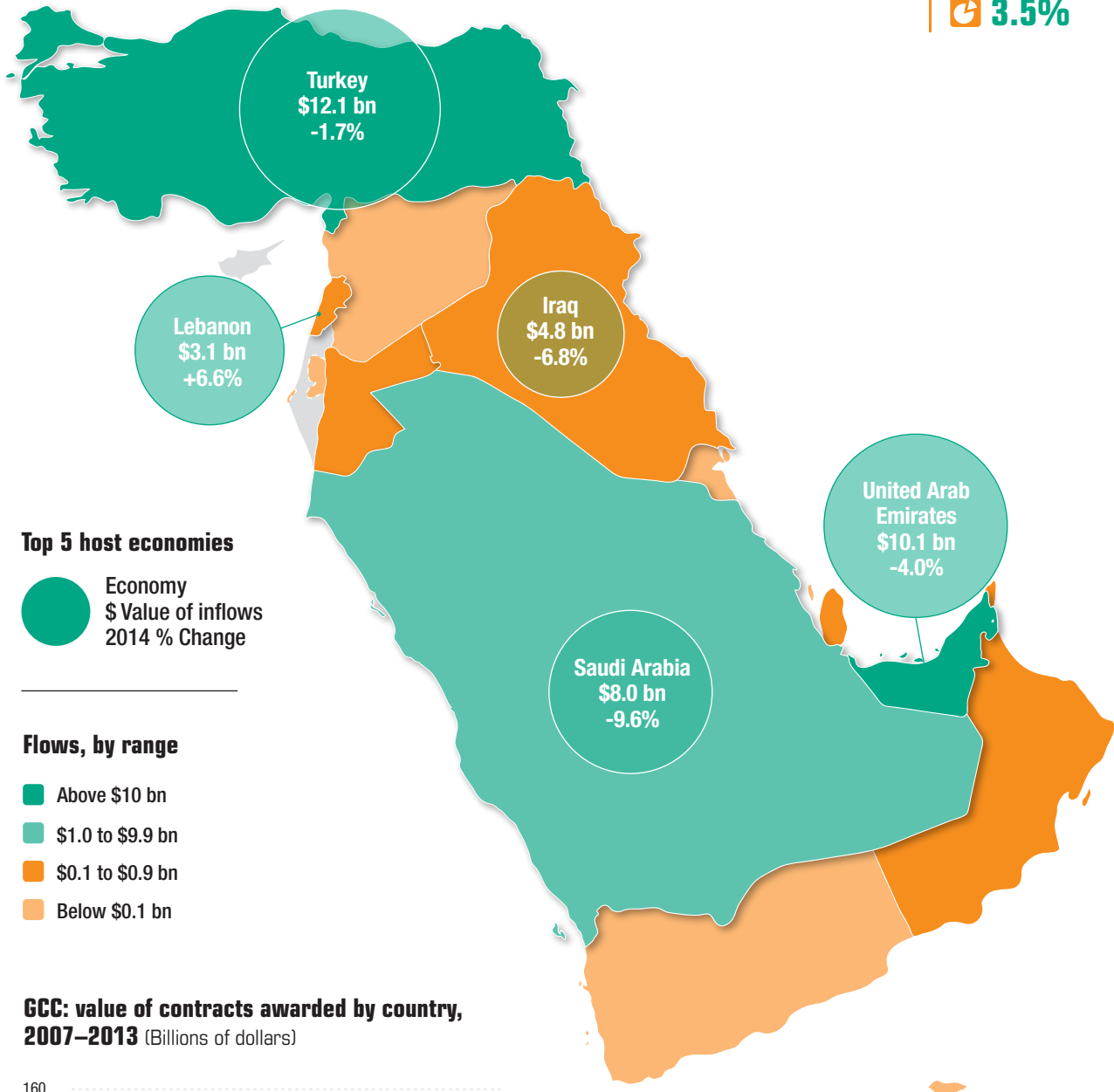
FDI inflows, top 5 host economies, 2014

(Value and change)

2014 Inflows
\$ 43 bn

2014 Decrease
-3.7%

Share in world
3.5%



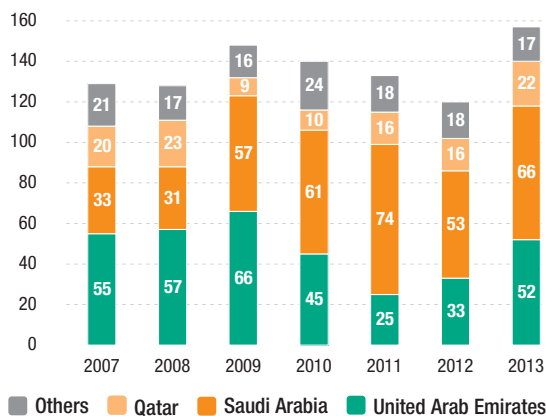
Top 5 host economies

● Economy
 ● \$ Value of inflows
 ● 2014 % Change

Flows, by range

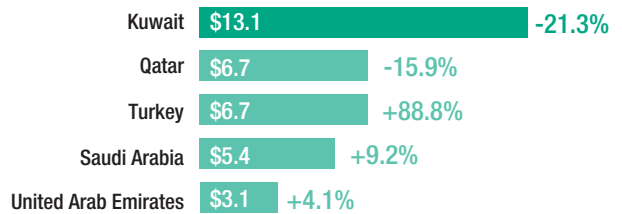
- Above \$10 bn
- \$1.0 to \$9.9 bn
- \$0.1 to \$0.9 bn
- Below \$0.1 bn

GCC: value of contracts awarded by country, 2007–2013 (Billions of dollars)



Outflows: top 5 home economies

(Billions of dollars, and 2014 growth)



Source: UNCTAD.

Note: The boundaries and names shown and the designations used on this map do not imply official endorsement or acceptance by the United Nations.

HIGHLIGHTS

- Regional conflict, political tensions still deter FDI
- Falling private investment, rising public investment
- Rise in non-equity modes of MNE operations in the GCC

Figure A.

FDI inflows, 2008–2014 (Billions of dollars)

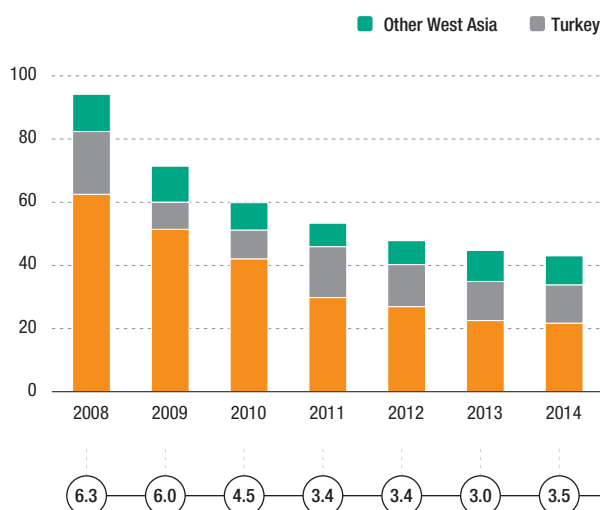


Figure B.

FDI outflows, 2008–2014 (Billions of dollars)



Table A.

Announced greenfield FDI projects by industry, 2013–2014 (Millions of dollars)

Sector/industry	West Asia as destination		West Asia as investors	
	2013	2014	2013	2014
Total	56 047	37 316	38 638	26 929
Primary	5 989	2 620	1 677	322
Manufacturing	18 976	14 739	18 067	8 062
Coke, petroleum products and nuclear fuel	3 754	5 277	9 655	2 088
Chemicals and chemical products	4 503	1 623	209	1 660
Machinery and equipment	756	634	254	18
Motor vehicles and other transport equipment	5 770	3 790	97	145
Services	31 082	19 957	18 895	18 545
Electricity, gas and water	13 759	3 210	1 725	1 020
Construction	2 239	5 215	3 281	7 150
Hotels and restaurants	3 605	2 871	3 246	1 631
Finance	1 791	1 871	2 499	4 751
Business services	6 131	4 770	3 961	1 230

Table B.

Announced greenfield FDI projects by region/country, 2013–2014 (Millions of dollars)

Partner region/economy	West Asia as destination		West Asia as investors	
	2013	2014	2013	2014
World	56 047	37 316	38 638	26 929
Developed economies	27 560	14 907	4 539	5 567
Europe	15 903	8 366	2 392	4 782
United States	9 894	2 683	1 954	381
Developing economies	15 671	21 329	30 397	20 490
Africa	301	1 551	5 842	5 932
Egypt	86	1 307	1 588	4 048
Asia and Oceania	15 326	19 778	24 318	14 336
India	1 209	7 899	2 088	4 407
West Asia	11 701	5 323	11 701	5 323
United Arab Emirates	9 178	4 035	833	655
Transition economies	12 816	1 081	3 703	872
Russian Federation	12 748	974	1 345	289

Table C.

Cross-border M&As by industry, 2013–2014 (Millions of dollars)

Sector/industry	Sales		Purchases	
	2013	2014	2013	2014
Total	2 055	2 729	8 077	10 705
Primary	357	-283	476	3 455
Mining, quarrying and petroleum	344	-286	466	3 455
Extraction of crude petroleum and natural gas	344	-311	-	3 305
Manufacturing	451	988	61	130
Computer, electronic, optical products and electrical equipment	46	283	-	-
Non-metallic mineral products	14	624	-	-
Services	1 248	2 024	7 540	7 120
Electricity, gas, water and waste management	140	226	1 908	-
Accommodation and food service activities	-	75	-99	-1 429
Information and communication	21	27	1 137	4 794
Financial and insurance activities	456	201	3 972	3 020
Business activities	371	533	184	-7

Table D.

Cross-border M&As by region/country, 2013–2014 (Millions of dollars)

Region/country	Sales		Purchases	
	2013	2014	2013	2014
World	2 055	2 729	8 077	10 705
Developed economies	181	1 738	2 739	3 944
European Union	714	783	1 312	1 609
North America	-573	530	69	2 335
Developing economies	1 375	377	4 913	6 614
Africa	29	-	3 194	6 420
North Africa	-	-	3 150	5 708
Egypt	-	-	3 150	29
Morocco	-	-	-	5 659
Latin America and the Caribbean	54	160	266	1 000
Asia and Oceania	1 293	217	1 454	-806
West Asia	1 039	-321	1 039	-321
Transition economies	3	-191	425	146

FDI flows to West Asia maintained their downward trend in 2014 for the sixth consecutive year, decreasing by 4 per cent to \$43 billion. This continuing decline stems from the succession of crises that have hit the region, starting with the impact of the global economic crisis, followed quickly by the eruption of political unrest that swept across the region and, in some countries, escalated into conflicts. This is deterring FDI not only in the countries directly affected – such as Iraq, the Syrian Arab Republic and Yemen – but also in neighbouring countries and across the region.

Turkey remained the largest FDI recipient in the region, with flows registering a 2 per cent decrease to \$12 billion. Growth was uneven: Real estate acquisitions increased for the third consecutive year and at a faster rate (29 per cent), reaching \$4 billion and accounting for 25 per cent of total FDI flows to the country in 2014. FDI in services dropped by 28 per cent, to \$5 billion, mainly due to declining flows into public utilities (–44 per cent to \$1 billion) and financial services (–55 per cent to \$2 billion). FDI in the manufacturing sector rebounded by 30 per cent to \$3 billion after a steep fall in 2013, still short of its 2011–2012 level.

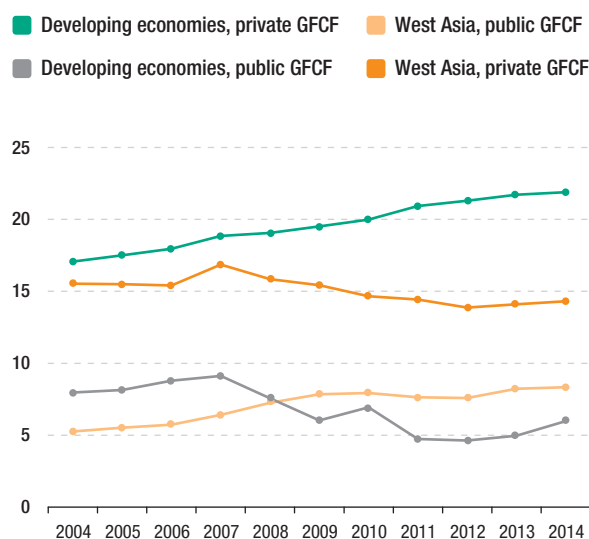
FDI remained sluggish even in the oil-rich Gulf Cooperation Council (GCC) countries (–4 per cent to \$22 billion), which have been relatively spared from political unrest and enjoyed robust economic growth in recent years. In this group of countries – the region's main FDI destination (61 per cent over 2009–2014) – FDI flows have also failed to recover since 2009. Flows to the United Arab Emirates and Saudi Arabia – the region's second and third largest recipients – registered slight declines and remained about \$10 billion and \$8 billion, respectively.

While flows to Jordan and Lebanon remained stable, deteriorating security cut short the recent resurgence of FDI to Iraq, where a significant part of FDI targets the oil sector. Although most of the country's giant oilfields are located in the south, where relative security prevails, disruptions have severed land connections to the north, affecting the supply chain by this route. The crisis might cause delays in oilfield development and – together with the strong decrease in oil prices at the end of 2014 – is likely to deter new investors.

Outward FDI from West Asia also declined by 6 per cent in 2014, driven mainly by divestment (negative intracompany loans) from Bahrain. Kuwait, which has been the region's largest overseas investor, saw FDI

Figure II.7.

West Asia and developing economies: Share of public/private GFCF in GDP, current prices, 2004–2014
(Per cent)



Source: UNCTAD, based on IMF 2015.

Note: The State of Palestine and Syrian Arab Republic are not included. GFCF = gross fixed capital formation.

outflows decline by 21 per cent to \$13 billion. Outward FDI from Turkey jumped by 89 per cent to \$6.7 billion, driven mainly by equity outflows which rose by 61 per cent to \$5 billion.

The decline of FDI flows to West Asia has occurred within a regional context of weakening private investment in relation to GDP starting from 2008 (figure II.7), affected by the same factors that prompted the fall in FDI. In all West Asian countries, except Lebanon and the United Arab Emirates, the average annual ratio of private investment to GDP decreased during 2009–2014 compared with 2003–2008 (table II.5). In Bahrain, Lebanon and Turkey, even the absolute value of private gross fixed capital formation (GFCF) has exhibited a downward trend in recent years.¹⁸ The decline of private investment and increase of public investment in relation to GDP in West Asia contrasts with the trend in developing economies as a whole, where the opposite occurred.

The decline of the share of private investment in GDP in West Asia has been more than offset, at the regional level, by the increase of the share of public investment, with the average annual ratio

of total GFCF to GDP rising from 21.9 per cent in 2003–2008 to 22.3 per cent in 2009–2014. However, the situation varies by country and subregion, as the increase in public investment took place mainly in the GCC countries – financed by their income from oil revenues – and most strongly in Saudi Arabia and Kuwait (table II.5).

The increasing weight of public investment was most evident in GCC economies and has translated into State-led construction growth that focuses on infrastructure and oil and gas development. Capital spending was higher as a share of GDP in all GCC countries between 2009 and 2014, and the public share of total investment increased significantly – in all except the United Arab Emirates – reaching almost 40 per cent (table II.5). This has translated into a construction boom different from the one that took place in the early part of the preceding decade, Saudi Arabia’s being the largest in the region (figure II.8). The residential and commercial megaprojects that defined that boom – most dynamic in the United Arab Emirates – have been replaced by government-led projects in infrastructure, especially in Qatar and Saudi Arabia, and in oil and gas. Ambitious plans for infrastructure upgrading and development were implemented, with a growing emphasis on rail projects. For example, in 2013 more than \$30 billion worth of contracts were awarded for the Riyadh and Doha metro projects alone. In contrast,

the residential and commercial buildings segment, largely privately owned, was hit hard by the crisis and was unable to recover until 2013 (figure II.9). Oil and gas projects benefited from the oil price spike in 2008 that – together with the collapse in the price of building materials and in engineering, procurement, and construction services after the onset of the global financial crisis – enabled national oil companies such as Saudi Aramco, Abu Dhabi National Oil Company and Qatar Gas to proceed with project plans.

This State-led construction growth has an impact on the mode of foreign involvement. The segments of the construction industry¹⁹ that most benefited from expanded State-led investment – oil and gas, and transport – are those with a significant presence of foreign contractors, in contrast to the residential and commercial buildings segment, where local contractors dominate. This shift within the construction sector has opened further opportunities for foreign contractors to engage in new projects through NEMs. From the perspective of a foreign investor, NEMs reduce exposure to risks associated with the region’s evolving instability.

Local contracting companies predominate in terms of contracts awarded, but foreign contractors are preponderant in terms of projects under execution. Local contracting companies picked up 62 per cent of the \$88 billion worth of

Table II.5.

Share of public/private GFCF in GDP and in total GFCF, current prices, 2003–2008 and 2009–2014 (Per cent)

Region/economy	Share of private GFCF in GDP		Share of public GFCF in GDP		Share of public sector in GFCF	
	2003–2008	2009–2014	2003–2008	2009–2014	2003–2008	2009–2014
World	17.8	17.7	5.0	5.8	21.6	24.5
Developing economies	18.0	21.0	8.9	9.7	32.8	31.4
West Asia ^a	15.7	14.4	6.2	7.9	28.1	35.6
Iraq ^b	8.4	7.5	14.4	14.7	63.1	66.2
Jordan	20.3	17.2	7.1	5.1	26.0	22.9
Lebanon	20.7	22.3	2.4	1.8	10.2	7.5
Syrian Arab Republic ^c	11.0	9.9	9.5	9.5	46.3	49.2
Turkey	17.1	15.9	3.4	3.9	16.7	19.8
Yemen	10.2	5.7	7.4	3.5	41.8	38.3
GCC	15.2	14.4	7.4	9.5	32.6	39.7
Bahrain	23.7	13.9	5.8	6.0	19.6	30.0
Kuwait	13.3	11.3	3.8	5.9	22.3	34.1
Oman	14.4	11.0	14.1	14.8	49.5	57.3
Qatar	31.6	22.1	8.3	8.5	20.9	27.7
Saudi Arabia	13.8	12.6	7.6	11.4	35.4	47.4
United Arab Emirates	13.3	16.3	7.3	7.5	35.5	31.5

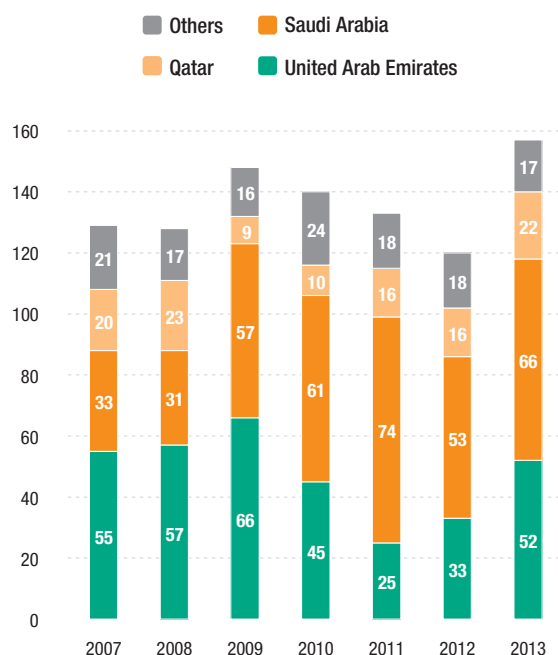
Source: UNCTAD, based on IMF 2015.

^a The State of Palestine is not included for lack of available data.

^b Data for 2003 are not available.

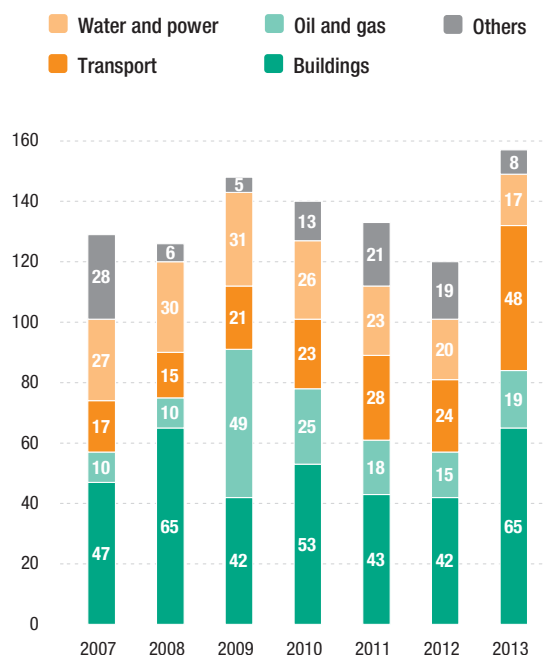
^c Data since 2011 are not available.

Figure II.8. GCC: Value of contracts awarded by country, 2007–2013 (Billions of dollars)



Source: UNCTAD, based on MEED Insight, "GCC Construction Projects Market 2015", August 2014.

Figure II.9. GCC: Value of contracts awarded by segment, 2007–2013 (Billions of dollars)



Source: UNCTAD, based on MEED Insight, "GCC construction projects market 2015", August 2014.

contracts awarded in 2013 (the latest available data) to the largest contractors of each country and across all industries.²⁰ However, foreign contractors hold sway in work under way. For instance, in Saudi Arabia – the GCC's largest market – the share of foreign companies in the value of contracts awarded to the 10 largest contractors was 48 per cent in 2013, but foreign contractors held 53 per cent of the value of the 10 largest projects under execution as of June in that year. The difference is even bigger in the United Arab Emirates, the GCC's second largest market, where foreign companies won only 31 per cent of the value of contracts awarded to the 10 largest contractors in 2013, but held 88 per cent of the value of the 10 largest projects under execution as of May in that year.²¹ This difference could arise from a number of factors such as delays or cancellations of contracts awarded to local private companies, which may face greater funding challenges.

Data for Saudi Arabia and the United Arab Emirates show that in both countries foreign firms, especially from the Republic of Korea (table II.6, box II.3), make up most of the 10 largest contractors with work under

execution. However, local firms are also significant in Saudi Arabia: three are among the four largest contractors (table II.6), with Saudi Binladin by far the country's leading contractor, accounting for more than a quarter of the \$80 billion worth of work carried out by the largest contractors.

However, data on contracts awarded and on work under execution may underestimate the importance of foreign involvement, as they do not capture the subcontract market that has grown around GCC construction projects. This is especially the case with multibillion-dollar projects involving complex civil works, electromechanical systems and other vital infrastructure (Singapore Human Resources Institute, 2012).

The sharp fall in oil prices since mid-2014, particularly following the OPEC meeting in November, is likely to have a significant direct and indirect impact on the construction market in the GCC, particularly in planned oil and gas projects. Already in January 2015 two projects had been adversely affected by cheap oil prices: Qatar Petroleum and Royal Dutch Shell announced the

cancellation of their planned \$6.5 billion Al Karaana petrochemicals joint venture, and Saudi Aramco suspended plans to build a \$2 billion clean fuels plant at its largest oil refinery in Ras Tanura. The fiscal squeeze induced by falling oil prices is also likely to affect government spending, the major driver of the construction market in recent years. Oman and Saudi Arabia have already cut planned capital expenditures in their 2015 budgets by 11 and 25 per cent, respectively;²³ and spending plans will be revised downward in Abu Dhabi where the awards of new projects – such as the Etihad Railway network and the Zayed National and Guggenheim museums – are expected to be delayed.

However, huge fiscal reserves will still allow further State spending. Priority will most likely be given to ongoing and strategic projects, including a number of big infrastructure projects associated with the 2022 World Cup in Qatar, the World Expo 2020 in Dubai, the \$66 billion affordable housing construction programme in Saudi Arabia and infrastructure pipelines in Qatar – all set to provide major business opportunities over the medium term. If the oil price weakness persists, the GCC countries' strategy to prop up GDP growth through increased government spending may not be viable in the long run. Genuine economic diversification is crucial for GCC countries to reduce the dependence of economic growth on oil.²⁴

Table II.6.

Saudi Arabia and the United Arab Emirates: The 10 largest contractors by value of work in progress (Billions of dollars)

Saudi Arabia, June 2013			United Arab Emirates, May 2013		
Company name	Home country	Contract value	Company name	Home country	Contract value
Saudi Binladin Group (SBG)	Local	23.1	Samsung Engineering	Korea, Republic of	7.7
Daelim Industrial Company	Korea, Republic of	10.2	Hyundai E&C	Korea, Republic of	6.9
Al-Shoula consortium	Local	7.7	Habtoor Leighton Group	Local	6.2
Saudi Oger	Local	7.2	Petrofac	United Kingdom	5.5
SKE&C	Korea, Republic of	6.7	GS E&C	Korea, Republic of	5.3
Samsung Engineering	Korea, Republic of	6.7	Daewoo E&C	Korea, Republic of	4.1
Tecnicas Reunidas	Spain	5.2	Samsung C&T	Korea, Republic of	4
Doosan Heavy I&C	Korea, Republic of	5.1	Doosan Heavy I&C	Korea, Republic of	4
Samsung C&T	Korea, Republic of	4.6	Eni Saipem	Italy	3.5
Eni Saipem	Italy	3.7	China State Construction	China	3.1

Source: MEED Insight, "The UAE Projects Market 2013", July 2013; MEED Insight, "MENA Projects Market Forecast & Review 2014", July 2014.

Box II.3.

The rise of the Republic of Korea's engineering, procurement and construction contractors in the GCC

The presence of the Republic of Korea's construction companies in the GCC dates back to the 1970s, when pioneering companies such as Daelim, LG E&C and Hyundai E&C took advantage of the unprecedented scale of development projects sparked by the oil boom. The cumulative amount of overseas construction contracts signed by Korean firms since 1965 exceeded \$500 billion in June 2014. Orders from the Middle East represented 60 per cent, with Saudi Arabia having awarded the largest number: 8,638 projects valued at \$50 billion. Overall, because of their long-established presence in the GCC, as well as their scale, Korean contractors have built up a formidable capacity in the region to rapidly bid for contracts and execute them.

While GCC countries' share in all construction contracts of Korean firms is significant, in contrast their share in the Republic of Korea's outward FDI is small. Among the GCC countries, the United Arab Emirates has received the largest portion (a stock of \$721 million in 2012) of this FDI, and Saudi Arabia the second largest (\$468 million).

In 2009 Korean contractors made a major breakthrough, as GCC oil-producing countries found themselves flush with petrodollars from the oil price spike of 2008, amid tumbling prices for building materials brought on by the global financial crisis. Some GCC countries therefore took a strategic decision to weather the economic storm by promoting State-led construction activity in key sectors, thereby making the GCC one of the most active projects markets in the world. At the same time, the shift transformed the sector from one led by contractors to one led by project owners (States). Korean engineering, procurement and construction firms were in a position to take advantage of this shift and sought to displace competitors by bidding aggressively, with competitive cost structures.²²

Source: UNCTAD.

LATIN AMERICA & THE CARIBBEAN

FDI inflows, top 5 host economies, 2014

(Value and change)

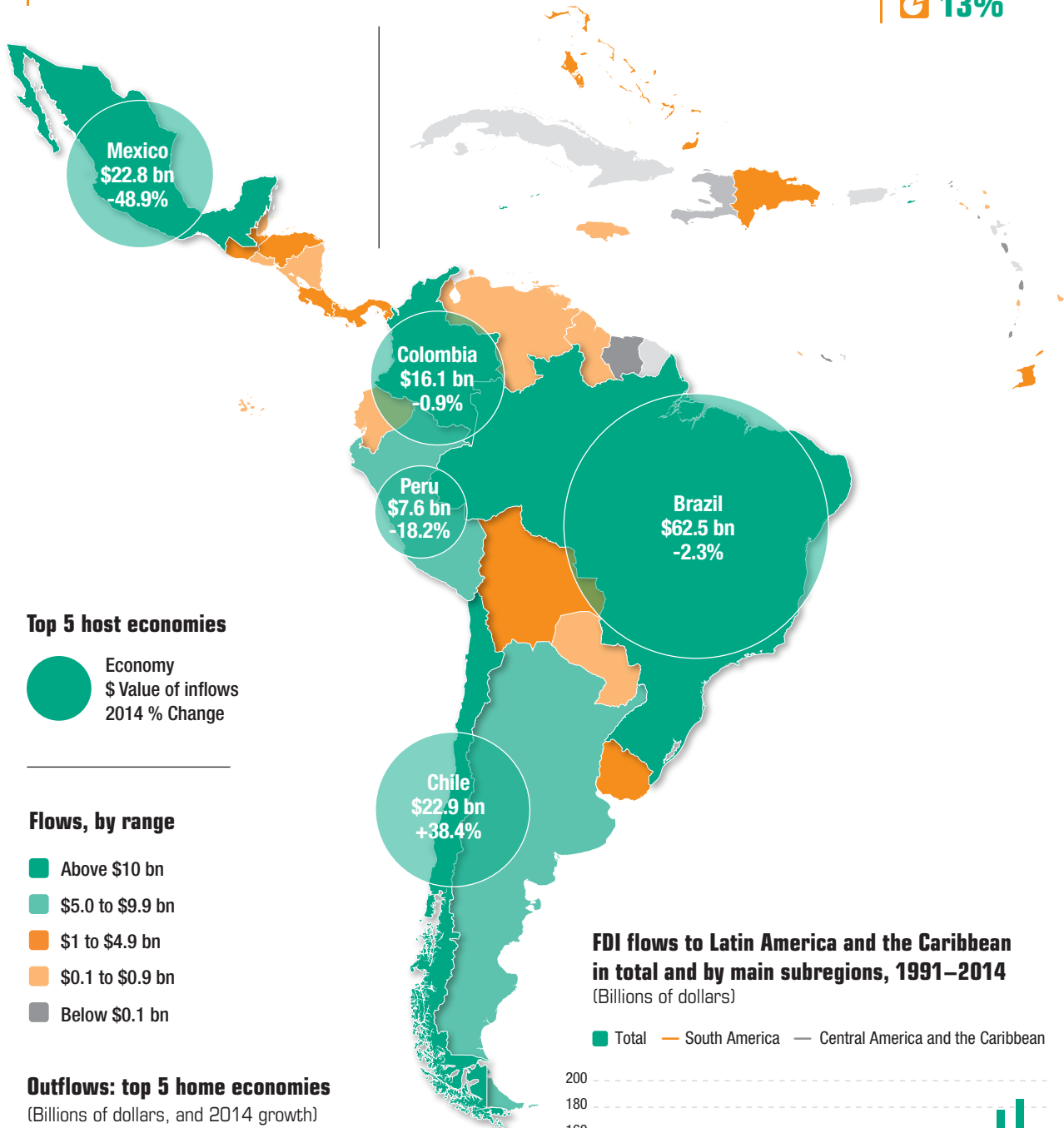
\$ 159.4 bn

2014 Decrease

-14.4%

Share in world

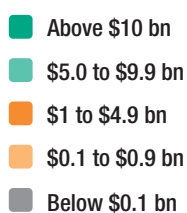
13%



Top 5 host economies

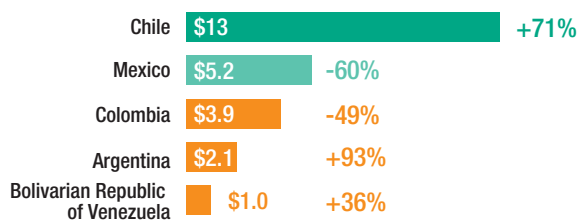


Flows, by range



Outflows: top 5 home economies

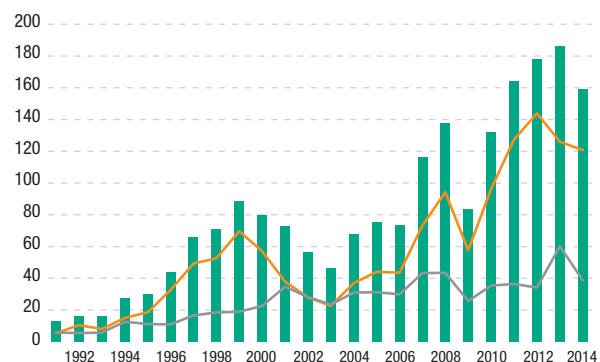
(Billions of dollars, and 2014 growth)



FDI flows to Latin America and the Caribbean in total and by main subregions, 1991–2014

(Billions of dollars)

■ Total — South America — Central America and the Caribbean



Source: UNCTAD.

Note: The boundaries and names shown and the designations used on this map do not imply official endorsement or acceptance by the United Nations.

HIGHLIGHTS

- Inflows fall with commodity prices and cross-border M&As
- European, Asian and regional investors gain ground
- FDI being re-evaluated for post-2015 development agenda

Figure A.

FDI inflows, 2008–2014 (Billions of dollars)

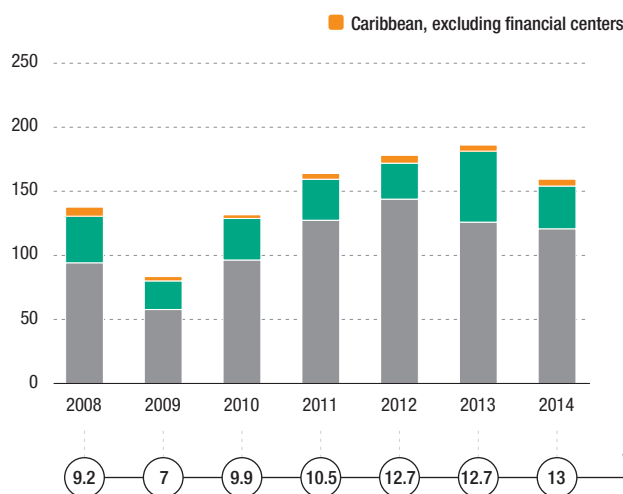


Figure B.

FDI outflows, 2008–2014 (Billions of dollars)

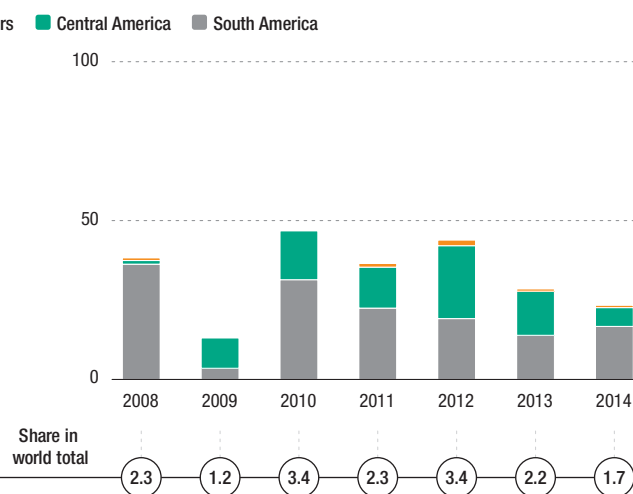


Table A.

Announced greenfield FDI projects by industry, 2013–2014 (Millions of dollars)

Sector/industry	LAC as destination		LAC as investors	
	2013	2014	2013	2014
Total	153 023	89 446	20 499	8 689
Primary	12 568	11 097	4 000	22
Manufacturing	38 427	32 127	6 937	3 652
Food, beverages and tobacco	3 956	2 726	1 741	1 579
Metals and metal products	4 197	2 638	89	207
Electrical and electronic equipment	2 687	3 029	406	86
Motor vehicles and other transport equipment	13 517	16 229	128	263
Services	102 028	46 222	9 562	5 015
Electricity, gas and water	17 067	13 363	809	453
Trade	3 652	2 446	1 255	1 012
Transport, storage and communications	19 380	18 018	4 403	2 215
Finance	5 090	4 135	805	994
Business services	49 701	6 152	1 493	186

Table B.

Announced greenfield FDI projects by region/country, 2013–2014 (Millions of dollars)

Partner region/economy	LAC as destination		LAC as investors	
	2013	2014	2013	2014
World	153 023	89 446	20 499	8 689
Developed economies	81 987	71 167	1 539	1 760
Europe	39 167	30 526	684	551
Canada	4 553	10 358	10	-
United States	26 304	26 190	805	1 151
Developing economies	70 071	18 170	18 864	6 651
Asia and Oceania	52 250	11 790	931	481
China	3 258	8 154	377	282
Hong Kong, China	44 424	175	143	29
Latin America and the Caribbean	17 737	6 084	17 737	6 084
South America	12 341	3 229	14 447	4 201
Central America	5 152	2 576	2 477	1 120
Transition economies	965	109	96	278

Table C.

Cross-border M&As by industry, 2013–2014 (Millions of dollars)

Sector/industry	Sales		Purchases	
	2013	2014	2013	2014
Total	34 797	25 457	16 239	8 440
Primary	1 287	391	288	-2 759
Extraction of crude petroleum and natural gas	345	184	207	-2 600
Mining of metal ores	928	-1	74	26
Manufacturing	25 138	2 929	7 117	3 830
Food, beverages and tobacco	23 848	-42	4 644	1 953
Coke and refined petroleum products	-	-5 317	-	-
Chemicals and chemical products	-116	3 796	156	923
Pharmaceuticals, medicinal chemicals and botanical products	317	3 603	25	11
Services	8 372	22 137	8 834	7 369
Electricity, gas, water and waste management	3 720	4 805	85	840
Transportation and storage	1 488	5 510	628	400
Financial and insurance activities	2 371	5 994	7 953	5 071

Table D.

Cross-border M&As by region/country, 2013–2014 (Millions of dollars)

Region/country	Sales		Purchases	
	2013	2014	2013	2014
World	34 797	25 457	16 239	8 440
Developed economies	19 678	17 949	5 118	8 131
Europe	11 870	-1 269	2 913	4 214
North America	6 792	10 899	2 092	3 916
Other developed countries	1 016	8 319	113	-
Developing economies	14 401	6 797	11 134	309
Africa	-	1 094	-430	400
Latin America and the Caribbean	10 731	-251	10 731	-251
South America	7 928	248	6 177	-1 091
Central America	2 803	-499	3 927	840
Asia and Oceania	3 670	5 954	833	160
South, East and South-East	3 404	4 954	779	-
Asia	-	-	-	-
Transition economies	-	596	-13	-

FDI flows to Latin America and the Caribbean – excluding the Caribbean offshore financial centres – decreased by 14 per cent to \$159 billion in 2014, after four years of consecutive increases.

This fall was mainly the consequence of a 72 per cent decline in cross-border M&As in Central America and the Caribbean and of lower commodity prices, which reduced investment in the extractive industries in South America. The decline took place in both subregions but was stronger in Central America and the Caribbean (down 36 per cent to \$39 billion), where inflows returned to their normal values after the unusually high levels reached in 2013, which were due to a cross-border megadeal in Mexico. Flows to South America continued declining for the second consecutive year, down 4 per cent to \$121 billion, with all the main recipient countries, except Chile, registering negative FDI growth.

Brazil remained the region's leading FDI target with flows amounting to \$62 billion, down 2 per cent despite a significant increase in cross-border M&A sales (by 42 per cent to \$14 billion). The FDI decline was driven by a fall in the primary sector (–58 per cent to \$7 billion), while flows to manufacturing and services increased by 5 and 18 per cent to \$22 billion and \$33 billion, respectively. FDI to the motor vehicles industry registered the strongest increase in absolute value (\$1.4 billion) and reached a total amount of \$4 billion, placing this industry among the four largest FDI recipient sectors in 2014 after commerce (\$6.8 billion), telecommunications (\$4.2 billion), and oil and gas extraction (\$4.1 billion).

Chile recovered its place as the region's second largest target for FDI flows. Inflows to the country rose by 38 per cent to \$23 billion, boosted by exceptionally high levels of cross-border M&A sales, which increased more than three-fold to \$9 billion. Mexico registered the strongest decline in absolute value, with inflows dropping by almost half (\$23 billion) and bringing the country back to the third position in the ranks of FDI recipients. This resulted from a drop of cross-border sales after the exceptional levels reached in 2013 with the \$18 billion sale of the Modelo brewery (*WIR14*), intensified by the \$5 billion divestment by AT&T (United States) in 2014 of its stake in América Móvil. Bucking the general declining trend, the automobile industry continued to attract increasing amounts of FDI, which reached \$4.3 billion, up 21 per cent, representing

19 per cent of total inflows to the country and the highest amount received by all industries in 2014.

Declining investments in the extractive industry affected flows to Argentina (–41 per cent), Colombia (–1 per cent), Peru (–18 per cent) and the Bolivarian Republic of Venezuela (–88 per cent). In Argentina, the negative trend was accentuated by the \$5.3 billion compensation received by the Spanish oil company Repsol for the 2012 nationalization of 51 per cent of YPF, part of which is recorded in FDI flows through income (which affects reinvested earnings). In Colombia, the strong decline of FDI in the extractive industries (21 per cent to \$6.4 billion) was offset mainly by the rises registered in finance (54 per cent to \$2.5 billion), transport and communications (39 per cent to \$1.9 billion), and manufacturing (13 per cent to \$2.9 billion). In the Bolivarian Republic of Venezuela, a strong increase in reverse intracompany loans (the repayment of loans to the parent company) also contributed to the FDI decline.

In Panama – after strong growth registered in 2013 (up by 56 per cent) – flows increased only slightly (1.4 per cent) and remained close to \$5 billion as the peak in large-scale foreign investment related to the canal expansion continues to pass. In Costa Rica, flows decreased by 21 per cent to \$2.1 billion, affected by the closure of Intel's factory²⁵ and Bank of America's restructuring. Intel moved its operations (except R&D facilities) to Malaysia, Viet Nam and China, cutting 1,500 jobs in Costa Rica, while Bank of America laid off 1,400 workers as part of a global restructuring programme. Flows to Trinidad and Tobago increased by 21 per cent as the result of the \$1.2 billion acquisition of the remaining 57 per cent stake in Methanol Holdings Trinidad Limited by Consolidated Energy Company (Mauritius). In the Dominican Republic, FDI registered an 11 per cent rise to \$2.2 billion, partly explained by increased investment in free zones.²⁶

Outward FDI from Latin America and the Caribbean, excluding offshore financial centres, decreased by 18 per cent in 2014, to \$23 billion. Owing to the high incidence of intracompany loans and significant investment in offshore financial centres, outward FDI data may not accurately reflect reality. Brazil ranked last as the region's outward direct investor, registering negative flows (–\$3.5 billion) for the fourth consecutive year, but it remained the region's largest outward direct investor in terms of equity capital outward flows, which

increased by 32 per cent to \$20 billion in 2014 (half of which was directed to offshore financial centres). This is explained by the high amounts of loans from foreign affiliates to parent companies in Brazil, which surpassed by \$23 billion the loans granted by Brazilian parents to their affiliates abroad. Chile and Mexico are other examples of the effect of the high incidence of intracompany loans on total outward FDI flows. Chile was the region's main direct investor abroad in 2014, with flows increasing by 71 per cent to \$13 billion, despite a 26 per cent decline in equity capital outflows. Mexico – the region's second largest outward investor after Chile – saw a 60 per cent decline in outward FDI flows, to \$5.2 billion, driven mainly by a decline in intracompany loans.

Part of MNEs' activities abroad can be captured by their cross-border acquisitions. For Latin American MNEs, such acquisitions decreased by half in 2014, to \$8.4 billion, with Brazil registering the strongest decline (from \$3 billion in 2013 to –\$2.4 billion in 2014). The decrease was due to the small value of new cross-border purchases and the large divestment by Petrobras of its Peruvian oil and gas assets to PetroChina for \$2.6 billion. There has also been a strong decrease in cross-border purchases by MNEs from Chile (–73 per cent to \$750 million) and Colombia (–75 per cent to \$1.6 billion). Mexican MNEs raised the value of their acquisitions abroad by 40 per cent.

The most important deals included Grupo Bimbo's acquisition of Canada Bread for \$1.7 billion and América Móvil's purchase of a 34.7 per cent stake in Telekom Austria for \$1.5 billion.

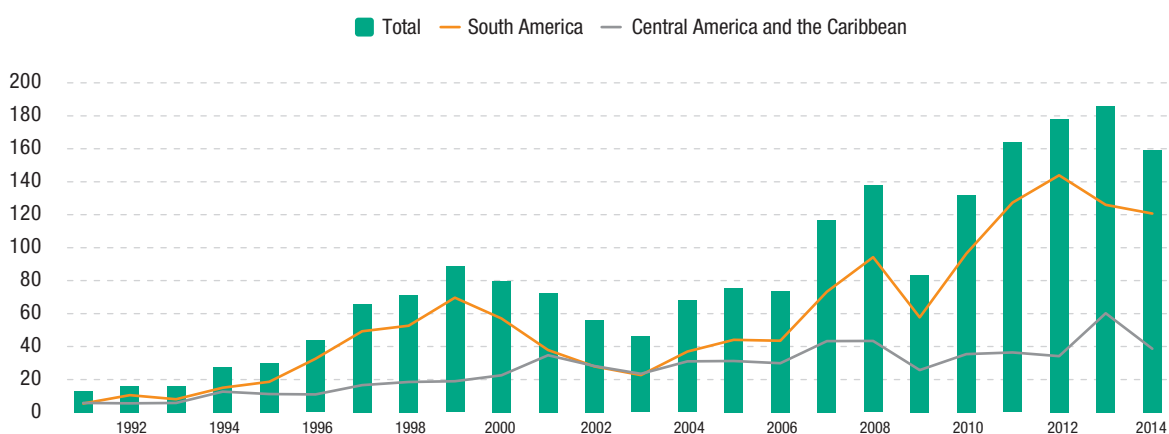
FDI to Latin America and the Caribbean: the current slowdown in a historical perspective

Historically, FDI in Latin America has been concentrated in manufacturing activities to supply highly protected domestic markets. A radical shift in economic policy orientation took place region-wide in the 1990s, opening up a new era for FDI flows into the region. This led to two main waves of FDI in succeeding decades (figure II.10).

The first wave began in the mid-1990s as a result of liberalization and privatization policies that encouraged FDI into sectors such as services and extractive industries, which had previously been closed to private and/or foreign capital. Significant flows of market-seeking FDI went towards non-tradable service activities – such as telecommunications, electricity generation and distribution, transportation and banking – mainly through cross-border acquisitions.²⁷ Simultaneously, large-scale resource-seeking FDI flows targeted the extractive industries mainly in South America, as Mexico kept its oil and gas sector

Figure II.10.

FDI flows to Latin America and the Caribbean in total and by main subregions, 1991–2014 (Billions of dollars)



Source: UNCTAD, FDI/MNE database (www.unctad.org/fdistatistics).

Note: Excludes Caribbean offshore financial centres.

closed to private capital. Finally, efficiency-seeking FDI expanded in Mexico as MNEs established plants in industries such as automobiles and auto parts, electrical and electronic equipment, garments and furniture. Many Central American and some Caribbean countries emulated Mexico's export-oriented model by establishing export processing zones, thereby also receiving efficiency-oriented FDI. This wave came to an end in the period 2000–2003 with a strong decline in FDI inflows, as a result of a number of factors including a period of economic stagnation across the region and globally.

The second wave began in the mid-2000s in response to a surge in commodity prices, leading to increased FDI in extractive industries in the region (especially South America). The effect was both direct and indirect, owing to higher prices for commodity exports, improved terms of trade and higher consumption, which encouraged market-seeking FDI, mainly in services but also in manufacturing (see *WIR12*).²⁸ However, with the abrupt collapse in commodity prices over the last few years, FDI flows began contracting in the primary and secondary sectors after 2012, while those in the tertiary sector began declining in 2013, although it is not clear yet whether the second wave is over (figure II.11). In

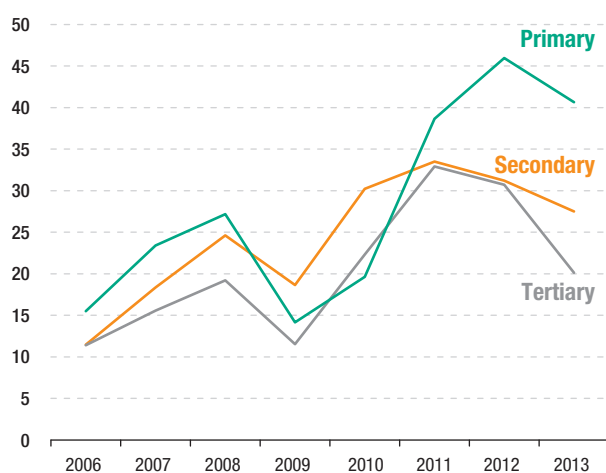
contrast to the situation in South America, FDI to most Central America and Caribbean countries expanded slowly during the 2000s and was more vulnerable to the global economic crisis.

Developed countries remain by far the largest source of FDI into Latin America and the Caribbean, excluding the offshore financial centres (82 per cent of total inward FDI stock in 2013), although intraregional FDI expanded in the 2000s. Half of FDI stock in 2013 was from Europe, while 27 per cent came from North America. The latter is the main foreign investor in the Central America and the Caribbean subregion with half of FDI stock there, while Europe has a greater share in South America. Developing and transition economies represent only 13 per cent of total inward FDI, the largest part of which is intraregional FDI (table II.7). Changes occurred between the two waves of FDI, however. There is a clear decline in the relative size of the United States and Spain: the combined share of these two countries in total FDI flows to the region declined from 50 per cent in 1996–2003 to 32 per cent in 2004–2013. Intraregional FDI expanded strongly during the “second wave”, representing 16 per cent of total FDI flows, compared with 12 per cent previously, but with an important part originating from regional offshore financial centres. Other developing and transition economies remain small, though FDI from China has recently been on the rise.

For example, Chinese acquisitions of enterprises in Latin America and the Caribbean, apart from financial centres, are estimated to have totalled only \$7 billion in the two decades prior to 2010, a year in which they jumped to an estimated \$14 billion before continuing at an estimated \$9 to \$10 billion annually (ECLAC, 2015). The four major Chinese oil companies (CNPC, Sinopec, CNOOC and Sinochem) have a presence in all oil-exporting Latin American countries, except Mexico and the Plurinational State of Bolivia; and Minmetals significantly expanded its investments in Peru in 2014 by purchasing the Las Bambas mine for \$5.85 billion. Initiatives to boost trade between the Atlantic and Pacific sides of Latin America and the Caribbean – for example, proposed new canals across Central America and connectivity across the Amazon – are likely to attract further interest by investors from Asia.

The rise of FDI income has raised the relative share of reinvested earnings in FDI components. Income on inward FDI has grown steadily since

Figure II.11. South America: FDI flows by sector, 2006–2013 (Billions of dollars)



Source: UNCTAD, FDI/MNE database (www.unctad.org/fdistatistics).

Note: Countries included are Argentina, the Plurinational State of Bolivia, Brazil, Chile, Colombia, Ecuador, Paraguay and Uruguay. These countries attracted 89 per cent of total FDI flows to South America in 2006–2013.

Table II.7.

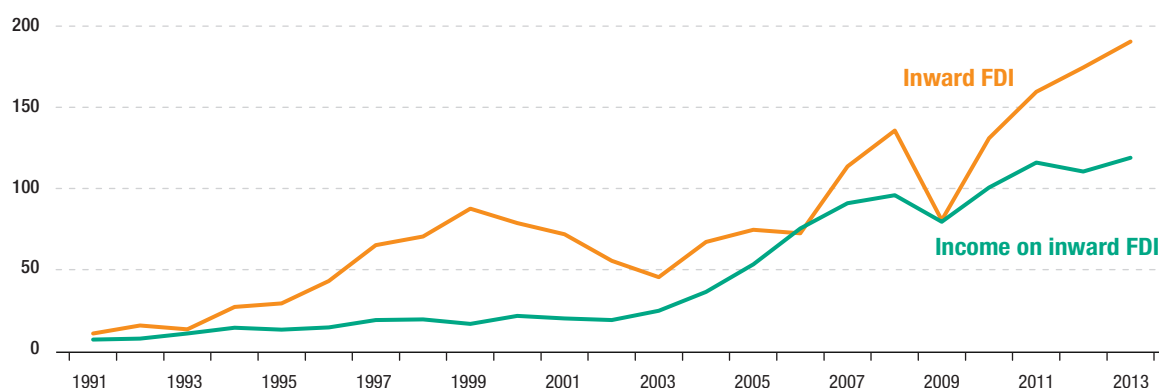
FDI to Latin America and the Caribbean by main home countries, group of economies and regions (Percentage shares in regional totals)

Home economy/region	Latin America and the Caribbean			South America			Central America and the Caribbean		
	Flows 1996–2003	Flows 2004–2013	Stocks 2013	Flows 1996–2003	Flows 2004–2013	Stocks 2013	Flows 1996–2003	Flows 2004–2013	Stocks 2013
United States	33.3	23.9	23.8	19.2	14.8	15.2	59.9	40.7	44.9
Netherlands	8.2	13.9	16.7	8.5	14.6	19.8	7.6	12.6	9.0
Spain	17.1	8.5	10.6	20.7	7.3	10.7	10.5	10.7	10.2
Belgium/Luxembourg	1.4	7.3	6.9	1.9	7.8	6.3	0.5	6.2	8.3
Canada	2.1	5.1	3.6	1.4	2.9	2.8	3.4	9.0	5.3
United Kingdom	3.3	4.2	3.7	2.8	5.0	3.3	4.2	2.8	4.5
Switzerland	1.3	3.7	2.4	0.8	4.9	2.4	2.2	1.6	2.5
France	4.1	3.2	3.1	6.3	4.4	4.0	-0.1	0.9	1.0
Japan	1.5	3.0	2.8	1.4	3.7	3.2	1.8	1.7	1.9
Mexico	0.2	3.0	2.0	0.1	3.9	2.4	0.3	1.3	1.1
Chile	0.6	2.6	1.4	0.9	3.9	1.8	0.2	0.2	0.2
Developed economies	81.2	80.6	81.8	74.3	75.2	77.4	94.3	90.5	92.4
Europe	42.8	46.4	49.8	50.2	50.6	53.9	29.0	38.7	39.9
North America	35.7	28.9	27.4	21.2	17.7	18.0	63.2	49.7	50.2
Developing economies	12.5	17.8	12.6	16.7	22.8	14.9	4.6	8.5	7.1
Latin America and the Caribbean	11.8	15.9	10.7	16.3	20.5	13.0	3.4	7.3	5.3
Financial centres	7.4	6.4	3.3	10.4	8.6	4.2	1.7	2.5	1.2
South America	2.4	5.8	4.8	3.3	7.8	6.0	0.6	2.0	1.9
Central America and the Caribbean	2.1	3.7	2.4	2.6	4.1	2.5	1.1	2.8	2.2
Asia and Oceania	0.7	1.9	1.8	0.4	2.3	1.7	1.2	1.2	1.8
South-East Europe and CIS	0.0	0.1	0.1	0.0	0.2	0.1	0.0	0.0	0.0
Unspecified	6.3	1.5	5.5	9.0	1.8	7.6	1.1	1.0	0.5

Source: UNCTAD, FDI/MNE database (www.unctad.org/fdistatistics).

Note: Host countries in South America: Argentina, the Plurinational State of Bolivia, Brazil, Chile (only stocks), Colombia (only flows), Ecuador (only flows), Paraguay, Peru, Uruguay (only stocks, 2012) and the Bolivarian Republic of Venezuela (flows data cover only 1996–2012). In Central America and the Caribbean: Costa Rica, the Dominican Republic (only flows), El Salvador (flows data cover only 1998–2012), Honduras, Mexico, and Trinidad and Tobago (flows data cover only 1996–2012; stocks data are 2012).

Figure II.12. FDI flows and income on FDI in Latin America and the Caribbean, 1991–2013
(Billions of dollars)



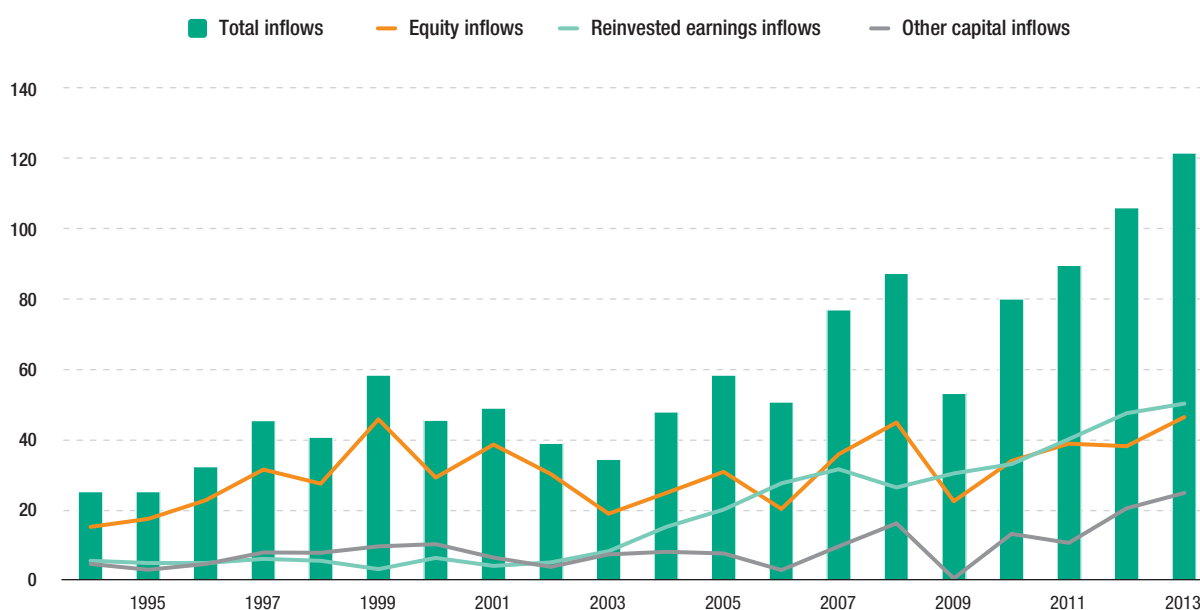
Source: UNCTAD, FDI/MNE database (www.unctad.org/fdistatistics).

Note: Excludes offshore financial centres. Host countries in South America: Argentina, the Plurinational State of Bolivia, Brazil, Chile, Colombia, Ecuador, Guyana, Paraguay, Peru, Suriname, Uruguay and the Bolivarian Republic of Venezuela. In Central America: Belize, Costa Rica, El Salvador, Guatemala, Honduras, Mexico, Nicaragua and Panama. In the Caribbean: the Dominican Republic, Jamaica, and Trinidad and Tobago.

Figure II.13.

Latin America and the Caribbean: FDI inflows, total and by components, 1994–2013

(Billions of dollars)



Source: UNCTAD, FDI/MNE database (www.unctad.org/fdistatistics).

Note: Excludes offshore financial centres. Brazil is not included because data on reinvested earnings are not available. Countries included in South America: Argentina, Bolivia, Chile, Colombia, Ecuador, Guyana, Paraguay, Peru, Surinam, Uruguay and the Bolivarian Republic of Venezuela. In Central America and the Caribbean: Costa Rica, El Salvador, Guatemala, Honduras, Mexico, the Dominican Republic, and Trinidad and Tobago.

2003–2004 (mainly because of the high prices and profits enjoyed in the extractive industry until recently), approaching the scale of inflows in the latter part of the 2000s (figure II.12). As a result, reinvested (or retained) earnings became the main component of FDI inflows in the 2000s, in contrast to the 1990s when this FDI component was marginal and equity capital predominant (figure II.13).

The current slowdown in FDI flows to the region is an occasion for a reflection on the experience of the two FDI waves across the region.

In the context of the post-2015 development agenda, policymakers may consider potential policy options on the role of FDI for the region's development path. Lessons from the past include the following:

- The commodity “bonanza” in part distracted policymakers from carefully designed development strategies in which FDI can play a role in supporting Latin American and Caribbean economies' entry into, and growth within, global value chains (*WIR13*). A re-evaluation of development policies is needed, based on a careful assessment of spillovers from

FDI, the capacities needed by domestic firms to benefit from them, and options to establish effective linkages between MNEs and local enterprises.

- The impact of FDI entry on the balance of payments is broader than a mere assessment of flows and income generated. The consequences depend, among others, on FDI motivations – i.e. resource-seeking, market-seeking, efficiency-seeking, or just “parking” assets. In light of MNEs' high retained investment income across the region, it is essential for policymakers to encourage the use of such income for productive reinvestments and longer-term benefits.
- Across the region, MNEs are hampered by the slowdown in commodity prices, lower economic growth and flat domestic demand. Policymakers may consider the broader role of FDI in local development pathways. Prospects for reduced relative importance of commodities-related FDI may provide opportunities for diversification of FDI flows, including into sectors key for sustainable development.

TRANSITION ECONOMIES

FDI inflows, top 5 host economies, 2014

(Value and change)

2014 Inflows

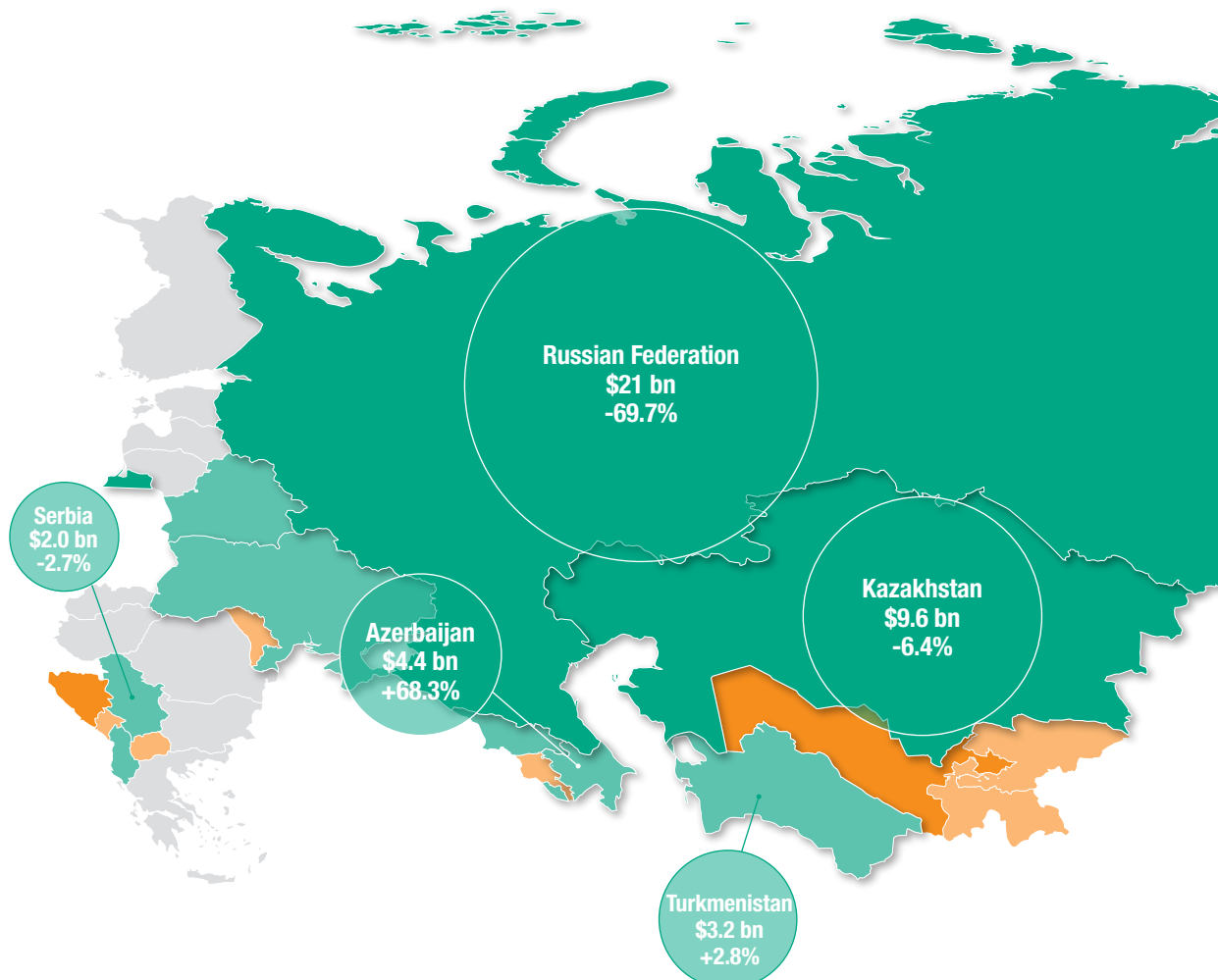
\$ 48.1 bn

2014 Decrease

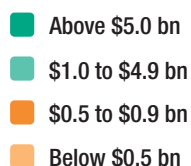
-51.7%

Share in world

3.9%



Flows, by range

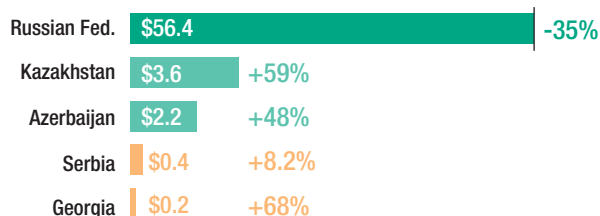


Top 5 host economies



Outflows: top 5 home economies

(Billions of dollars, and 2014 growth)



The five largest greenfield FDI projects announced in the transition economies, 2014 (Millions of dollars)

Name of investing company	Source country	Destination	Value
China Triumph International Engineering	China	Russian Federation	3 000
Hawtai Motor Group	China	Russian Federation	1 100
TERNA	Italy	Montenegro	1 000
Hareon Solar Technology	China	Bosnia and Herzegovina	636
Great Wall Motors (GWM)	China	Russian Federation	520

Source: UNCTAD.

Note: The boundaries and names shown and the designations used on this map do not imply official endorsement or acceptance by the United Nations.

HIGHLIGHTS

- Geopolitical risk, regional conflict weighed down flows to the CIS
- Developing-economy MNEs becoming large investors
- FDI to decline in 2015 with continued recession and low oil prices

Figure A.

FDI inflows, 2008–2014 (Billions of dollars)

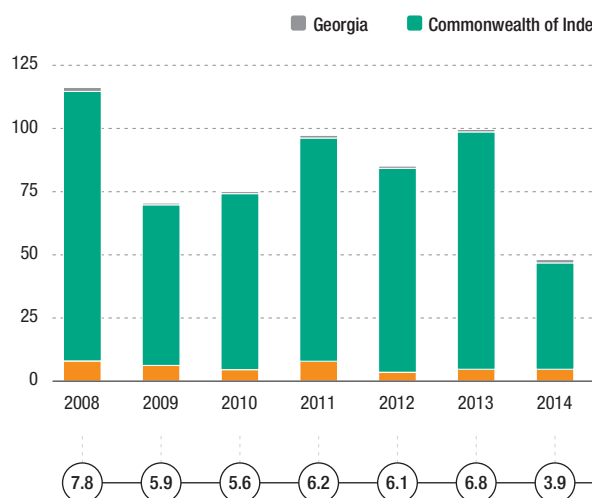


Figure B.

FDI outflows, 2008–2014 (Billions of dollars)

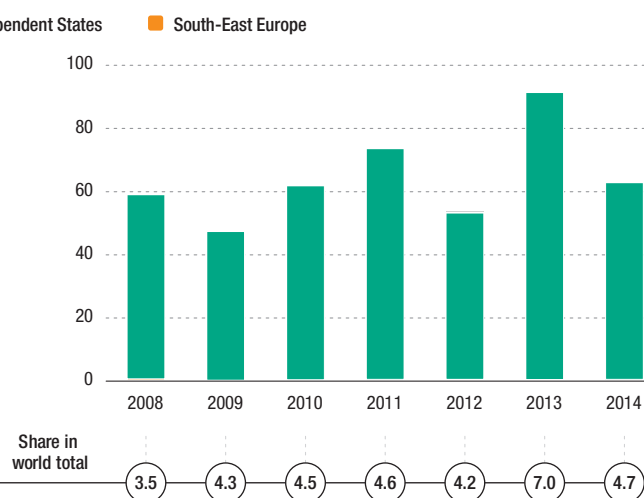


Table A.

Announced greenfield FDI projects by industry, 2013–2014 (Millions of dollars)

Sector/industry	Transition economies as destination		Transition economies as investors	
	2013	2014	2013	2014
Total	29 345	25 650	18 818	5 801
Primary	551	391	3 135	931
Mining, quarrying and petroleum	551	391	3 135	931
Manufacturing	10 920	15 682	2 559	1 701
Food, beverages and tobacco	890	1 938	248	376
Non-metallic mineral products	834	1 194	-	402
Machinery and equipment	655	3 373	174	87
Motor vehicles and other transport equipment	2 065	4 278	696	319
Services	17 874	9 578	13 123	3 169
Electricity, gas and water	5 468	3 172	10 335	355
Construction	3 045	1 458	-	97
Transport, storage and communications	2 727	1 335	734	989
Finance	2 490	1 798	1 434	1 042

Table B.

Announced greenfield FDI projects by region/country, 2013–2014 (Millions of dollars)

Partner region/economy	Transition economies as destination		Transition economies as investors	
	2013	2014	2013	2014
World	29 345	25 650	18 818	5 801
Developed economies	20 914	12 537	2 266	1 630
European Union	15 679	9 842	2 126	1 465
Germany	2 773	1 942	158	116
Italy	972	1 900	-	-
United States	2 775	1 747	40	34
Developing economies	6 385	11 116	14 506	2 173
Africa	74	-	101	90
East and South-East Asia	1 643	9 681	550	789
China	757	8 332	89	665
West Asia	3 703	872	12 816	1 081
Latin America and the Caribbean	96	278	965	109
Transition economies	2 046	1 998	2 046	1 998

Table C.

Cross-border M&As by industry, 2013–2014 (Millions of dollars)

Sector/industry	Sales		Purchases	
	2013	2014	2013	2014
Total	-3 820	4 220	3 054	1 831
Primary	-3 726	3 011	1 771	2 526
Mining, quarrying and petroleum	-3 726	3 011	1 771	2 526
Manufacturing	2 813	1 309	-24	-2 491
Chemicals and chemical products	2 000	-	30	-
Pharmaceuticals, medicinal chemicals and botanical products	-34	379	-	-
Basic metal and metal products	425	24	-59	-2 406
Motor vehicles and other transport equipment	60	750	-	-
Services	-2 907	-100	1 307	1 797
Electricity, gas, water and waste management	857	-1 267	597	-
Telecommunications	-2 326	5	-	-
Financial and insurance activities	-164	-305	-17	1 757
Business activities	-73	1 361	72	-

Table D.

Cross-border M&As by region/country, 2013–2014 (Millions of dollars)

Region/country	Sales		Purchases	
	2013	2014	2013	2014
World	-3 820	4 220	3 054	1 831
Developed economies	-7 191	1 536	1 682	-251
European Union	-3 987	200	243	2 184
Cyprus	-234	5 085	-	20
Italy	-1 905	-2 803	357	1 588
United Kingdom	-487	-1 013	5	-
United States	-3 580	487	30	-2 414
Developing economies	2 572	1 363	600	852
Asia	2 585	1 369	600	256
South, East and South-East Asia	2 160	1 223	597	447
China	2 000	1 642	-	-
Transition economies	771	1 231	771	1 231
Russian Federation	607	1 374	817	-173

FDI inflows of the transition economies of South-East Europe, the Commonwealth of Independent States (CIS) and Georgia fell by more than half in 2014 compared with the previous year, to \$48 billion – a value last seen in 2005. In the CIS, regional conflict coupled with falling oil prices and international sanctions reduced foreign investors' confidence in the strength of local economies. In South-East Europe, FDI flows remained flat at \$4.7 billion.

In South-East Europe, foreign investors mostly targeted manufacturing. In contrast to previous years, when the largest share of FDI flows was directed to the financial, construction and real estate industries, in 2014 foreign investors targeted manufacturing, buoyed on the back of competitive production costs and access to EU markets. Serbia and Albania, both EU accession candidates, remained the largest recipients of FDI flows in the subregion at \$2 billion and \$1 billion, respectively.

Geopolitical risk and regional conflict weighed heavily on FDI flows to the transition economies of the CIS. FDI flows to Ukraine fell by 91 per cent to \$410 million – the lowest level in 15 years – mainly due to the withdrawal of capital by Russian investors, and investors based in Cyprus (partly linked to round-tripping from the Russian Federation and Ukraine). The Russian Federation – the region's largest host

country – saw its flows fall by 70 per cent to \$21 billion because of the country's negative growth prospects as well as an adjustment after the exceptional level reached in 2013 (due to the large-scale Rosneft–BP transaction (WIR14)). FDI flows to Kazakhstan fell by 6 per cent in 2014, as a rise in equity investments was offset by a decline in intracompany loans. Geological exploration activities by foreign investors continued, accounting for more than half of FDI stock in the country. Other transition economies in the CIS saw their FDI flows rise in 2014. Flows to Azerbaijan almost doubled to \$4.4 billion, with investments in the oil and gas industry accounting for three quarters of the total (primarily BP exploration in Shahdeniz).

In 2014, developing and transition economies became the largest investors in the region in terms of value of announced greenfield investment projects. China, with projects worth more than \$8 billion, is by far the largest greenfield investor in the region. Among the top 10 greenfield projects announced, seven were by Chinese investors (table II.8). In 2014, China became the fifth largest FDI investor in the Russian Federation, up 13 positions since 2007. In the oil and gas industry, for instance, the State-owned China National Petroleum Corp acquired a 20 per cent stake in OAO Yamal SPG, for \$1.1 billion. In the automotive industry, Great Wall Motor (China) started to build an automotive plant in

Table II.8.

The 10 largest greenfield FDI projects announced in the transition economies, 2014

Rank	Name of investing company	Source country	Destination	Sector	Key Business Function	Estimated capital expenditures (Millions of dollars)	Jobs created
1	China Triumph International Engineering	China	Russian Federation	Industrial Machinery, Equipment & Tools, All other industrial machinery	Manufacturing	3 000	3 000
2	Hawtai Motor Group	China	Russian Federation	Automotive OEM, Automobiles	Manufacturing	1 100	3 000
3	TERNA	Italy	Montenegro	Coal, Oil and Natural Gas, Other electric power generation	Electricity	1 000	292
4	Hareon Solar Technology	China	Bosnia and Herzegovina	Alternative/Renewable energy, Solar electric power	Electricity	636	306
5	Great Wall Motors (GWM)	China	Russian Federation	Automotive OEM, Automobiles	Manufacturing	520	2 500
6	New Hope Group (NHG)	China	Russian Federation	Food & Tobacco, Animal food	Manufacturing	500	1 267
6	Dongfeng Motor	China	Russian Federation	Automotive OEM, Automobiles	Manufacturing	500	2 931
7	Weibo	China	The former Yugoslav Republic of Macedonia	Textiles, Textiles & Textile Mills	Manufacturing	400	4 500
8	IKEA	Sweden	Serbia	Consumer Products, Furniture, homeware & related products	Retail	373	2 789
9	EVN	Austria	Russian Federation	Chemicals, Basic chemicals	Manufacturing	343	785
10	Valorem	France	Ukraine	Alternative/Renewable energy, Wind electric power	Electricity	335	161

Source: UNCTAD, based on information from the Financial Times Ltd, fDi Markets (www.fdimarkets.com).

the Tula region with an estimated value of \$500 million. Although the presence of Indian investors is still small, it might strengthen. For example, in 2014, the Russia Direct Investment Fund and IDFC Ltd., India's leading financial services company, agreed to jointly invest in infrastructure projects worth \$1 billion.

Developed-country MNEs continued their divestments in 2014, selling their assets to either domestic or foreign investors. For example, ENI Spa (Italy) sold 60 per cent of Artic Russia BV – an oil and gas exploration and production company – to OOO Yamal Razvitiye (Russia Federation), for \$3 billion; while AO Samruk-Energo, a wholly owned subsidiary of Kazakhstan's State-owned AO Fond Natsionalnogo Blagosostoyaniya Samruk-Kazyna, acquired the remaining 50 per cent in TOO Ekibastuzskaya GRES-1, an electric utility company, from Kazakhmys PLC (United Kingdom), for \$1.25 billion.

FDI outflows fell by 31 per cent to \$63 billion. Natural-resources-based MNEs, mainly from the Russian Federation, reduced their investment abroad in the face of constraints in international financial markets (see below), low commodity prices and strong depreciation of the rouble. Almost 60 per cent of outflows from the Russian Federation went to Cyprus, Switzerland, the Netherlands and Bermuda.

FDI to and from transition economies is expected to decline further in 2015 owing to the continued economic recession and low oil prices. The GDP of the Russian Federation is expected to experience negative growth in 2015 – a 3 per cent contraction, according to latest estimates (United Nations, 2015).

The impact of sanctions on FDI in transition economies of the CIS

Since March 2014, a number of countries have implemented a series of sanctions against the Russian Federation. Coupled with the strong depreciation of the rouble and other macroeconomic factors, these sanctions began affecting inward and outward FDI in the second half of 2014, an effect that is expected to continue in 2015.

Direct impact on FDI inflows. In the last 10 years, annual FDI inflows to the Russian Federation grew almost five-fold, from \$15 billion in 2004 to \$69 billion in 2013, before they fell dramatically in 2014. Driven by high expected rates of return, foreign MNEs increased

their investments in energy and natural-resources-related projects. Foreign investors have entered the Russian energy market mainly through two channels: asset swaps and technology provision deals. Oil and gas firms of the Russian Federation were allowed to enter downstream markets in developed countries in exchange for allowing MNEs from those countries to take minority participations in those firms' domestic exploration and extraction projects. For example, Wintershall (Germany) acquired a stake in the Yuzhno-Russkoye gas field in Siberia, and Eni (Italy) gained access to exploration and production facilities in the Russian Federation. In return, Gazprom (Russian Federation) acquired parts of those companies' European assets in hydrocarbons transportation, storage and distribution. In some oil and gas projects that require high technology, such as the development of the Shtokman field, the involvement of developed-country MNEs such as StatoilHydro (Norway) and Total (France) was necessary because of their expertise.

After a period of growth, FDI in natural-resources-related industries has come to a standstill. Sanctions have had an impact on both channels. For example, in November 2014, BASF (Germany) and Gazprom (Russian Federation) agreed to scrap a \$14.7 billion asset swap that would have given Gazprom full control of a jointly operated European gas trading and storage business, including the biggest underground gas storage facility in Europe. In return, BASF's Wintershall affiliate was set to gain stakes in two west Siberian gas fields.²⁹ The oil industry was also affected by a ban on the exports of a wide range of goods, services and technology to Russian oil projects, in particular those in Arctic, deep-water and shale areas. The enormous Siberian oilfields developed in Soviet times are ageing, and without the development of new resources – from the Arctic to Siberia – Russian oil production could fall. Some foreign affiliates have already begun to hold back in some projects in the Arctic. For example, ExxonMobil (United States) had to freeze all 10 of its joint ventures with Rosneft in this region, including the Kara Sea project. Similarly, a Shell (United States) joint project with Gazprom Neft for the development of the Bazhenov field had to be suspended, as did the Total (France) project with Lukoil.

Indirect impact on FDI inflows. The Russian economy has suffered from the sanctions in three ways: (i) massive capital outflows, which have made

the foreign exchange market more volatile and caused a significant depreciation of the rouble; (ii) restricted access to international financial markets for some Russian banks and firms, making external borrowing very expensive for others; and (iii) the low confidence of domestic businesses and consumers in future growth prospects reducing consumption and investment (World Bank, 2015).

In the last 10 years, foreign investors in the Russian Federation responded positively to the country's fast-growing consumer market and the liberalization of selected industries. Rising market opportunities and improvements in the business environment resulted in a sharp increase in cross-border M&A sales of firms in the country's manufacturing industries. Although the presence of foreign affiliates does not dominate the Russian economy, those in several key industries, such as the automotive, beverages and tobacco, and power generation industries, have become important in recent years.³⁰

In the automotive industry in recent years, leading international car manufacturers such as Renault, Volkswagen, Toyota and General Motors have established production facilities in the Russian Federation, prompted also by the country's industrial assembly policy, which allows for zero customs duties on a long list of auto parts. However, as consumer confidence declined and the falling value of the rouble raised the prices of imports and components in the first eight months of 2014, there was a significant drop in automotive sales in the Russian Federation.

As a result, some foreign automotive companies are cutting their production in the country (e.g. Volkswagen will reduce its production in Kaluga), while others will divest. General Motors announced its withdrawal from the Russian Federation by December 2015, with production in St. Petersburg ceasing in the middle of the year. The contract for manufacturing Chevrolet vehicles held by Russian car manufacturer GAZ will also end. Some other companies continue to maintain confidence in the country despite declines in sales. Ford Motor (United States), for example, took control of its Russian joint venture, Ford-Sollers, providing it with additional financial support.³¹

Foreign firms are reassessing their position in the market. In the beverages and tobacco industry, large soft-drink MNEs PepsiCo (United States) and

Coca-Cola Hellenic (Greece), which control a large share of the juice market in the Russian Federation, have announced plans to halt production at key plants. PepsiCo will close a fruit juice plant in the Ramenskoye; Coca-Cola Hellenic has already closed its plant in Nizhny Novgorod.³² Carlsberg (Denmark), the world's fourth-largest brewer, will close 2 of its 10 breweries in the country.³³ As examples of slumps in other market-seeking industries, German retailer Metro has postponed a listing of its Russian unit on the London stock exchange, while in December 2014 the blue-chip health care company Fresenius (Germany) cancelled a planned pharmaceutical joint venture with a Russian partner.

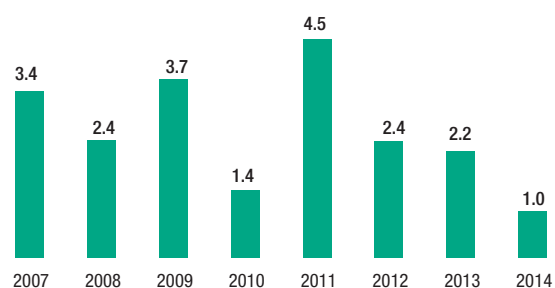
Impact on FDI outflows. Russian State-owned and privately owned firms participated in outward investment, ensuring their control over the value chains of their products in natural resources (metals, oil and gas) and services (telecommunications, banking). The most important destinations for this outward FDI are Europe – accounting for over one quarter of the total (*WIR14*) – and the United States. The interests of Russian MNEs may be affected, e.g. through the reviewing of cross-border M&As.

In addition, as the amounts involved in large international transactions require the active participation of banks and other financial institutions, the sanctions are intensifying difficulties already faced by Russian companies following the onset of the financial crisis. Sanctions against State-controlled banks such as VTB, Sberbank, Gazprombank and Vnesheconobank, as well as other big financiers of Russian MNEs investing abroad, represent one of the biggest threats to Russian investment abroad. The sanctions make it harder for those banks to raise equity and to borrow in developed countries.

In other transition economies of the former Soviet countries in Central Asia, the current sanctions also had an impact on FDI as Russian investors – among the largest investors in the region – began to reduce their presence (figure II.14). For example, in Kyrgyzstan, Russian energy giant Inter RAO is having difficulties financing the Kambarata-1 hydro project, while State oil company Rosneft could not take over the Manas International Airport and its affiliates. As the transition economies of Central Asia are economically closely linked to the Russian Federation, the sanctions will affect their economies as well. Tajikistan may face the

Figure II.14.

**FDI outflows from
Russian Federation to
CIS countries, 2007–2014**
(Billions of dollars)



Source: UNCTAD, FDI/MNE database (www.unctad.org/fdistatistics).

Note: Data for 2014 are estimated on the basis of the first three quarters of 2014.

most severe and direct consequences of a Russian economic slowdown, as 47 per cent of its GDP come from remittances by migrant workers in the Russian Federation. Such a slowdown may affect FDI inflows negatively in an indirect way.

DEVELOPED COUNTRIES

FDI inflows, top 5 host economies, 2014

(Value and change)

2014 Inflows

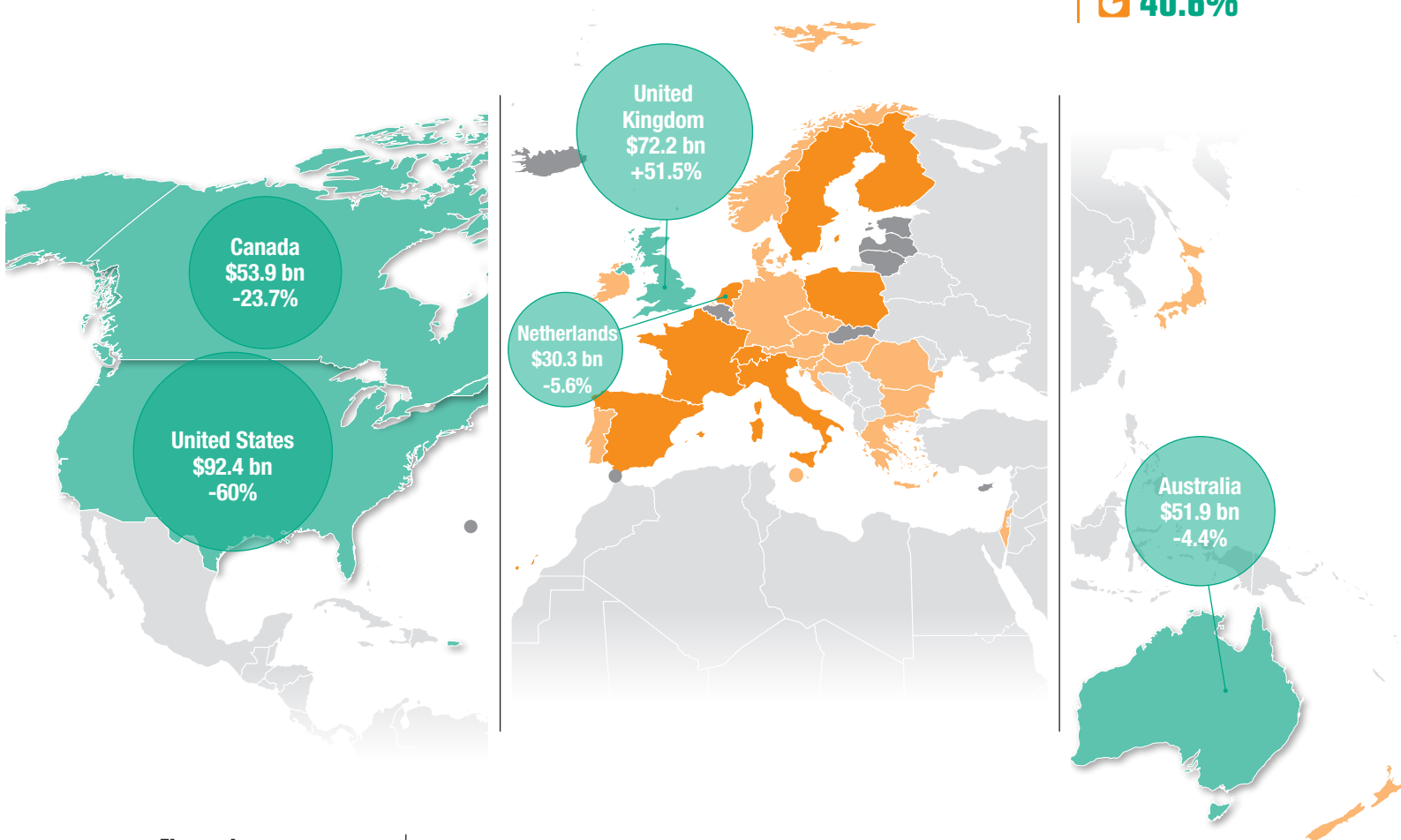
\$ 498.8 bn

2014 Decrease

-28.4%

Share in world

40.6%



Flows, by range

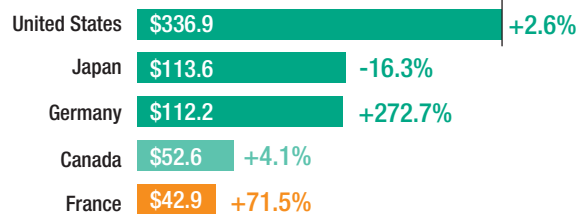
- Above \$100 bn
- \$50 to \$99 bn
- \$10 to \$49 bn
- \$1 to \$9 bn
- Below \$1 bn

Top 5 host economies

- Economy
- \$ Value of inflows
- 2014 % Change

Outflows: top 5 home economies

(Billions of dollars, and 2014 growth)



United States and Japan: Current account balance, 2006 and 2013 (Billions of dollars)

Current account items	United States		Japan	
	2006	2013	2006	2013
Balance on goods	-837	-702	95	-90
Balance on services	76	231	-32	-36
Balance on primary income	43	200	122	176
Primary income receipts	693	780	172	233
Investment income on FDI	333	467	41	79
Primary income payments	650	580	50	57
Investment income on FDI	159	176	11	17
Balance on current account	-807	-400	175	40

Source: UNCTAD.

Note: The boundaries and names shown and the designations used on this map do not imply official endorsement or acceptance by the United Nations.

HIGHLIGHTS

- Inflows fell for third year, outflows held steady
- Key factors: an exceptional divestment, rapid changes in intracompany loans
- MNE operations: growing impact on balance of payments

Figure A.

FDI inflows, 2008–2014
(Billions of dollars)

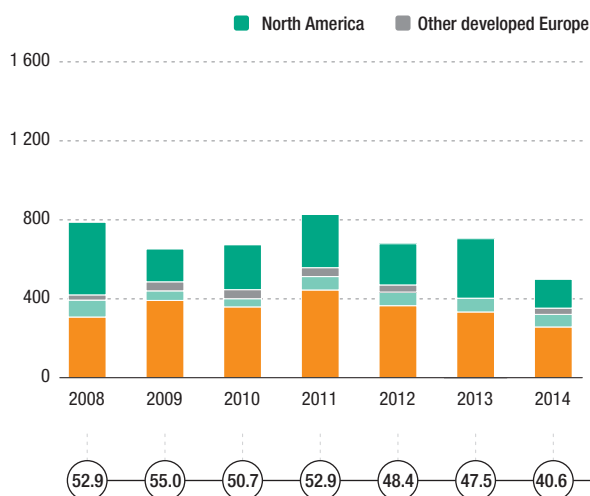


Figure B.

FDI outflows, 2008–2014
(Billions of dollars)

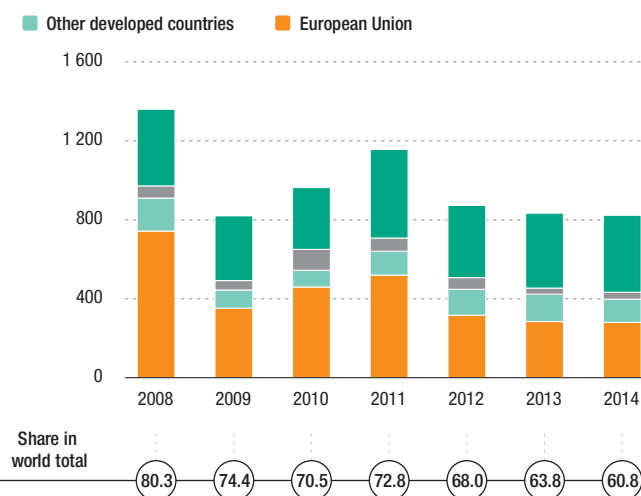


Table A.

Announced greenfield FDI projects by industry, 2013–2014 (Millions of dollars)

Sector/industry	Developed countries as destination		Developed countries as investors	
	2013	2014	2013	2014
Total	225 555	222 378	479 064	481 443
Primary	1 700	1 920	18 848	35 543
Mining, quarrying and petroleum	1 696	1 920	16 258	35 543
Manufacturing	98 034	100 445	207 972	218 396
Textiles, clothing and leather	13 785	17 402	18 835	22 057
Coke, petroleum products and nuclear fuel	2 115	5 311	6 538	25 767
Chemicals and chemical products	16 346	14 818	33 632	32 207
Motor vehicles and other transport equipment	18 319	21 871	54 474	60 145
Services	125 820	120 013	252 245	227 505
Electricity, gas and water	25 817	16 660	69 638	48 563
Construction	13 120	20 225	20 167	25 233
Transport, storage and communications	19 039	17 706	42 703	44 710
Business services	35 489	35 801	58 921	55 159

Table B.

Announced greenfield FDI projects by region/country, 2013–2014 (Millions of dollars)

Partner region/economy	Developed countries as destination		Developed countries as investors	
	2013	2014	2013	2014
World	225 555	222 378	479 064	481 443
Developed economies	192 338	181 085	192 338	181 085
Europe	116 954	106 572	110 253	100 049
North America	57 182	54 654	60 107	61 161
Other developed countries	18 201	19 859	21 978	19 875
Japan	11 472	12 732	8 296	5 995
Developing economies	30 952	39 664	265 812	287 822
Africa	2 742	1 112	28 010	63 024
Asia and Oceania	26 671	36 792	155 815	153 631
China	10 919	19 655	53 469	47 051
India	3 557	2 728	14 511	17 919
Latin America and the Caribbean	1 539	1 760	81 987	71 167
Transition economies	2 266	1 630	20 914	12 537

Table C.

Cross-border M&As by industry, 2013–2014 (Millions of dollars)

Sector/industry	Sales		Purchases	
	2013	2014	2013	2014
Total	237 516	274 549	178 870	228 389
Primary	39 337	27 842	-14 302	-920
Mining, quarrying and petroleum	37 897	25 975	-14 553	-1 178
Manufacturing	84 807	152 185	80 051	128 229
Food, beverages and tobacco	19 708	30 534	25 278	34 340
Chemicals and chemical products	19 232	23 611	4 822	25 172
Pharmaceuticals, medicinal chemicals and botanical products	742	44 058	20 443	45 165
Computer, electronic, optical products and electrical equipment	10 753	24 247	11 808	14 877
Services	113 373	94 522	113 121	101 081
Trade	7 406	28 483	-2 067	23 551
Information and communication	29 273	-73 170	22 476	-87 172
Financial and insurance activities	9 077	29 728	64 197	100 908
Business services	35 799	65 929	22 220	28 260

Table D.

Cross-border M&As by region/country, 2013–2014 (Millions of dollars)

Region/country	Sales		Purchases	
	2013	2014	2013	2014
World	237 516	274 549	178 870	228 389
Developed economies	165 726	201 150	165 726	201 150
Europe	35 455	24 853	112 622	169 943
North America	84 976	125 234	40 618	13 485
Other developed countries	45 296	51 063	12 487	17 722
Japan	44 872	37 906	2 576	3 947
Developing economies	62 869	58 789	20 335	25 703
Africa	2 288	1 670	-8 953	-8 317
Asia and Oceania	55 463	48 988	9 609	16 072
China	37 405	24 353	6 201	2 385
India	1 883	-880	3 346	5 327
Latin America and the Caribbean	5 118	8 131	19 678	17 949
Transition economies	1 682	-251	-7 191	1 536

FDI inflows to developed countries contracted for the third successive year, falling by 28 per cent to \$499 billion, the lowest level since 2004. Inflows declined in 24 of the 39 developed economies. Outflows from developed economies held steady at \$823 billion. Across individual economies, FDI flows fluctuated widely from year to year as MNEs actively engaged in M&As, acquiring as well as disposing of assets. Against the backdrop of a global savings glut – including saving by MNEs – intracompany loans continued to have major impacts, adding to volatility.

Europe was host to inflows worth \$289 billion (down 11 per cent from 2013) accounting for 24 per cent of the world total in 2014. Inflows fell in 18 European economies, including major recipients in 2013 such as Belgium, France and Ireland. In contrast, some of the European countries that made the largest gains in 2014 were those that had received negative inflows in 2013, such as Finland and Switzerland. FDI to the United Kingdom jumped to \$72 billion, leaving it in its position as the largest recipient country in Europe. Inflows to North America halved to \$146 billion, mostly due to an exceptional M&A divestment. The share of North America in global FDI flows was reduced to 12 per cent (compared with 21 per cent in 2013). Inflows to the United States decreased to \$92.4 billion, mainly due to one large divestment (Vodafone-Verizon). However, the United States remained the largest host developed country. In Asia-Pacific, FDI flows to Australia and Japan contracted, while those to New Zealand rebounded.

Outflows from European countries were virtually unchanged at \$316 billion, or 23 per cent of the global total. Reflecting the highly volatile trends at the level of individual economies, Germany almost trebled its outflows, becoming the largest direct investor country in Europe in 2014. France also increased its outflows sharply, to \$43 billion. In contrast, FDI from other major investor countries in Europe plummeted; FDI from the Netherlands (the largest European investor country in 2013) lost 28 per cent, and flows from Luxembourg (the second largest in 2013) fell to a negative value. United Kingdom outflows fell to -\$60 billion (largely owing to the mirror effect of the Vodafone-Verizon divestment). In North America, both Canada and the United States increased their outflows modestly. FDI from Japan declined by 16 per cent, ending a three-year run of expansion.

Upturn in M&A activities, including divestments.

Cross-border M&As reflected a general upturn in global M&As, rising to a gross value of \$1.2 trillion, of which \$911 billion was targeted at assets in developed countries. Health care industries (e.g. pharmaceutical, chemical) and the telecommunications industry were particularly active, with the former contributing to the large increase in M&A purchases by German firms. The latter raised M&A sales in France.

However, increased cross-border M&A activity was partially offset by significant divestments. The Vodafone-Verizon deal pushed divestments in the United States by foreign MNEs to \$176 billion in 2014, more than double the average during 2011–2013 of \$68 billion.

Effects of volatile intracompany loans. Some of the largest swings in FDI flows in 2014 were caused by rapid changes in the volume or even direction of intracompany loans. A reversal in intracompany loans from \$8 billion to -\$28 billion accounts for the large decline of inflows to Germany (table II.9). A similar reversal in intracompany loans to Ireland reduced total inflows to just \$7.7 billion (compared with \$37 billion in 2013). By contrast, a large increase in intracompany loans boosted inflows to the United Kingdom.

Changes in intracompany loans also played a major role in the huge increase in outflows from Germany. Over the period 2011–2013, intracompany loans from affiliates of German MNEs abroad back to their parent companies averaged \$31 billion, in effect suppressing German outward FDI. Loans back to parent companies diminished to \$3.8 billion in 2014. Although loans from German parent companies to their affiliates also decreased (from \$22 billion in

Table II.9.

Intracompany loans, selected European countries, 2013 and 2014 (Billions of dollars)

	2013	2014
Inward		
Germany	8.2	-28.1
Ireland	4.3	-24.9
United Kingdom	-3.9	32.6
Outward		
Germany	-15.3	19.0
Luxembourg	47.0	0.2
United Kingdom	1.9	44.4

Source: UNCTAD, FDI/MNE database (www.unctad.org/fdistatistics).

2013 to \$15 billion), the combined effect led to a rise in intracompany loans to \$19 billion (table II.9). Changes of similar magnitudes were observed in Luxembourg and the United Kingdom.

Resilience of natural-resource-related FDI.

Although weaker commodity markets have had some influence on FDI to resource-rich countries, natural resources MNEs have generally maintained their investment plans. For instance, inflows to Australia declined for the third successive year to \$52 billion. However, foreign MNEs remain extensively involved in oil and gas projects, including 12 of the 13 oil and gas projects at the “committed stage”, with a combined value of \$177 billion (A\$197 billion).³⁴ In Canada, flows into the energy and mining sector in 2014 were worth \$13 billion, down from \$21 billion in 2013 but still substantial, considering that the average for 2010–2012 was \$11 billion. Canadian outward FDI in this sector bounced back from –\$2.5 billion in 2013 to \$6.5 billion. Acquisitions of assets by Canadian MNEs contributed to the rise; an example is Encana’s bid for the United States oil and gas production and exploration company Athlon Energy for \$6.8 billion.

Mixed picture in flows from developed to developing economies.³⁵

FDI from the United States to developing regions increased by 8 per cent to \$110 billion. If those economies are excluded, United States FDI to developing regions was \$52 billion, up 5 per cent from the year before. United States FDI to Africa almost doubled, to \$5.4 billion, the highest level since 2010. FDI to developing economies in Asia and the Pacific (excluding Singapore) increased by 32 per cent to \$25 billion. In contrast, Japanese FDI to developing regions (excluding offshore financial centres) declined by 15 per cent to \$39 billion.³⁶ FDI from Japan to developing Asia also lost ground, declining by 24 per cent to \$28 billion. In contrast, Japanese FDI to Africa rose to \$4.5 billion, a record high.

FDI data from the United States and Japan appear to contradict trends in M&As, which show that developed-country MNEs continued to divest assets in Africa (from –\$3.8 billion in 2013 to –\$8.3 billion in 2014). However, M&A data for Africa are often skewed by a few large deals. The large value of divestment in 2014 was accounted for mostly by just three M&A transactions: Vivendi’s sale of its majority stake in the telecommunications services provider Itissalat (Morocco) for \$5.7 billion; the sale of Nigerian assets

by ConocoPhillips for \$1.79 billion; and the sale of a stake in Tanzanian gas fields by Ophir Energy (United Kingdom) for \$1.3 billion. These divestments do not signal diminishing interest in Africa among MNEs. Announcement-based data suggest that greenfield projects by developed-country MNEs in Africa are on the rise, with the total value of such projects announced in 2014 rising to \$63 billion, the highest level since 2008.

The growing impact of MNE operations on the balance of payments of the United States and Japan

Global FDI and international production by MNEs has generally grown faster than GDP or international trade. Consequently, the impact of MNE operations on the balance of payments has increased, not only through FDI flows (on the financial account), but also through trade and investment income (on the current account). Data for the United States and Japan show that outward FDI creates avenues for exports of knowledge-intensive services. Growing investment income from outward FDI also has the effect of counterbalancing trade deficits (table II.10).

United States

In the early 2000s, the current account deficit of the United States began to grow, driven by trade in goods. By 2006, it had reached 5.8 per cent of GDP, raising concerns over its sustainability. Since then, the growing surplus in services trade and primary income³⁷ has helped narrow the current account deficit; in 2014, it was down to 2.4 per cent of GDP.

Table II.10.

**United States and Japan:
Current account balance,
2006 and 2013**
(Billions of dollars)

Current account items	United States		Japan	
	2006	2013	2006	2013
Balance on goods	-837	-702	95	-90
Balance on services	76	231	-32	-36
Balance on primary income	43	200	122	176
Primary income receipts	693	780	172	233
Investment income on FDI	333	467	41	79
Primary income payments	650	580	50	57
Investment income on FDI	159	176	11	17
Balance on current account	-807	-400	175	40

Source: UNCTAD, based on data from the United States Department of Commerce, Bureau of Economic Analysis, and Japan’s Ministry of Finance.

Intra-firm trade of United States MNEs (i.e. trade between a parent company and foreign affiliates) contributed to the overall deficit in goods and the surplus in services (table II.11). Intra-firm trade in goods is a relatively small part of the overall deficit, although its share has grown in recent years. In services, intra-firm trade accounted for 22 per cent of total United States exports in 2012. Half (\$73 billion) of intra-firm services exports were charges for the use of intellectual property, such as industry process and computer software, which suggests the knowledge-intensive nature of intra-firm trade in services.

	Intra-firm trade of United States MNEs, 2012 (Billions of dollars)		
	Exports (parent to affiliates)	Imports (affiliates to parent)	Balance
Goods	278	331	-53
Services	144	73	71

Source: UNCTAD, based on data from the United States Department of Commerce, Bureau of Economic Analysis.

Though significant, the value of exports by the parent companies of United States MNEs are dwarfed by the value of goods and services supplied by their foreign affiliates (figure II.15). Total sales of foreign affiliates are many times the value of all United States exports. FDI is clearly a more significant modality for United States firms to reach foreign markets.

As foreign affiliates are likely to use some inputs imported from the United States, a part of their revenues will find its way to the United States balance of payments in the form of exports of goods and services to foreign affiliates of United States MNEs. Another route is through investment income.

FDI income receipts amounted to \$474 billion in 2014, a multiple of the deficit in intra-firm trade in goods. In comparison, investment income payments (earnings of foreign affiliates in the United States) amounted to \$178 billion. Thus, investment income on FDI is an important factor offsetting the deficit in trade in goods.

A peculiar aspect of the United States investment income balance is that it remains in surplus despite the net negative investment position of the United States. At the end of 2014, the value of foreign investment

(FDI, as well as portfolio and “other”³⁸ investment) in the United States (liabilities for the United States) exceeded that of United States investment abroad (United States assets) by \$6.9 trillion. Yet investment income receipts exceeded payments by \$227 billion. Recent research suggests that FDI is primarily responsible for this phenomenon and highlights the role of intangible assets and taxation (box II.4).

Japan

Since 2011, Japan’s current account surplus has diminished rapidly, primarily owing to increased energy imports. A longer-term trend is the slowdown of Japanese exports, due to the relocation of the Japanese manufacturing base. Since the 1980s, Japanese manufacturing MNEs have invested extensively in low-cost export locations, as well as in developed countries, in industries where proximity to markets matters.

Increased overseas production has partly replaced exports from Japan. In recent years, Japanese merchandise exports have stagnated as sales by foreign affiliates of Japanese manufacturing MNEs

Figure II.15. United States MNEs: Goods and services exported by parent companies and supplied by majority-owned foreign affiliates, 2012
(Trillions of dollars)



Source: UNCTAD, based on data from the United States Department of Commerce, Bureau of Economic Analysis.

Note: Goods and services exported by parent companies refer only to intra-firm trade, which accounted for 38 per cent of total exports of goods by parent companies in the United States in 2012. Goods and services supplied by foreign affiliates exclude those exported back to the United States.

Box II.4.

Why is United States outward FDI so profitable?

Despite maintaining a negative net international investment position since 1989, investment income that the United States receives from abroad has been consistently higher than the income foreign investors receive from their investment in the United States. The rates of return on United States assets abroad are higher (3.8 per cent on average over 1999–2014) than those earned by foreign investors in the United States (2.7 per cent).

Recent studies find that this difference in returns is due to income on FDI. The returns on other types of assets were similar for United States assets abroad and foreign-owned assets in the United States; if anything, returns on foreign-owned assets were slightly higher. In contrast, returns for FDI were, on average, 7.0 per cent for United States outward FDI and 3.1 per cent for inward FDI.

Common explanations for this phenomenon include the higher risks associated with investing outside the United States, and the age of investments. Recent studies suggest that intangible assets and the treatment of taxes on the balance of payments can explain large parts of the return differentials (Curcuru et al., 2013; Bridgman, 2014).

Investment in intangible assets (e.g. R&D activities) can be a source of the returns gap by, first, depressing the profitability of inward FDI in the United States and, second, understating the value of United States outward FDI.

The United States is a prime location for R&D because of its infrastructure, its networks of scientists and its accounting rules, which allow investments in R&D to be deducted as expenses. This causes R&D activities to reduce the apparent profitability of foreign affiliates in the United States. In fact, R&D expenditures of foreign affiliates in the United States are high relative to sales (box table II.4.1).

Box table II.4.1.

United States MNEs: R&D expenditures, sales and net income of foreign affiliates, average over 2009–2012 (Billions of dollars)

	Foreign affiliates in the United States	Affiliates of United States MNEs abroad
R&D expenditures	49	42
Sales	3 665	6 396
Net income	113	1 098

Source: UNCTAD, based on data from the United States Department of Commerce, Bureau of Economic Analysis.

Furthermore, for parent companies of United States MNEs, the share of R&D expenditures in total fixed investment for 2009–2012 was 30 per cent.³⁹ The operations of United States MNEs abroad are likely to benefit from intangible assets created at home. Thus, the outward FDI stock of the United States could underestimate the true extent of its assets, resulting in artificially higher rates of returns for United States businesses abroad.

Another factor explaining the rate differentials is the tax system. The United States applies a worldwide taxation system in which the parent company in the United States is also liable for taxes on the income of its affiliates abroad. Taxes paid abroad by affiliates are deducted from the total tax liabilities. Since the United States corporate income tax rate is higher than in many other countries, the parent company in the United States needs to pay the difference when the profits abroad are repatriated. This repatriation tax does not appear on the balance of payments. Investment income on United States direct investment abroad reported in the balance of payments is net of foreign taxes, but the United States taxes that the parent company would have to pay are not deducted. In contrast, the United States taxes are already deducted from the earnings of foreign affiliates in the United States. Effectively, investment income on United States direct investment abroad is pre-tax (or partially taxed) income, whereas investment income on FDI in the United States is after-tax income, giving rise to the seemingly higher earnings of outward FDI of the United States.

Curcuru et al. (2013) argue that the effects of such tax issues add up to 1.8 per cent to annual returns on United States outward FDI. Bridgeman (2014) concludes that taking into account intangible assets and repatriation taxes reduces the difference in returns on FDI from 4.2 per cent to 1.7 per cent for the period 1994–2010.

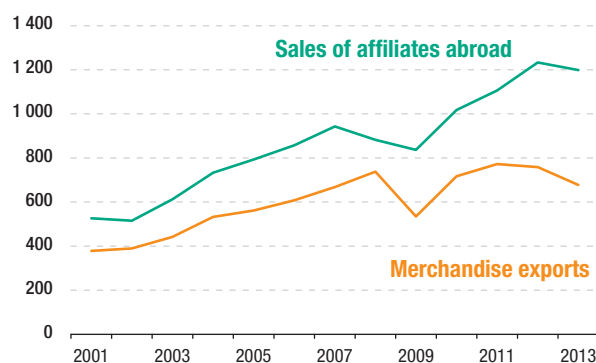
Source: UNCTAD, based on various sources.

grew substantially (figure II.16). In 2014, Japanese auto manufacturers' overseas production increased by 4.3 per cent over 2013 while their exports from Japan declined by 4.5 per cent.⁴⁰ Furthermore, Japanese manufacturers' overseas production bases are also serving the Japanese market, as seen from the gradual increase in their exports to Japan (figure II.17). Thus, the internationalization of Japanese MNEs' production system has, to an extent, negatively affected Japan's trade balance.

However, the internationalization of Japanese MNEs is also positively contributing to the current account. First, foreign production does not always substitute domestic production but may also complement it. The proliferation of global value chains means that increased foreign production often requires more inputs from the home country. According to Japanese survey data, almost 60 per cent of exports by Japanese parent companies are destined for their foreign affiliates (figure II.17). Foreign affiliates of Japanese MNEs are importing more from Japan than they export to the country, although the share of locally procured inputs has been rising gradually in recent years. Second, despite the trade deficit, the current account remained in surplus due to growing investment income. In gross terms, investment income receipts in 2013 amounted to \$233 billion, 34 per cent of which were returns on FDI. The share of FDI is relatively small but has been rising in recent years. Finally, royalty payments on intellectual property are adding to the positive current account balance. The balance of "charges for the use of intellectual property" up to 2003 was negative, but since then it has been in surplus, rising to \$14 billion in 2013. Of gross receipts worth \$32 billion, over 40 per cent come from royalties from foreign affiliates.

From the viewpoint of the current account balance, outward FDI can make positive contributions in the long run, as seen from the experience of the United States and Japan. Thus, short-term impacts, such as loss of export capacity, must be seen in the overall context of a longer time horizon.

Figure II.16. Merchandise exports of Japan and sales of foreign affiliates in manufacturing, 2001–2013 (Billions of dollars)



Source: UNCTAD, based on data from the Bank of Japan and Ministry of Economy, Trade and Industry.

Figure II.17. Japanese MNEs: Trade with Japan by foreign affiliates, 2001–2013 (Billions of dollars)



Source: UNCTAD, based on data from the Ministry of Economy, Trade and Industry.

B. TRENDS IN STRUCTURALLY WEAK, VULNERABLE AND SMALL ECONOMIES

LEAST DEVELOPED COUNTRIES

FDI inflows, top 5 host economies, 2014

(Value and change)

2014 Inflows

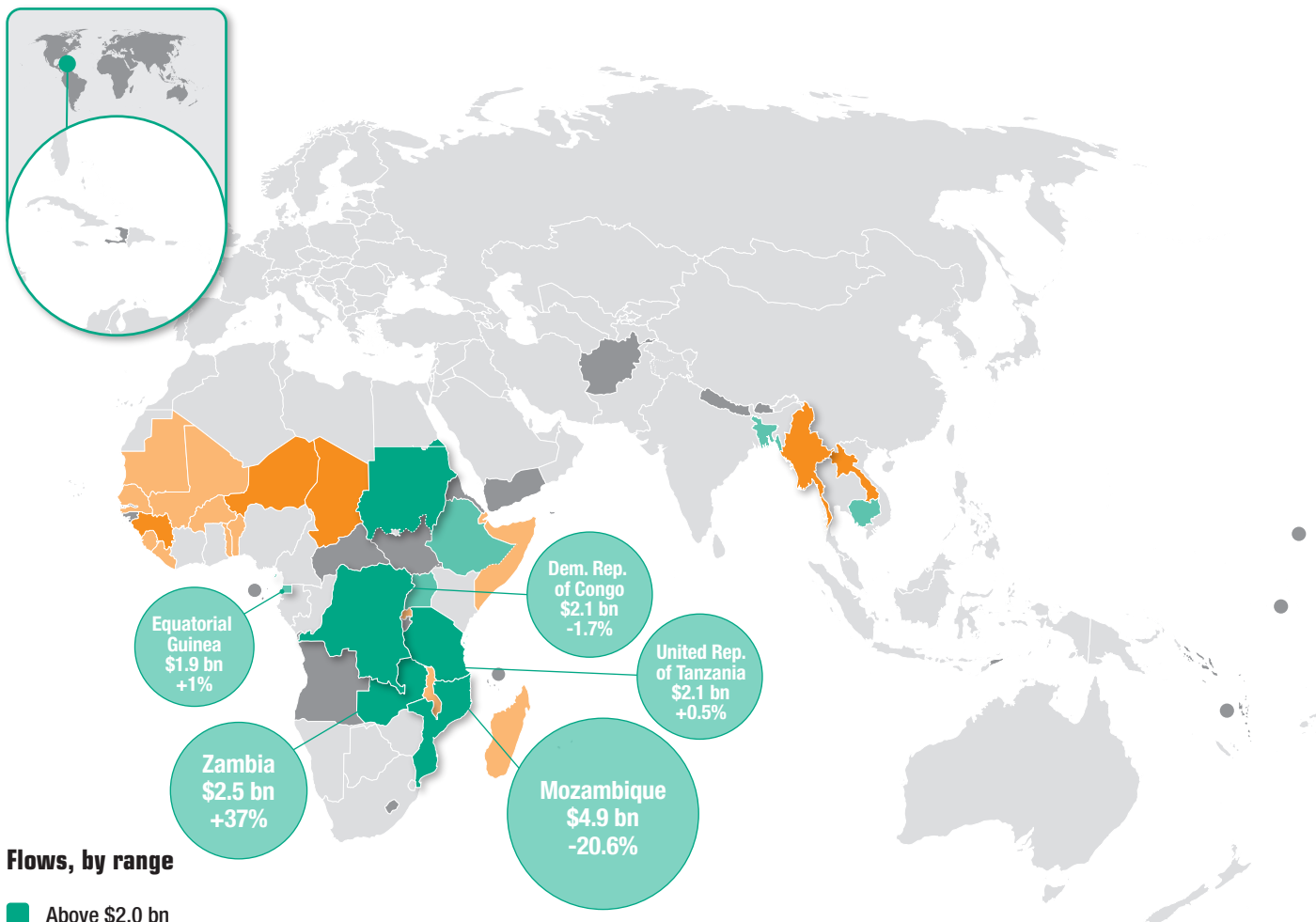
\$ 23.2 bn

2014 Increase

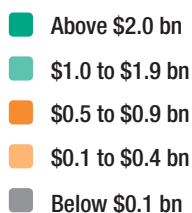
+4%

Share in world

1.9%



Flows, by range

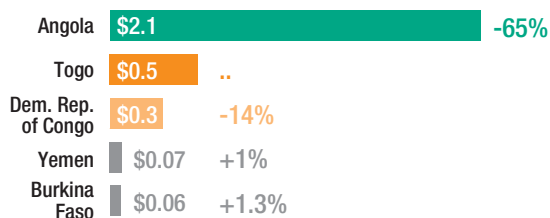


Top 5 host economies



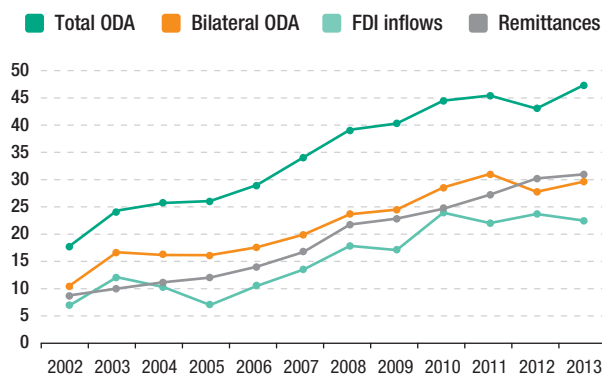
Outflows: top 5 home economies

(Billions of dollars, and 2014 growth)



FDI inflows, ODA flows and remittances to LDCs, 2002–2013

(Billions of dollars)



Source: UNCTAD.

Note: The boundaries and names shown and the designations used on this map do not imply official endorsement or acceptance by the United Nations. Final boundary between the Republic of Sudan and the Republic of South Sudan has not yet been determined. Final status of the Abyei area is not yet determined. Dotted line in Jammu and Kashmir represents approximately the Line of Control agreed upon by India and Pakistan. The final status of Jammu and Kashmir has not yet been agreed upon by the parties.

HIGHLIGHTS

- FDI stock tripled during 2004–2014
- FDI flows are just 2 per cent of global inflows, smaller than ODA and remittances
- FDI in manufacturing, services gravitates to larger, mineral-rich LDCs

Figure A.

FDI inflows, 2008–2014 (Billions of dollars)

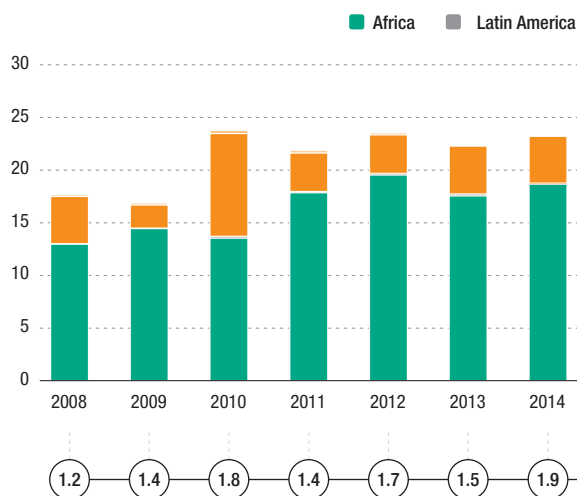


Figure B.

FDI outflows, 2008–2014 (Billions of dollars)

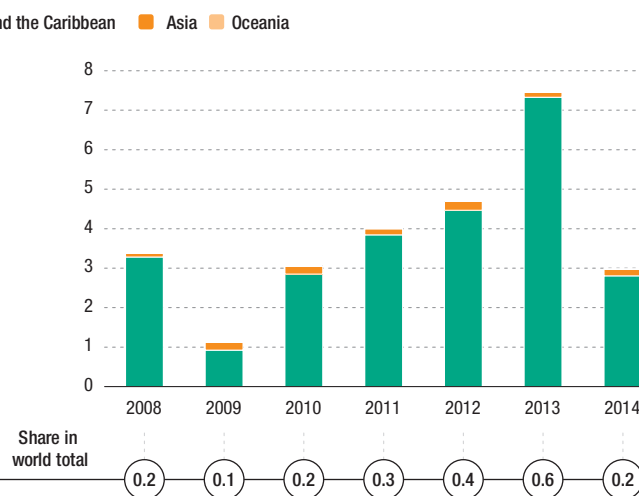


Table A.

Announced greenfield FDI projects by industry, 2013–2014 (Millions of dollars)

Sector/industry	LDCs as destination		LDCs as investors	
	2013	2014	2013	2014
Total	40 279	47 680	1 624	1 604
Primary	3 884	17 165	7	-
Mining, quarrying and petroleum	1 519	17 165	7	-
Manufacturing	8 407	9 578	395	294
Textiles, clothing and leather	519	2 019	-	38
Coke, petroleum products and nuclear fuel	1 764	1 246	-	-
Non-metallic mineral products	3 234	1 952	262	-
Services	27 988	20 937	1 222	1 311
Construction	590	6 802	-	-
Trade	833	2 138	-	4
Transport, storage and communications	5 092	3 500	92	15
Finance	2 086	2 198	691	639
Business services	1 213	4 814	37	624

Table B.

Announced greenfield FDI projects by region/country, 2013–2014 (Millions of dollars)

Partner region/economy	LDCs as destination		LDCs as investors	
	2013	2014	2013	2014
World	40 279	47 680	1 624	1 604
Developed economies	25 448	32 429	123	76
European Union	7 000	24 435	82	66
Switzerland	411	1 701	-	-
United States	1 205	4 507	-	10
Japan	11 484	1 269	-	-
Developing economies	14 831	15 251	1 464	1 508
Africa	6 073	6 477	1 049	1 045
South Africa	2 791	3 564	-	11
Latin America and the Caribbean	170	69	9	281
South, East and South-East Asia	8 020	8 162	354	168
West Asia	568	544	52	14
Transition economies	-	-	37	21

Table C.

Cross-border M&As by industry, 2013–2014 (Millions of dollars)

Sector/industry	Sales		Purchases	
	2013	2014	2013	2014
Total	26	3 734	2	23
Primary	16	2 661	2	2
Mining, quarrying and petroleum	16	2 661	2	2
Manufacturing	37	120	-	-
Food, beverages and tobacco	20	12	-	-
Textiles, clothing and leather	2	2	-	-
Pharmaceuticals, medicinal chemicals and botanical products	15	51	-	-
Non-metallic mineral products	-	56	-	-
Services	-27	952	-	20
Electricity, gas, water and waste management	-	-86	-	-
Transportation and storage	-	400	-	-
Information and communication	3	112	-	-
Financial and insurance activities	-42	516	-	25

Table D.

Cross-border M&As by region/country, 2013–2014 (Millions of dollars)

Region/country	Sales		Purchases	
	2013	2014	2013	2014
World	26	3 734	2	23
Developed economies	-4 020	-1 201	2	25
European Union	-4 409	-1 361	2	25
North America	-338	10	-	-
Other developed countries	-33	114	-	-
Developing economies	4 046	4 869	-	-2
Africa	5	-18	-	2
Latin America and the Caribbean	-430	400	-	-
South, East and South-East Asia	4 427	3 975	-	-4
India	15	2 702	-	-
Singapore	9	1 333	-	-
West Asia	44	512	-	-
Transition economies	-	-	-	-

FDI flows to LDCs rose by 4 per cent to \$23 billion in 2014, representing 2 per cent of global inflows. Both cross-border M&A sales and greenfield FDI projects were driven by large-scale projects in extractive industries. FDI flows in LDCs remain smaller than official development assistance (ODA) and remittances, but FDI stock has increased three-fold over the past 10 years. FDI can play a catalytic role in economic development, enhancing productive capacity and creating jobs and expertise. An integrated policy approach to investment promotion, coupled with international community support for greater inward investment, would help quadruple FDI stock in LDCs by 2030, including into the SDG sectors.

FDI inflows to LDCs rebounded in 2014. The top five recipients were Mozambique (\$4.9 billion, down 21 per cent), Zambia (\$2.5 billion, up 37 per cent), the United Republic of Tanzania (\$2.1 billion, up by 1 per cent), the Democratic Republic of the Congo (\$2.1 billion, down by 2 per cent) and Equatorial Guinea (\$1.9 billion, a gain of 1 per cent). These five countries accounted for 58 per cent of total FDI inflows to LDCs.

The share of LDCs in global inflows remained virtually unchanged from 2013 at 1.9 per cent. Among developing economies, the change in LDCs' share stayed close to its 2013 level at 3.4 per cent.

African LDCs registered a 6 per cent rise in FDI inflows from 2013 to 2014, owing to a substantial reduction in divestment in Angola. FDI inflows to a dozen recipients contracted, and robust gains were recorded in only two LDCs: Ethiopia (an increase of 26 per cent to \$1.2 billion) and Zambia (up 37 per cent to \$2.5 billion). The outbreak of Ebola may have had some impact on investment in West Africa (see the Africa section), where FDI inflows to LDCs shrank by 15 per cent. However, in two Ebola-affected countries, Guinea and Sierra Leone, FDI inflows more than tripled.

Asian LDCs saw a 2 per cent drop in FDI inflows, a negative growth for the first time in four years. This was mainly owing to declines in seven Asian LDCs, including Bangladesh (\$1.5 billion, a decrease of 5 per cent), Cambodia (\$1.7 billion, an 8 per cent fall), and Yemen (\$1 billion of divestment), despite strong FDI growth in the Lao People's Democratic Republic (69 per cent) and Myanmar (62 per cent). FDI inflows to Haiti faced a 50 per cent reduction. In Oceania,⁴¹ FDI inflows were down for the fourth consecutive year to

below \$3 million, a decline of 92 per cent. Continued divestment in Vanuatu further dampened already weakened FDI flows to this region.

Record (net) sales in cross-border M&As. The net value of cross-border M&A sales in LDCs jumped to \$3.7 billion in 2014, on the back of acquisitions by Asian investors in African LDCs. The value of assets in LDCs sold by developed-country MNEs to other foreign investors continued to rise, exceeding the value of their purchases in LDCs. Cross-border M&A sales in LDCs to investors from developing economies were driven by two oil and gas deals in Africa involving Asian State-owned MNEs. The largest, a \$2.6 billion deal in which India's State-owned Oil and Natural Gas Corporation Limited acquired a 10 per cent stake in an oil and gas exploration block in Mozambique, represented more than 70 per cent of net sales in all LDCs.

In financial services, Qatar National Bank, aspiring to become the largest bank in Africa and West Asia by 2017,⁴² acquired a 23.5 per cent stake in Ecobank Transnational (Togo), a deal that helped the industry register a record-high net sales value of \$0.5 billion in LDCs. Acquisitions initiated by developing-economy investors more than doubled the number of deals in financial and insurance activities (from 6 in 2013 to 13 in 2014).⁴³ A net sales value of \$0.4 billion in the transportation and storage industry was attributable to a single deal in Liberia, in which a Bahamas-based company acquired a 30 per cent stake in a provider of deep-sea freight transportation services.

Announced greenfield investment hit a six-year high. A \$16 billion oil and gas project in Angola (table II.12)⁴⁴ alone contributed more than a third of total greenfield investment announced for all LDCs in 2014 (\$48 billion, more than twice as much as total reported FDI inflows). The second largest project, announced by a Belgian investor (table II.12) pushed the value of LDCs' greenfield investment in construction to new heights. The third largest real estate project by a South African MNE (table II.12) helped South Africa rank as the largest source of greenfield investment in LDCs in 2014. Although the share of announced services sector investment tumbled from 69 per cent of the total in 2013⁴⁵ to 44 per cent in 2014, the value of services sector greenfield investment was the second highest on record.

In manufacturing, two industries saw a jump in announced greenfield investments. In textiles,

clothing and leather, 20 announced projects, with a combined value of over \$2 billion, propelled activity in this industry to a new high in 2014. Over \$1.8 billion of the investment (in 11 projects) went to Ethiopia, one of the beneficiary countries under the African Growth and Opportunity Act (AGOA), which confers preferential treatment on apparel exports to the United States. MNEs from Asia, in particular, are increasing their presence in Ethiopia. In 2014, two major projects targeted the country: an Indian company announced a \$550 million investment to construct Africa's largest plant to produce cotton yarn for export,⁴⁶ and a Chinese MNE announced another project to build a \$500 million textile plant by creating more than 20,000 jobs.⁴⁷ In non-metallic and mineral products, almost \$2 billion worth of greenfield FDI was recorded in 13 projects for the manufacture of cement and concrete products and targeted at a dozen LDCs. The largest of these projects (\$370 million with 1,500 new jobs to be created) will be built in the Lao People's Democratic Republic by Thai investors.

The value of FDI in LDCs remains concentrated in a small number of mineral-rich economies.

Despite weaker prices of key primary commodity exports, extractive industries in LDCs continue attracting foreign investors. Judging from announced FDI greenfield projects in 2014, the skewed distribution of FDI inflows among LDCs will continue for some time. Investment in extractive industries is reinforced by FDI in the manufacturing and services sectors (including infrastructure), which also tends to be drawn to larger, mineral-rich LDCs. The expected extension of AGOA for another 15 years may support more diversified FDI flows to LDCs, but it is unlikely to affect patterns of

FDI to nearly 30 eligible LDCs in Africa in the short run, considering the weight of crude oil exports to the United States under AGOA since 2000 (USITC, 2014).⁴⁸

Among Asian LDCs, Myanmar is expected to see further growth in FDI, with the implementation of announced projects commencing in various sectors and industries. In association with the development of the country's first special economic zone (SEZ), led by a Myanmar-Japanese joint venture,⁴⁹ 8 of 41 registered companies, of which 21 are Japanese MNEs, will start operations in 2015.⁵⁰ Greenfield activity from Japan to Myanmar suggests an increase in projects in the services sector, supporting Japanese manufacturers that are set to operate in the SEZ. Two other ASEAN LDCs (namely, Cambodia and the Lao People's Democratic Republic) will also benefit from enhanced infrastructural connectivity (see the East and South-East Asia section) and may be in a better position than other LDCs to attract export-oriented FDI and donor-funded large-scale infrastructure projects.⁵¹

The acceleration of existing regional integration efforts in Africa may also lead to more FDI and external funding for infrastructure development. Trends in announced greenfield investment suggest that some LDCs rich in natural resources (e.g. Mozambique, which is expected to become a major exporter of liquefied natural gas in the coming years) have started attracting market-seeking FDI projects in the services sector, alongside large-scale projects in the extractive industries and auxiliary infrastructure development (such as electricity, petroleum bulk stations and terminals).

Table II.12.

LDCs: Five largest greenfield investment projects announced in 2014

Host economy (destination)	Industry segment	Investing company	Home economy	Estimated capital expenditures (Millions of dollars)
Angola	Oil and gas extraction	Total	France	16 000 ^a
Mozambique	Commercial and institutional building construction	Pylos	Belgium	5 189 ^b
Mozambique	Real estate	Atterbury Property Developments	South Africa	2 595 ^c
Zambia	Building material, garden equipment and supplies dealers	Enviro Board	United States	2 078
Bangladesh	Natural, liquefied and compressed gas	Chevron Corporation	United States	1 048

Source: UNCTAD, based on information from the Financial Times Ltd, fDi Markets (www.fDimarkets.com).

^a Most likely product-sharing contract.

^b Sum of six projects for the same amount.

^c Sum of three projects for the same amount.

FDI trends in LDCs since the Monterrey Conference

FDI flows are an important external source of finance for LDCs. While ODA remains by far the largest external financial flow to LDCs, FDI has been on an upward trajectory since 2002 and is larger than other private flows (figures II.18 and II.19). Remittances also remain an important private external flow for this group of countries.

FDI flows to LDCs have outpaced portfolio investment for the entire period of 2002–2014; they also have been less volatile than “other investment” (mainly bank lending) (figure II.19).

FDI stock in LDCs tripled in the last decade (2004–2014). FDI inflows grew at an annual average rate of 11 per cent since the Monterrey Consensus (figure II.20). This rate of growth was similar to that for developing economies as a whole and well above the rate for the world (table II.13). At the subregional level, the bulk of FDI went to African LDCs, followed by Asian LDCs. Although FDI stock as a percentage of GDP is smaller for LDCs than for both developing countries and the world, FDI inflows represent a potentially greater contribution to GFCF.

The number of LDCs hosting inward stock of more than \$10 billion increased from one (Angola) in 2002 to seven

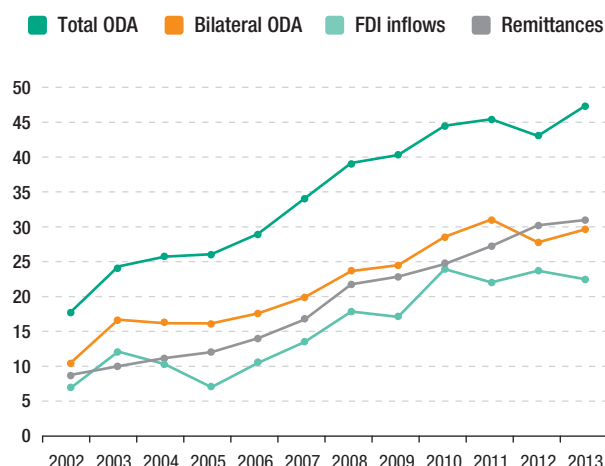
in 2014. The five largest recipients – Mozambique (\$26 billion), Sudan (\$23 billion), Myanmar (\$18 billion), and Equatorial Guinea and the United Republic of Tanzania (\$17 billion each) – hold 45 per cent of total inward FDI stock in all LDCs. This concentration of FDI in a small number of LDCs appears to be reinforced by the export specialization of these LDCs.⁵² Robust gains in FDI inflows have been seen in mineral-exporting LDCs since 2002. Mixed exporters have started attracting more FDI since 2010, again largely due to just two mineral-rich LDCs (Myanmar and the United Republic of Tanzania). Flows to fuel-exporting LDCs have dipped in recent years (especially in Angola and Yemen, which recorded negative inflows).

Some policy implications. An integrated policy approach is essential to ensure that FDI and other sources of finance – domestic and external – are deployed effectively to help LDCs advance their development objectives and goals. FDI, for instance, can complement domestic investment but will not replace it as the main driver of sustainable development and structural transformation (UNCTAD, 2014). Thus, to take advantage of FDI or links with MNEs and participate in global value chains, LDCs must build indigenous productive capacities through capital accumulation, skills development and innovation (UNCTAD, 2011).

To enhance productive capacities through FDI, UNCTAD produced a Plan of Action for Investment in LDCs for the fourth UN conference on the LDCs in Turkey in 2011. The plan called for an integrated policy approach to investment, capacity-building and enterprise development in the following five areas:

Figure II.18.

FDI inflows, ODA flows and remittances to LDCs, 2002–2013 (Billions of dollars)



Source: UNCTAD, FDI/MNE database (www.unctad.org/fdistatistics) (for FDI inflows), OECD (for ODA flows) and World Bank (for remittances).

Table II.13.

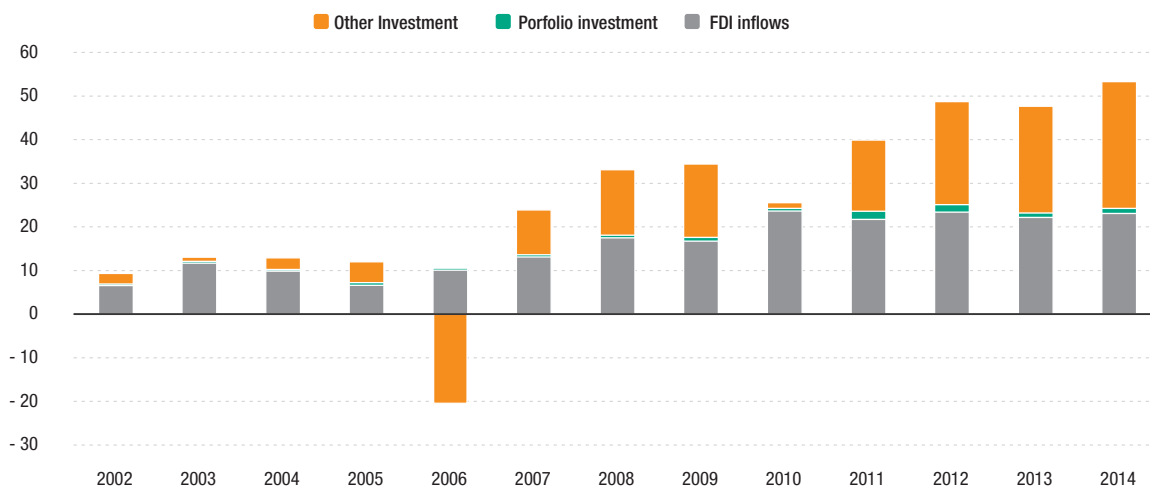
Selected FDI indicators, 2002–2014 (Per cent)

Indicator	LDCs	Developing economies	World
FDI inflows, annual growth	11	12	6
Inward FDI stock as % of GDP, 13-year average	22	26	27
FDI inflows as % of GFCF, 13-year average	13	10	9

Source: UNCTAD, FDI/MNE database (www.unctad.org/fdistatistics); World Bank for GDP and GFCF data.

Note: Annual growth computed as compound annual growth rate over the period considered. LDCs = least developed countries.

Figure II.19. LDCs: Private capital inflows by type, 2002–2014 (Billions of dollars)

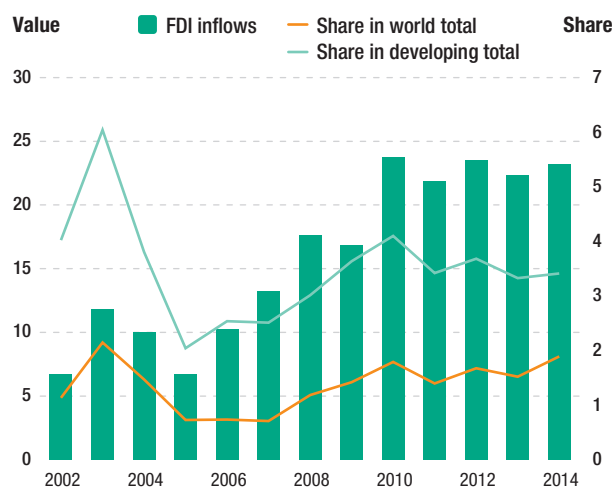


Source: UNCTAD, FDI/MNE database (www.unctad.org/fdistatistics) (for FDI inflows) and IMF (for portfolio and other investments).

- Strengthening public-private infrastructure development efforts.** Poor physical infrastructure constrains domestic and foreign investment and LDCs’ integration into the global economy. A new partnership for infrastructure development in LDCs is called for to address the problem.
- Boosting international development assistance for productive capacity.** A shortfall in “soft” infrastructure also presents a hurdle to attract foreign investors and develop productive capacities in LDCs. A partnership to build skills commensurate with productive capacity needs is critical.
- Enabling firms of all sizes to capture untapped business opportunities.** Large MNEs often bypass investment opportunities in LDCs, where markets are typically small and operating conditions are more challenging than in other countries. Efforts need to be stepped up to encourage small- and medium-scale international investors to tap into underexploited business opportunities and to promote the types of FDI that offer a good match with LDCs’ needs.
- Fostering local business and easing access to finance.** Foreign investors are typically attracted by countries where the local business sector is thriving, and they need a minimum level of local services and suppliers to operate. New initiatives

Figure II.20.

LDCs: FDI inflows and share in world and developing country inflows, 2002–2014
(Billions of dollars and per cent)



Source: UNCTAD, FDI/MNE database (www.unctad.org/fdistatistics).

to support local business and the development of linkages with MNEs are essential.

- Implementing a new wave of regulatory and institutional reforms.** While significant reforms of regulatory frameworks for investment have been carried out, much remains to be done in most

LDCs. A new wave of reforms should attempt to co-opt business as partners for development and emphasize aspects of regulations that could shape FDI impact and strengthen State institutions and public services (such as taxation and governance).

These efforts need support by the international community, including a viable programme to boost inward investment. To be effective, the programme would require elements such as multi-agency

technical assistance consortia, and partnerships between IPAs promoting inward investment in LDCs and IPAs of major investment home countries promoting outward investment (*WIR14*). The principal aims of the programme would be to deepen and spread investment within LDCs and across the group, especially in sectors pertinent to the sustainable development goals (SDGs). An overall target in pursuit of these aims would be to quadruple the stock of FDI in LDCs over the next 15 years.

LANDLOCKED DEVELOPING COUNTRIES

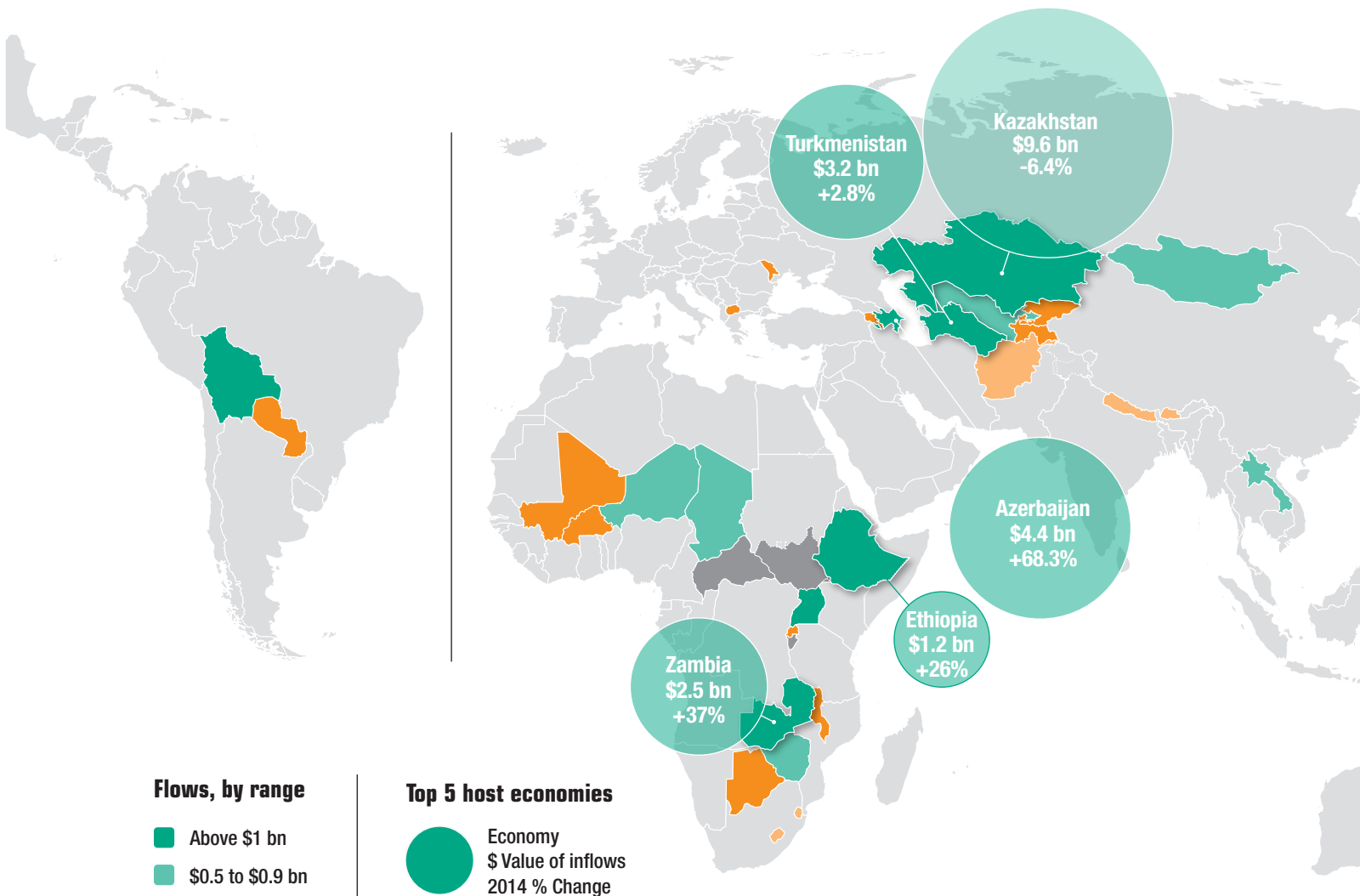
FDI inflows, top 5 host economies, 2014

(Value and change)

2014 Inflows
\$ 29.2 bn

2014 Decrease
-2.8%

Share in world
2.4%



Flows, by range

- Above \$1 bn
- \$0.5 to \$0.9 bn
- \$0.1 to \$0.5 bn
- \$10 to \$99 mn
- Below \$10 mn

Top 5 host economies

- Economy
- \$ Value of inflows
- 2014 % Change

Outflows: top 5 home economies

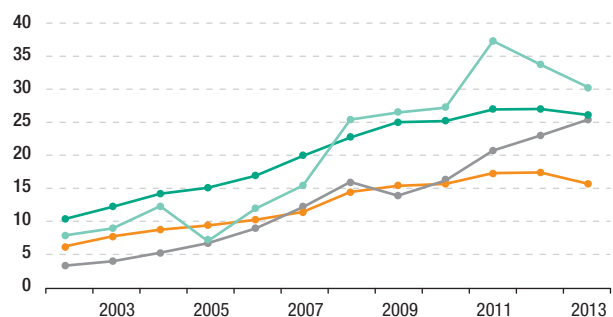
(Billions of dollars, and 2014 growth)

Kazakhstan	\$3.6	+59%
Azerbaijan	\$2.2	+48%
Mongolia	\$0.1	+147%
Zimbabwe	\$0.07	+167%
Burkina Faso	\$0.06	+1.3%

FDI inflows, ODA flows and remittances to LLDCs, 2002–2013

(Billions of dollars)

- Total ODA
- Bilateral ODA
- FDI inflows
- Remittances



Source: UNCTAD.

Note: The boundaries and names shown and the designations used on this map do not imply official endorsement or acceptance by the United Nations. Final boundary between the Republic of Sudan and the Republic of South Sudan has not yet been determined. Final status of the Abyei area is not yet determined. Dotted line in Jammu and Kashmir represents approximately the Line of Control agreed upon by India and Pakistan. The final status of Jammu and Kashmir has not yet been agreed upon by the parties.

HIGHLIGHTS

- FDI flows: largest external capital flow to LLDCs
- Top five economies receive 71 per cent of flows
- Developed countries: largest holders of FDI stock in LLDCs

Figure A.

FDI inflows, 2008–2014 (Billions of dollars)

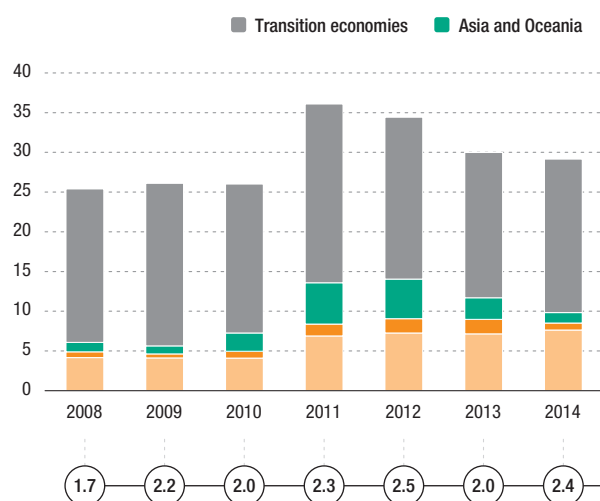


Figure B.

FDI outflows, 2008–2014 (Billions of dollars)

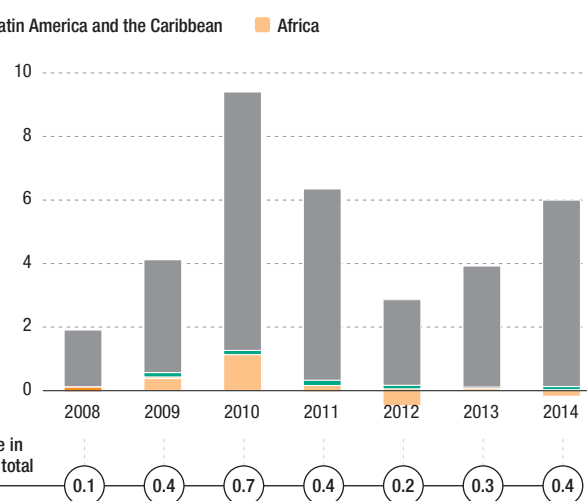


Table A.

Announced greenfield FDI projects by industry, 2013–2014 (Millions of dollars)

Sector/industry	LLDCs as destination		LLDCs as investors	
	2013	2014	2013	2014
Total	17 712	16 398	1 047	1 220
Primary	1 201	402	-	-
Mining, quarrying and petroleum	1 201	402	-	-
Manufacturing	5 410	8 661	404	654
Textiles, clothing and leather	308	2 446	39	-
Non-metallic mineral products	1 634	2 488	75	-
Metals and metal products	279	738	69	-
Motor vehicles and other transport equipment	613	773	-	-
Services	11 102	7 335	643	566
Electricity, gas and water	5 213	982	-	-
Trade	524	2 023	132	11
Transport, storage and communications	2 427	1 238	138	399
Finance	1 535	1 481	354	149

Table B.

Announced greenfield FDI projects by region/country, 2013–2014 (Millions of dollars)

Partner region/economy	LLDCs as destination		LLDCs as investors	
	2013	2014	2013	2014
World	17 712	16 398	1 047	1 220
Developed economies	9 943	6 127	186	56
France	912	543	-	-
Iceland	4 000	-	-	-
United States	513	2 770	3	-
Australia	560	-	35	-
Developing economies	6 575	8 723	525	1 076
South Africa	931	864	42	15
China	380	1 893	-	395
Korea, Republic of	130	529	35	-
India	742	810	52	-
Transition economies	1 194	1 548	335	89
Russian Federation	729	1 414	34	-

Table C.

Cross-border M&As by industry, 2013–2014 (Millions of dollars)

Sector/industry	Sales		Purchases	
	2013	2014	2013	2014
Total	258	-1 062	6	270
Primary	-22	44	2	-250
Mining, quarrying and petroleum	-22	34	2	-250
Manufacturing	257	285	-	57
Food, beverages and tobacco	177	12	-	-
Paper and paper products	-	-101	-	-
Pharmaceuticals, medicinal chemicals and botanical products	15	51	-	-
Non-metallic mineral products	-	314	-	-1
Services	23	-1 391	3	463
Electricity, gas, water and waste management	-	-1 279	-	-
Transportation and storage	-	30	-	4
Information and communication	20	1	-	-
Financial and insurance activities	3	-158	3	459

Table D.

Cross-border M&As by region/country, 2013–2014 (Millions of dollars)

Region/country	Sales		Purchases	
	2013	2014	2013	2014
World	258	-1 062	6	270
Developed economies	99	-2 456	2	14
Luxembourg	20	-277	-	-
Netherlands	359	-1 374	-	-
United Kingdom	-448	-1 152	2	-
Switzerland	331	319	-	-
Developing economies	160	216	3	257
South Africa	-	-125	-	-
Peru	-	307	-	-
China	56	526	-	-
Hong Kong, China	-77	-507	-	-
Transition economies	-	1 177	-	-1
Russian Federation	-	1 147	-	-1

FDI flows to the landlocked developing countries (LLDCs) fell by 3 per cent to \$29 billion in 2014, the third consecutive yearly decline for this group of economies. Investment in the group became more concentrated in the top five economies, which increased their share from 62 per cent to 71 per cent of total flows. Ethiopia entered the top five for the first time, in terms of value of inflows, while Mongolia dropped out of the top five owing to a precipitous 76 per cent fall in flows. The largest investors in LLDCs last year came from developing countries, which increased their share of flows in the grouping from 44 per cent to 63 per cent. Over the past decade, FDI stock in LLDCs quadrupled.

As a group, the LLDCs accounted for 2.4 per cent of total global FDI inflows, up slightly from 2013 despite the fall in their value. The Asian group of LLDCs (5 countries) saw FDI to the subregion fall again, due to the continuing decline in flows to Mongolia, which dropped from \$2.1 billion to \$508 million. In the transition economy group (9 countries), flows rose by more than \$1 billion, despite a 6 per cent decrease in FDI to Kazakhstan, the largest economy in the subregion. Transition economies increased their share in the group to 66 per cent. Flows to the African group (16 countries) went up by over 6 per cent to \$7.6 billion, owing to large increases in FDI to Zambia and Ethiopia. FDI to the Latin America group (2 countries) fell by more than half as a result of a big drop in flows to the Plurilateral State of Bolivia, following four years of steady increases.

Outward investment by the LLDCs, although they represent only 0.4 per cent of total global outflows, increased by almost 50 per cent to \$5.8 billion. This was mostly accounted for by investors from Kazakhstan and Azerbaijan.

Announced greenfield investments to the LLDCs fell in 2014. Announced greenfield investment in the LLDCs has been erratic since its peak in 2008, which it still has not passed in terms of the number or value of deals. In 2014, the number of greenfield deals declined by 5 per cent to 315, representing just 2 per cent of the world total.

The number of deals in the primary sector has been declining in recent years, and their value accounted for just 2 per cent of total announced greenfield investment in LLDCs, at \$402 million, despite the prevalence of extractive industries in several LLDC economies. Greenfield investments in manufacturing

remain strong, in particular in the textiles industry, where their value jumped from \$308 million in 2013 to \$2.45 billion in 2014.⁵³ The non-metallic minerals industry also registered strong performance, with the value of announced investments rising from \$1.63 billion to \$2.45 billion in 2014. A large share of this was accounted for by cement manufacturing firms, investing particularly in African LLDCs.

In the services sector, the number of deals in nearly all industries fell in 2014. Announced greenfield investment projects in the electricity, gas and water industries fell sharply, from \$5.2 billion to \$982 million, although these industries had experienced exceptional growth in 2013. In the transport, storage and communications industries, the value of announced greenfield projects halved in 2014 to \$1.2 billion. One bright spot was trade, as greenfield investments grew from \$524 million to \$2 billion.

Investors from developing and transition economies accounted for 63 per cent of all greenfield investment in the LLDCs, up from 44 per cent in 2013, although this large change in share is partly explained by a single investment made by Reykjavik Geothermal (Iceland) in Ethiopia in 2013. The United States was the single largest greenfield investor in the LLDCs in 2014, followed by China and the Russian Federation.

M&A activity negative in 2014. Investors' purchases were -\$1 billion, meaning that the value of divested assets was greater than the value of acquired assets. Investors from the United Kingdom made the largest divestment, roughly \$1.2 billion, principally in Kazakhstan, where AO Samruk-Energo, a subsidiary of a Kazakh State-owned sovereign wealth fund, bought the remaining 50 per cent stake in the electric utility company, TOO Ekibastuzskaya GRES-1. Sappi Ltd (South Africa) also made a sizable \$100 million divestment of Usutu Forests Products Co Ltd in Swaziland to local investors. The largest M&A investment was made by Polymetal International PLC (Russian Federation), which acquired the entire share capital of Altynalmas Gold Ltd (Kazakhstan), for over \$1.1 billion. In terms of sectoral trends, the services sector suffered the most and in particular the electricity, gas and water industries.

Developed countries remain the largest holders of FDI stock in LLDCs, but China is now a stronger presence, and the Republic of Korea is also an emerging force. Data on bilateral FDI stock for

25 of the 32 LLDCs reveal that, as of 2012, developed economies accounted for 67 per cent of FDI stock in this group of economies.

Among developing- and transition-economy investors, China and the Russian Federation, as well as Turkey, the United Arab Emirates and the Republic of Korea, have become the most important investors in the Central Asian region (table II.14). In Azerbaijan, Turkish investors hold the largest FDI stock; they are the third largest group of developing-country investors in Central Asia as a whole. Indeed, among developing-country investors, there is growing competition for investments in the region, which is also reflected in FDI stock held by investors from the United Arab Emirates, the Republic of Korea and the Islamic Republic of Iran.

The Republic of Korea was the largest investor in LLDCs in 2012, according to greenfield data, and has been promoting growing investment ties with Central Asian LLDCs. Its 2013 the “Eurasia Initiative” aims to boost connectivity and economic ties between the Korean peninsula and Europe (see section A.2). The country has strong trade ties with the region, particularly Uzbekistan, and is one of the largest foreign investors there, together with the Russian Federation, China and Kazakhstan.⁵⁴ Businesses from the Republic of Korea are also heavily invested in Turkmenistan, with over \$5 billion worth of projects. During the visit by that country’s president to Uzbekistan in 2014, a further \$5 billion worth of FDI in the natural gas and chemicals sectors was announced.⁵⁵

FDI inflows to Mongolia showed a decline for the fourth successive year. Political and policy instability coupled with an economic slowdown (GDP growth fell from 12 to 6 per cent in 2014) has led to reduced investor interest. One potential area for FDI growth concerns the construction of a gas pipeline between the Russian

Federation and China that could pass through Mongolia, as the Russian Federation explores increasing trade and investment cooperation with China. For the time being, though, growth in FDI to the country is weak.

FDI trends in the LLDCs since the Monterrey Conference

FDI developments in the LLDCs during the 13 years since the Monterrey Conference fall in two periods: relatively modest flows prior to 2007, followed by increasing flows with slightly more diverse regional distribution after 2008 (figure II.21). However, flows to the LLDCs remain dominated by few countries: just five economies account for over 70 per cent of total FDI in the group.

The growth of FDI flows to the LLDCs since 2002 has been faster than the global rate of FDI growth but the same as that for developing economies as a whole (table II.16). As reported in *WIR14*, FDI has been an important source of finance for the LLDCs in terms of both the value of FDI stock as a percentage of GDP and the contribution of FDI to capital formation (GFCF). For both these indicators, FDI has been of greater significance in the LLDCs than it has been for developing economies in general and for the world since 2002 (figure II.22).

At the subregional level, FDI growth in the LLDCs has been strongest among the Asian and transition group of LLDCs, although this growth is mainly accounted for by the rapid inflows to Mongolia in the mining sector, and to Kazakhstan. In the two Latin American LLDCs, FDI growth has been positive but much weaker than in other regions (table II.16).

The Monterrey Consensus intended to mobilize international capital flows, which includes private capital flows

Table II.14.

Central Asian LLDCs: Inward FDI stock held by selected developing and transition economies, 2012 (Millions of dollars)

Home country	Armenia	Azerbaijan	Kazakhstan	Kyrgyzstan	Mongolia	Tajikistan	Total in region
China	4	170	4 512	334	3 727	476	9 224
Russian Federation	2 450	478	1 933	132	296	-	5 289
Turkey	-	1 933	549	68	7	2	2 559
United Arab Emirates	1	413	1 203	9	1	-	1 627
Korea, Republic of	-	76	1 068	71	365	-	1 580
Iran, Islamic Republic of	17	910	40	4	1	-	972

Source: UNCTAD, FDI/MNE database (www.unctad.org/fdistatistics).

Note: The position of the Russian Federation may be understated due to indirectly held FDI stock.

Table II.15. Selected FDI indicators, 2002–2014 (Per cent)

Indicator	LLDCs	Developing economies	World
FDI inflows, annual growth	12	12	6
Inward FDI stock as % of GDP, 13-year average	33	26	27
FDI inflows as % of GFCF, 13-year average	19	10	9

Source: UNCTAD, FDI/MNE database (www.unctad.org/fdistatistics).

Note: Annual growth computed as compound annual growth rate over the period. LLDCs = landlocked developing countries.

Table II.16. LLDCs: FDI inflows, by subregion, 2002–2014 (Millions of dollars and per cent)

	2002	2014	Growth (%)
Landlocked countries (LLDCs)	7 872	29 151	12
LLDCs-Africa	2 501	7 631	10
LLDCs-Latin America and the Caribbean	682	884	2
LLDCs-Asia and Oceania	129	1 317	21
LLDCs-Transition economies	4 559	19 319	13

Source: UNCTAD, FDI/MNE database (www.unctad.org/fdistatistics).

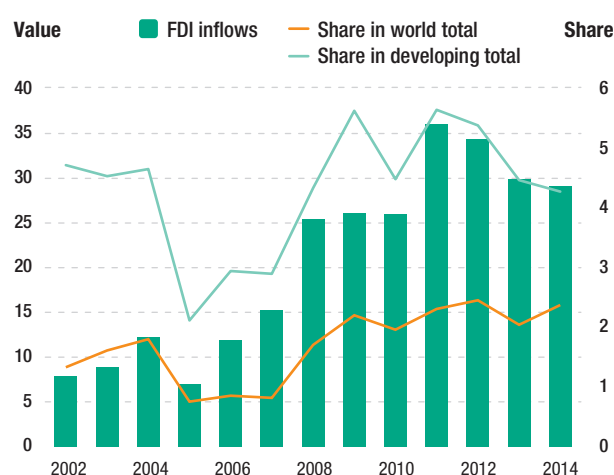
Note: Growth computed as compound annual growth rate over the period 2004–2013. LLDCs = landlocked developing countries.

such as FDI, portfolio investments and “other” investment (mainly bank lending). In the LLDCs, FDI has provided the bulk of private capital flows, with portfolio investment less significant and more volatile⁵⁶ (figure II.23).

With regard to increasing international assistance, which was also highlighted by the Monterrey Consensus, a comparison of FDI inflows to aid flows (ODA) shows that FDI flows were mostly higher than bilateral aid flows during the period; they overtook total ODA in 2008 and now represent the largest external capital flow to the LLDCs (figure II.24). However, it is important to note variations among the LLDCs: the bulk of FDI flows to the LLDCs has been concentrated in a few countries only, mainly resource-rich, mineral-exporting economies; ODA has been more widely distributed among LLDCs, and its role in government budget support is often critical for the provision of essential services and infrastructure. Migrant remittances have also been an important source of external capital flows for several LLDCs, notably Tajikistan and Kyrgyzstan, where they accounted for 47 per cent and 31 per cent of GDP, respectively, in 2012. Nevertheless, FDI to the LLDCs plays a catalytic role in building productive and export capacities in the region, as well as transferring technology, skills and management practices that can

Figure II.21.

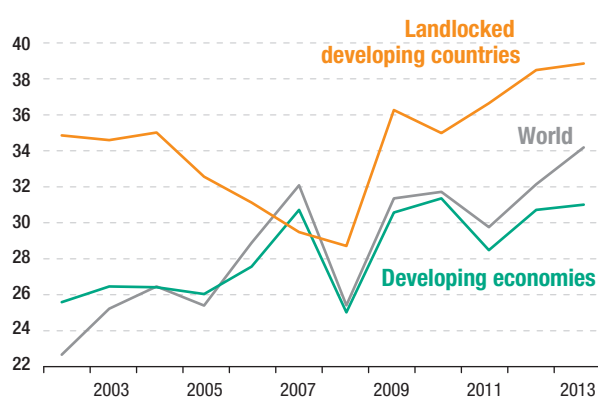
LLDCs: FDI inflows and their share in world and developing-country inflows, 2002–2014
(Billions of dollars and per cent)



Source: UNCTAD, FDI/MNE database (www.unctad.org/fdistatistics).

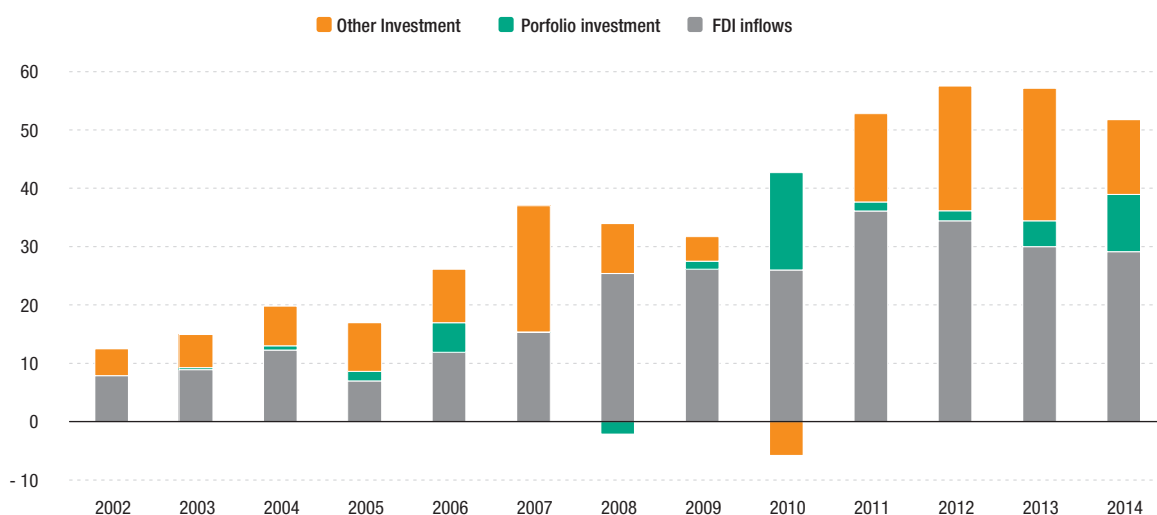
Figure II.22.

LLDCs: FDI stock as a percentage of GDP compared with developing countries and world, 2002–2013
(Per cent)



Source: UNCTAD, FDI/MNE database (www.unctad.org/fdistatistics).

Figure II.23. LLDCs: Private capital inflows by type, 2002–2014 (Billions of dollars)



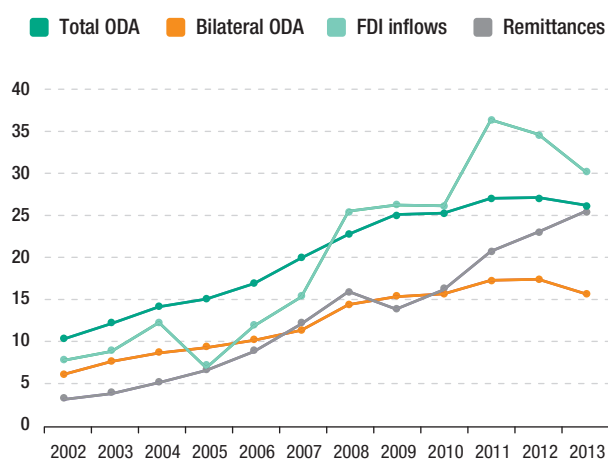
Source: UNCTAD, FDI/MNE database (www.unctad.org/fdistatistics) (for FDI inflows) and IMF (for portfolio and other investments).

further enhance the competitiveness of this group of economies.

Policy implications. Although FDI has become the most important external capital flow to the LLDCs and will remain essential for the development financing strategies of this group of countries, it should be seen as part of an overall financing strategy that involves domestic as well as foreign sources, and public as well as private ones (*WIR14*). Moreover, beyond their shared geographic characteristic, the LLDCs should not be considered a homogenous group. There are clear regional and country differences, which policymakers and the international community should consider when setting policies so as to spread the benefits of foreign investment beyond a relatively small group of economies and sectors.

The *Vienna Programme of Action (POA)*, the outcome document of the Second United Nations Conference on Landlocked Developing Countries held in November 2014, highlighted a number of areas for action to address infrastructure and connectivity in the LLDCs. The document called for travel times for the transport of cargo to be reduced, which will require significant investment in transport infrastructure as well as attention to trade facilitation, including customs harmonization and streamlined inspections and certification. The growth of regional economic

Figure II.24. LLDCs: FDI inflows, ODA flows and remittances, 2002–2013 (Billions of dollars)



Source: UNCTAD, FDI/MNE database (www.unctad.org/fdistatistics) (for FDI inflows), OECD (for ODA flows) and World Bank (for remittances).

agreements could also help create efficiencies in time and cost by reducing the number of border stops and associated costs (as well as create larger regional markets, which would be attractive to market-seeking FDI).

SMALL ISLAND DEVELOPING STATES

FDI inflows, top 5 host economies, 2014

(Value and change)

2014 Inflows

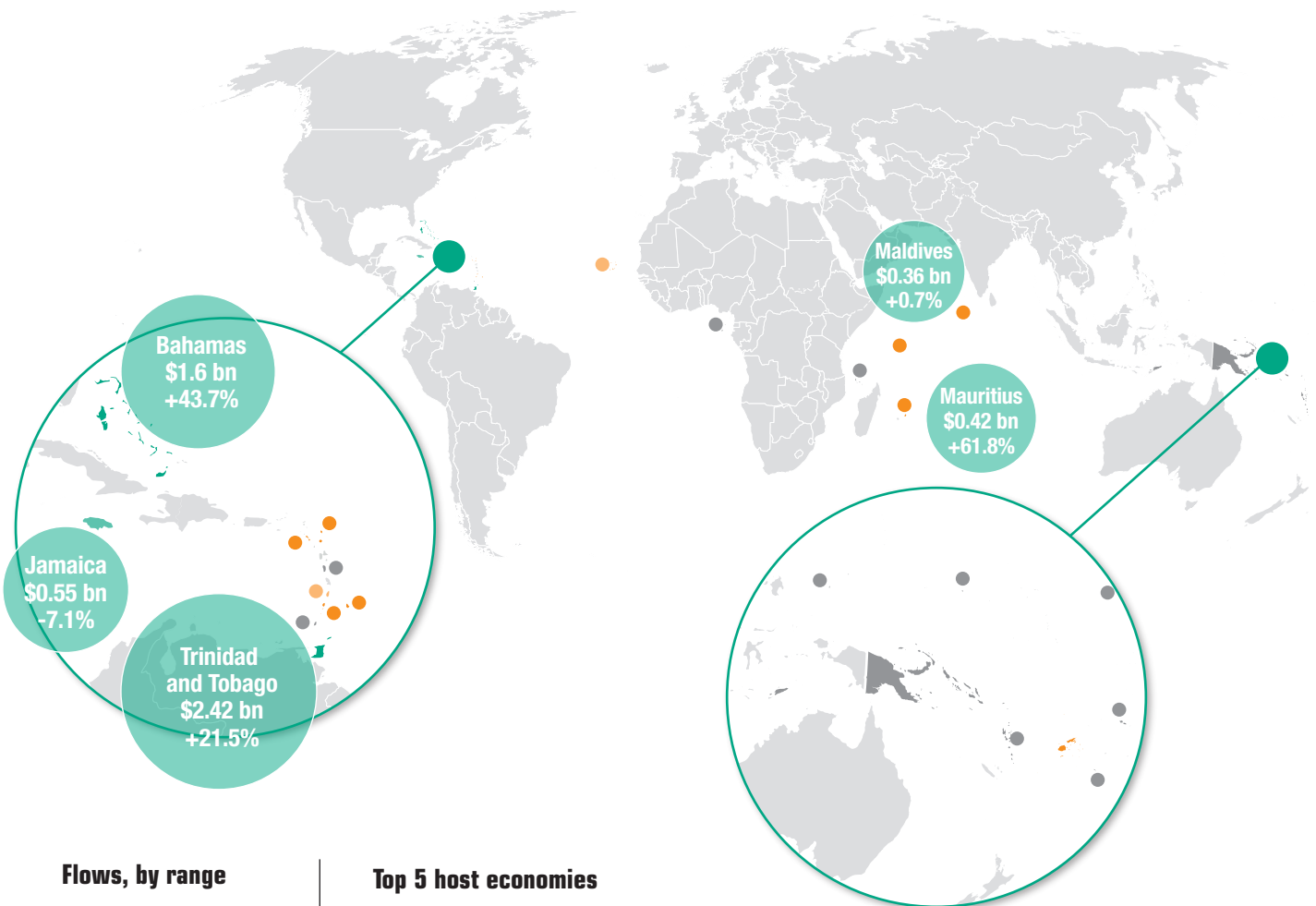
\$ 6.9 bn

2014 Increase

+21.8%

Share in world

0.6%



Flows, by range

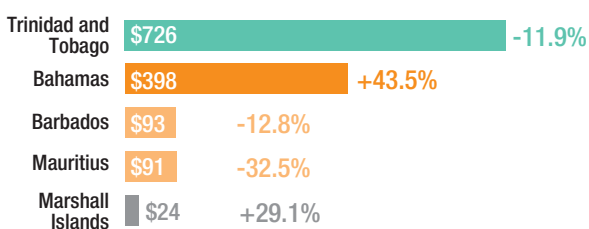
- Above \$1 bn
- \$500 to \$999 mn
- \$100 to \$499 mn
- \$50 to \$99 mn
- Below \$50 mn

Top 5 host economies

- Economy
- \$ Value of inflows
- 2014 % Change

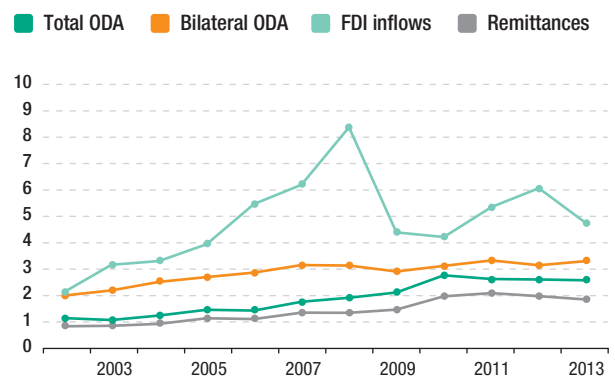
Outflows: top 5 home economies

(Millions of dollars, and 2014 growth)



FDI inflows, ODA flows and remittances to SIDS, 2002–2013

(Billions of dollars)



Source: UNCTAD.

Note: The boundaries and names shown and the designations used on this map do not imply official endorsement or acceptance by the United Nations. Final boundary between the Republic of Sudan and the Republic of South Sudan has not yet been determined. Final status of the Abyei area is not yet determined. Dotted line in Jammu and Kashmir represents approximately the Line of Control agreed upon by India and Pakistan. The final status of Jammu and Kashmir has not yet been agreed upon by the parties.

HIGHLIGHTS

- FDI remains largest external source of financing
- ODA has role to play, especially in Africa and Oceania
- International community can coordinate sustainable investment

Figure A.

FDI inflows, 2008–2014 (Billions of dollars)

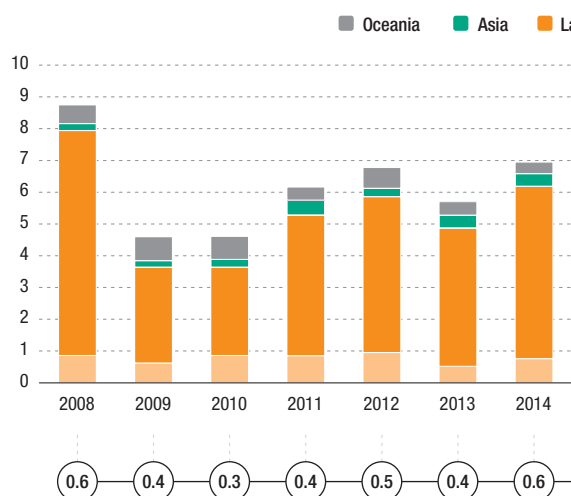


Figure B.

FDI outflows, 2008–2014 (Billions of dollars)

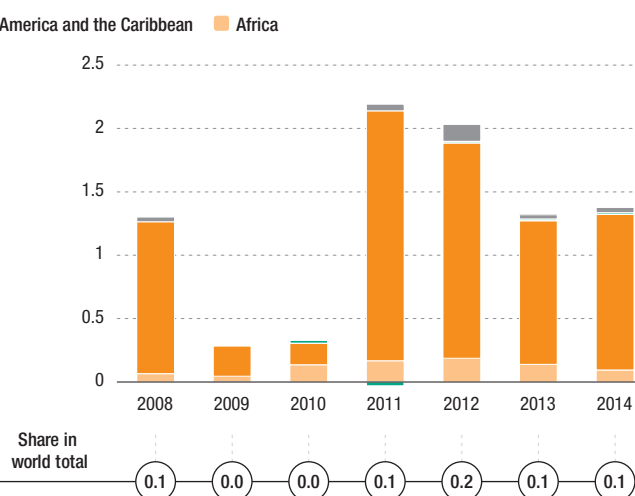


Table A.

Announced greenfield FDI projects by industry, 2013–2014 (Millions of dollars)

Sector/industry	SIDS as destination		SIDS as investors	
	2013	2014	2013	2014
Total	6 504	4 841	3 605	2 021
Primary	2 532	22	-	-
Manufacturing	1 984	223	-	262
Coke, petroleum products and nuclear fuel	1 048	-	-	-
Chemicals and chemical products	850	-	-	-
Metals and metal products	-	160	-	-
Services	1 989	4 596	3 605	1 760
Electricity, gas and water	-	1 298	-	125
Construction	1 350	2 000	-	-
Hotels and restaurants	65	234	-	-
Transport, storage and communications	477	588	1 648	1 369
Finance	22	186	210	67
Business services	47	190	1 748	161

Table B.

Announced greenfield FDI projects by region/country, 2013–2014 (Millions of dollars)

Partner region/economy	SIDS as destination		SIDS as investors	
	2013	2014	2013	2014
World	6 504	4 841	3 605	2 021
Developed economies	2 812	1 964	3	81
Europe	253	1 707	3	2
United States	1 380	211	-	7
Australia	316	45	-	35
Japan	863	-	-	-
Developing economies	3 692	2 877	3 602	1 941
Africa	56	59	3 192	1 720
Kenya	-	-	461	86
Nigeria	-	-	2 296	1 148
Asia and Oceania	3 624	2 773	177	-
China	3 250	2 429	162	-
Latin America and the Caribbean	13	45	233	221

Table C.

Cross-border M&As by industry, 2013–2014 (Millions of dollars)

Sector/industry	Sales		Purchases	
	2013	2014	2013	2014
Total	-596	1 503	-294	2 065
Primary	-600	5	-14	-
Extraction of crude petroleum and natural gas	-600	-7	-	-
Mining of metal ores	-	12	-14	-
Manufacturing	-5	1 175	-	-
Chemicals and chemical products	-	1 175	-	-
Services	9	323	-280	2 065
Electricity, gas, water and waste management	-	-2	-	1 175
Transportation and storage	-	258	-	-81
Information and communication	4	-	7	-
Financial and insurance activities	-	68	-286	-183
Business activities	5	-	-	12
Public administration and defence; compulsory social security	-	-	-	1 116

Table D.

Cross-border M&As by region/country, 2013–2014 (Millions of dollars)

Region/country	Sales		Purchases	
	2013	2014	2013	2014
World	-596	1 503	-294	2 065
Developed economies	-604	74	-333	1 149
European Union	280	3 307	-367	-328
United States	-600	-142	2	194
Australia	-	-2 857	20	1 098
Developing economies	3	1 428	39	916
Africa	5	1 175	-	12
Mauritius	5	1 175	-	-
Zimbabwe	-	-	-	12
Latin America and the Caribbean	-	-	-	895
Trinidad and Tobago	-	-	-	1 175
Asia and Oceania	-2	253	39	9
Singapore	60	-1	9	-

FDI flows to small island developing States (SIDS) increased by 22 per cent to \$6.9 billion, mostly due to a strong rise in cross-border M&A sales. Between 2004 and 2014, FDI stock in the SIDS tripled. The third International Conference on SIDS (in September 2014, in Samoa) highlighted the need for further efforts to harness financing for economic diversification to foster greater resilience and sustainability in these countries.

Caribbean SIDS received the bulk of FDI flows (78 per cent of the total), followed by African SIDS (11 per cent), Asian SIDS (6 per cent) and Pacific SIDS (5 per cent). Cross-border M&As turned from negative values (because of divestment) in 2013 (–\$600 million) to \$1.5 billion in 2014.

Trinidad and Tobago, the Bahamas, Jamaica and Mauritius were the largest destinations for FDI flows to SIDS in 2014, accounting for 72 per cent of the total. Flows to Trinidad and Tobago – 35 per cent of the total – increased by 21 per cent to \$2.4 billion as a result of the \$1.2 billion acquisition of the remaining 57 per cent stake in Methanol Holdings Trinidad Limited by Consolidated Energy Company (Mauritius). Mauritius also registered strong growth of FDI flows, which reached \$418 million (up 62 per cent), boosted by the \$68 million acquisition of CIEL Investment Limited – a provider of investment services – by an investor group of mostly French companies. Total cross-border acquisitions in Mauritius – including deals that involved changes of ownership between non-residents – have renewed their growth since 2012 and reached \$574 million in 2014. On the other hand, flows to Jamaica – the group's second largest recipient – decreased by 7 per cent to \$551 million, despite new equity inflows in infrastructure and tourism projects.

Although Papua New Guinea and Timor-Leste have hosted a number of big projects in the extractive industry, they continued to register modest FDI flows, partly due to non-equity investment (e.g. production sharing), and partly due to incomplete coverage of

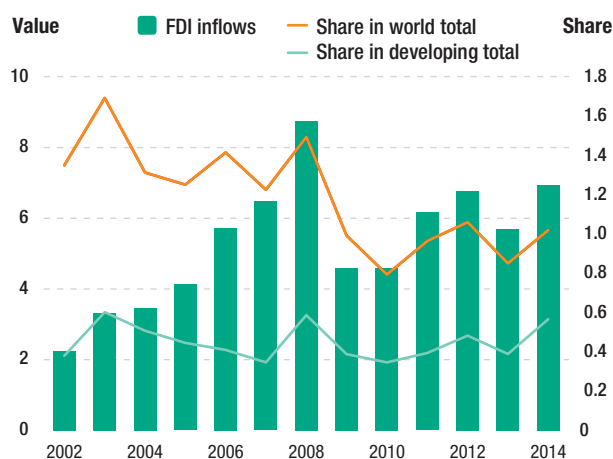
data. Foreign investors' involvement in Papua New Guinea's oil and gas industry is reflected by the number of cross-border M&As megadeals that took place in 2014, totalling \$4 billion, and all involving the sale by InterOil Corp (Singapore) of its upstream and downstream business to Total (France), Oil Search (Australia) and Puma Energy Singapore (Netherlands).

FDI trends in the SIDS since the Monterrey Conference

FDI flows to the SIDS have grown more slowly than to developing economies as a whole, and they took a particular hit after the onset of the financial crisis. The annual growth of FDI inflows to SIDS over 2002–2014, while sizeable and keeping pace with the world average, was much slower than to developing countries as a whole (table II.17). In addition, FDI to SIDS fell considerably after the onset of the financial crisis and have not yet recovered (figure II.25).

Figure II.25.

SIDS: FDI inflows and their share in world and developing-country inflows, 2002–2014
(Billions of dollars and per cent)



Source: UNCTAD, FDI/MNE database (www.unctad.org/fdistatistics).

Table II.17. Selected FDI indicators, 2002–2014 (Per cent)

Indicator	SIDS	Developing countries	World
FDI inflows, annual growth	10	12	6
Inward FDI stock as % of GDP, 13-year average	70	26	27
FDI inflows as % of GFCF, 13-year average	32	10	9

Source: UNCTAD, FDI/MNE database (www.unctad.org/fdistatistics).

Note: Annual growth computed as compound annual growth rate over the period considered.

Nevertheless, FDI stock in SIDS as a group tripled during the past decade (2004–2014).

FDI to the 29 SIDS is very small in absolute value but relatively high in relation to the size of their economies. Annual average flows amounted to only \$6 billion (0.4 per cent of the world's total) and average annual stocks to \$62 billion (0.36 per cent) over the past decade. However, these flows are relatively high when comparing the size of SIDS economies with the world and developing-economy averages (table II.17). This is partly due to the sizeable fiscal advantages offered to foreign investors in a number of SIDS, and some very large investments in natural resources. The ratio of FDI stock to GDP during 2002–2014 and FDI inflows as a percentage of GFCF were each almost three times as high as the world and developing-economy average over the same period.

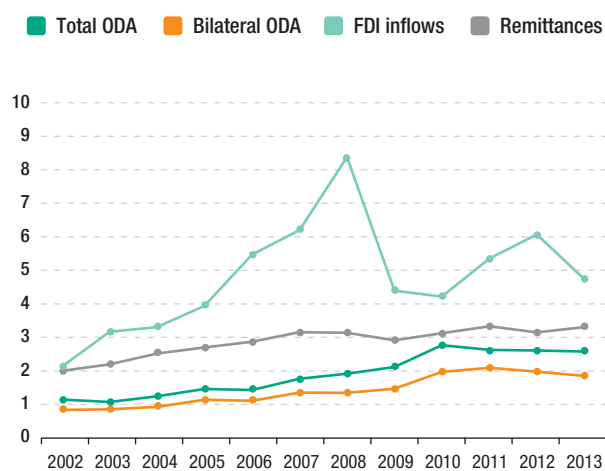
The bulk of FDI into the SIDS is concentrated in a few regions and economies. The Caribbean SIDS received the lion's share of FDI flows to the group, at 77 per cent of total flows during 2002–2014, followed by Africa (especially in recent years) and Oceania. Trinidad and Tobago alone accounted for 27 per cent of total FDI stocks in SIDS in 2014, owing to the presence of large oil and gas resources, coupled with proximity to North America. The Bahamas, which enjoys the highest GDP per capita among SIDS, accounted for 19 per cent. Jamaica, which has metal mineral deposits and is the second most populated of the SIDS after Papua New Guinea, received 14 per cent. Among the 10 largest host countries of FDI stock to the SIDS, three are rich in mineral deposits (Papua New Guinea, Trinidad and Tobago, and Jamaica), four are home to the bulk of the SIDS population (Papua New Guinea, Jamaica, Trinidad and Tobago, and Mauritius), and some offer fiscal advantages (e.g. the Bahamas, Barbados, Mauritius and Seychelles, among others).

At the bottom of the ranking, eight countries⁵⁷ for which data are available account for less than 2 per cent of total FDI stock in the group: \$2.1 billion or just \$264 million per country. Of these countries, three are LDCs, all but three have fewer than 200,000 inhabitants, none (except Timor-Leste) has significant mineral resources, and six are Pacific SIDS, which are among the smallest and most remote.

Across the SIDS group as a whole, there has been a shift in the relative share of different sources of

Figure II.26.

SIDS: FDI inflows, ODA flows and remittances, 2002–2013
(Billions of dollars)



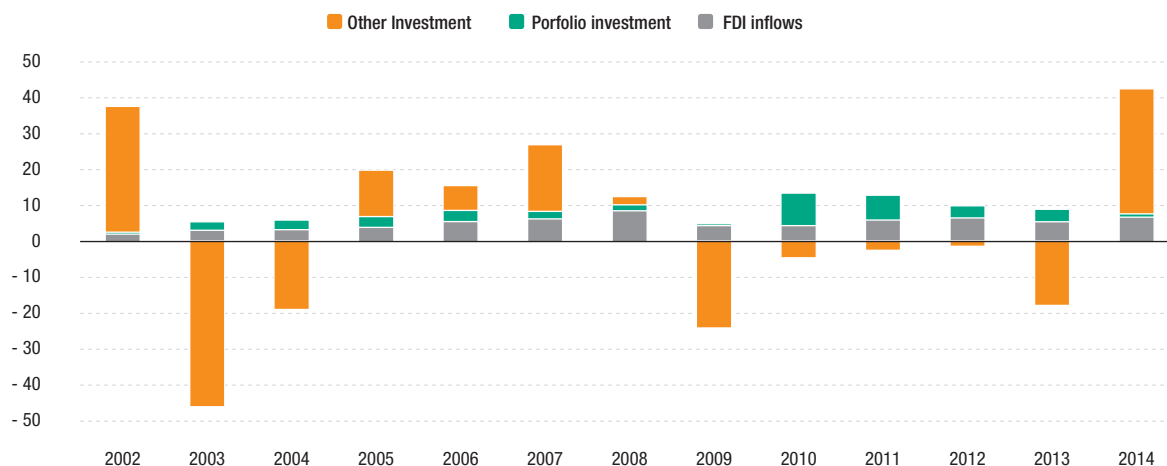
Source: UNCTAD, FDI/MNE database (www.unctad.org/fdistatistics) (for FDI flows), IMF (for portfolio investment), OECD (for ODA) and World Bank (for remittances).

external finance. FDI, despite a dip after the financial crisis, remains the largest external source of financing to the group. Since 2002, ODA has declined in relative importance but remains a stable source of external finance (figure II.26). Comparing FDI with other private sector sources of financing and investment shows that “other” investment (mostly bank loans) has become an increasingly important source of external finance for SIDS. However, it is much less stable than FDI (figure II.27).⁵⁸

Among SIDS, there are major country and subgroup differences in the composition of flows, and these need to be taken into account by policymakers in their diversification strategies. Caribbean SIDS attracted more than three quarters of FDI flows in 2002–2013 (figure II.28). Oceania SIDS absorbed 57 per cent of ODA and only 9 per cent of FDI. More than half of the overall amount of ODA aimed at SIDS in 2002–2013 went to four countries, the largest recipient being Papua New Guinea, followed by Timor-Leste and the Solomon Islands – two LDCs – and Cape Verde. ODA is vital for many SIDS, being equivalent to more than 10 per cent of GDP for 13 of them, and more than 50 per cent for countries such as Tuvalu (70 per cent) and the Marshall Islands (54 per cent).

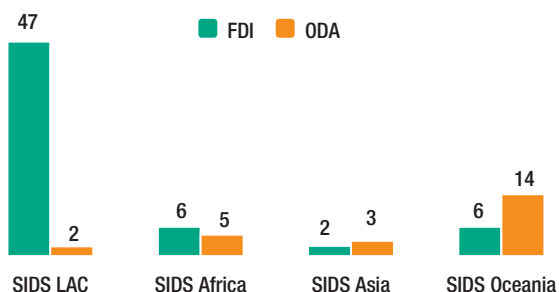
Policy implications. For the most part, small market size, a narrow resource base, remote locations, and

Figure II.27. SIDS: Private capital inflows by type, 2002–2014 (Billions of dollars)



Source: UNCTAD, FDI/MNE database (www.unctad.org/fdistatistics) (for FDI inflows) and IMF (for portfolio and other investment).

Figure II.28. SIDS: FDI flows and ODA flows by region, 2002–2013 (Millions of dollars)



Source: UNCTAD, FDI/MNE database (www.unctad.org/fdistatistics) (for FDI flows) and OECD (for ODA flows).

high vulnerability to natural disasters affect the nature and the scope of economic activities that can be developed in SIDS.

Nevertheless, in pursuing diversification and sustainable development, SIDS have to mobilize and effectively channel a range of domestic and external sources of development finance, such as ODA, FDI, portfolio investment, bank lending and remittances for

economic development and long-term sustainability. Efforts on three fronts are required:

- A tailored, long-term industrial strategic plan, focusing on investment in sustainable investment.
- A rigorous assessment of current and potential sources of financing realistically available to them, recognizing that the composition of flows varies by country.
- A careful matching of the characteristics of available flows to specific development goals and objectives, including building relevant capabilities, to ensure that the most suitable sources of financing and investment are utilized in any project, scheme or sector. In many cases, for instance for investment related to climate change mitigation and adaptation, this will entail PPPs relying on multiple sources of financing, both domestic and foreign.

Coordinated efforts by the international community are needed to support SIDS in working towards these goals, including in helping smooth the systemic challenges and constraints they face. Quadrupling the FDI stock in the next decade and a half and ensuring its positive contribution to the SDG sectors is a challenging but achievable goal.

Notes

- ¹ The other five are mobilizing domestic financial resources, harnessing trade as an engine for development, increasing international financial assistance (ODA) and technical cooperation, providing debt relief, and addressing systemic issues and coherence between the international monetary, financial and trading systems.
- ² See <http://apparel.edgl.com/news/The-New-Kid-on-the-Block--Africa-Is-Vying-for-a-Larger-Share-of-the-Global-Textile-and-Apparel-Pie96802>.
- ³ They include several by Dubai-based private equity firm Abraaj Group into consumer sectors and by Dubai's DP World, which currently operates 12 terminals in six African countries, with projects under way in Egypt and Senegal. The Investment Corporation of Dubai (the country's sovereign wealth fund) invested \$300 million in Dangote Cement (Nigeria) in 2014. The Emirates Investment Authority (United Arab Emirates) acquired 53 per cent of the Morocco-based telecommunications company, Itissalat (France). See also http://web.dpwworld.com/wp-content/uploads/2014/05/22294_DP_World_RA14_Web_v2.pdf.
- ⁴ A simple categorization of FDI by firm type rather than project type can be misleading. For example, SRK Consulting, a prominent mining consulting service firm, has invested in several African countries over recent years to support mineral extraction. Although in UNCTAD's greenfield investment database, the firm's investments are counted as being in "business services", i.e. in the services sector, they constitute a mining investment in terms of FDI data as the firm's activity is incidental to mining.
- ⁵ The ICBC deal was also the largest investment outside of China by a Chinese bank at the time. This meant that by 2012, some 10.5 per cent of South Africa's inward FDI stock was in the banking industry.
- ⁶ See <http://mg.co.za/article/2014-03-25-mtn-said-to-start-selling-mobile-tower-networks>.
- ⁷ Information comes from UNCTAD's database on foreign affiliates, which is based on Bureau van Dijk's Orbis.
- ⁸ "HK Foreign Direct Investment", *InvestHK Newsletter*, January 2015.
- ⁹ "Foreign investors worried Vietnamese minimum wages jump 17-fold over 15 years", *NIKKEI Asian Review*, 18 November 2014.
- ¹⁰ InfraPPP (www.infrappworld.com) and Indonesia Investments (www.indonesia-investments.com). See e.g. "Soekarno-Hatta Railway Project Indonesia: Tendered to Private Sector" (www.indonesia-investments.com/business/business-columns/soekarno-hatta-railway-project-fully-tendered-to-private-sector/item2718).
- ¹¹ Jack Goodman, "Sri Lanka's Growing Links with China: Trade, investment and a strategic Indian Ocean location bring the two countries closer together", *The Diplomat*, 6 March 2014.
- ¹² For example, in 2014, Asian Paints (India) started to build a plant with an investment of \$81 million, and r-pac International Corporation (United States) announced plans to invest \$107 million in a production facility in Sri Lanka.
- ¹³ Large Chinese companies, such as China International Water & Electric Corp. and Three Gorges International Corp., are investing in hydroelectricity plans in Nepal. In 2014, agreements were signed with two Indian companies in the same sector, each investing about \$1 billion.
- ¹⁴ Automobile Industry in India, India Brand Equity Foundation (IBEF), January 2015.
- ¹⁵ See, e.g. Bhasker (2013).
- ¹⁶ These Indian automakers started operating in the passenger car market first with multi-utility vehicles and, later, with small cars (see e.g. Kumaraswamy et al., 2012).
- ¹⁷ See, e.g. Okada and Siddharthan (2007).
- ¹⁸ Starting in 2009 in Bahrain, 2012 in Lebanon and Turkey, and 2013 in Iraq.
- ¹⁹ The segments of the construction industry include residential and commercial buildings, water and energy, transport, oil and gas, among others. In the absence of official statistics, data on contract awards and on work under execution are the main bases for gauging the trends shaping the GCC construction market since 2008–2009, and assessing the importance of foreign contractors in this market.
- ²⁰ The \$88 billion awarded to the largest contractors represented 56 per cent of the value of total contracts awarded in the GCC in 2013 (see MEED Insight, "GCC Construction Projects Market 2015", August 2014; and "Local firms dominate GCC construction", MEED (Middle East Economic Digest), 58(3), 17 January 2014).
- ²¹ See "Local firms dominate GCC construction", *MEED*, 58(3), 17 January 2014; MEED Insight, "MENA projects market and review 2014", July 2014; MEED Insight, "The UAE projects market 2013, A comprehensive forecast and review of opportunities in the United Arab Emirates' projects market", www.meedinsight.com.
- ²² Korean firms have won the vast majority of their projects by using lump-sum turnkey contracts to submit aggressive prices and to employ stringent project management (aimed at finishing the scheme ahead of schedule wherever possible), and by using highly effective procurement strategies to ensure that they bring the project in on time and on budget.
- ²³ Economist Intelligence Unit, "GCC companies face challenging 2015", 22 January 2015.
- ²⁴ Although significant efforts have been made since the early 2000s to diversify GCC economies, progress toward genuine diversification has been modest. Growth in non-oil output averaged 6.8 per cent during 2001–13, and the share of the non-oil sector in total real GDP rose by 12 percentage points to 70 per cent, driven mainly by Saudi Arabia and the United Arab Emirates (Callen et al., 2014). However, "non-oil growth is in most cases concentrated in service industries that rely on demand generated by oil revenues; moreover, in many cases, productivity in the non-oil economy has been declining" (IMF, 2014: 25).

- ²⁵ Intel's operations in Costa Rica are worth about \$2 billion a year, making up about 20 per cent of the country's exports. The firm accounted for 11 per cent of net FDI over 2000–12. ("Business in Costa Rica, Intel outside", *The Economist*, 19 April 2014).
- ²⁶ "Dominican Rep. Investment in Free Zones Up 6%", *CentralAmericaData.com*, 21 April 2015.
- ²⁷ During 1996–2000, roughly half of FDI flows were related to M&As in connection with the privatization of State-owned utilities and domestic banks (Elson, 2006).
- ²⁸ Brazil attracted 69 per cent of FDI flows to South America's secondary sector in 2006–2013, and Argentina 18 per cent.
- ²⁹ "BASF, Gazprom Fall Victim to Sanctions as Asset Swap Ends", *Bloomberg Business*, 19 December 2014.
- ³⁰ Within manufacturing, basic metals and metal products were the largest industries in terms of FDI stock in 2013. However, these investments often represent round-tripping FDI undertaken by Russian investors. For example, the second largest Russian steel company, Evraz, is owned by offshore companies in which Russian investors have key interests (Kuznetsov, 2012).
- ³¹ "Ford bullish on Russia as it takes control of local JV", <http://europe.autonews.com/article/20150410/ANE/150419998/ford-bullish-on-russia-as-it-takes-control-of-local-jv>.
- ³² "PepsiCo and Coca-Cola close plants in Russia", http://rbth.com/news/2015/03/04/pepsico_and_coca-cola_close_plants_in_russia_44207.html.
- ³³ "Carlsberg Forced to Close 2 Russian Breweries", *The Moscow Times*, 29 January 2015.
- ³⁴ Australia, Bureau of Resources and Energy Economics. www.industry.gov.au. Projects at the "Committed Stage" have completed all commercial, engineering and environmental studies; received all required regulatory approvals; and finalized the financing for the project.
- ³⁵ At the time of writing, apart from the United States and Japan, few other major investor countries had made available geographical breakdowns of 2014 FDI data.
- ³⁶ For estimating geographical breakdowns of Japanese FDI, directional principle (BPM5) data are used for 2013 while the asset/liabilities principle data (BPM6) are used for 2014. For developing regions excluding offshore financial centres, the two methodologies should produce more or less the same data.
- ³⁷ Primary income refers to investment income and compensation of employees earned abroad (receipts) or owed to foreign entities (payments). For the United States, investment income accounted for 99 per cent of primary income receipts and 97 per cent of primary income payments in 2014.
- ³⁸ The category "other investment" includes currency and deposits, loans, trade credits, etc.
- ³⁹ Total fixed investment is estimated by adding capital expenditures and R&D expenditures of United States parent companies.
- ⁴⁰ Measured by number of vehicles. Data are from the Japan Automobile Manufacturers Association (www.jama.or.jp).
- ⁴¹ Due to the unavailability of FDI data for Tuvalu, this group is represented by three LDCs: Kiribati, Solomon Islands and Vanuatu.
- ⁴² "Qatar National Bank increases stake in African lender Ecobank", 15 September 2014, *Financial Times*.
- ⁴³ The transaction value was not available for the majority of these deals; thus, the total value of cross-border M&A sales in LDCs is likely to be higher.
- ⁴⁴ An ultra-deep offshore oil development project, in which France's Total (30 per cent) formed a joint venture with two local companies (50 per cent), ExxonMobil (15 per cent) from the United States and Galp Energia (5 per cent) from Portugal ("Angola: Total launches the development of Kaombo, an ultra-deep offshore project", 14 April 2014, press release, www.total.com/en/media/news/press-releases/angola-total-launches-development-kaombo-ultra-deep-offshore-project?%FFbw=kludge1%FF). This is most likely a product-sharing contract; thus, no impact is expected on FDI inflows to Angola.
- ⁴⁵ In 2013, announced greenfield investment in electricity and gas amounted to \$18 billion, while primary sector investment was at \$4 billion.
- ⁴⁶ "Ethiopia: Indian firm to plant Africa's largest cotton mill here", 3 May 2014, allafrica.com.
- ⁴⁷ "Ethiopia: Chinese textile giant eyes U.S. \$500 million plant", 6 September 2014, allafrica.com.
- ⁴⁸ Throughout the period 2000–2013, crude petroleum accounted for almost 90 per cent of AGOA exports to the United States. Refined petroleum products contributed to the major part of growth in non-crude oil exports from AGOA to the United States in this period (USITC, 2014).
- ⁴⁹ It comprises private and public entities from Myanmar (51 per cent); Japanese MNEs, including general trading companies Mitsui, Marubeni and Sumitomo (about 40 per cent); and the Japan International Cooperation Agency (about 10 per cent). Upon the completion of the first phase of development in 2016, this special economic zone is expected to create 50,000 jobs by hosting some 100 companies.
- ⁵⁰ "After decades of decay, Myanmar bets on Thilawa to lead industrial boom", 7 May 2015, www.reuters.com; "Eight companies set to begin operations in Thilawa SEZ", 29 April 2015, *The Myanmar Times*.
- ⁵¹ For example, China has pledged \$11 billion to develop the Trans-Asian Railway to connect the Greater Mekong Subregion, consisting of Cambodia, China, the Lao People's Democratic Republic, Myanmar, Thailand and Viet Nam ("High-quality trains to speed up GMS connectivity", 21 December 2014, news.xinhuanet.com). It has pledged an additional \$1 billion for infrastructure development to improve inter-connectivity within the subregion ("Cambodia welcomes Chinese premier's pledge of over 3 bln USD aid to GMS countries", 20 December 2014, news.xinhuanet.com).
- ⁵² Based on exports accounting for 45 per cent of a country's total exports of goods and services during

2010–2012, LDCs are classified into six categories of export specialization: food and agricultural exporters, fuel exporters, manufactures exporters, mineral exporters, mixed exporters and services exporters (UNCTAD, 2014, p. xiii).

⁵³ Investments by Jiangsu Lianfa Textile (China) in Ethiopia, and Weibo (China) in the former Yugoslav Republic of Macedonia, as well as Shrivallabh Pittie Group (India) in Ethiopia, were among the six largest projects by value, totalling \$1.4 billion. Ethiopia also attracted other large greenfield investments in the textiles industry from India, Turkey, Pakistan and the Republic of Korea (see LDCs section).

⁵⁴ Uzbekistan is not included in table II.15 because of a lack of reported bilateral FDI data; the analysis is based on announced greenfield and M&A deals only.

⁵⁵ www.jamestown.org/single/?tx_ttnews%5Btt_news%5D=42623&no_cache=1#.WWMhPE-qpBc.

⁵⁶ Other investments have been more significant than portfolio investment but similarly erratic, increasing in value and share in recent years but recording a decline in 2014.

⁵⁷ Vanuatu, Sao Tome and Principe, Samoa, Timor-Leste, Tonga, the Comoros, Palau, Kiribati.

⁵⁸ In addition, there are “other” investment flows, which are even more volatile, especially for Caribbean SIDS.

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10
11

Recent Policy Developments and Key Issues

CHAPTER III

10
11



A. NATIONAL INVESTMENT POLICIES

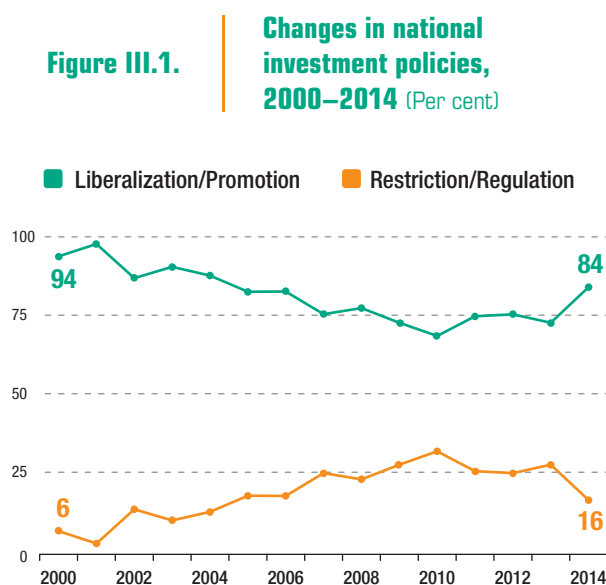
1. Overall trends

Countries' investment policy measures continue to be predominantly directed towards investment liberalization, promotion and facilitation. Measures geared towards investment in sectors important for sustainable development are still relatively few.

In 2014, according to UNCTAD's count, 37 countries and economies adopted 63 policy measures affecting foreign investment. Of these measures, 47 related to liberalization, promotion and facilitation of investment, while 9 introduced new restrictions or regulations on investment (table III.1). The share of liberalization and promotion increased significantly, from 73 per cent in 2013 to 84 per cent in 2014 (figure III.1).¹

a. Investment promotion and facilitation predominant – focus on legal and institutional improvement

A number of countries introduced or amended their investment laws or guidelines to grant new investment incentives or to facilitate investment procedures. *Algeria* reorganized the institutional framework for the mining sector. *Argentina* improved investment conditions for the hydrocarbon industry by amending the Federal Hydrocarbons Law. The *Plurinational State of Bolivia* introduced an investment promotion law (Ley de Promoción de Inversiones) which, inter alia, provides that the State may offer general and specific incentives. *China* introduced new rules on the administration of China's Outward Direct Investment. Henceforth, only



Source: UNCTAD, Investment Policy Monitor.

outward direct investment in countries or regions and industries identified as “sensitive” require the approval of the Ministry of Commerce (MOFCOM). Outward direct investment in all other countries or regions and industries only need to be registered with MOFCOM. *Cuba* approved a new law on foreign investment offering guarantees and incentives to investors and simplifying investment approval procedures. *Ethiopia* established an Investment Board and Investment Commission. *Kazakhstan* introduced “Rules of Granting Investment Subsidies”, describing the procedures in detail. *South Africa* approved guidelines for the new Medium and Heavy Commercial

Table III.1.	Changes in national investment policies, 2000–2014 (Number of measures)														
Item	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014
Number of countries that introduced changes	46	52	44	60	80	78	71	50	41	47	55	49	54	59	37
Number of regulatory changes	81	97	94	125	164	144	126	79	68	88	121	80	86	87	63
Liberalization/Promotion	75	85	79	113	142	118	104	58	51	61	80	59	61	61	47
Restriction/Regulation	5	2	12	12	20	25	22	19	15	23	37	20	20	23	9
Neutral/Indeterminate ^a	1	10	3	-	2	1	-	2	2	4	4	1	5	3	7

Source: UNCTAD, Investment Policy Monitor database.

^a In some cases, the expected impact of the policy measures on the investment is undetermined.

Vehicles Automotive Investment Scheme, providing a non-taxable cash grant of various degrees to qualifying investments in productive assets. The *United Arab Emirates* established the Dubai Investment Development Agency, providing a strategic plan and incentives for the attraction of investment. *Uzbekistan* signed a law amending foreign investment regulations. Changes include the introduction of a one-stop shop for foreign businesses, the easing of migration regulations for foreign investors, a guarantee of investors' rights to repatriate funds and a pledge of stable tax legislation and customs tariffs for foreign investors for a decade after a firm is registered. *Viet Nam* revised the Law on Investment which defines in detail the terms "foreign investor" and "foreign invested enterprise", streamlines registration procedures, reduces the mergers and acquisitions (M&A) transaction period and decreases the number of prohibited and conditional business lines. *Viet Nam* also revised the Law on Enterprises which, inter alia, simplifies the procedures for business registration, shortens the time frame to issue an Enterprise Registration Certification, and limits the time frame for capital contribution to 90 days.

Some countries introduced special economic zones (SEZs) or revised policies related to existing SEZs. *Ethiopia* extended various kinds of incentives for investment in industrial development zones and in manufacturing and agriculture. The *Republic of Korea* halved the minimum "foreign investment amount" and "factory construction area ratio" applied to foreign investors in "complex-type foreign investment areas". *Mozambique* approved the Mocuba Special Economic Zone in the Lugela District, which will be used for establishing agro-processing-driven industries in particular. *South Africa* introduced a "Special Economic Zone Act" providing for the designation, promotion, development, operation and management of SEZs.

As regards the general business environment, several countries reformed their tax systems. For instance, the *Russian Federation* amended its tax code, providing more favourable tax treatment in priority territories for social and economic development, and *Saudi Arabia* revised its income tax law, repealing joint tax liabilities of companies on capital gains. In terms of corporate income tax levels, a survey of 32 countries shows that 6 countries announced decreases in headline corporate income tax rates for 2014.

b. FDI liberalization ongoing – most active in Asian emerging economies

Several countries liberalized entry and establishment conditions for foreign investors. In most cases, they relaxed restrictions on foreign ownership limitations or opened up new business activities to foreign investment. As in previous years, countries in Asia were most active, in particular *China*, *India* and *Indonesia* – the three largest emerging economies in Asia. *India* liberalized foreign investment in railway infrastructure that was hitherto closed to FDI and raised the FDI cap in the defence sector from 26 per cent to 49 per cent. *Indonesia* increased the foreign investment cap in several industries, including for pharmaceuticals to 85 per cent from 75 per cent, for venture capital operations to 85 per cent from 80 per cent and for power plant projects carried out as public-private partnerships to 100 per cent from 95 per cent. *Kuwait* approved new rules permitting foreign banks to open multiple bank branches in the country. *Myanmar* removed 11 items from the prohibited list for foreign investors. These items are related to jade and gemstone prospecting, exploration and production; small- and medium-scale mineral production; and distribution of newspapers, magazines and journals in Burmese and other national ethnic languages.

Australia eased some foreign ownership restrictions on the Australian flag carrier Qantas. *Ethiopia* opened the electricity generation and distribution sector to private investors. *Mexico* established the regulatory framework for the participation of FDI up to 100 per cent in telecommunications and satellite communications, and up to 49 per cent in the broadcasting sector, subject to reciprocity from the country of the ultimate investor.

In 2015, *Canada* amended the Investment Canada Regulations. The amendments change how the value of an acquisition of a Canadian enterprise is assessed for acquisitions or sale by private investors from WTO countries; they gradually raise the threshold that triggers a review under the Investment Canada Act for acquisitions by foreign private investors. *China* revised its "Catalogue for the Guidance of Foreign Investment Industries". It stipulates in which industry sectors foreign investment is "encouraged", "restricted" or "prohibited". Compared with its predecessor, the revised catalogue lifts restrictions on foreign inward investment by reclassifying individual sectors, in particular in the manufacturing sector. *India* raised the

ceiling for foreign investment in insurance from 26 per cent to 49 per cent and authorised foreign investment in pension funds up to an ownership ceiling of 49 per cent. FDI up to 26 per cent is allowed in pension funds under the automatic route. Also, FDI in medical devices is now exempt from the rules applicable to the pharmaceutical industry, and 100 per cent FDI is permitted under the automatic route.

In addition to liberalizing investment, numerous countries improved business licensing conditions. For instance, *China* amended the Company Law. It applies to Chinese joint ventures with foreign investors. It removes the requirement that the contribution in cash by all shareholders be not less than 30 per cent of the registered capital of the company. *Côte d'Ivoire* adopted a new mining code which extends the permit holding period from 7 years to 10 years, with the possibility of prolonging the period by a further two years. *Mozambique* amended a law that allows the government to issue new gas and oil exploration licenses. *Myanmar* finalized the granting of telecommunications licenses to Telenor Myanmar and Ooredoo. *Rwanda* amended a law providing for a broader variety in the duration of mining licenses. *Viet Nam* permitted wholly foreign-invested enterprises to provide almost all types of logistical services in the country, subject to proper licensing.

Another important feature of investment liberalization in 2014 was privatization. *Cyprus* passed a new law on the privatization of semi-governmental organizations. *Serbia* adopted a Law on Privatization, setting the formal and institutional conditions for the continuation and completion of the restructuring and privatization process. *Turkmenistan* signed into law a bill titled “Denationalization and Privatization of State Property” which outlines the basic principles of denationalization (i.e. the transformation of State firms into joint-stock companies in which the State is a partner) and privatization (i.e. the transfer to private individuals of property rights in State assets in return for payment).

c. Some new investment restrictions or regulations – mainly on national security grounds and for strategic sectors

Some countries introduced new investment restrictions or regulations. They related mainly to national

security considerations, strategic sectors and land ownership.

France extended the coverage of the review mechanism for inward foreign investment to six additional activities: (i) energy supply (electricity, gas, hydrocarbons or other sources of energy), (ii) water supply, (iii) transport networks and services, (iv) electronic communications networks and services, (v) operations of buildings and installations for defence reasons and (vi) protection of public health. It applies to safeguarding national interests in public order, public security and national defence. *Italy* established procedures for the exercise of special powers by the government in connection with investments in the defence and national security sector, as part of a security-related investment review mechanism created in 2012. *Indonesia* reduced the foreign ownership ceiling in several industries. For example, onshore oil production facilities which foreign investors could own up to 95 per cent are no longer open to foreign investment and the foreign ownership ceiling for data communications system services was reduced from 95 per cent to 49 per cent. The *Russian Federation* extended coverage of its review mechanism to the transport sector and related services. The review mechanism applies to investments in business entities of strategic importance for national defence and state security. The country also amended the Federal Law on Foreign Investment in Commercial Entities with Strategic Importance for National Defence and National Security; it now covers acquisitions of property classified as fixed production assets in “strategic companies” if the value of these assets exceeds 25 per cent of the total value of the company’s assets.

In 2015, *Canada* amended its National Security Review of Investment Regulations to provide the government with the flexibility to extend time periods for the review of investments that could be injurious to national security.

Fiji amended the Land Sales Act to prevent any land within town boundaries from being sold to foreigners for residential purposes. It also requires foreigners who already own undeveloped land to build a house within two years. *Seychelles* discontinued the sale of state land to non-Seychellois.

d. Developments regarding investment for sustainable development

More private investor involvement in sectors and industries related to sustainable development is crucial to achieve the Sustainable Development Goals (SDGs) (WIR14). Private investment can play an important role in infrastructure development, health, education and climate change mitigation activities. This section provides a brief overview of recent investment policy developments in these areas, covering the period from 2010 to 2014.

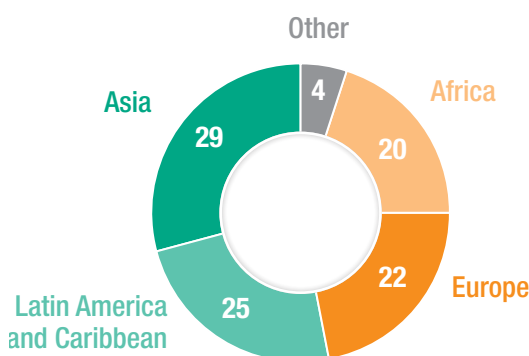
Thirty-two countries undertook 45 investment policy measures in one or several of the above-mentioned sectors or activities between 2010 and 2014. The share of such policy measures among all reported investment policy measures during this period is small – only approximately 8 per cent. Liberalization or promotion measures accounted for about three quarters, i.e. in their majority countries aimed to attract more private investment into SDG sectors.

By region, investment policy measures related to SDG sectors were reported mainly for countries in Asia, followed by countries in Latin America (figure III.2). Interestingly, all reported measures from Asian countries aim at improving entry conditions and facilitating foreign investment. For instance, *India* permitted foreign investment in diverse industries including railways, health and medical services. Another example is *Indonesia*, which liberalized the construction sector, health services and electricity generation.

By sector, investment policy measures related to infrastructure development (including roads, ports, airports, energy generation and distribution, water supply and sanitation) dominated (53 per cent). For example, numerous countries liberalized or facilitated private investment in energy generation and distribution as well as water supply. As shown in figure III.3, investment policies related to education came next (17 per cent). Investment measures related to health services were less prominent. For example, *China* allowed foreign investors to own hospitals in several regions as part of a pilot test, and the *Russian Federation* exempted education and health care services from the corporate profit tax.

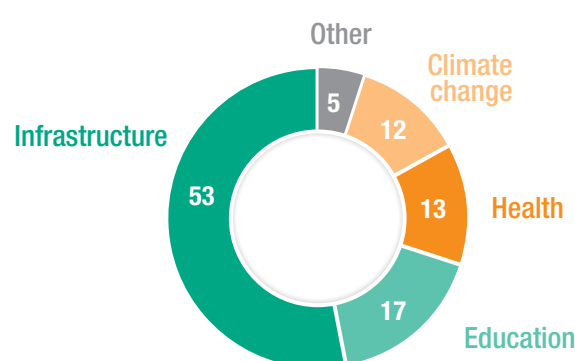
Overall, countries appear to have paid little attention so far to the importance of channelling investment into sectors that are particularly important for sustainable development, and more pro-active policy measures are needed to increase investment flows into these sectors. At the same time, it is important to keep in mind that liberalization and promotion policies related to investment in sectors related to sustainable development do not in themselves guarantee a positive development impact of the investment. It is equally important that host countries have in place a sound regulatory framework that seeks to maximize positive development impacts of investment and to minimize associated risks by safeguarding public interests in these politically sensitive sectors. This implies, in particular, balancing the need for attractive risk-return rates for investors with the need for accessible and affordable services (see WIR14).

Figure III.2. SDG-related investment policy measures by region, 2010–2014 (Per cent)



Source: UNCTAD, Investment Policy Monitor.

Figure III.3. SDG-related investment policy measures by sector, 2010–2014 (Per cent)



Source: UNCTAD, Investment Policy Monitor.

B. INTERNATIONAL INVESTMENT POLICIES

1. Trends in the conclusion of IIAs

The expansion of the IIA universe continues, with intensified efforts at the regional level.

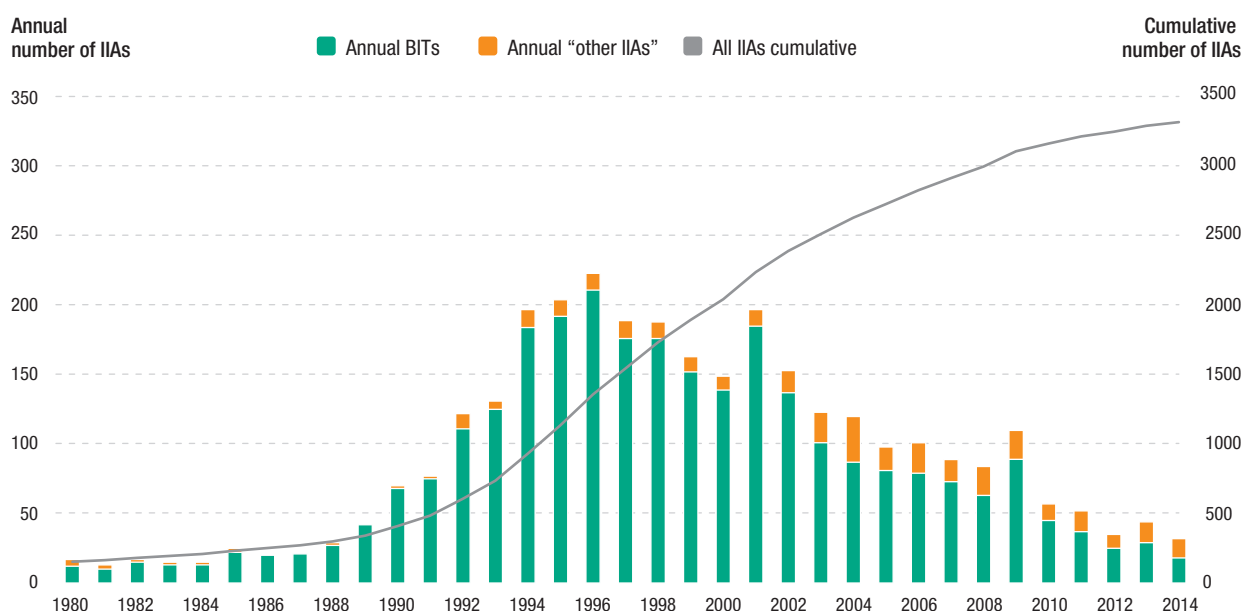
a. Overall trends

The conclusion in 2014 of 31 international investment agreements (IIAs) – 18 bilateral investment treaties (BITs) and 13 “other IIAs”² – brought the total number of IIAs to 3,271 (2,926 BITs and 345 “other IIAs”) by year-end (figure III.4). Between January and April 2015, five more treaties (of which three were BITs) were added. Most active in concluding IIAs in 2014 were Canada with seven and Colombia, Côte d’Ivoire and the European Union (EU) with three each. Overall, the annual number of “other IIAs” has remained stable over the past few years, while the annual number of BITs continues to decline (see annex).

“Other IIAs” signed between January 2014 and April 2015 can be grouped into the three broad categories identified in WIR12:

- *Eight agreements with BIT-equivalent provisions.* The Australia–Japan EPA, the Australia–Republic of Korea FTA, the Canada–Republic of Korea FTA, the Japan–Mongolia EPA, the Mexico–Panama FTA, the Additional Protocol to the Framework Agreement of the Pacific Alliance (between Chile, Colombia, Mexico and Peru), the Treaty on the Eurasian Economic Union (between Armenia, Belarus, Kazakhstan and the Russian Federation) and the Agreement on Investment under the Framework Agreement on Comprehensive Economic Cooperation between ASEAN and India fall in the category of IIAs that contain obligations commonly found in BITs, including substantive standards of investment protection and investor–State dispute settlement (ISDS). It should be noted that the Australia–Japan EPA does not provide for ISDS.
- *Five agreements with limited investment provisions.* The EU–Georgia Association Agreement, the EU–Moldova Association Agreement and the

Figure III.4. Trends in IIAs signed, 1980–2014



Source: UNCTAD, IIA database.

EU–Ukraine Association Agreement fall in the category of agreements that provide limited investment-related provisions (e.g. national treatment with respect to commercial presence or free movement of capital relating to direct investments). Also, the Cooperation and Facilitation Investment Agreements (CFIAs) signed by Brazil with Angola and Mozambique in 2015 (based on Brazil's new model – see below) belong to this category, as they emphasize investment promotion and facilitation while containing also a number of investment protection provisions – although no ISDS clause.

- *Two agreements with investment cooperation provisions and/or a future negotiating mandate.* The ECOWAS–United States Trade and Investment Framework Agreement (TIFA), and the Malaysia–Turkey FTA contain general provisions on cooperation in investment matters and/or a mandate for future negotiations on investment.

In 2014, 84 double taxation treaties (DTTs) were concluded. These treaties govern the fiscal treatment of cross-border investment operations between host and home States. The network of DTTs and BITs grew together, and there are now over 3,000 DTTs in force worldwide.³ In fact, two thirds of BIT relationships are also covered by a DTT (and half of DTT relationships are also covered by a BIT). Where two countries have both BITs and DTTs, in a quarter of cases they were signed in the same year, and in more than a third of cases within two years. DTTs have a separate settlement mechanism for disputes between investors and both home and host States (the mutual agreement procedure or MAP), which is generally considered weaker than the dispute settlement system for BITs. In some tax-related disputes, investors have resorted to BITs (e.g. *Vodafone v. India*).

b. IIA-related developments in 2014–2015

Several other developments beyond treaty-making left their mark on the IIA universe:

- Negotiations on megaregional agreements continued, involving close to 90 countries (*WIR14*). The ninth negotiating round of the TTIP took place in New York (20–24 April 2015). For the TPP negotiations, a series of meetings of chief negotiators and trade ministers took

place pursuant to the 19th round of negotiations that was held in Brunei (22–30 August 2013). The most recent TPP officials' meeting took place in Maryland, United States, from 23 to 26 April 2015. With regard to RCEP, the seventh round of negotiations took place in Thailand in February 2015, with investment discussions focusing on the approach to the scheduling of commitments. Concerning PACER, Fiji accepted the May 2014 Pacific Islands Forum Leaders' invitation to participate in the PACER Plus negotiations. The tenth inter-sessional negotiating meeting took place in Port Vila, Vanuatu (5–7 May 2015); parties intend to conclude the negotiations by July 2016. The third meeting of the COMESA–EAC–SADC Tripartite Technical Committee on movement of business persons was held in Mauritius (3–6 November 2014). The second phase of the Tripartite negotiations, scheduled for the second half of 2015, will focus on investment, trade in services, intellectual property rights, competition policy and consumer protection. The trilateral FTA is expected to be launched during the Third Tripartite Summit to be held in Egypt in June 2015.

- In January 2015, Italy gave official notice to the Energy Charter Treaty of its intent to withdraw from the treaty (the withdrawal will take effect in January 2016, but the treaty will apply for another 20 years to investments made before or at the day of withdrawal).
- In October 2014, African independent legal experts met in Djibouti to discuss and review the draft Pan African Investment Code (PAIC). This follows the 2008 African Union (AU) Commission mandate to “develop a comprehensive investment code for Africa with a view to promoting private sector participation”.
- At the 26th session of the UN Human Rights Council, held in Geneva 9–27 June 2014, a resolution drafted by Ecuador and South Africa and signed by Bolivia, Cuba and the Bolivarian Republic of Venezuela – and supported by 20 countries⁴ – called for the Council “to establish an open-ended intergovernmental working group with the mandate to elaborate an international legally binding instrument on Transnational Corporations and Other Business Enterprises with respect to human rights”. The Human Rights

Council adopted the resolution (by majority) on 26 June 2014 and decided that the working group should hold its first session in 2015.

- In May 2014, Ecuador, the Dominican Republic and the Bolivarian Republic of Venezuela presented a proposal to establish a Southern Observatory for investment assistance. The observatory's envisaged activities include to report periodically on the state of international investment disputes; identify procedures to monitor the action of international arbitration tribunals in investment; analyse and propose mechanisms to reform such arbitration proceedings; and promote the creation of mechanisms for coordination and mutual consultation between the judicial systems of Latin American countries to ensure the validity of national decisions on disputes between States and MNEs.

c. Countries and regions search for IIA reform

An increasing number of countries are reviewing their model IIAs in line with recent developments in international investment law. At least 50 countries or regions are currently revising or have recently revised their model IIAs. This trend is not limited to a specific group of countries or regions but includes at least 12 African countries, 10 countries from Europe and North America, 8 Latin American countries, 7 Asian countries and 6 economies in transition. In addition, at least 4 regional organizations have reviewed or are reviewing their models. Three new approaches (by Brazil, India and Indonesia) were revealed at the UNCTAD expert meeting on the Transformation of the IIA Regime, held in February 2015.⁵ In May 2015, the European Commission published a concept paper on "Investment in TTIP and beyond – the path for reform", the German Federal Ministry for Economic Affairs and Energy published a suggestion for a model investment protection treaty for developed countries, and Norway put forward a new draft model BIT for public consultation.

- Brazil's model CFIA has been developed on the basis of extensive domestic consultations, including with the private sector, and the experience of other countries and international organizations.⁶ The model's objectives of

promoting cooperation between the parties and facilitating and encouraging mutual investments are pursued through three main features: (i) the improvement of institutional governance, with the establishment of Focal Points and of a Joint Committee; (ii) the identification of ongoing agendas for investment cooperation and facilitation; and (iii) the creation of mechanisms for risk mitigation and dispute prevention. Focal Points (ombudsmen) act as intermediaries between investors and host States in order to solve problems related to investments and suggest improvements in the business environment. As such, they also act to prevent disputes and facilitate their resolution. The Joint Committee, made up of government representatives from both parties, shares information on investment opportunities in the two contracting parties, monitors the implementation of the agreement and solves possible disagreements in an amicable manner. The private sector can participate in Joint Committee hearings and ad hoc working groups. The CFIA also focuses on specific thematic agendas as a way of encouraging and promoting a business-friendly environment. This includes cooperation on business visas, corporate social responsibility (CSR), transfer of funds and transparency of procedures. In addition to these new features, the model includes substantive provisions dealing with expropriation, national treatment (subject to the applicable law) and most-favoured-nation (MFN) treatment, compensation for losses, and transparency. The model also includes a compulsory mechanism for dispute prevention prior to the establishment of a State-State arbitration procedure.

- The European Commission proposed new approaches to key IIA provisions related to the right to regulate and ISDS in its concept paper on "Investment in TTIP and beyond – the path for reform", launched in May 2015 (European Commission, 2015). The paper recognizes the achievements of the concluded negotiations with Canada and Singapore and addresses issues that could be further explored, as a result of the TTIP public consultations. Four areas are identified for such further improvement: (i) the protection of the right to regulate, (ii) the establishment and functioning of

arbitral tribunals, (iii) the review of ISDS decisions by an appellate body, and (iv) the relationship between domestic judicial systems and ISDS. Concretely, some of the notable suggestions concern the host State's right to regulate in the public interest; the paper suggests the inclusion of a treaty article expressly recognizing the right of States to take measures in pursuance of legitimate public policy objectives according to the level of protection they deem appropriate. For ISDS, the Commission's paper elaborates on arbitrator selection and qualifications, third-party submissions, and the establishment of a permanent bilateral appeals mechanism. The latter would review awards with respect to errors of law and manifest errors in the assessment of facts. The concept paper advances the idea that it could be modelled in good part on the basis of the WTO Appellate Body's institutional set-up. Finally, the proposal envisions the eventual creation of a permanent court and its possible multilateralization (European Commission, 2015).

- The German Federal Ministry for Economic Affairs and Energy made public in May 2015 a memorandum ("Gutachten") on a model BIT for developed countries with a functioning legal system (BMW, 2015). The model agreement addresses reform issues that arose during the TTIP consultation process. It intends to safeguard the State's right to regulate through public policy exceptions and provide options for conferring on foreign investors rights no greater than those enjoyed by domestic investors. For this reason, the model agreement circumscribes and clarifies the content of the fair and equitable treatment (FET) and of the expropriation standard with greater precision than the CETA draft. Notably, the model suggests the introduction of a new investment protection mechanism: a bilateral tribunal or court would be created for each specific treaty (e.g. EU-US Permanent Investment Tribunal) with judges pre-selected by the parties to the agreement and individual cases being assigned to the judges by abstract rules. The parties to the dispute would not have any influence on the composition of the panel of judges. This first instance would have exclusive jurisdiction to hear investment disputes arising under the agreement.

The proposed tribunal mechanism is complimented by a standing appellate body. This appellate body would as a second instance "undertake comprehensive scrutiny of the law and restricted scrutiny of the facts" in respect of the awards rendered by the first instance. Submission of a claim by an investor is subject to the exhaustion of domestic remedies, unless such remedies are unavailable or manifestly ineffective. An alternative suggestion conditions initiation of proceedings to the investor's waiver of any rights to start proceedings under national courts or tribunals.

- India made available its new draft model BIT for public comments, although the review process is not yet complete.⁷ The new model includes several innovative provisions: a detailed clarification of what is meant by "real and substantial business operations" under the definition of the term "enterprise"; a careful definition of the scope of the treaty; a national treatment provision applicable to investments in "like circumstances"; a new approach to the equitable treatment that lists State obligations, including a prohibition on the denial of justice, the duty to afford due process and the requirement to refrain from manifestly abusive treatment involving continuous, unjustified and outrageous coercion or harassment (without explicitly including a FET clause); a test for determining whether indirect expropriation occurred; and a free transfer of funds clause, subject to a detailed list of exceptions. It does not include an MFN clause. The model also includes provisions on investor obligations. It further contains a detailed investor-State dispute mechanism that provides for, among other matters, strict time frames for the submission of a dispute to arbitration, the selection of arbitrators and the prevention of conflict of interest. The model stipulates that investors must first submit their claim before the relevant domestic courts or administrative bodies for the purpose of pursuing domestic remedies, where available. If after exhausting all judicial and administrative remedies no resolution has been satisfactory to the investor within three years, the investor may commence a proceeding under the ISDS article by transmitting a notice of dispute to the respondent party.
- Indonesia has embarked on reforming its IIA policy on several fronts. The country has

initiated the termination of its BITs, while developing a new model BIT for (re)negotiation. The new model BIT will consider the exclusion of portfolio investment from the definition of investment and will add a contribution to economic development requirement in its definition clauses. National treatment will be subject to exceptions related to special treatment in favour of domestic small and medium enterprises and investments and measures affecting natural resources. The new model will also clarify in greater detail the scope of the FET standard and will provide a list of State obligations including a prohibition against denial of justice in criminal, civil or administrative proceedings and assurance of police protection from any physical harm. Finally, investor-State arbitration will be subject to host country consent. An investor may submit a case to international arbitration if the host country provides a specific consent letter.

- Norway developed a new draft model BIT and opened a public consultation in May 2015.⁸ The draft model circumscribes indirect expropriation, which may be found “[i]n rare circumstances”, by offering a list of elements that need to be taken into account in order to determine whether such an expropriation has taken place, e.g. the economic impact and duration of the measure and whether it interferes with “reasonable, investment-backed expectations” of investors. It contains exceptions relating to essential security interests, cultural policy, prudential regulation and taxation. The draft model BIT also establishes a joint committee that is tasked, among other things, with supervising the implementation of the agreement, attempting to resolve disputes regarding the interpretation of the agreement, working to remove barriers to investment, amending the agreement when necessary, and potentially adopting codes of conduct for arbitrators.

These new approaches converge in their attempt to modernize IIAs and further improve their sustainable development dimension. UNCTAD’s Investment Policy Framework, which represents a new generation of investment policies, has been widely used as a main reference in the above processes.

At the same time, countries continued to terminate their BITs. South Africa terminated its BITs with

Austria, Denmark and Germany, and discussions are ongoing with regard to new impending terminations of BITs. Indonesia discontinued 18 of its 64 BITs.⁹ Both countries are in the process of formulating a new strategy for international investment policies. Botswana and Namibia are currently reconsidering their approaches to BITs.

2. Content of new IIAs

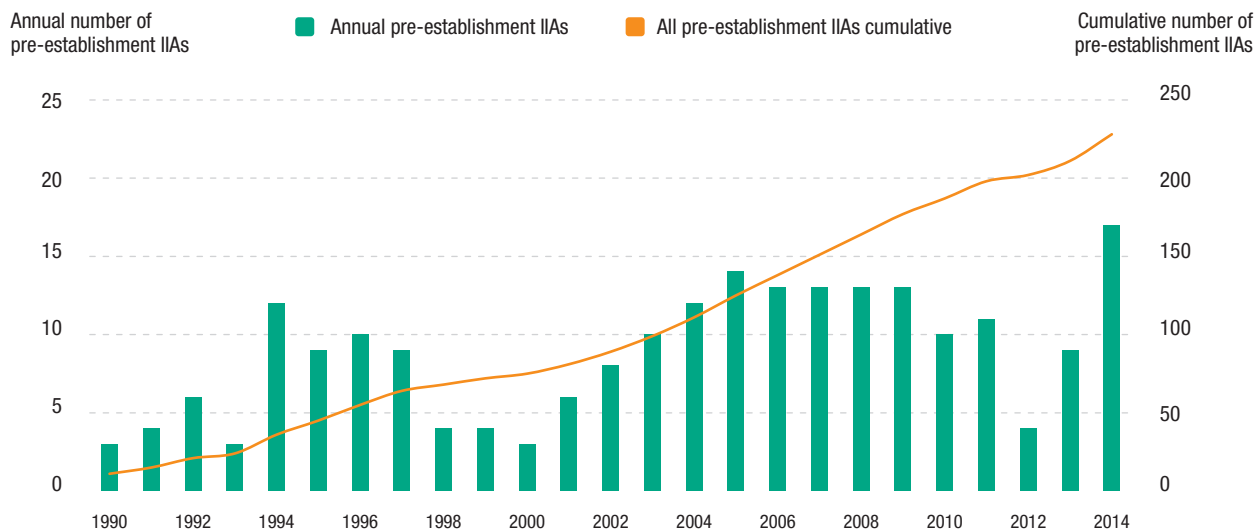
A small but growing number of IIAs include pre-establishment commitments; new treaties include provisions safeguarding the right to regulate for sustainable development objectives.

a. Pre-establishment IIAs are on the rise

In recent years, an increasing number of IIAs has included pre-establishment commitments, extending national treatment and MFN obligations to the “establishment, acquisition and expansion” of investments. By the end of 2014, pre-establishment IIAs totalled 228 (125 “other IIAs” and 103 BITs) (figure III.5), most of which involved developed economies, in particular the United States, Canada, Finland, Japan, and the EU (figure III.6). Taken together, these economies are party to 70 per cent of all pre-establishment IIAs signed worldwide. Also, a few developing countries in Asia and Latin America have also been actively concluding pre-establishment IIAs; they include Chile, Costa Rica, the Republic of Korea, Peru and Singapore.

Pre-establishment commitments in these IIAs use either a positive or a negative list approach. In addition, some treaties include a “market access” clause which prohibits certain non-discriminatory practices that can inhibit the right of establishment. The positive list approach offers selective liberalization by drawing up a list of industries in which investors enjoy pre-establishment rights, i.e. listing the industries or sectors where liberalization commitments are undertaken. The negative list approach offers liberalization across the board with the exception of those industries and sectors that are specifically listed, i.e. for which no liberalization commitments are made. In treaty practice to date, the negative list approach has been prevalent under both approaches, treaty obligations that are given a pre-establishment dimension (i.e. that apply to “establishment, acquisition and expansion” of investments) usually include national treatment, MFN

Figure III.5. Trends in pre-establishment IIAs signed, 1990–2014



Source: UNCTAD, IIA database.

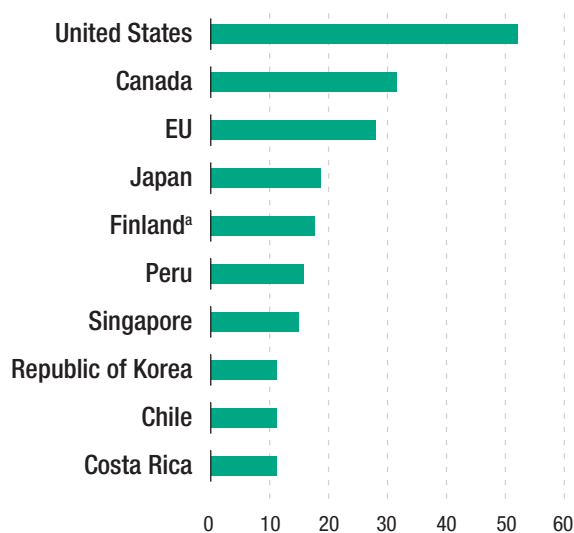
treatment, prohibition of performance requirements, and prohibition of nationality requirements for senior management and board members.

Countries frequently lodge reservations to these obligations to preserve (maintain) existing non-conforming measures (“standstill”) and/or to retain the right to adopt new non-conforming measures in the future. Reservations are particularly important when making commitments on a negative list basis because of its “list or lose” nature. They can take the form of sectoral reservations (for economic sectors, industries or activities); government-level reservations (for non-conforming measures adopted by a certain level of government, e.g. provincial or municipal); policy area reservations (e.g. for land rights, privatization, subsidies and other specific policy areas); and government procedure reservations (e.g. for screening and approval procedures for certain foreign investments).

In addition, some treaties include “safety valves” that allow parties to modify their reservation schedules after the treaty enters into force (subject to certain conditions). Furthermore, treaties sometimes exclude pre-establishment matters from the scope of ISDS so that any disputes on these issues are subject to State-State dispute resolution only.

The rise of pre-establishment IIAs is gradually moving policies related to the establishment of foreign

Figure III.6. Top signatories of pre-establishment IIAs (Number of agreements)



Source: UNCTAD, IIA database.

^a Excluding EU pre-establishment IIAs.

investment from the realm of the domestic regulatory framework of host countries to the international level. From the host-country perspective, pre-establishment commitments may improve the country’s

attractiveness as an investment destination, while from the home-country perspective, they help to “lock in” the existing level of openness, make the regulatory environment more transparent and, in some instances, open new investment opportunities. At the same time, making pre-establishment commitments requires a sophisticated domestic regulatory regime as well as sufficient institutional capacity to conduct a thorough audit of existing domestic policies and to consider possible future regulatory needs.

b. Provisions safeguarding the right to regulate for sustainable development objectives continue to be included

A review of 18 IIAs concluded in 2014 for which texts are available (11 BITs and 7 “other IIAs”) shows that most of the treaties include provisions safeguarding the right to regulate for sustainable development objectives, such as those identified in UNCTAD’s Investment Policy Framework for Sustainable Development (IPFSD) (table III.2). Of these agreements, 14 have general exceptions – for example, for the protection of human, animal or plant life or health, or the conservation of exhaustible natural resources. Another 14 treaties contain a clause that explicitly recognizes that the parties should not relax health, safety or environmental standards in order to attract investment. Twelve treaties refer to the protection of health and safety, labour rights, the environment or sustainable development in their preambles.

These sustainable development features are supplemented by treaty elements that aim more broadly at preserving regulatory space for public policies of host countries and/or at minimizing exposure to investment arbitration. These elements include clauses that (i) limit treaty scope (for example, by excluding certain types of assets from the definition of investment); (ii) clarify obligations (for example, by including more detailed clauses on FET and/or indirect expropriation); (iii) contain exceptions to transfer-of-funds obligations or carveouts for prudential measures; and (iv) carefully regulate ISDS (for example, by limiting treaty provisions that are subject to ISDS, excluding certain policy areas from ISDS, setting out a special mechanism for taxation and prudential measures, and/or restricting the allotted time period within which claims can be submitted). Notably, all but one of the treaties concluded in 2014 that were reviewed omit the so-called umbrella clause.

The inclusion of provisions safeguarding the right to regulate for sustainable development objectives does not translate to a reduced level of investment protection. Most of the IIAs signed in 2014 also included high investment protection standards.

3. Investment dispute settlement

There were fewer new ISDS cases, with a continued high share of cases against developed States.

a. Latest trends in ISDS

In 2014, investors initiated 42 known ISDS cases pursuant to IIAs (UNCTAD, 2015). This is lower than the record high numbers of new claims in 2013 (59 cases) and 2012 (54 cases) and closer to the annual averages observed in the period between 2003 and 2011. As most IIAs allow for fully confidential arbitration, the actual number is likely to be higher.

Last year’s developments brought the overall number of known ISDS claims to 608 (figure III.7). Ninety-nine governments around the world have been respondents to one or more known ISDS claims.

- *Respondent States.* The relative share of cases against developed States is on the rise. In 2014, 40 per cent of all cases were brought against developed countries. In total, 32 countries faced new claims last year. The most frequent respondent was Spain (5 cases), followed by Costa Rica, the Czech Republic, India, Romania, Ukraine and the Bolivarian Republic of Venezuela (2 cases each). Three countries – Italy, Mozambique and Sudan – faced their first (known) ISDS claims in history. Overall, Argentina, the Bolivarian Republic of Venezuela and the Czech Republic have faced the most cases to date (figure III.8).
- *Home country of investor.* Of the 42 known new cases in 2014, 35 were brought by investors from developed countries and 5 were brought by investors from developing countries. In two cases the nationality of the claimants is unknown. The most frequent home States were the Netherlands (with 7 cases brought by Dutch investors), followed by the United Kingdom and the United States (5 each), France (4), Canada (3) and Belgium, Cyprus and Spain (2 each). This corresponds to the historical trend in

Table III.2. Selected aspects of IIAs signed in 2014

Selected aspects of IIAs	Policy Objectives																							
	Sustainable development enhancing features	Focus on investments conducive to development	Preserve the right to regulate in the public interest	Avoid overexposure to litigation	Stimulate responsible business practices	Mexico–Panama FTA	Israel–Myanmar BIT	Treaty on Eurasian Economic Union	Japan–Kazakhstan BIT	Egypt–Mauritius BIT	Colombia–Turkey BIT	Colombia–France BIT	Canada–Serbia BIT	Canada–Senegal BIT	Canada–Nigeria BIT	Canada–Mali BIT	Canada–Republic of Korea FTA	Canada–Côte d'Ivoire BIT	Canada–Cameroun BIT	Australia–Republic of Korea FTA	Australia–Japan EPA	ASEAN–India Investment Agreement	Additional Protocol to the Framework Agreement of the Pacific Alliance	
References to the protection of health and safety, labour rights, environment or sustainable development in the treaty preamble	X	X	X		X			X	X	X		X	X	X	X	X	X	X	X	X	X	X	X	X
Refined definition of investment (reference to characteristics of investment; exclusion of portfolio investment, sovereign debt obligations or claims of money arising solely from commercial contracts)		X		X		X	X			X	X	X	X	X	X	X	X	X	X	X	X	X	X	X
A carve-out for prudential measures in the financial services sector			X	X	X			X		X	X	X	X	X	X	X	X	X	X	X	X	X	X	X
Fair and equitable treatment equated to the minimum standard of treatment of aliens under customary international law			X	X	X				X	X		X	X	X	X	X	X	X	X	X	X	X	X	X
Clarification of what does and does not constitute an indirect expropriation			X	X	X						X	X	X	X	X	X	X	X	X	X	X	X	X	X
Detailed exceptions from the free-transfer-of-funds obligation, including balance-of-payments difficulties and/or enforcement of national laws			X	X		X	X	X	X	X	X	X	X	X	X	X	X	X	X	X	X	X	X	X
Omission of the so-called “umbrella” clause				X	X	X	X		X	X	X	X	X	X	X	X	X	X	X	X	X	X	X	X
General exceptions, e.g. for the protection of human, animal or plant life or health; or the conservation of exhaustible natural resources	X		X	X	X				X	X		X	X	X	X	X	X	X	X	X	X	X	X	X
Explicit recognition that parties should not relax health, safety or environmental standards to attract investment	X	X			X	X	X	X		X	X	X	X	X	X	X	X	X	X	X	X			X
Promotion of Corporate and Social Responsibility standards by incorporating a separate provision into the IIA or as a general reference in the treaty preamble	X										X	X	X	X	X	X	X	X	X					X
Limiting access to ISDS (e.g. limiting treaty provisions subject to ISDS, excluding policy areas from ISDS, limiting time period to submit claims, no ISDS mechanism)			X	X	X			X	X	X	X	X	X	X	X	X	X	X	X	X	X	X	X	X

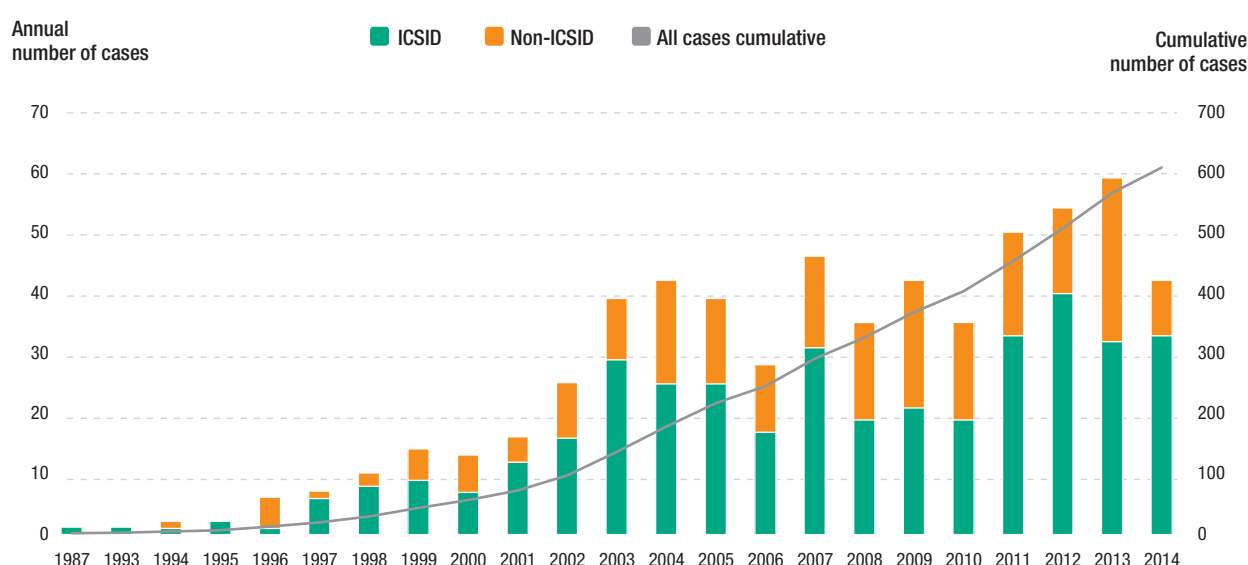
Source: UNCTAD.

Note: Based on IIAs concluded in 2014 for which the text was available; does not include “framework agreements”, which do not include substantive investment provisions.

which developed-country investors – in particular, those from the United States, Canada and a few EU countries – have been the main ISDS users, responsible for over 80 per cent of all claims (figure III.9).

- *Intra-EU disputes.* A quarter of all known new disputes (11) are intra-EU cases, which is lower than the year before (in 2013, 42 per cent of all new claims were intra-EU cases). Half of them were brought pursuant to the Energy Charter Treaty, and the rest on the basis of intra-EU BITs. The year's developments brought the overall number of intra-EU investment arbitrations to 99, i.e. approximately 16 per cent of all cases globally.
- *Arbitral forums and rules.* Of the 42 new known disputes, 33 were filed with the International Centre for Settlement of Investment Disputes (ICSID) (three of them under the ICSID Additional Facility Rules), 6 under the arbitration rules of UNCITRAL, 2 under the arbitration rules of the Stockholm Chamber of Commerce (SCC) and 1 under those of the International Chamber of Commerce. These numbers are roughly in line with overall historical statistics.
- *Applicable investment treaties.* The majority of new cases (30) were brought under BITs. Ten cases were filed pursuant to the provisions of the Energy Charter Treaty (twice in conjunction with a BIT), two cases under the Central America–Dominican Republic–United States Free Trade Agreement (CAFTA), one case under the North American Free Trade Agreement (NAFTA) and one case under the Canada–Peru FTA. Looking at historical statistics, the Energy Charter Treaty has now surpassed the NAFTA as the IIA invoked most frequently (60 and 53 cases, respectively). Among BITs, the Argentina–United States BIT remains the agreement most frequently used (20 disputes).
- *Economic sectors involved.* About 61 per cent of cases filed in 2014 relate to the services sector. Primary industries account for 28 per cent of new cases, while the remaining 11 per cent arose out of investments in manufacturing.
- *Affected sustainable development sectors.* A number of ISDS claims concerned key sustainable development sectors such as infrastructure and climate-change mitigation, including, in particular,

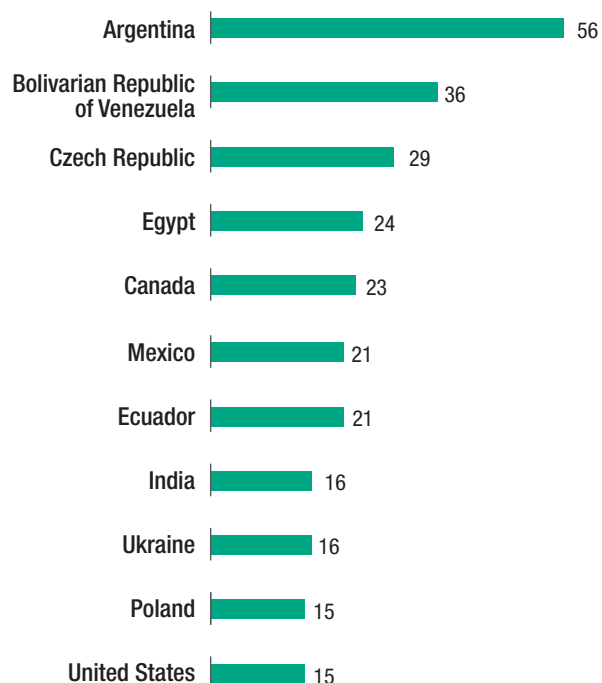
Figure III.7. Known ISDS cases, annual and cumulative, 1987–2014



Source: UNCTAD, ISDS database.

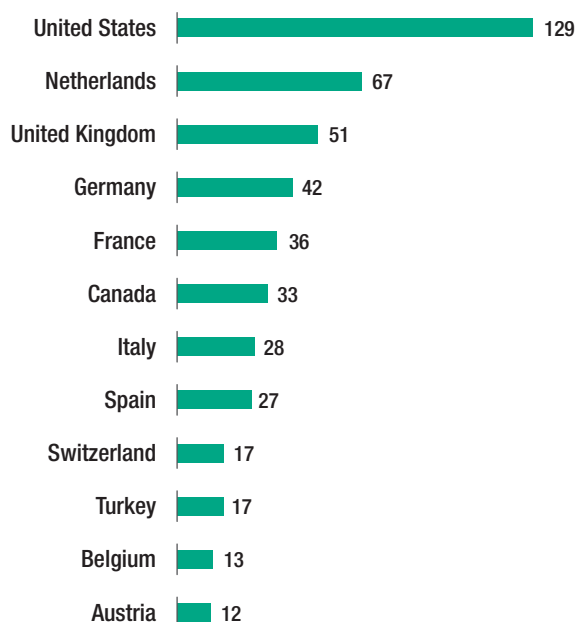
Note: Information about 2014 claims has been compiled on the basis of public sources, including specialized reporting services. This part does not cover cases that are based exclusively on investment contracts (State contracts) or national investment laws, or cases in which a party has signaled its intention to submit a claim to ISDS but has not commenced the arbitration. Annual and cumulative case numbers are continuously adjusted as a result of verification and may not exactly match case numbers reported in previous years.

Figure III.8. Most frequent respondent States, total as of end 2014
(Number of known cases)



Source: UNCTAD, ISDS database.

Figure III.9. Most frequent home States of claimants, total as of end 2014
(Number of known cases)



Source: UNCTAD, ISDS database.

the supply of electricity, gas and water, port modernization, and the regulation of renewable energy producers. A number of cases involved measures taken by governments on environmental grounds.

- Measures challenged.* The two types of State conduct most frequently challenged by investors in 2014 were (i) cancellations or alleged violations of contracts or concessions (at least nine cases), and (ii) revocation or denial of licenses or permits (at least six cases). Other challenged measures included legislative reforms in the renewable energy sector, alleged discrimination against foreign investors relative to domestic ones, alleged direct expropriations of investments, alleged failure on the part of the host State to enforce its own legislation and alleged failure to protect investments, as well as measures related to taxation, regulation of exports, bankruptcy proceedings and water tariff regulation. Information about a number of cases is lacking. Some of the new cases concern public policies, including environmental issues, anti-money laundering and taxation.
- Amounts claimed.* Information regarding the amounts sought by investors is scant. For cases where this information has been reported, the amount claimed ranges from \$8 million to about \$2.5 billion.

b. ISDS outcomes

In 2014, ISDS tribunals rendered at least 43 decisions in investor-State disputes, 34 of which are in the public domain (at the time of writing). Of these public decisions, 11 principally addressed jurisdictional issues, with 6 decisions upholding the tribunal's jurisdiction (at least in part) and 5 decisions rejecting jurisdiction. Fifteen decisions on the merits were rendered in 2014, with 10 accepting – at least in part – the claims of the investors, and 5 dismissing all of the claims. The other 8 public decisions relate to annulments and preliminary objections.

Of the 10 decisions finding the State liable, 6 found a violation of the FET provision and 7 a violation of the expropriation provision. At least 8 decisions rendered in 2014 awarded compensation to the investor, including a combined award of approximately \$50 billion in 3 closely related cases, the highest known

award – by far – in the history of investment arbitration. Five decisions on applications for annulment were issued in 2014 by ICSID *ad hoc* committees, all of them rejecting the application for annulment.

Ten cases were reportedly settled in 2014, and another five proceedings discontinued for unknown reasons.

By the end of 2014, the overall number of concluded cases had reached 405. Out of these, 36 per cent (144 cases) were decided in favour of the State (all claims dismissed either on jurisdictional grounds or on the merits), and 27 per cent (111 cases) ended in favour of the investor (monetary compensation awarded). Approximately 26 per cent of cases (105) were settled and 9 per cent of claims (37) discontinued for reasons other than settlement (or for unknown reasons). In the remaining 2 per cent (8 cases), a treaty breach was found but no monetary compensation was awarded to the investor (figure III.10).

Out of the 144 decisions that ended in favour of the State, almost half (71 cases) were dismissed by tribunals for lack of jurisdiction.¹⁰

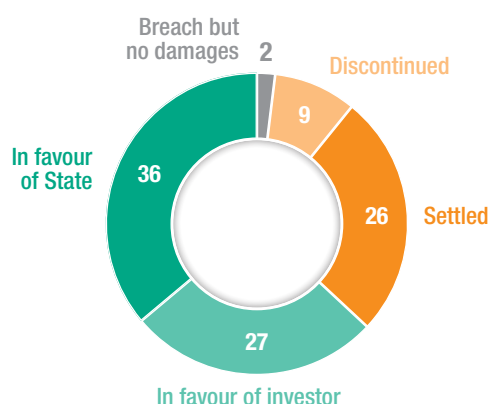
Looking at the decisions on the merits only, 60 per cent were decided in favour of the investor, and 40 per cent in favour of the State (figure III.11).

c. Other developments in ISDS

In 2014 and early 2015, a number of multilateral developments related to ISDS took place:

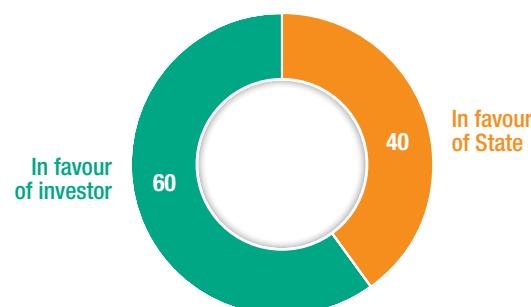
- *The UNCITRAL Rules on Transparency in Treaty-based Investor-State Arbitration came into effect on 1 April 2014.* The UNCITRAL Transparency Rules provide for open oral hearings in ISDS cases as well as the publication of key documents, including notices of arbitration, pleadings, transcripts, and all decisions and awards issued by the tribunal (subject to certain safeguards, including protection of confidential information). By default (in the absence of further action), the Rules apply only to UNCITRAL arbitrations brought under IIAs concluded after 1 April 2014, and thus exclude the pre-existing IIAs from their coverage.
- *The United Nations General Assembly adopted the Convention on Transparency in Treaty-based Investor-State Arbitration on 10 December 2014.* The aim of the Convention is to give those States (as well as regional economic integration organizations) that wish to make the UNCITRAL Transparency Rules applicable to their existing

Figure III.10. Results of concluded cases, total as of end 2014
(Per cent)



Source: UNCTAD, ISDS database.

Figure III.11. Results of decisions on the merits, total as of end 2014
(Per cent)



Source: UNCTAD, ISDS database.

Note: Excluding cases (1) dismissed by tribunals for lack of jurisdiction, (2) settled, (3) discontinued for reasons other than settlement (or for unknown reasons), and (4) in which a treaty breach was found but no monetary compensation was awarded to the investor.

IAs a mechanism to do so. Specifically, and in the absence of reservations by the signatories, the Transparency Rules will apply to disputes where (i) both the respondent State and the home State of the claimant investor are parties to the Convention; and (ii) only the respondent State is party to the Convention but the claimant investor agrees to the application of the Rules. A signing ceremony was held on 17 March 2015 in Port Louis, Mauritius, opening the convention for signature, and by mid-May 2014, 11 countries had signed.¹¹

- *On April 18, 2015, the Republic of San Marino deposited its Instrument of Ratification of the ICSID Convention with the World Bank. San Marino signed the ICSID Convention on 11 April 2014. The ratification marks the last step in the membership process for San Marino to become an ICSID Contracting State.*

Notes

¹ For more information about these investment policy measures, please visit UNCTAD's Investment Policy Hub at <http://investmentpolicyhub.unctad.org>. Percentage figures exclude "neutral" measures.

² "Other IAs" refers to economic agreements other than BITs that include investment-related provisions, e.g. investment chapters in economic partnership agreements (EPAs) and free trade agreements (FTAs), regional economic integration agreements and framework agreements on economic cooperation.

³ Based on International Bureau of Fiscal Documentation (IBFD) database. www.ibfd.org.

⁴ Algeria, Benin, Burkina Faso, China, the Congo, Côte d'Ivoire, Cuba, Ethiopia, India, Indonesia, Kazakhstan, Kenya, Morocco, Namibia, Pakistan, the Philippines, the Russian Federation, South Africa, the Bolivarian Republic of Venezuela and Viet Nam.

⁵ <http://unctad-worldinvestmentforum.org/followup-events/media-center/>.

⁶ Brazil signed 14 BITs in the 1990s; however none of these treaties entered into force.

⁷ The new draft Indian model BIT is available at <https://mygov.in/group-issue/draft-indian-model-bilateral-investment-treaty-text/>.

⁸ See <https://www.regjeringen.no/nb/dokumenter/horing---modell-for-investeringsavtaler/id2411615/>.

⁹ Between January 2014 and May 2015, Indonesia sent notices of termination to Bulgaria, Cambodia, China, Egypt, France, Hungary, India, Italy, Kyrgyzstan, the Lao People's Democratic Republic, Malaysia, the Netherlands, Romania, Singapore, Slovakia, Spain, Turkey and Viet Nam.

¹⁰ These are cases in which a tribunal found, for example, that the asset/transaction did not constitute a "covered investment", that the claimant was not a "covered investor", that the dispute arose before the treaty entered into force or fell outside the scope of the ISDS clause, that the investor had failed to comply with certain IIA-imposed conditions (e.g. the mandatory local litigation requirement) or other reasons for dismissal.

¹¹ Canada, Finland, France, Germany, Italy, Mauritius, Sweden, Switzerland, the Syrian Arab Republic, the United Kingdom and the United States.

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Reforming the International Investment Regime: An Action Menu

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INTRODUCTION

Growing unease with the current functioning of the global international investment agreement (IIA) regime, together with today's sustainable development imperative, the greater role of governments in the economy and the evolution of the investment landscape, have triggered a move towards reforming international investment rule making to make it better suited for today's policy challenges. As a result, the IIA regime is going through a period of reflection, review and revision.

As evident from UNCTAD's October 2014 World Investment Forum (WIF), from the heated public debate taking place in many countries, and from various parliamentary hearing processes, including at the regional level, a shared view is emerging on the need for reform of the IIA regime to ensure that it works for all stakeholders. The question is not about *whether* to reform or not, but about the *what, how* and *extent* of such reform.

WIR15 responds to this call by offering an action menu for IIA reform. It builds on UNCTAD's earlier work in this area, including UNCTAD's Investment Policy Framework (*WIR12*), UNCTAD's reform paths for investment dispute settlement (*WIR13*), and its reform paths for IIA reform (*WIR14*), as well as on contributions by others.

The chapter addresses *five main reform challenges* (safeguarding the right to regulate for pursuing sustainable development objectives, reforming investment dispute settlement, promoting and facilitating investment, ensuring responsible investment, and enhancing systemic consistency). It offers policy options for *key areas of IIA reform* (i.e. substantive IIA clauses, investment dispute settlement, and systemic issues) and for *different levels of reform-oriented policymaking* (national, bilateral, regional and multilateral).

The policy options provide reform-oriented formulations for standard IIA elements. They include mainstream IIA provisions as well as more idiosyncratic options that have so far been used by fewer countries or are only found in model agreements.

This *WIR* takes a *holistic approach*. It covers, in a single chapter, all the key aspects of IIA reform (i.e. substantive, procedural and systemic). It identifies reform *objectives, areas* and *solutions* in the form of an *action menu*, outlining a common *road map* for the reform process and inviting countries to use the action menu and to define their own, individual road maps for IIA reform.

This *WIR* takes an *approach that focuses on policy coherence*. It proposes that reform be guided by the need to harness IIAs for sustainable and inclusive growth. It suggests that the investment promotion and facilitation function of IIAs should go hand in hand with their function of protecting investment. And, it emphasizes that IIAs must be coherently embedded in countries' overall sustainable development strategies.

Finally, this *WIR* stresses the importance of a *multilateral approach* towards IIA reform. Given the large number of existing IIAs, the only way to make the IIA regime work for all is to collectively reform its components. In today's dynamic environment, where one change reverberates throughout the whole system, it is important to work towards a common vision and common rules of engagement. Only a common approach can ensure that reform does not lead to further fragmentation and incoherence, but is for the benefit of all, without leaving anyone behind. And only a common approach will deliver an IIA regime in which stability, clarity and predictability help achieve the objectives of all stakeholders, effectively harnessing international investment relations for the pursuit of sustainable development.

The chapter first takes stock of 60 years of international investment rule making, draws lessons learned and identifies today's reform needs and objectives. It then develops the design criteria and strategic choices, pinpoints the reform areas and tools, and advances detailed policy options for reform in the five identified reform objectives. The chapter closes with Guidelines for IIA Reform and suggested possible actions and outcomes at the national, bilateral, regional, and multilateral levels.

A. SIX DECADES OF IIA RULE MAKING AND LESSONS LEARNED

1. Six decades of IIA rule making

International investment agreements (IIAs) – like most other treaties – are a product of the time when they are negotiated.

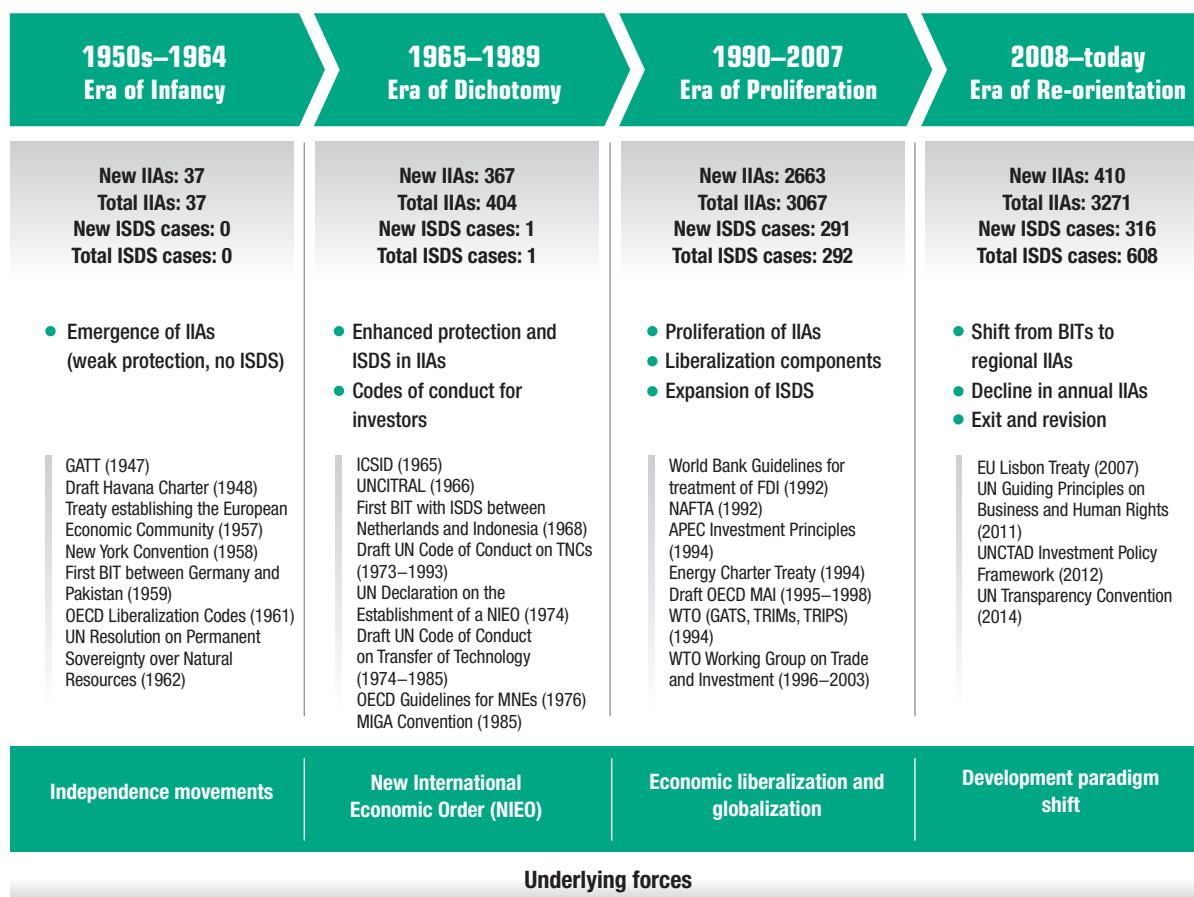
IIAs are concluded in a specific historic, economic and social context and respond to the then-existing needs and challenges. As more than half a century has passed since the first bilateral investment treaty (BIT) was concluded, it is no surprise that IIAs have gone through a significant evolutionary process during this period. Four main phases can be identified (figure IV.1).

a. Era of infancy (end of World War II until mid-1960s)

The BIT is born as a new type of instrument concluded between developed and developing countries, although with relatively few investment protections and without ISDS. The ICSID Convention is signed, later to become the main piece of ISDS infrastructure.

In the first half of the 20th century, customary international law (CIL) was the primary source of international legal rules governing foreign investment. The emergence of a number of major investment disputes

Figure IV.1. Evolution of the IIA regime



Source: UNCTAD.

Note: Years in parentheses relate to the adoption and/or signature of the instrument in question.

between foreign investors and their host countries after 1945¹ showed the significant limitations of protection afforded under CIL and through the system of home-State diplomatic protection, and triggered a move towards international investment treaty making.

A first attempt at multilateral investment rules was made in 1948 within the framework of the proposed Havana Charter, designed to establish an International Trade Organization. With respect to investment negotiations, developed, developing and socialist countries could not agree on the interpretation of customary international law and the content of an international minimum standard of treatment for foreign investors. The Charter never entered into force despite the fact that it was intended to supplement the other building stones of the post-war international economic order consisting of the Bretton Woods Institutions (1944) and the United Nations (1945) (UNCTAD, 2008). This earlier era of IIAs reflected the split between market economies (where private property was recognized) and countries under communist rule (where private property was not recognized).

Somewhat greater success was achieved through regional or plurilateral instruments that dealt with the establishment and treatment of foreign investment. The 1957 Treaty establishing the European Economic Community included the freedom of establishment and the free movement of capital as core pillars of European integration. Other early examples include the OECD Code of Liberalization of Capital Movements and Code on Current Invisible Operations of 1961.

In 1959, the first bilateral investment treaty (BIT), between Germany and Pakistan, was signed, following the example of existing bilateral treaties of “friendship, commerce and navigation” concluded by a number of countries in the inter-war years and following World War II. From that time on, BITs became the main instrument to govern investment relationships among countries of different levels of economic development. In terms of content, the BITs (or IIAs) had a focus on protection against expropriation and nationalization, as investors from developed countries perceived expropriation and nationalization as the main political risks when investing in developing countries. To a considerable extent, these first-generation BITs resembled the 1959 Abs-Shawcross Draft Convention on Investments Abroad, a private initiative, and the 1962 OECD Draft Convention on the Protection of Foreign Property

(revised and adopted in 1967 but never opened for signature) (Vandevelde, 2010).²

Another landmark development was the establishment of the International Centre for Settlement of Investment Disputes (ICSID) in 1965, providing a specialized facility for the resolution of investment disputes between investors and host States. In 1958, the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards was concluded, facilitating the enforcement of international arbitral awards.

b. Era of dichotomy (mid-1960s until late 1980s)

Investment protections in BITs are enhanced, including by adding ISDS provisions. At the same time, multilateral attempts to establish rules on investor responsibilities fail.

On the one hand, from the mid-1960s to the late 1980s, IIAs expanded in number and substance, although at a relatively slow pace and with the participation of a limited number of countries. The main signatories of IIAs during this period were developed countries from Europe and those developing countries – including in Africa, Asia and Latin America – that considered FDI an important contribution to their economic development strategies. Many countries, however – among them the Soviet Union, countries in Central and Eastern Europe, China, India and Brazil – stayed out of the IIA regime altogether or joined only at a relatively late stage. At the end of the 1980s, the global IIA regime consisted of fewer than 400 BITs.

In terms of substance, the main development in IIAs was the increasing inclusion of ISDS provisions. The earliest known example of ISDS is the BIT between Indonesia and the Netherlands of 1968. Several other countries followed in the 1970s and 1980s, until ISDS became a standard provision in BITs from the 1990s onward. Investment protection was also strengthened in other substantive provisions.

On the other hand, during this period, there were multilateral attempts towards strengthening States’ sovereign powers and towards emphasizing investor responsibilities. These policies were backed by two UN Resolutions, one on “Permanent Sovereignty over Natural Resources” in 1962 and one on “Establishment of a New Economic Order” in 1974.

In addition, in the early 1970s, a second attempt to establish multilateral investment rules was launched when the UN initiated negotiations on a Code of Conduct on Transnational Corporations and a Code of Conduct on the Transfer of Technology. However, no solution could be found for how to reconcile the interests of developed countries in establishing strong and unambiguous protection for international investment, and the interests of developing and socialist countries in preserving a maximum of their sovereign right to treat multinational enterprises (MNEs) according to their own laws and regulations. Although these negotiations proved unsuccessful, the “Set of Multilaterally Agreed Equitable Principles and Rules for the Control of Restrictive Business Practices” was adopted by the General Assembly in 1980.

c. Era of proliferation (1990s until 2007)

The global IIA regime expands at great speed. BITs signed are broadly similar, although some countries add the investment liberalization component. In the late 1990s, investors “discover” ISDS; the fast-growing number of claims reveal the true “power” of IIAs as well as some of their inherent problems.

IIA rule making – and international economic cooperation in general – substantially gained momentum in the 1990s. The fall of the Berlin Wall in 1989 and the dissolution of the Soviet Union caused a tectonic shift in geopolitics, in which political confrontation and economic separation gave way to political cooperation and economic integration. The transformation of former communist States brought about their recognition of private property. A few years earlier, China had adopted its “Open Door” policy with the explicit aim of attracting foreign investment for its economic development. These events significantly contributed to economic globalization, with a large and growing number of developing countries opening up to and actively competing for foreign investment, and more and more investors from developed countries seeking production locations abroad to reduce costs and gain market access.

The universe of BITs expanded rapidly, with almost three new agreements signed per week on average. Although only 381 BITs existed at the end of the 1980s, their number multiplied by five throughout the next decade to reach 2,067 by end of 2000. Most countries, both developed and developing, considered participation in

the IIA regime as a “must” in the global competition for foreign investment, so that by the mid-2000s hardly any country did not have at least a few BITs. Countries such as China and India, with enormous potential as both recipients and source of FDI, rapidly expanded their treaty networks. Brazil signed several IIAs but never ratified them.

In parallel, regional and plurilateral IIA rule making increased substantially. A landmark event was the establishment of the WTO in 1994, with several WTO agreements containing rules applicable to foreign investment (GATS, TRIMs, TRIPS). In the same year, the Energy Charter Treaty was concluded; today it comprises more than 50 contracting parties from Europe, Asia and Oceania, and contains detailed investment provisions as one of its pillars. At the regional level, countries concluded the North American Free Trade Agreement (NAFTA) (1992) and adopted the APEC Non-Binding Investment Principles (1994). Within the OECD, negotiations took place on the Multilateral Agreement on Investment (MAI) from 1995 to 1998. However, unexpected differences emerged on core principles of investment protection (e.g. investment definition, degree of investment liberalization, indirect expropriation, ISDS, cultural exception, labour and environmental issues) which resulted in the ultimate demise of the undertaking.

At the multilateral level, the Convention Establishing the Multilateral Investment Guarantee Agency (MIGA), as a member of the World Bank Group, was concluded in 1985 and the World Bank Guidelines on the Treatment of Foreign Direct Investment were launched in 1992 (UNCTAD, 2004). Within the WTO, the 1996 Singapore Ministerial Conference initiated a work programme on the relationship between international trade and investment; due to diverging interests in investment negotiations and in other policy areas the programme was abandoned after the Fifth Ministerial Conference (held in 2003 in Cancún, Mexico).

While the vast majority of BITs concluded in this period covered only the post-establishment phase of investment, many free trade agreements (FTAs) went one step further and included in their investment (and/or services) chapters commitments on non-discriminatory treatment of establishment by foreign investors as a means to facilitate market access. The 1990s also witnessed the start of a move towards renegotiating first-generation BITs with the objective of

further enhancing investment protection by including protection elements hitherto missing. In 1990, the first award in a treaty-based case was issued.³ This was followed by a number of new cases during the 1990s and a rapid increase in the 2000s (chapter III).

d. Era of re-orientation (2008 until today)

The “IIA rush” of the 1990s gradually slows down. Many countries refine treaty content. States’ increased exposure to ISDS cases, the global financial crisis, a paradigm shift towards “sustainable development” and important changes at regional levels mark the beginnings of a concerted move towards IIA reform.

By April 2015, the IIA regime had grown to close to 3,300 treaties. Several developments in the second half of the 2000s lead to a new era of IIA rule making, which can be characterized as a period of reorientation.

The experience of Canada and the United States as respondents in NAFTA investment arbitrations, prompted them to create, already in 2004, new Model BITs aimed at clarifying the scope and meaning of investment obligations, including the minimum standard of treatment and indirect expropriation. In addition, these new models included specific language aimed at making it clear that the investment protection and liberalization objectives of IIAs must not be pursued at the expense of the protection of health, safety, the environment and the promotion of internationally recognized labour rights. Canada and the United States also incorporated important innovations related to ISDS proceedings such as open hearings, publication of related legal documents and the possibility for non-disputing parties to submit amicus curiae briefs to arbitral tribunals. Also included, following on from NAFTA, were special regimes of substantive protection and dispute resolution for investments in the financial services industry, as well as specialized mechanisms for disputes by investors based on host-country tax measures. The United States Model BIT was slightly revised in 2012.

The global financial and economic crisis that broke out in September 2008 – following the Asian and Argentine financial crises a number of years before – emphasized the importance of solid regulatory frameworks for the economy, including for investment. Growing dissatisfaction with the existing IIA regime and its impact on contracting parties’ regulatory powers to pursue public interests and to enhance sustainable

development led countries to reflect on, review and reconsider their policies relative to IIAs.

The rise in ISDS cases, from 326 in 2008 to 608 known cases at the end of 2014, involving both developed and developing countries as defendants, contributed to this development (UNCTAD, 2015). In addition, investment disputes became more complex, raising difficult legal questions about the borderline between permitted regulatory activities of the State and illegal interference with investor rights for which compensation has to be paid. At the same time, as the number of ISDS cases began to rise sharply, so did the amount of compensation sought by investors in their claims and awarded by arbitral tribunals in a number of high-profile cases.

Accordingly, governments have entered into a phase of evaluating the costs and benefits of IIAs and reflecting on their future objectives and strategies as regards these treaties. Mounting criticism from civil society plays a role as well. As a result, several countries have embarked on a path of IIA reform by revising their BIT models with a view to concluding “new generation” IIAs and renegotiating their existing BITs. This move is based in part on UNCTAD’s Investment Policy Framework for Sustainable Development (IPFSD), which was developed to provide guidance to the reform of investment policies at the national and international levels and which is increasingly being used by developing and developed countries (box IV.1 and chapter III). Countries have started to clarify and “tighten” the meaning of individual IIA provisions and to improve ISDS procedures, with the objective of making the process more elaborated, predictable and transparent and of giving contracting parties a stronger role therein. Improved transparency is also the outcome of the recently adopted UNCITRAL Rules on Transparency in Treaty-based Investor-State Arbitration and the UN Transparency Convention (see chapter III).

Other countries, by far a smaller group, have announced a moratorium on future IIA negotiations, while still others have chosen a more radical approach by starting to terminate existing IIAs. A few countries have also renounced their membership in ICSID (UNCTAD, 2010a).

Although bilateral treaty making lost much of its dynamism, regional IIA making accelerated (see chapter III). This is partially a reaction to the failure to establish

Box IV.1

UNCTAD's Investment Policy Framework for Sustainable Development (IPFSD)

UNCTAD's Investment Policy Framework for Sustainable Development (IPFSD) (UNCTAD, 2012a), the special theme of *WIR12*, responds to the recognition that at a time of persistent crises and pressing social and environmental challenges, mobilizing investment and ensuring that it contributes to sustainable development objectives is a priority for all countries. In so doing, the UNCTAD Framework built on the emerging new generation of investment policies.

The Framework first details the drivers of change in the investment policy environment and the challenges that need to be addressed; it then proposes a set of Core Principles for investment policymaking which serve as “design criteria” for national and international investment policies. On this basis it presents guidelines for national investment policies and policy options for the formulation and negotiation of IIAs. UNCTAD's IPFSD has since served as a reference point for policymakers in formulating national investment policies and negotiating IIAs, as a basis for building capacity on investment policies, and as a point of convergence for international cooperation on investment issues.

Source: UNCTAD.

multilateral investment rules, leaving regional approaches as a “second best solution”. In addition, the entry into force of the Treaty of Lisbon in December 2009 triggered a trend towards intensifying and upscaling regional IIA treaty making. By transferring competence in FDI from the EU member States to the EU, with potential implications for almost half of the IIA universe, the Treaty of Lisbon enables the EU to negotiate IIAs with post-establishment provisions (earlier, EU treaties only covered pre-establishment). Examples are the Canada–EU Comprehensive Economic and Trade Agreement (CETA, draft 2014), the EU–Singapore Free Trade Agreement, and negotiations for the EU–United States Transatlantic Trade and Investment Partnership (TTIP). Outside the EU, megaregional negotiations are ongoing for the Trans-Pacific Partnership (TPP), the Regional Comprehensive Economic Partnership Agreement (RCEP), and negotiations for the COMESA-EAC-SADC Tripartite Agreement (chapter III). For IIA treaty making, regionals and, even more so, megaregionals offer opportunities to consolidate today's multifaceted and multilayered treaty network. However, without careful drafting, they can also create new inconsistencies resulting from overlaps with existing agreements (*WIR14*).

2. Lessons learned

IIA reform can build on lessons learned from 60 years of IIA rule making.

Sixty years of IIA rule making reveal a number of lessons on how IIAs work in practice and what can be learned for future IIA rule making.

The expected key function of IIAs is to contribute to predictability, stability and transparency in investment relations, and to help to move investment disputes

from the realm of State-to-State diplomatic action into the realm of law-based dispute settlement and adjudication. IIAs can help improve countries' regulatory and institutional frameworks, including by adding an international dimension to them and, by promoting the rule of law and enhancing good governance. IIAs can reduce risks for foreign investors (i.e. act as an insurance policy) and, more generally, contribute to improving the investment climate. Through all of this, IIAs can help facilitate cross-border investment and become part of broader economic integration agendas, which, if managed properly, can help achieve sustainable development objectives. At the same time, experience has shown that IIAs “bite” (i.e. their protection provisions can and have been enforced by arbitral tribunals at sometimes huge costs to the State), and that – like any other international treaty – they limit the regulatory space of the contracting parties. As a result, concerns have been raised that these limits on regulatory space go too far, were not properly understood at the point of entry into IIAs or are inadequately balanced by safeguards for governments or by obligations on MNEs.

Lesson 1: IIAs bite and may have unforeseen risks – take safeguards

IIAs are legally binding instruments and not “harmless” political declarations. As shown by the surge in ISDS cases during the last 15 years, they “bite”. Broad and vague formulation of IIA provisions has allowed investors to challenge core domestic policy decisions, for instance in the area of environmental, energy and health policies. Whereas in the past, it was mostly developing countries that were exposed to investor claims, there are nowadays also more and more developed countries as defendants (chapter III).

The language used in IIAs has generated unanticipated (and at times inconsistent) interpretations by arbitral tribunals, and has resulted in a lack of predictability as to what IIAs actually require from States. As a result, there is today a broadly shared view that treaty provisions need to be clear and detailed, and drafted on the basis of a thorough legal analysis of their actual and potential implications.

Anticipating IIAs' effect on regulatory space is not straightforward. Although ISDS cases expose the constraints that IIAs can place on regulatory powers, there is no clear methodology for conducting regulatory impact assessments and for managing attendant risks. The IIA impact will depend on the actual drafting and design of the IIA and the capacity of national and subnational entities to effectively implement the treaty.

Lesson 2: IIAs have limitations as an investment promotion and facilitation tool, but also underused potential

IIA rule making needs to be informed by a proper cost-benefit analysis. However, determining the impact of IIAs on FDI flows is not a straightforward exercise. IIAs can help encourage cross-border investment flows by reducing political risks for foreign investors, liberalizing investment flows (depending upon the treaty's provisions) and, more generally, signalling a better investment climate to international investors, especially in countries with weak domestic investment frameworks and enforcement. However, IIAs are only one of many determinants of FDI decision-making, and their importance is contingent on other variables. IIAs cannot substitute for sound domestic policies and regulatory and institutional frameworks. IIAs alone cannot turn a weak domestic investment climate into a strong one, like other treaties, they cannot guarantee market outcomes in the form of inflows of foreign investment (UNCTAD, 2014a).

Yet, IIAs have underused potential as an instrument for sustainable development objectives. First, they can do more to promote and facilitate investment and channel it to sustainable development. Today, increasing the quantity of investment is not enough. What matters is its quality, i.e. the extent to which investment delivers concrete sustainable development benefits. In light of the financing gap for meeting the Sustainable Development Goals (SDGs) (developing countries face an annual gap of \$2.5 trillion), investment needs to be channelled to specific SDG sectors (*WIR14*).

Second, IIAs can do more to enhance responsible investment. Although (foreign) investment can create positive conditions for improving peoples' lives, it can also carry the risk of negatively impacting on the environment, peoples' health and the enjoyment of their human rights. These effects can be aggravated due to domestic regulatory lacunae. It is important, therefore, that while IIAs continue to provide a firm basis for investment protection, they should also begin to address more directly investor responsibilities.

Lesson 3: IIAs have wider implications for policy and systemic coherence, and capacity-building

IIA negotiations are not only about investment policies per se, but also have implications for numerous other policy areas at all levels of policymaking within countries (national, subnational, municipal). Given their broad scope of application and the wide range of foreign investment operations, IIA disciplines interact with policies on trade, labour and social issues, taxation, intellectual property, land rights, sector-specific policies, national security issues, cultural policies, health and environmental protection, and many others. The far-reaching scope of these agreements and the obligations they create calls for broad internal policy coordination – both at and within the national and subnational levels – when developing a country's IIA negotiation strategy and in the negotiation process itself. Care needs to be taken to ensure coherence between IIA obligations and domestic policies, and to achieve consistency between IIAs and other international obligations of the IIA contracting parties.

Ensuring this degree of coordination can be a daunting challenge. The complexity of IIA negotiations and their likely impact on domestic policies calls for more capacity-building in developing countries, in particular least developed countries (LDCs). Without an in-depth knowledge of international investment law and pertinent arbitral decisions, countries risk concluding IIAs that do not properly reflect their interests and objectives. Moreover, without such coordination, countries risk entering into commitments that they cannot implement at either the national or subnational levels or that inadvertently (and unnecessarily) limit the pursuit of government policies. In addition, lack of capacity and negotiation skills also negatively affect countries' bargaining power.

B. STRATEGIC APPROACH AND POLICY OPTIONS

1. Reform needs and objectives

IIA reform responds to a new context for investment policymaking and should address five main challenges.

As recognized in UNCTAD's Investment Policy Framework for Sustainable Development (IPFSD) (*WIR12*), the reorientation in IIA rule making responds to a new context for investment policymaking, nationally and internationally.

A new sustainable development paradigm

The conservation of natural resources, environmental protection and social well-being did not feature prominently on the international policy agenda some 50 years ago. Today, however, these objectives have become universally recognized guiding principles for all policymaking in developed and developing countries, including in investment policymaking (Hindelang et al., 2015). Accordingly, investment policies (and IIAs) can no longer be designed in isolation, but need to be harmonized with, and made conducive to, the broader goal of sustainable development. This is even more so, given the importance of international investment for achieving the SDGs as part of the post-2015 development agenda, and for living up to the commitments of the forthcoming third "Financing for Development" Conference in Addis Ababa.

As the global community's views on development have evolved, societies' expectations about the role of foreign investment have become more demanding. Today, it is no longer enough that investment creates jobs, contributes to economic growth or generates foreign exchange. Countries increasingly look for investment that is not harmful for the environment, which brings social benefits, promotes gender equality, and which helps them to move up the global value chain.

Moreover, concerns about the strength and conduct of individual foreign investors have brought foreign investment in general under closer domestic and international scrutiny. Investors are increasingly expected to do more than the minimum required by law. Increasingly, investment behaviour is assessed on whether it complies with international standards, such as the UN Guiding Principles on Business

and Human Rights, the revised OECD Guidelines on Multinational Enterprises, and the FAO/World Bank/UNCTAD/IFID Principles on Responsible Agricultural Investment (PRAI). In addition to standards developed by international organizations, investors are expected to develop their own corporate social responsibility (CSR) codes and to report on the actions they have taken in order to comply with them (*WIR11*).

A new investor landscape

Developing countries and economies in transition nowadays attract more than half of global FDI flows, and their importance as FDI recipients continues to increase. Emerging economies have not only become important hosts of FDI; they are increasingly large sources of investment themselves, with their share in world outflows exceeding one third. While these countries previously looked at IIAs mainly from a host-country perspective, they now also consider their interests as home countries to investment abroad.

The greater role of governments in the economy

Following the global financial crisis in 2008, governments have become less reticent about regulating and steering their economies. While private sector capital remains the chief engine of global economic growth and innovation, more and more governments are moving away from the deregulation approach to economic growth and development that has predominated since the 1990s. Industrial policies and industrial development strategies are proliferating in developing and developed countries alike (*WIR11*). These strategies often contain elements of targeted investment promotion or restriction, increasing the importance of integrated and coherent development and investment policies.

Similarly, a stronger role for State regulation manifests itself with regard to sustainable development. As the goals and requirements of sustainable development have come to be widely accepted, new social and environmental regulations are being introduced and existing rules reinforced – all of which have implications for investment policy. The trend for policymakers to intervene more in the economy, and to steer

investment activity, is visible in the overall increasing share of regulatory and restrictive policies in total investment policy measures over the last decade (see chapter III). This trend reflects, in part, a new realism about the economic and social costs of unregulated market forces but it has also given rise to concerns about investment protectionism.

When placing these lessons learned into the new context of today's investment for today's development paradigm, a number of concrete reform needs and objectives emerge.

(i) Safeguarding the right to regulate

While IIAs contribute to a favourable investment climate, they inevitably place limits on contracting parties' sovereignty in domestic policymaking. Given the rising concerns that such limits go too far, especially if combined with effective enforcement, IIA reform needs to ensure that countries retain their right to regulate for pursuing public policy interests, including sustainable development objectives (e.g. for the protection of the environment, the furtherance of public health or other social objectives) (WIR12). Safeguarding the right to regulate may also be needed for implementing economic or financial policies (WIR11). At the same time, however, policymakers must be vigilant that providing the necessary policy space for governments to pursue bona fide public goods does not inadvertently provide legal cover for investment protectionism or unjustified discrimination.

(ii) Reforming investment dispute settlement

Originally modelled on the system of ad hoc confidential commercial arbitration between private parties, today, the ISDS system suffers from a legitimacy crisis. There are concerns that the current mechanism exposes host States to additional legal and financial risks, often unforeseen at point of entering into the IIA and in circumstances beyond clear-cut infringements on private property, without necessarily bringing any benefits in terms of additional FDI flows; that it grants foreign investors more rights as regards dispute settlement than domestic investors; that it can create the risk of a "regulatory chill" on legitimate government policymaking; that it results in inconsistent arbitral awards; and that it is insufficient in terms of ensuring transparency, selecting independent arbitrators, and guaranteeing due process. IIA reform needs to address these concerns.

(iii) Promoting and facilitating investment

As said above, promoting and facilitating investment is crucial for the post-2015 development agenda, with developing countries facing an annual SDG-financing gap of \$2.5 trillion (WIR14). Thus far, however, the majority of existing IIAs do not include efficient investment promotion and facilitation provisions, and reserve this issue for domestic policymaking. A third reform objective, therefore, is to expand the investment promotion and facilitation dimension of IIAs together with domestic policy tools, and to target them towards foreign investment capable of promoting sustainable development.

(iv) Ensuring responsible investment

Foreign investment can make positive contributions for development, but it can also negatively impact the environment, health, labour rights, human rights or other public interests (WIR14). Typically, IIAs set out few, if any, responsibilities on the part of investors in return for the protection that they receive. One objective of IIA reform therefore is ensuring responsible investor behaviour. This includes two dimensions: maximizing the positive contribution that investors can bring to societies ("doing good") and avoiding negative impacts ("doing no harm").

(v) Enhancing systemic consistency

In the absence of multilateral rules for investment, the atomised, multifaceted and multilayered nature of the IIA regime gives rise to gaps, overlaps and inconsistencies, between IIAs, between IIAs and other international law instruments, and between IIAs and domestic policies. IIA reform therefore should seek coherence in these various relationships.

2. Designing a future IIA regime

IIA reform needs to be guided by design criteria and strategic choices that will inform the areas, tools and best possible policy options for implementing reform.

When designing a future IIA regime that meets the above-mentioned five reform challenges, countries can be guided by a number of design criteria for investment policymaking. They also need to make a number of strategic choices, with a view to identifying reform areas, reform tools and best possible policy options for implementing reform.

Table IV.1. Core Principles for investment policymaking for sustainable development

Area	Core Principles
1. Investment for sustainable development	<ul style="list-style-type: none"> The overarching objective of investment policymaking is to promote investment for inclusive growth and sustainable development.
2. Policy coherence	<ul style="list-style-type: none"> Investment policies should be grounded in a country's overall development strategy. All policies that impact on investment should be coherent and synergetic at both the national and international levels.
3. Public governance and institutions	<ul style="list-style-type: none"> Investment policies should be developed involving all stakeholders and embedded in an institutional framework based on the rule of law that adheres to high standards of public governance and ensures predictable, efficient and transparent procedures for investors.
4. Dynamic policymaking	<ul style="list-style-type: none"> Investment policies should be regularly reviewed for effectiveness and relevance and adapted to changing development dynamics.
5. Balanced rights and obligations	<ul style="list-style-type: none"> Investment policies should be balanced in setting out rights and obligations of States and investors in the interest of development for all.
6. Right to regulate	<ul style="list-style-type: none"> Each country has the sovereign right to establish entry and operational conditions for foreign investment, subject to international commitments, in the interest of the public good and to minimize potential negative effects.
7. Openness to investment	<ul style="list-style-type: none"> In line with each country's development strategy, investment policy should establish open, stable and predictable entry conditions for investment.
8. Investment protection and treatment	<ul style="list-style-type: none"> Investment policies should provide adequate protection to established investors. The treatment of established investors should be non-discriminatory in nature.
9. Investment promotion and facilitation	<ul style="list-style-type: none"> Policies for investment promotion and facilitation should be aligned with sustainable development goals and designed to minimize the risk of harmful competition for investment.
10. Corporate governance and responsibility	<ul style="list-style-type: none"> Investment policies should promote and facilitate the adoption of and compliance with best international practices of corporate social responsibility and good corporate governance.
11. International cooperation	<ul style="list-style-type: none"> The international community should cooperate to address shared investment-for-development policy challenges, particularly in least developed countries. Collective efforts should also be made to avoid investment protectionism.

Source: UNCTAD.

a. Design criteria and strategic choices

UNCTAD's Investment Policy Framework sets out 11 Core Principles for investment policymaking, which aim to guide policymaking at both the national and international levels. To this end, they translate the challenges of investment policymaking into a set of "design criteria" for investment policies (table IV.1). As such, the Framework's principles are also a useful guide for IIA reform.

Before embarking on IIA reform, countries need to make a number of strategic choices:

(1) Whether or not to have IIAs

The first strategic choice is about whether "to have or not to have" an IIA. This requires a careful assessment of the pros and cons of such agreements (summarized in table IV.2). Countries may come to different conclusions, depending on their individual development strategies, their domestic investment policies, their role

as a home or host country of investment, their prior experience with IIAs/ISDS and the way they conduct their international investment relations.

(2) Whether to disengage from IIAs

Since most countries are – to various degrees – already members of the global IIA regime, the question of having or not having IIAs is not only about concluding new treaties, but also about whether to maintain or terminate existing agreements. For some States, disengaging from existing IIAs may be appealing where IIA-related concerns feature particularly high in the domestic policy debate and where policymakers no longer consider IIAs to be an important element of their investment promotion strategies, both inward and outward. Also, this option becomes more and more available since many BITs have reached an "age" where contracting parties have the right to denounce them.

Countries considering this path need to keep in mind that treaty termination through denunciation is

Table IV.2. Summary of arguments put forward in favour and against IIAs

Main arguments made in favour of IIAs	Main arguments made against IIAs
<p>IIAs:</p> <ul style="list-style-type: none"> • Contribute to a favourable investment climate. • Contribute to fostering and expanding economic and political cooperation between contracting parties. • Contribute to the stability and predictability of the policy framework, foster good governance and the rule of law. • Provide protection rights that are independent from host countries' domestic legislation (superiority of international law over national law). • Compared with customary international law, improve legal certainty as protection rights are specified by treaty. • Reduce political risks of investing abroad. • May facilitate the granting of investment guarantees by the home country. • Help to avoid politicization of investment disputes. 	<p>IIAs:</p> <ul style="list-style-type: none"> • Do not guarantee additional investment inflows. • May negatively affect host countries' sovereign right to regulate in the public interest. • Expose host States to ISDS and associated financial risks. • Privilege foreign investors over domestic investors. • Only provide for investor rights, not obligations. • Reflect a negotiated outcome that is influenced by the bargaining power of the negotiating parties. • May result in overlapping and inconsistent IIA obligations of contracting parties. • Are difficult to amend in case of changing circumstances.

Source: UNCTAD.

not permitted before the IIA has reached a certain “age”, set by the duration provision of the treaty. In addition, denunciation does not immediately liberate contracting parties from their treaty obligations, since IIAs usually contain a “survival clause”, protecting existing investment in the host country for a certain additional period, typically between 10 and 20 years. Finally, treaty denunciation done without consulting the other contracting party risks negatively affecting foreign relations.

(3) Whether to engage in IIA reform

The next strategic choice is whether or not to engage in IIA reform. Refraining from substantive changes to international investment policymaking sends an image of continuity and investor friendliness. It may be particularly attractive for countries with a strong outward investment perspective and with no – or little – ISDS experiences. Not engaging in reform, however, comes with serious drawbacks in that it does not address any of the challenges arising from today's global IIA regime and keeps the country exposed to risks created by IIAs in their traditional form. Moreover, mounting pressure for reform from existing treaty partners and other constituencies in many countries will make it increasingly difficult to maintain the status quo.

(4) How to reform IIAs

Should a country decide to embark on IIA reform, further strategic considerations come into play, relating to both substantive and procedural aspects.

What extent and depth should the reform agenda have?

Pursuing IIA reform requires decisions on the sequencing of individual reform steps. Gradual, incremental reform steps may be easier to realize than a holistic approach. It may be advantageous to prioritize those areas for reform (e.g. certain IIA clauses or ISDS reform elements) where consensus among the respective actors is most likely to emerge.

Limited, i.e. selective, adjustments that address specific concerns may be particularly attractive for those countries that wish to respond to the challenges posed by IIAs but, at the same time, wish to demonstrate their continued engagement with the investment regime. Selective modifications, while leaving the treaty core untouched, permit countries to address both changes which seem most readily achievable (i.e. “low-hanging fruit”) and addressing concerns that appear most relevant and pressing. It also allows the tailoring of the modification to a particular negotiating counterpart so as to suit a particular economic relationship. Indeed, introducing selective adjustments may appear as an appealing option for reducing the mounting pressure on IIAs.

At the same time, however, selective adjustments cannot comprehensively address the challenges posed by the existing stock of treaties. It cannot fully deal with the interaction of treaties with each other, unless the selective adjustments address the most-favoured-nation (MFN) clause. Without addressing MFN application, selective adjustments may lead to

“treaty shopping” and “cherry-picking” and thereby undermine improved formulations of treaty provisions. And, throughout all of this, selective adjustments may lay the groundwork for further change, thus creating uncertainty instead of stability.

By contrast, pursuing systematic and comprehensive reform means overhauling international commitments in a way that ensures the promotion of sustainable development. It implies addressing the key challenges to the IIA regime in all dimensions, with regard to substantive and procedural issues, treaty network issues and ISDS, as well as resolving incoherence, filling systemic gaps, and eliminating loopholes. Taking reform steps in respect of all five reform objectives and addressing future and existing treaties is the most comprehensive approach to reforming the current IIA regime.

Systematic and comprehensive reform presents a number of challenges. It may be time- and resource-intensive. Its result may be perceived as reducing the protective value of the agreements and offering a less attractive investment climate. It requires dealing with the stock of existing IIAs. And amendments or renegotiation may require the cooperation of a potentially large number of treaty counterparts. At the same time, however, this course of action is the only one that can bring about comprehensive and coherent IIA reform. It is also the one best suited for fostering a common response from the international community to today’s shared challenge of promoting investment for the SDGs.

How to balance investment protection and the need to safeguard the right to regulate?

IIA reform steps can be moderate or far-reaching. Care needs to be taken that individual reform steps or the cumulative effects of a whole reform package do not deprive the IIA of its investment protection function, but rather achieve a balance between the foreign investors’ adequate protection and the host countries’ need to preserve sufficient regulatory space. How to strike this balance is a strategic choice and depends on individual country preferences and policies.

In addition, there is a risk that individual reform steps only create an illusion of retaining regulatory space (e.g. emphasising the right to regulate while noting that any measure must be otherwise consistent with the IIA). Accordingly, the pursuit of comprehensive reform requires a careful choice of options, bearing in mind the interaction between them.

How to reflect home and host countries’ strategic interests?

The strategic position of countries towards IIA reform will depend on whether they approach reform from the perspective of a host or also as a home country of foreign investment. While as host countries, they may wish to focus on ensuring regulatory space and reducing exposure to ISDS, as home countries they will be interested in providing adequate protection for their own investors abroad. They may also be interested in establishing entry rights for foreign investors in IIAs. As more and more countries become both host and home bases of foreign investment, they need to reconcile these strategic interests in the IIA reform debate.

How to synchronize IIA reform with domestic investment policies?

IIA reform needs to take into account the interaction and “division of labour” between IIAs and domestic investment policies (noting a key difference between the two, namely that domestic law can be unilaterally amended, while this is not possible for IIAs). One strategic choice therefore is how much protection to grant under domestic law and how much under IIAs. Similar considerations apply with regard to the issue of whether to reform at the domestic or the international level, or both. In an optimal architecture, both policy levels will complement each other (e.g. with regard to investment protection, promotion and investor responsibility). In other areas (in particular dispute settlement), decisions may need to be made about whether domestic and international dispute settlement procedures should be complementary or mutually exclusive.

Whether to consolidate the IIA network instead of continuing fragmentation?

As countries reform and replace individual IIAs, there will be more cases where “old” and “new” IIAs coexist. IIA reform therefore risks bringing about – at least initially – a further fragmentation of the IIA regime. At the same time, IIA reform offers an opportunity for consolidating the IIA network, provided that a sufficient number of countries participate in the process. Regional IIA reform efforts – both at the intraregional and at the interregional level – offer particular opportunities for treaty consolidation. Such regional IIAs can replace existing BITs between the participating States, unless the latter wish that the “old” agreements continue to exist. Allowing old bilateral agreements to coexist with new regional agreements heightens the risk of

fragmentation and systemic incoherence and this may be further exacerbated where MFN clauses remain unreformed.

Overall, the response to these strategic considerations will depend on country-specific circumstances and preferences. Relevant factors include the kind of treaties that make up a country's IIA network, its individual experience with ISDS, the role it allocates to IIAs as part of its overall development strategy and the extent of IIA reform desired, including by its domestic stakeholders.

b. Reform areas

The starting point for IIA reform is the lessons learned from the past, which translate into the five reform objectives identified above. These reform objectives can be pursued by addressing a number of “reform areas”, which largely correspond to key IIA clauses. For each of these, there are a number of sustainable-development-oriented policy options. Together, the reform objectives, the corresponding reform areas and the policy options for pursuing them offer an action menu for IIA reform.

Approach to designing reform elements

By and large, the policy options address the standard elements included in an IIA. The options discussed below include both mainstream IIA provisions (e.g. clarification of indirect expropriation) as well as more idiosyncratic options that have so far been used by fewer countries or that are found only in model agreements or policy statements and concept notes (e.g. an international investment court). Many of the options had already been set out in UNCTAD's Investment Policy Framework in 2012.

Another possibility would be to develop new approaches to international investment law and policymaking from “scratch”. Such an exercise could be based on a review of existing standards of protection (and respective gaps) in domestic laws and policies, and analysis of their pros and cons and suitability for use at the international level. Similarly, new IIA elements could be designed based on inputs from outward investors regarding the type of protections and support initiatives they would consider beneficial for them. Such an approach was partly undertaken by

Brazil, when devising its Cooperation and Facilitation Investment Agreements (CFIAs) (chapter III).

Approach to choosing a combination of reform elements

Today's efforts towards comprehensive IIA reform face the specific challenge of properly harnessing IIAs, including their investment protection elements, for promoting sustainable and inclusive development. Finding the right balance between investor protection, on the one hand, and safeguarding the right to regulate, on the other, is of particular importance. Some combinations of policy options may result in a treaty that is largely deprived of its basic investment protection *raison d'être*, wherein the cumulative compound effect of all modifications renders the treaty's commitments meaningless. Ultimately, it is the blend of policy options that determine where on this spectrum a particular IIA is located. Accordingly, the pursuit of comprehensive reform requires a careful choice of options, bearing in mind the interactions between them.

This need for balance is already reflected in the UNCTAD Policy Framework's principles, which include the principles of openness to investment, investment protection and treatment, as well as principles such as the right to regulate and balanced rights and obligations.

There are many ways to pursue the five reform objectives identified. Table IV.3 offers a menu for doing so. Countries can use this menu with a view to identifying the most suitable combination of reform objectives and reform areas for them.

c. Reform tools

When pursuing IIA reform and designing new-generation agreements, countries have a number of reform tools at hand. Table IV.4 provides an overview of these tools and the various entry points to which they can be applied. These tools can be grouped into eight partially overlapping categories of actions. Several tools can be used jointly with respect to one particular IIA entry point or clause.

- **Adding new provisions.** The impact of this tool on the pursuit of reform objectives varies, depending on the content of the new provision. For example, adding a clause can help safeguard the right to regulate (e.g. if it is a “safety valve” such as a general or national security exception).

Table IV.3. Objectives and areas for IIA reform

Reform objectives	Reform areas
1. Safeguarding the right to regulate	<p>Circumscribed (clearly defined) IIA standards of protection</p> <ul style="list-style-type: none"> • Fair and equitable treatment • Indirect expropriation • MFN <p>“Safety valves”; e.g. exceptions for</p> <ul style="list-style-type: none"> • Public policies • National security • Balance-of-payments crises
2. Reforming investment dispute settlement	<p>Clauses that</p> <ul style="list-style-type: none"> • Fix the existing ISDS mechanism by improving transparency, limiting investors’ access, enhancing the contracting parties’ control and introducing local litigation requirements • Add new elements to the existing ISDS mechanism (e.g. building in effective alternative methods of dispute resolution, introducing an appeals facility) • Replace the existing ISDS mechanism (e.g. by creating a standing international investment court, reliance on State-State dispute settlement and/or reliance on domestic dispute resolution)
3. Promoting and facilitating investment	<p>Clauses that</p> <ul style="list-style-type: none"> • Strengthen promotion measures (inward and outward) • Target promotion measures to sustainable development • Foster cooperation in this regard
4. Ensuring responsible investment	<p>Clauses that</p> <ul style="list-style-type: none"> • Prevent the lowering of environmental or social standards • Ensure compliance with domestic laws • Strengthen corporate social responsibility (CSR) and foster cooperation in this regard
5. Enhancing systemic consistency	<p>Clauses and mechanisms that manage interaction between</p> <ul style="list-style-type: none"> • IIAs and other bodies of international law • IIAs and domestic investment and other policies • Different IIAs within a country’s network

Source: UNCTAD.

Adding a clause can promote responsible investor behaviour (e.g. if it is a not lowering of standards or CSR clause) or foster investment promotion (e.g. if the addition relates to home-country measures or a joint committee charged with pursuing promotion-related activities).

- **Omitting existing provisions.** Again, the impact of this tool depends on the content of the respective clause. For example, refraining from including certain types of clauses that have proven controversial or that are susceptible to receiving contradictory interpretations by arbitral tribunals can increase legal certainty (e.g. omitting the umbrella clause), help safeguard the right to regulate and improve investment dispute settlement.
- **Reformulating existing provisions.** Reformulations usually clarify or circumscribe the scope of provisions. *Clarifying* clauses supports both investors and host countries, as ultimately both benefit from enhanced legal clarity and predictability.
- **Carving out aspects.** Carve-outs can circumscribe the treaty’s scope of application (e.g. limiting the scope of protected investments) or the reach of specific clauses (e.g. limiting the situations to which ISDS applies). Carve-outs can also relate to specific sectors, industries or policies. Generally, carve-outs can help safeguard the right to regulate.
- **Linking provisions.** Linking provisions usually results in a situation where protections offered are conditioned on certain circumstances. An example would be to make IIA protections or ISDS subject to investor compliance with domestic laws or to require tribunals to take into account States’ different level of development when interpreting protection standards (e.g. fair and equitable treatment). Conditioning protections usually weakens the protective dimension of an IIA. At the same time, linking can also strengthen the treaty’s impact in inducing responsible investor behaviour.

Table IV.4. Reform tools	
Reform tools	Examples
1. Adding new provisions	<ul style="list-style-type: none"> Public policy exceptions Clause on compliance with domestic laws Clause on not lowering of standards Clause on CSR
2. Eliminating (omitting) existing provisions	<ul style="list-style-type: none"> FET, MFN, umbrella clause, ISDS
3. Reformulating existing provisions	Clarifying the content of <ul style="list-style-type: none"> FET Indirect expropriation
4. Carving-out aspects	Circumscribing (in IIA clauses or reservations) the <ul style="list-style-type: none"> Scope of the treaty Scope of protected investments/investors Scope of application of key clauses (e.g. MFN, national treatment) Scope of access to ISDS
5. Linking provisions	Conditioning protections on <ul style="list-style-type: none"> Investor behaviour
6. Calibrating the normative intensity of provisions	<ul style="list-style-type: none"> Hortatory language Transition phases/phase-ins Differentiated obligations
7. Creating/strengthening institutional mechanisms	Within the IIA, a joint committee, council or working group, coordinating and facilitating dialogue and cooperation on <ul style="list-style-type: none"> Investment promotion, the prevention of disputes, the interpretation of provisions, the review of the agreement Beyond the IIA, <ul style="list-style-type: none"> An appeals facility, an international investment court
8. Referring to other bodies of law	Managing the interaction between IIAs and other bodies of law with a view to avoiding inconsistencies and seeking synergies, e.g. <ul style="list-style-type: none"> Preamble References to CSR instruments Reaffirmations of contracting parties' commitments under other international law instruments References to the Vienna Convention on the Law of Treaties ISDS rules

Source: UNCTAD.

- Calibrating provisions.** Calibrating provisions implies managing the normative intensity of provisions. Examples include the use of hortatory language (e.g. for CSR issues), the establishment of differentiated responsibilities (e.g. less stringent obligations for the less developed treaty partner) or the delayed implementation of treaty obligations (e.g. phase-in periods for the less developed treaty partner). The former (e.g. hortatory language for CSR) have typically been used for strengthening the sustainability/responsibility dimension of IIAs; the latter (phase-ins) have traditionally been used in the context of special and differential treatment. It has to be noted, though, that such treatment, while being a regular feature in the WTO legal system, is not yet integrated in international investment law.
- Creating mechanisms.** This can include changes to existing committees or councils, or the creation of new mechanisms (e.g. an appeals facility, an international investment court). Given that most first-generation BITs do not have institutional structures or follow-up mechanisms, this tool will usually imply the addition of new provisions or elements, and so it is likely to overlap with the first tool. In terms of impact on reform objectives, this tool can address ISDS-related challenges (e.g. when creating an appeals facility or an international investment court), strengthen the promotion dimension of the IIA (e.g. when establishing a body charged with cooperating on promotion-related issues), increase the IIA's impact on inducing responsible investor behaviour

(e.g. when establishing a mechanism charged with reviewing CSR-related issues) and strengthen the role of countries as masters of their treaties (e.g. when establishing a body charged with reviewing the IIA or with submitting interpretative guidance to arbitral tribunals).

- **Referring to other bodies of law.** This can include references to other bodies of law, with a view to fostering coherence between IIAs and such other bodies of law (e.g. human rights, environment, public health); to CSR rules, as part of an effort to foster responsible investor behaviour; to the Vienna Convention on the Law of Treaties, with a view to ensuring consistent interpretation (in case of conflict); or to international conventions or rules regarding investment dispute settlement.

The tools discussed above not only differ in their nature and impact, but also in the ease with which they can be used. *Additions*, particularly when they concern “enforceable” provisions, can raise questions about their potential implications and their unanticipated side effects. When additions also include new concepts, such as investor obligations, they can give rise to the argument that such novel concepts do not belong in an IIA (particularly, when the IIA is considered as an agreement aimed in essence at protecting investors). *Omissions*, particularly when they concern key protection standards, may raise concerns that they weaken the IIA and its potential investment-promotion effect.

Additions and *omissions* are the tools that go furthest in terms of departing from the model of a “typical IIA”. They come closest to an approach of conceptualizing IIA reform, as overhauling instead of improving the current system. All of these considerations will impact policymakers’ selection of elements for their country’s individual road map for IIA reform.

3. Policy options for reform

UNCTAD presents policy options for meeting the five IIA reform challenges.

This section offers numerous policy options for the key IIA clauses and entry points. It discusses how the options contribute to reaching the reform objectives outlined above and their respective pros and cons. The discussion of reform options in this section is further supported by tables (available online, at [http://](http://investmentpolicyhub.org)

investmentpolicyhub.org) listing the particular reform option, offering selected treaty examples and providing information on the prevalence of the reform option in current State practice. Actual drafting language, as found in actual treaties, can be found in the APEC-UNCTAD Handbook for IIA Negotiators (APEC and UNCTAD, 2012).

To a large extent, the reform options reflect the respective policy options for IIAs contained in UNCTAD’s Investment Policy Framework (IPFSD). This Report takes a different approach and includes only those options that contribute to IIA reform by addressing the above-mentioned five challenges. It focuses on the most pressing issues (e.g. MFN, FET, indirect expropriation, ISDS) in more detail.

Some of the options for individual IIA clauses are alternatives, others can be used together.

a. Safeguarding the right to regulate

Options include clarifying or circumscribing provisions such as most-favoured-nation (MFN) treatment, fair and equitable treatment (FET) and indirect expropriation, as well as including exceptions, e.g. for public policies or national security.

The right to regulate in the public interest is addressed in IIAs mainly through provisions related to the standard of treatment that the treaty affords to foreign investors. Among the provisions particularly implicated in delineating the balance between investment protection and the right to regulation in the public interest are MFN clauses, the FET standard, expropriation provisions, and provisions on safeguards and exceptions, which may be either built into particular substantive standards of protection or drafted as generally applicable clauses. These issues are at the heart of the IIA reform debate and will be dealt with in detail in this section. Other IIA provisions (ranging from the preamble, to the scope and definition clauses, national treatment, the umbrella clause, and provisions related to remedies and compensation) also have a bearing on the right to regulate; they are equally important for States to consider, but they figure less prominently in the reform discussion. They are therefore covered in a more abbreviated manner in the second part of this section. A number of other IIA provisions that can have an impact on the right to regulate (e.g. performance requirements or pre-establishment treatment) are not covered in this report.

Standards of treatment

- **MFN**

The MFN clause is a crucial provision for IIA reform. Failure to take appropriate action with respect to the MFN clause can undermine improved formulations of treaty provisions.

MFN clauses, routinely included in traditional IIAs, aim to prevent less favourable treatment of investors from the signatory State vis-à-vis comparable investors from any third country (i.e. nationality-based discrimination). The MFN principle thereby aims to ensure a level playing field between investors of different foreign nationalities (UNCTAD, 2010b).

In actual ISDS practice, investors have relatively infrequently alleged that they have been discriminated against by virtue of the host States' more favourable application of domestic measures to investors of third states. Instead, investors have most often invoked the MFN clause to access more "investor-friendly" provisions in IIAs concluded by the host State with third countries.

In particular, investors have relied on the MFN clause to avoid dispute resolution requirements imposed by the applicable IIA (e.g. a set period of time for which they must pursue local remedies before turning to international arbitration). Several tribunals have deemed this circumvention possible in cases involving broadly drafted MFN clauses in which the claimant has been able to point to an IIA signed by the host State in which such pre-arbitration requirements were absent. In other cases, investors have invoked the MFN clause to benefit from higher protection standards

than the ones found in the base treaty ("base treaty" is the treaty pursuant to which the claim is brought). For example, in situations in which an IIA with a third country has contained additional investor protections or more favourable formulations, as compared to the base treaty, a number of tribunals have decided that it is possible for the investor to take advantage of these more favourable provisions to "replace" or "add to" the provisions in the base treaty.

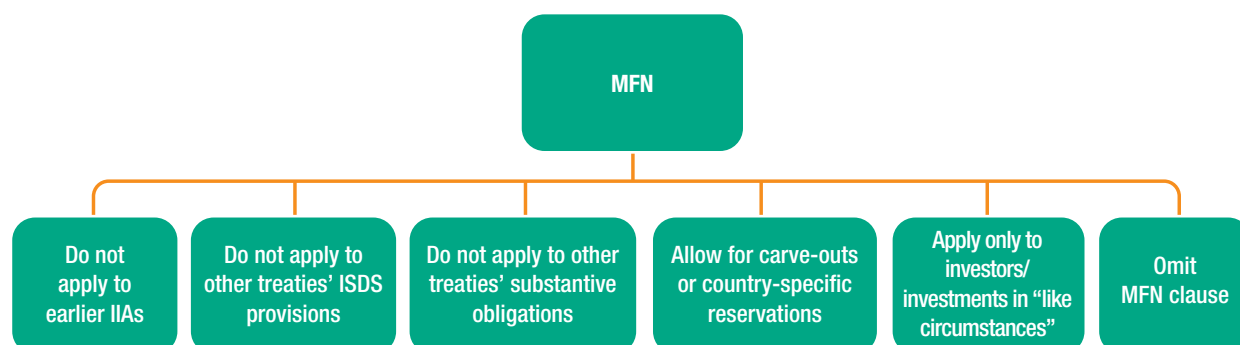
Application of MFN clauses in this way can result in investors "cherry picking" the most advantageous clauses from different treaties concluded by the host State, thereby potentially undermining individual treaty bargains and sidelining the base treaty. For example, treaty commitments may clash, or hard-won concessions in a negotiation (e.g. on flexibility in performance requirements) may be undone through the application of a broadly worded MFN clause, as interpreted by arbitral tribunals. This concern is particularly heightened given countries' current efforts to reform their IIA regimes, which implies a refinement and rebalancing of treaty standards. Clearly, States will need and want to be careful that the desired effects of newly crafted treaty provisions are not obviated by the application of a broadly worded MFN clause.

There are a number of options to address these challenges (figure IV.2).

A first option is to specify that the MFN clause does not allow for the importation of substantive or ISDS-related elements contained in older treaties. This option ensures that a country's IIA reform efforts are not compromised by provisions contained in its stock of older treaties.

Figure IV.2.

Options for IIA reform: MFN



A second option is to specify that MFN treatment does not apply to ISDS provisions found in other IIAs, existing or future.

A third option is to specify that the MFN clause does not apply to substantive obligations undertaken in (existing or future) IIAs. Similarly, a treaty can clarify that substantive obligations in other IIAs do not in themselves constitute “treatment”, absent measures adopted by a State pursuant to such obligations (e.g. see Canada–EU CETA, draft 2014).

All of these approaches support IIA reform and avoid the undoing of modernization efforts – however they can raise concerns as to the diminution of the protective value of the agreement.

A fourth option is carving out from the MFN obligation certain sectors or industries or certain policy measures through a general carve-out (applicable to both parties) or through country-specific reservations. This option is particularly relevant for IIAs with a pre-establishment dimension.

A fifth option, frequently undertaken in recent agreements, clarifies that the MFN obligation requires comparison of investors/investments that are “in like circumstances”. Such a provision can go some way in safeguarding the right to regulate, but it can also raise questions about the specific criteria for comparison. Some recent treaties and models attempted to set out criteria for determining whether investors/investments are in “like circumstances” (Azerbaijan–Croatia BIT (2007)) (see also national treatment).

A final option, followed by some countries, is to omit the MFN clause altogether. The FTA between the EU and Singapore (2014), the FTA between India and Malaysia (2011), the ASEAN–Australia–New Zealand FTA (2009), the Japan–Singapore FTA (2002) and the SADC Model BIT (2012) are examples in point. Such an approach preserves a maximum of flexibility and can facilitate IIA reform. At the same time, omitting a standard that many consider to be one of the cornerstones of international economic law may raise concerns. In response, some have argued that in an IIA, the investment-enhancing effect of the MFN clause is less important as compared with other clauses and as compared with its presence in other international economic agreements (e.g. preferential trade agreements).

• FET

The FET standard is one of the IIA clauses that is at the core of today’s debate on IIA reform. The standard is designed to protect foreign investors from government misconduct not captured by other standards of protection. It is also sometimes said that the FET standard may serve to foster good governance in host States. In actual practice, owing to its open-ended and largely undefined nature, the FET standard, especially as it has been drafted in traditional IIAs, has turned into an all-encompassing provision that investors have used to challenge any type of governmental conduct that they deem unfair. In fact, almost all ISDS cases to date have included an allegation of a FET breach.

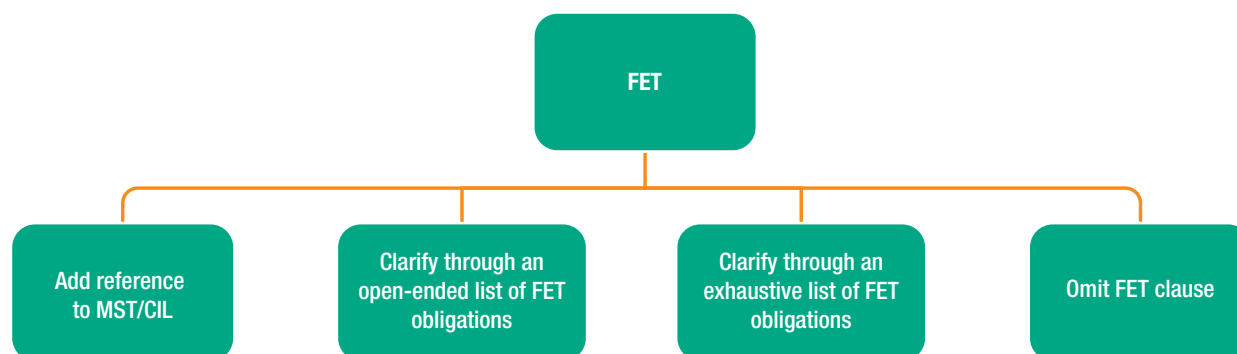
There is a great deal of uncertainty concerning the precise meaning of the concept of FET, because the notions of “fairness” and “equity” do not connote a clear set of legal prescriptions and are open to subjective interpretations. Moreover, the relationship between FET and principles of customary international law, such as the international minimum standard of treatment, has raised significant issues of interpretation, especially where the IIA text contains no express link between FET and customary international law. As a result, the task of determining the meaning of the FET standard has been effectively left to ad hoc arbitral tribunals (UNCTAD, 2012b).

A particularly challenging issue that has arisen through arbitral practice relates to the use of the FET standard to protect investors’ “legitimate expectations”. Given the potentially far-reaching application of the concept of “legitimate expectations”, there is a concern that the FET clause can restrict countries’ ability to change investment-related policies or introduce new policies – including those for the public good – if they have a negative impact on individual foreign investors.

Traditional first-generation IIAs typically included an unqualified FET standard, which has given rise to some of the problems identified above. New-generation IIAs contain a number of more precise drafting options to choose from (see figure IV.3 on the next page).

A first option is to qualify the FET standard by reference to the minimum standard of treatment of aliens under customary international law (MST/CIL). Depending on a particular tribunal’s reading of MST/CIL, this approach may raise the threshold of State liability

Figure IV.3. Options for IIA reform: FET



Source: UNCTAD.

(e.g. the challenged conduct will need to be found to amount to egregious or outrageous mistreatment of foreign investors) and help to preserve States' ability to adapt their policies in light of changing objectives. However, the contours of MST/CIL are far from clear, and a reference to this concept could engender a new, significant uncertainty, for both States and investors. Moreover, in light of the arguments about the nature and development of CIL, not all countries may feel comfortable in referring to this concept.

A second option is to clarify the FET standard with an open-ended list of State obligations. The formulation may be "positive", specifying what the standard includes (e.g. the obligation not to deny justice in criminal, civil or administrative adjudicatory proceedings), or "negative", explaining what the standard does not include (e.g. establishing that the FET standard does not include a stabilization obligation that would prevent the host State from changing its legislation), or a combination thereof. This option has the advantage of clarifying the meaning of FET by indicating examples of what it covers and what it does not cover. One of its disadvantages is that the open-ended, indicative list of obligations, by its nature, leaves open the potential for expansion of the meaning of FET through subsequent arbitral interpretation.

A third option is to clarify or replace the general FET clause with an exhaustive, i.e. "closed" list of more specific obligations (e.g. a prohibition to deny justice or flagrantly violate due process, engage in manifestly abusive or arbitrary treatment). Although agreeing on such a list may be a challenging endeavour, its

exhaustive nature would help minimize unanticipated and far-reaching interpretations by tribunals. As a further option, the contracting parties may wish to include a requirement for a periodic review of the list or the content of the FET obligation.

A final option that some countries have implemented in some of their IIAs is omitting the FET clause altogether (e.g. Bangladesh–Uzbekistan BIT (2000), Australia–Singapore FTA (2003)) or reducing it to a softer commitment; for example, by referring to FET in the preamble but not in the main treaty text (e.g. Turkey–United Arab Emirates BIT (2005) or Azerbaijan–Estonia BIT (2010)).⁴ This approach reduces States' exposure to investor claims, but also reduces the protective value of the agreement.

- **Indirect expropriation**

The expropriation provision is a key IIA element that mitigates an important risk faced by investors. Expropriation clauses do not take away States' right to expropriate property, but make the exercise of this right subject to certain conditions (UNCTAD, 2011a).⁵ Expropriation provisions usually cover both "direct" and "indirect" forms of expropriation. "Indirect expropriation" covers acts, or series of acts, whose effects are "tantamount to" or "equivalent to" a direct, formal taking. These are acts that generally involve total or near-total deprivation of an investment or destruction of its value but without a formal transfer of title to the State or outright seizure.

Investors have used provisions on indirect expropriation to challenge general non-discriminatory

regulations that have had a negative effect on their investments (e.g. a ban or the imposition of restrictions on a certain economic activity on environmental or public health grounds). This raises the question of the proper borderline between expropriation (for which compensation must be paid) and legitimate public policymaking (for which no compensation is due).

Historically, IIAs have not contained any criteria for distinguishing between State action amounting to an indirect expropriation and State action of a general regulatory nature for which no compensation is due. More recent IIAs, however, typically set out a number of criteria and a few recent agreements go so far as to omit an explicit reference to indirect expropriation (e.g. Serbia–Morocco BIT (2013)). While the omission of a reference to indirect expropriation may serve to limit (or even eliminate) State exposure to liability for non-direct takings, it may also increase investors' perception of country risk and susceptibility to opportunistic regulatory behaviour.

There are a number of policy options in this regard (figure IV.4).

A first option is to limit the protection in case of indirect expropriation by establishing criteria that need to be met in order for an indirect expropriation to be found. This can include reference to (i) the economic impact of the government action; (ii) the extent of government interference with distinct, reasonable investment backed expectations; or (iii) the character of the government action (e.g. whether it is discriminatory or disproportionate to the purpose of the measure under challenge). Another possible criterion is

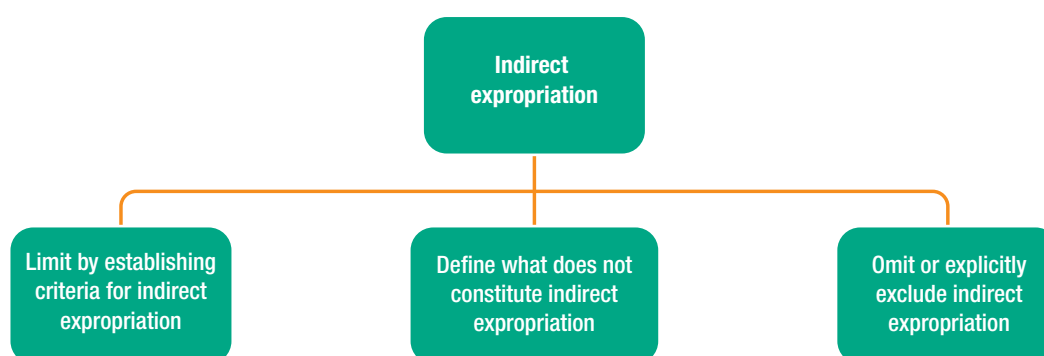
whether the measure(s) alleged to constitute an expropriation have produced a direct economic benefit for the State.

A second option is to define, in general terms, which measures do not constitute indirect expropriation. For example, it can be specified that “normal regulatory activities” (e.g. non-discriminatory, good faith regulations relating to public policy objectives) do not constitute indirect expropriation. Similarly, it can be clarified that a measure's adverse effect on the economic value of the investment is not enough to establish an indirect expropriation. A variant of this option is to clarify that certain specific measures (e.g. compulsory licensing in accordance with WTO rules) do not constitute indirect expropriation.

A third option is to omit a reference to indirect expropriation from the IIA or even explicitly exclude it from the treaty coverage. Depending upon drafting, the simple omission of a specific reference to “indirect” expropriation may not eliminate the possibility of liability for indirect expropriations: a bare reference to “expropriation” in an IIA may be interpreted as subsuming both direct and indirect expropriation in subsequent arbitral proceedings. In contrast, expressly excluding indirect expropriation from the coverage of an IIA may be perceived as considerably reducing the protective value of the IIA as it would leave investors unprotected from the types of indirect expropriation that are unrelated to States' regulatory conduct, such as “creeping” (through a series of damaging measures) or disguised (under a guise of lawful measures, e.g. tax enforcement) expropriation.

Figure IV.4.

Options for IIA reform: Indirect expropriation



All of the above variations give guidance to arbitral tribunals that is presently lacking in most IIAs. None of these options exclude the risk of liability altogether (except perhaps for the express exclusion of protection for indirect expropriations), but rather allow for a better and clearer balancing of investor and State interests. In so doing, these options can help safeguard the right to regulate non-discriminatorily in the general public interest, while simultaneously providing greater legal certainty to investors with respect to the scope of IIA rights. Although explicit exclusion of protection for indirect expropriation is also an option that States can consider, such an option must be viewed as a rarity in contemporary State practice and may be perceived by investors as significantly lowering the protective value of the IIA. From the investors' perspective, such protection is particularly desirable in governance-weak economies where protection from measures of this nature under the domestic laws of the relevant host State may not be seen as reliable. In the absence of IIA protection for indirect expropriation, investors may seek investment insurance from private or public providers.

Safeguards

For the IIA elements below, the policy options are structured around a number of aspects, each requiring a choice between different options.

- **Public policy exceptions**

Investors may bring claims against public interest measures that have a negative effect on an investment's profitability. Whereas traditional IIAs typically do not contain express public policy exceptions, an increasing number of new treaties do include them. The formulation of such exceptions is often similar to the language found in the WTO's GATT Article XX and GATS Article XIV. These provisions aim at balancing investment protection with other public policy objectives and at reducing States' exposure to investor challenges of such measures. Public policy exceptions can also have an important signalling effect towards the general public, indicating an agreement's compatibility with sustainable development and public policy considerations.

At the same time, the absence of express public policy exceptions does not mean that States cannot take public policy measures at all. Instead, such measures either may not be in conflict with IIA obligations in the

first place or may be justified based on other principles of international law that inform the interpretation of IIA obligations. Nevertheless, including public policy exceptions expressly in an IIA increases legal certainty for host States: public policy exceptions explicitly allow for measures – which might otherwise be challengeable under the agreement – to be taken under specified circumstances. In so doing, they can have an important effect of increasing certainty and predictability about the scope of the IIA's obligations.

It should be noted that adding exceptions provisions raises questions about their relationship with some traditional investor protections, e.g. the provision on direct expropriation (if a direct expropriation corresponds to one of the objectives included in the exception clause, does this relieve the State of the duty to pay compensation?) or the FET standard (e.g. does the State's creation of protected legitimate expectations foreclose its later reliance on an exceptions clause?). Hence the relationship between an exceptions clause and each IIA obligation needs to be considered carefully. The Energy Charter Treaty's Article 24 on "Exceptions" for example, does not apply to the article on expropriation.

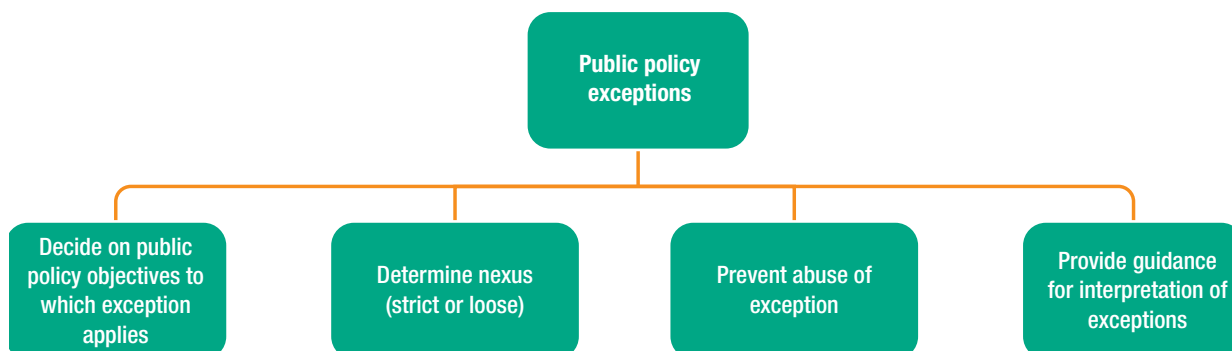
Assuming countries wish to include such exceptions into IIAs, they have a number of options at hand (figure IV.5), all with their pros and cons.

The first set of options relates to the type of situations that are covered. Countries can specifically list the public policy objectives to which they want the exception to apply (e.g. the protection of public health, public order and morals, the preservation of the environment). This list can be inspired from the relevant WTO (GATT and GATS) clauses but can also include other objectives, such as the provision of essential social services (e.g. health, education, water supply); the prevention of tax evasion; the protection of national treasures of artistic, historic or archaeological value (or "cultural heritage"); cultural diversity; and media diversity, or allow for the pursuit of broader objectives, such as the host countries' trade, financial and developmental needs. The exact content of such a list would depend on the negotiating partners' policy preferences.⁶

A second set of options relates to defining the required relationship (i.e. the "nexus") between a measure and the policy objective it pursues. This determines how easy or difficult it is for a State to use an exception. For example, the IIA can provide that the measure

Figure IV.5.

Options for IIA reform: Public policy exceptions



Source: UNCTAD.

must be “necessary” to achieve the policy objective (strict test) or that it must simply be “related to” (“aimed at”, “directed to” or “designed to achieve”) the policy objective (less strict test): the stricter the relationship, the stronger the protective character of the agreement.

A third set of options aims at preventing potential abuse of exceptions. For example, an IIA can clarify that “exceptional” measures must be applied in a non-arbitrary manner and not be used as disguised investment protectionism. Again, these options can be inspired by the respective WTO (GATT and GATS) clauses.

A fourth option establishes guidance for tribunals in the interpretation of exceptions clauses. For example, IIAs can establish a mandatory mechanism whereby cases in which a respondent State invokes a public policy exception are referred to a joint committee of the contracting parties. The committee could guide the interpretation or, alternatively, issue a binding determination of whether or not a measure falls within the scope of the public policy exception. This allows States to retain a certain degree of control over the application of an exceptions clause.

- **National security exception**

A number of policy developments raise concerns about the constraints that IIAs potentially impose on host States’ measures that are designed to protect their national security interests.

In traditional IIAs, national security exceptions were included only sporadically. Their inclusion has been much more frequent in recent treaties (UNCTAD,

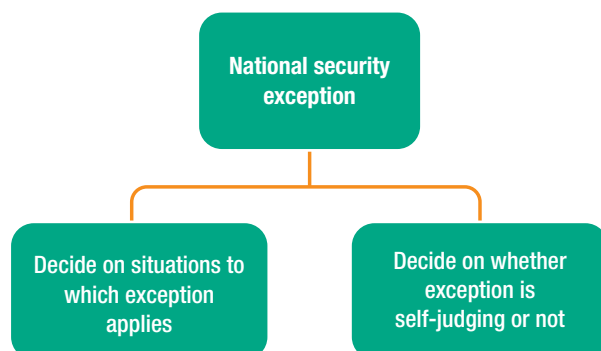
2009). At the domestic level, recent years have witnessed an expansion of the role of domestic screening and monitoring mechanisms for inward FDI (WIR13). In some cases, countries justify the imposition of investment restrictions or regulations on grounds of national security. Internationally, countries have invoked national security arguments in ISDS cases (e.g. in several cases brought against Argentina concerning measures taken to address the country’s economic and financial crisis). National security issues figure prominently in a number of negotiations, particularly those in which pre-establishment commitments are under consideration (e.g. States may wish to retain their right to refuse the admission of foreign investors/ investments where doing so would pose a risk to the State’s security interests).

A national security exception enables a State to introduce emergency measures when its essential security interests are threatened or for the maintenance of international peace and security, even if these measures contradict substantive IIA obligations. Such measures may include the freezing of assets, other types of sanctions, or discriminatory treatment of investors of certain nationalities (or of foreign investors in general). In the pre-establishment context, such measures may include refusal of access to specific projects or transactions in industries considered as strategically important (such as manufacturing of arms, telecommunications, transportation, energy or water supply).

Assuming countries wish to include a national security exception into IIAs, they have a number of options at hand, all with their pros and cons (figure IV.6).

Figure IV.6.

Options for IIA reform: National security exception



Source: UNCTAD.

The first set of options relates to the types of situations that are covered and the degree of specificity that is applied to this policy choice. Countries can use a broadly formulated national security exception, e.g. for measures necessary for the protection of (or, with a looser nexus requirement, “directed to” or “designed to” protect) the State’s “essential security interests”. A related option is to define national security more specifically, e.g., as including measures taken to address a serious economic crisis situation or to maintain international peace and security.

Countries may take other steps to fine-tune, i.e. circumscribe, the coverage of treaty exceptions; for example, by including a reference to actions taken in pursuance of States’ obligations under the UN Charter or by specifying that the exception covers only certain types of measures such as those relating to trafficking in arms or nuclear non-proliferation, applied in times of war or armed conflict, etc. Finally, a national security exception can also refer to “public order” or to the protection of “public security”, with or without a clarification that this applies only to situations in which a genuine and sufficiently serious threat is posed to one of the fundamental interests of society.

Although national security exceptions are sometimes seen as reducing or limiting the protective strength of a treaty, clarifying and fine-tuning exceptions can help to increase predictability in the application of the clause and the circumscription of its application. A reference to the UN Charter can also help foster coherence between different bodies of law.

A second set of options relates to the standard of review which ISDS tribunals should apply to measures invoked for national security reasons. Here, the important parameter of a national security clause is whether it is formulated as “self-judging”. If this is the case, the appropriateness of the measure in given circumstances is judged only by the invoking State itself (e.g. “measures which it considers to be in its essential security interests”). A “self-judging” exception gives host States a wide margin of discretion in its application and may trigger the perception that the treaty’s protective value is somewhat reduced. It should be noted, however, that depending on the formulation chosen, a tribunal may still be able to review whether the exception is being relied upon in good faith and without manifest abuse.

In addition to these provisions, other IIA clauses have a bearing on safeguarding the right to regulate in the public interest. Although they figure less prominently in the reform discussion, they are equally important for States to consider. These clauses include the preamble, provisions related to other substantive standards of treatment and provisions that delineate the scope and operative definitions of the treaty.

- **Preamble**

The preamble is a clause with a cross-cutting impact. It plays a role in interpreting all other IIA obligations and can help address all of the five reform objectives identified. Thus, by identifying and clarifying the treaty objectives in the preamble, contracting parties provide important guidance for tribunals in investment disputes.

As regards the specification of treaty objectives, contracting parties can clarify that the IIA is not only about investment protection and promotion, but also is intended to serve other public policy interests, such as sustainable development, job creation, technology and know-how transfer. Another option is to state that the treaty is not intended to override national development objectives and that the parties preserve the right to regulate for legitimate policy objectives (e.g. public health, safety, environment, public morals, cultural diversity). The preamble can also clarify that the treaty is meant to be in line with the parties’ other international obligations (e.g. treaties on human rights,

environment, cultural heritage), and that the parties should not derogate from such obligations in order to promote and protect investment.

- **Scope of the treaty**

Typically, IIAs are broadly formulated, covering all sectors of economic activities and all domestic measures that affect foreign investment. Nevertheless, countries may have an interest in carving out specific sectors or policy areas from the treaty scope (UNCTAD, 2010c).

Sensitive industries may include social sectors (e.g. education, health, the provision of water), cultural industries, or defence. Exclusion can be full (from all treaty obligations) or partial (from some obligations only). As regards the carving out of policy areas, a potential candidate is taxation or issues related to the restructuring of sovereign debt (UNCTAD, 2011b). Again, this can be a full or partial exclusion. For example, taxation measures – while often excluded from the treaty scope – are sometimes kept subject to the expropriation and certain other IIA provisions (Japan–Mozambique BIT (2013)). Broad exclusions can help preserve the right to regulate, but they can also raise concerns that the treaty does not offer sufficient protections.

- **Definition of covered investment**

A traditional, open-ended definition of investment grants protection to all types of assets. Although such an approach may be aimed at promoting an investment-attraction effect, it can also cover economic transactions not contemplated by the parties or expose States to unexpected liabilities – hence, the importance of clarifying the scope of covered investments (UNCTAD, 2010c).

One possibility is to require investments to fulfil specific characteristics. Treaty practice has converged on a number of such characteristics, notably, the commitment of capital, the expectation of profit and the assumption of risk. Some IIAs include further criteria, e.g. “a certain duration” (Canada–EU CETA (draft, 2014)) or “establishing lasting economic relations” (Nigeria–Turkey BIT (2011)). A policy debate is under way as to whether an investment’s positive contribution to (sustainable) development should constitute an additional criterion, and what indicators to use in this regard (draft Indian model BIT (2015)). Although some tribunals have looked at the investment’s contribution to “economic development”, such an additional criterion may be difficult to apply

in practice and reduce predictability. The practice of some political risk insurers can, however, offer useful insights in this regard (OPIC, 2012).

IIAs could also compile an exhaustive list of covered investments or expressly exclude specific types of assets. Examples of assets that could be considered for exclusion are short-term, speculative or portfolio investments; sovereign debt obligations; claims to money arising from commercial contracts; or intellectual property rights that are not protected under the host State’s law. There is also the possibility of adopting a narrow, enterprise-based definition of investment (e.g. the draft Indian model BIT (2015)). A final option, complementary to any of the above, is to include a legality requirement; i.e. to specify that investment must be made in accordance with the laws and regulations of the host State.

- **Definition of covered investors**

An IIA’s definition of “investor” determines which investors are protected and able to bring claims against host States. Increasing policy attention has been given to “treaty shopping” (i.e. the channelling of investment through a “mailbox” company established in the territory of a Party in order to obtain treaty protection) and investment “round-tripping” (i.e., when domestic investors expatriate investment capital for reinvestment in their home State through a foreign corporate vehicle in order to take advantage of IIA protections not otherwise available to domestic investors) (UNCTAD, 2010c).

There are several policy options to focus or narrow the range of protected investors. A first option is to include additional criteria in the definition of “investor”. For instance, it could be clarified that the investor (legal entity) must not only be incorporated but also engaged in “real/substantial business activities” in the home country.

A second option is to include a “denial of benefits” (DoB) clause to allow States to deny treaty benefits to “mailbox” companies (which are identified using the criteria of “substantial business activity” and the nationality of the company’s ultimate controller) as well as to investors from countries with no diplomatic relations with the host State and/or investors from countries under economic embargo. When designing a DoB clause, attention needs to be given to the time when the clause can be invoked. Several tribunals have held that the DoB clause may not be invoked against

an investor after it initiates a formal arbitration claim, severely limiting the effective scope of these clauses.

With respect to natural persons, there may be a need to decide whether individuals with dual nationality should be protected under the treaty or not.

- **National treatment**

The national treatment clause protects covered investors against nationality-based discrimination and guarantees them a level playing field with comparable domestic investors. For a number of reasons, countries – in particular developing countries – may have an interest in limiting the scope of the national treatment principle. For example, States may wish to accord more favourable treatment to socially or economically disadvantaged minorities or ethnic groups.

A number of options exist to address these policy challenges. One option, included in a number of IIAs, is to clarify that the principle of non-discrimination applies only to investors “in like circumstances” and to establish criteria for making this assessment (e.g. COMESA Investment Agreement (2007, not in force), draft Indian model BIT (2015)).

A second option is to exclude sensitive policy areas (e.g. support programs for local start-ups or economic support for specific ethnic groups) from the national treatment obligation. A third option, rarely used, would be to make national treatment “subject to domestic laws and regulations”. Finally, some IIAs omit the national treatment clause altogether (e.g. United Arab Emirates–Viet Nam BIT (2003)).

- **Umbrella clause**

An “umbrella” clause, frequently included in traditional IIAs, requires a host State to respect any obligation that it has assumed with regard to a specific investment (e.g. obligations undertaken in an investment contract or concession agreement). The clause thus brings these contractual obligations under the “umbrella” of the IIA, meaning that their breach becomes a violation of the IIA.

Umbrella clauses have proven problematic in application, both with respect to the scope of the obligation undertaken and with respect to the potential for parallel dispute settlement proceedings (e.g. one proceeding to address the breach of contract claim and a parallel proceeding to address the alleged breach of the umbrella clause). Countries wishing to

avoid the potentially far-reaching legal consequences of an umbrella clause can clarify and reduce its scope. For instance, States can clarify that the clause covers only “written obligations” and that the obligations must be “entered into” with respect to specific investments. They can also indicate that the umbrella clause applies only to conduct that constitutes an exercise of sovereign powers by a government, i.e. not an ordinary breach of contract by the State. Another option is to exclude the applicability of the IIA dispute settlement mechanism to claims arising out of the umbrella clause. Finally, an increasing number of treaties omit the umbrella clause (chapter III).

- **Remedies and compensation**

Traditional IIAs do not specify the type of legal remedies a tribunal can order against a State. Furthermore, these IIAs contain no provisions as to the appropriate measure of compensation in the event of a breach of the treaty, with the notable exception of provisions on expropriation which have long included language regarding compensation. Several concerns have emerged in this connection. First, some arbitral tribunals have affirmed their power to grant any remedy they consider appropriate, including non-pecuniary remedies (e.g. an order to a State to revoke, amend or abstain from applying certain legislative, administrative or judicial acts). There are concerns that this type of remedy unduly interferes with States’ sovereignty, especially if ordered by an ad hoc tribunal; others argue that there would be benefits in leaving the State the freedom to choose between pecuniary and non-pecuniary remedies. Second, some arbitral tribunals have granted monetary awards perceived as exorbitant in light of the State’s public finances and compared with what the investor could conceivably obtain under the domestic rules.

There are several policy options – which can be used in a complementary manner – to deal with these concerns.

A first option is to set express limits on the remedial powers of tribunals. The growing trend has been to limit the available remedies to two forms: monetary damages and restitution of property, excluding the order to withdraw or amend a measure.

A second option concerns the standard of compensation for expropriation. The majority of IIAs set out a standard of prompt, adequate and effective compensation (the so-called “Hull formula”), rigidly

connected to the investment's fair market value. This standard may result in high amounts of compensation, especially if the expropriated investment is valued using certain valuation methods such as the discounted cash flow analysis. Countries concerned about this possibility could consider terms such as “appropriate”, “fair” or “equitable” compensation and “relax” the link between the standard of compensation and the market value of investment (SADC model BIT (2012), draft Indian model BIT (2015)). Another approach would be to provide that – in case of lawful expropriation – arbitrators should rely on asset-based valuation methods (as opposed to methods based on future cash flows) and that, in any case, the award may not exceed the amount of capital invested plus interest at a commercially reasonable rate.

A third option is to include provisions that address the calculation of damages for treaty breaches that do not involve expropriation, with a view to limiting the extent of States' financial liabilities (BMW, 2015).

- **Exceptions to free transfer of funds obligation**

Most IIAs contain a clause granting investors the right to transfer funds, profits, capital and other payments freely and without delay. In times of economic or financial crises, this guarantee may be in conflict with the regulatory needs of host countries to impose capital controls or to put in place prudential measures aimed at ensuring the integrity and soundness of the financial system. Accordingly, the IMF has issued an official “institutional view” that encourages nations to regulate capital flows under certain circumstances and has begun recommending such measures to member countries (IMF, 2012). The WTO similarly includes safeguards that allow nations to regulate the inflow and outflow of capital. Specifically, the GATS includes a “prudential carve-out” (Article 2, Annex on Financial Services) and a balance-of-payments exception (Article XII).

There are a number of options for addressing these challenges in IIAs. A first, increasingly used option is to include an exception for situations when a country experiences (or there is a threat of) serious balance-of-payments difficulties or other serious financial and economic crises (e.g. serious difficulties for macroeconomic management, in particular, monetary and exchange rate policies). A second option is to provide an exhaustive list of the types of funds that are freely transferable. A third, more general option is to make the free-transfer obligation subject to

investors' compliance with certain key laws that aim at the protection of third parties (e.g. creditors) and prevention of illegal activities. The Austria–Nigeria BIT (2013) and Canada–Colombia FTA (2008) provide examples of this approach.

b. Reforming investment dispute settlement

Options include reforming the existing mechanism of ad hoc arbitration for ISDS while keeping its basic structure, and replacing existing ISDS arbitration systems.

Investor-State dispute settlement through international arbitration (ISDS) is at the heart of the IIA reform debate. The increase in the number of ISDS cases (box IV.2) in recent years, together with sometimes expansive, unexpected and inconsistent interpretations of IIA provisions by arbitral tribunals, has resulted in mounting criticism of the existing ISDS system (UNCTAD, 2015, 2014b, 2014c, 2013a). This situation has triggered a worldwide debate about the pros and cons and about whether “to have or not to have” ISDS (table IV.5). Responding to these developments, a number of countries have been reassessing their positions on ISDS and have already adopted certain reform measures.

Two broad alternatives exist: to keep and reform ISDS, as some countries have done (e.g. in the Canada–EU CETA (draft 2014)) or to abandon and/or replace ISDS (table IV.6). Maintaining the status quo is hardly an option, given today's criticism of the existing system.

This section offers a number of concrete policy options in this regard. Countries can pick and choose, and adapt and adopt the various options. They can use them in isolation or in combination, taking a hybrid approach. Whatever option countries prefer, they need to bear in mind three challenges: (i) what is needed is comprehensive reform, applying not only to ISDS but also to the substantive IIA provisions, since these are the root cause of many problems; (ii) reform steps ideally should not only apply to future treaties, but also address the stock of existing IIAs – the IIA “survival clause” poses challenges in this regard; and (iii) IIA reform is not enough – domestic capacity-building is needed for improving developing countries' administrative and judicial capacities, a prerequisite for some of the reform options suggested below.

Building on its past work on ISDS (e.g. the 2012 Policy Framework, *WIR13* and the Pink Series Sequel on ISDS (UNCTAD, 2014b)), UNCTAD identifies three sets

Box IV.2.**Facts and figures (as of end 2014)****The number of cases and countries involved**

- 608 known treaty-based ISDS cases brought
- 99 governments have been respondents
- 70 per cent of all known cases brought against developing and transition economies
- 80 per cent of all known claims brought by investors from developed countries

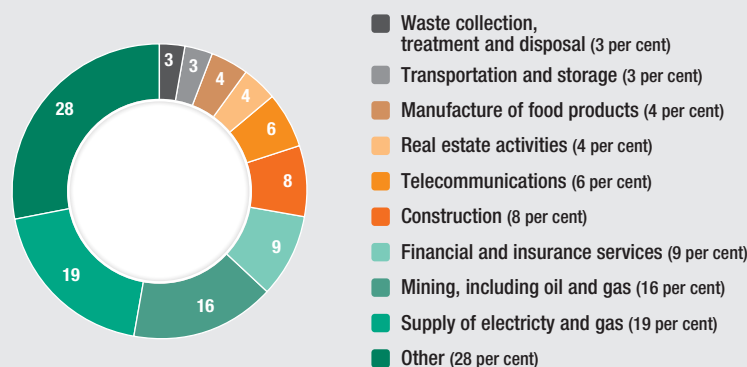
Results of 405 concluded ISDS cases (see chapter III)

- 36 per cent in favour of the State
- 27 per cent in favour of the investor
- 26 per cent settled

Amounts claimed and awarded

- \$1.1 billion in damages claimed in a case, on average (based on 447 cases for which this information is available)
- 65 known cases with claims exceeding \$1 billion
- 37 cases with claims between \$500 million and \$999 million
- \$575 million in damages awarded, on average (based on 106 cases for which this information is available; amounts do not include interest)
- \$40 billion – largest amount ever awarded by an investment tribunal (UNCTAD, 2015)

Figure box IV.2. | ISDS cases by economic sector
(Per cent)

**State conduct most commonly challenged by investors**

(preliminary data based on cases where information is available)

- Cancellations or breaches of investment contracts (29 per cent of cases)
- Legislative changes (25 per cent)
- Direct expropriation or seizure of investment (15 per cent)
- Tax-related measures (11 per cent)
- Refusal to grant or revocation of licenses (8 per cent)
- Abusive treatment or failure to protect investment (7 per cent)

Other challenged measures relate to judicial acts or omissions, withdrawal of incentives, freezing of bank accounts, sovereign debt restructuring, damage from armed conflict, interference with management of an investment, and measures to combat the 2001 financial crisis in Argentina.

The FDI background to ISDS (economic context)

- \$27 trillion in global FDI stock
- 100,000 multinational companies
- 890,000 foreign affiliates worldwide

Source: UNCTAD.

of options for improving investment dispute settlement (table IV.6), along the two prongs of actions: reforming the existing ISDS system or replacing it. Some of these reform options can be combined and tailored to meet several reform objectives.

Fixing the existing ISDS mechanisms

This set of reform options aims at reforming existing ISDS mechanisms *while keeping their basic structure*, namely that investors can bring claims against host States to ad hoc arbitral tribunals. Reform elements could be the inclusion in IIAs of new provisions

designed to (1) improve the arbitral process; (2) refine investors' access to investment arbitration; (3) establish filters for channelling sensitive cases to State-State dispute settlement; and (4) introduce local litigation requirements. These reform options could be implemented by contracting States in existing and future individual IIAs and would not require coordinated actions by a large number of countries.

1. Improving the arbitral process

This option focuses on reforming the way arbitration proceedings are conducted while preserving the main features of the ISDS system. The goals of such

Table IV.5. Summary of arguments put forward in favour and against ISDS

Main arguments made in favour of ISDS	Main arguments made against ISDS
<p>ISDS:</p> <ul style="list-style-type: none"> Provides an additional avenue of legal redress to covered foreign investors and enforces the substantive treaty obligations. Allows foreign investors to avoid national courts of the host State if they have little trust in their independence, efficiency or competence. Avoids recourse to diplomatic protection (investors do not need to convince their home State to bring claims or to exercise diplomatic protection). Ensures adjudication of claims by a qualified and neutral tribunal. Removes any State immunity obstacles that may complicate domestic legal claims in some States. May be faster than domestic court procedures in some countries. Allows recognition and enforcement of arbitral awards in many jurisdictions (under the ICSID Convention or the New York Convention). 	<p>ISDS:</p> <ul style="list-style-type: none"> Grants foreign investors greater rights than those of domestic investors, creating unequal competitive conditions. Exposes host States to legal and financial risks, without bringing any additional benefits, and can lead to "regulatory chill". Lacks sufficient legitimacy (is modelled on private commercial arbitration, lacks transparency, raises concerns about arbitrators' independence and impartiality). Fails to ensure consistency between decisions adopted by different tribunals on identical or similar issues. Does not allow for correcting erroneous decisions. Creates incentives for "nationality planning" by investors from third countries (or from the host State itself) in order to gain access to ISDS. Is very expensive for users. Holds little additional value in the presence of well-established and well-functioning domestic legal systems.

Source: UNCTAD.

Table IV.6. Sets of options for reforming investment dispute settlement

Reforming existing investor-State arbitration		Replacing existing investor-State arbitration
Fixing existing ISDS mechanisms	Adding new elements to existing ISDS mechanisms	
<ol style="list-style-type: none"> Improving the arbitral process, e.g. by making it more transparent and streamlined, discouraging submission of unfounded claims, addressing ongoing concerns about arbitrator appointments and potential conflicts. Limiting investors' access, e.g. by reducing the subject-matter scope, circumscribing the range of arbitrable claims, setting time limits, and preventing abuse by "mailbox" companies Using filters for channelling sensitive cases to State-State dispute settlement Introducing local litigation requirements as a precondition for ISDS 	<ol style="list-style-type: none"> Building in effective alternative dispute resolution Introducing an appeals facility (whether bilateral, regional or multilateral) 	<ol style="list-style-type: none"> Creating a standing international investment court Replacing ISDS by State-State dispute settlement Replacing ISDS by domestic dispute resolution

Source: UNCTAD.

modifications are to (i) enhance the legitimacy of the ISDS system, (ii) enhance the contracting parties' control over the interpretation of their treaties and/or to (iii) streamline the process and make it more efficient.

Specific reform steps may include the following:

- *Providing for more transparency*, for example, by granting public access to arbitration documents (including settlement agreements) and arbitral hearings and allowing the participation of interested non-disputing parties such as civil society organizations (UNCTAD, 2012c).
- Ensuring that *persons adjudicating disputes possess the requisite skills and are fully independent, impartial, free from conflicts of interest and "affordable"* to the parties, for example by creating rules on qualifications, conduct and/or remuneration of arbitrators (e.g. through a code of conduct).
- *"Breaking the link" between the parties to the dispute and the arbitrators*, for example, by establishing a roster of qualified arbitrators agreed upon by the contracting parties and determining by lot the arbitrators who sit on a specific case.
- *Enhancing the contracting parties' role in interpreting the treaty*, for example, by establishing mechanisms for the provision of binding joint party interpretations and facilitating interventions by the non-disputing contracting parties (UNCTAD, 2011c).
- *Strengthening the contracting parties' control over adjudication of certain sensitive issues*, for example, by requiring tribunals to refer certain matters (e.g. taxation, financial services (prudential carve-out), scheduled reservations) for joint determination in the first instance by the treaty parties, i.e. as a "filter" mechanism (see also (3) below) (Canada–EU CETA (draft, 2014), NAFTA (1992)).
- *Avoid wasting resources on full-length proceedings in case of manifestly unmeritorious claims*, for example, by including a mechanism for early discharge of frivolous claims.²⁴
- *Providing for a more equitable distribution of costs and discouraging submission of unfounded claims*, through appropriate allocation of legal costs (fees paid by each party to arbitrators, lawyers, experts and other costs); for example, by expressly adopting the "loser pays" or the "cost follows the event" principles.

- *Preventing investors from seeking relief for the same violation in multiple forums*, for example, by including a "waiver" ("no-U-turn") clause (in contrast to the "fork-in-the-road" clause, often included in traditional BITs, "waiver" clauses do not discourage investors from first trying to obtain redress in the domestic courts of the host State).

2. Limiting investors' access to ISDS

This approach aims to narrow the range of situations in which foreign investors may resort to international arbitration, thereby reducing States' exposure to legal and financial risks posed by ISDS.

There are several possibilities to achieve this objective:

- *Excluding certain types of claims from the scope of ISDS*. This could apply, for instance, to certain sectors considered particularly sensitive (e.g. for claims relating to financial institutions and real estate), specific treaty provisions (e.g. pre-establishment obligations) or sensitive policy areas (e.g. measures adopted on national-security grounds). Exclusions can be party-specific or apply to all contracting States.
- *Circumscribing admissible claims to treaty breaches only*. This approach would exclude all non-treaty-based claims (e.g. alleged violations of domestic law, customary international law or investment contracts), but still provide investors with means to enforce the substantive protections found in the IIA. It can be combined with an applicable-law clause that allows application of the treaty and international law only (but not domestic law).
- *Prohibiting recourse to ISDS after a certain time period has passed from the events giving rise to the claim ("limitations period")*, e.g. three years. This introduces a time factor that fosters certainty and predictability with regard to the assumed treaty obligations. Without it, claims could be filed any time, exposing States to uncertainty. It may be useful to clarify whether the limitation period includes the time that the investor spends pursuing its claims in domestic courts.
- *Preventing "abuse" of the treaty by denying ISDS access to investors who engage in "treaty shopping" or "nationality planning" through "mailbox" companies that channel investments but do not engage in any real business operations in the home State*.
- *Providing for State consent to international investment arbitration on a case-by-case basis*.

3. Using filters for channelling sensitive cases to State-State dispute settlement

This reform option provides for State-State dispute settlement if a joint committee fails to resolve a case. While maintaining the overall structure of today's ISDS mechanism, this constitutes a "*renvoi*" of disputes on sensitive issues to State-State dispute settlement; e.g. whether a measure is a "prudential" measure aimed at safeguarding the integrity and stability of the financial system or whether a taxation measure constitutes an expropriation. In this case, the ISDS proceeding is suspended until the State-to-State tribunal renders its decision. The latter is binding on the ISDS tribunal. This approach has been adopted in the BIT concluded between Canada and China in 2012 and in NAFTA (for investment disputes in financial services). The "filter" was evoked by the European Commission in its Public Consultation on the TTIP.

State-State dispute settlement (be it in the form of arbitration, judicial or other procedures) may be better suited for sensitive issues of systemic importance, such as those relating to the integrity and stability of the financial system, the global system of international tax relations, or public health. For example, States are likely to use only those legal arguments with which they would feel comfortable in cases directed against them.

4. Introducing local litigation requirements as a precondition for ISDS (including exhaustion of local remedies)

This reform option aims to promote recourse by foreign investors to domestic courts while retaining the option for investor-State arbitration, as a remedy of last resort. In so doing, it would respond to some of the concerns arising from the steep rise in ISDS cases over the last decade. Domestic resolution of investment disputes is available in virtually every jurisdiction.

Two options could be considered to foster the use of domestic courts, without foreclosing investors' resort to ISDS:

- The IIA could require investors to exhaust local remedies before accessing international arbitration.
- The IIA could set out a "local litigation requirement", i.e. specify that the recourse to international investment arbitration becomes possible only after a certain period of time (e.g. 18 months) of litigating the dispute in domestic courts.

Requiring dispute resolution before the domestic courts of the host country puts foreign investors on an equal footing with domestic investors (as well as with foreign investors from States which do not have an IIA with the host country). It would also help establish a level playing field among foreign investors, as the financial costs associated with international investment arbitration may preclude small and medium-sized enterprises from using it. In addition, national jurisdictions usually also include a right to appeal first-instance decisions and are well-suited to interpret and apply the domestic laws of the host State. Also, the argument has been made that reliance on ISDS is less important in countries with a sound legal systems, good governance and local courts' expertise. Finally, the argument is gaining ground that rather than focusing exclusively on ISDS, domestic reforms aimed at fostering sound and well-working legal and judicial institutions in host States are important. This may ultimately help remedy some of the host-State institutional deficiencies which IIAs and the ISDS mechanism were designed to address.

At the same time, however, there are concerns that some host States cannot guarantee an efficient and well-functioning domestic court system. Local courts may lack independence and be subject to political control and abuse by the State, including delaying tactics. Also, this approach would be particularly challenging in governance weak counties, where local court decisions could be difficult to enforce. In other jurisdictions, owing to the high workload of local tribunals, the exhaustion of local remedies may span a long period of time and thereby reduce the value of the investment arbitration option. Furthermore, if the investor switches to ISDS after local litigation as an "appeal" to a domestic court ruling, this would potentially increase the legitimacy concerns with ISDS. Finally, local courts may not have the legal competence to apply international law – many jurisdictions do not allow for the direct applicability of IIAs, which would be a prerequisite for local enforcement of treaty obligations. In order for local enforcement to function therefore, such countries would have to transform the treaty into national law.

Adding new elements to the existing ISDS mechanisms

These policy options add new elements to complement the existing investor-State arbitration mechanism.

They can be combined with the above-mentioned improvements of the mechanism.

- **Appeals facility**

This option would preserve the structure of the existing investment arbitration mechanism and add a new layer to it. An appeals facility could take two main forms: either a standing or an ad hoc body. It would have the competence to undertake a substantive review and correct the arbitral tribunals' first instance decisions.

An appellate mechanism would be given review jurisdiction that goes beyond the scope of review available under the existing annulment procedures under the ICSID Convention. The current ICSID annulment procedure, for example, does not entail a review of the merits and is limited to review on certain specified and limited grounds, e.g. irregular constitution or corruption of the arbitral tribunal, serious departure from a fundamental rule of procedure, failure to state reasons for the award or a manifest excess of power. As a result, an ICSID annulment committee may find itself unable to annul or correct an award, even after having identified "manifest errors of law". An appeals facility could be given this broader power of review. In so doing, it could serve to enhance the predictability of treaty interpretation and improve consistency among arbitral awards. All this could significantly contribute to enhancing the political acceptability of ISDS and the IIA regime as a whole.

A joint committee established under a treaty could be tasked to hold consultations on the establishment of an appellate mechanism and identify specific issues for consideration, including the nature and composition of an appellate mechanism, and the applicable scope and standard of review (Canada-EU CETA (draft 2014), United States model BITs (2004, 2012)).

Should countries decide to opt for establishing such an appeals mechanism, several sets of issues would need to be resolved:

- *First, issues regarding the establishment of such a body, notably whether it would have a bilateral, regional or multilateral nature.* Although an appeals body may be easier to set up in a bilateral context, its expected function of fostering legal consistency and predictability would be more pronounced in a pluri- or multilateral context. In this connection, one would need to consider how the new mechanism could

be reconciled with, and perhaps integrated into, the ICSID Convention (e.g. to replace the existing annulment procedure), the UNCITRAL Arbitration Rules, the rules of other arbitral forums used in ISDS and potentially other relevant international instruments such as the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards. Furthermore, developing an appeals facility capable of promoting interpretive harmonization and legal consistency would seem to require a mechanism under which it has the competence for reviewing all awards rendered under a particular treaty.

- *Second, issues regarding whether the appeals facility would be permanent (an appellate body) or ad hoc.* Although ad hoc mechanisms would be easier to realize and involve lower costs, a permanent body may be more apt to ensure coherence in arbitral practice. An appellate body with permanent judges, appointed by States from a pool of eminent jurists, would allow the appeals facility to become an authority capable of delivering consistent – and balanced – opinions, which would rectify some of the legitimacy concerns about the current ISDS regime. Authoritative pronouncements by an appeals facility on issues of law would guide both the disputing parties (when assessing the merits of their respective cases) and arbitrators adjudicating disputes. At the same time, however, an appellate body with the authority to issue rulings with the force of precedents could place new limitations on the sovereignty of contracting parties through the establishment of an independent body of jurisprudence.

- *Third, issues regarding organization and institutional set-up of such a body.* For example, who would elect the members of an appeals facility? How would they be elected? What would be the length of their tenure? What principles or code of conduct would govern their activities both with respect to their work within the facility and without it? What type of secretarial support would they receive? Who would finance it? Where would it be located?

- *Fourth, issues with regard to the added time and cost of the proceedings.* The introduction of an appellate stage would add another layer of proceedings to the arbitration process, and care would need to be taken to put in place an efficient process, including timelines (e.g. as for the WTO Appellate Body).

Further, proceedings at an appellate stage would also involve additional costs for both investors and host States.

- *Fifth, issues related to the competence of such a body.* These issues include the type of review available, the standard of review to be applied and the type of IIA decisions/awards which the body would be competent to address. For example, would the body be able to review only issues of law or also issues of fact? Would the body be able to remand an erroneous decision for reconsideration only by the tribunal that adopted it, or would it have the power to correct errors directly? Would the appellate facility have review power only over final awards or also over other decisions, e.g. on provisional measures and on jurisdictional issues?

- **Building in effective alternative dispute resolution**

This approach to ISDS reform promotes the use of alternative dispute resolution (ADR) mechanisms as a step before the commencement of international investment arbitration (UNCTAD, 2010d, UNCTAD 2010e). Although ADR cannot in itself solve key ISDS-related challenges, it can reduce the number of disputes which result in full-scale arbitration. This renders it a complementary, rather than a stand-alone, avenue for ISDS reform.

Whereas arbitration – like adjudication – follows an adversarial procedure leading to a binding decision by a third party, the outcome of ADR mechanisms ultimately requires acceptance by both parties. ADR has value because it can help resolve disputes at an early stage, thereby preventing them from severely and permanently damaging the relationship between the investor and host country. Because of its consensual nature, ADR may be particularly useful in cases of disputes where the parties consider it important to continue their investment cooperation beyond the present dispute. ADR also tends to be more informal and flexible than investor-State arbitration: its purpose is to find a solution that will be acceptable to both parties. If successful, therefore, ADR can help save time and money.

A limitation of ADR is that there is no guarantee that ADR procedures will lead to the resolution of a dispute; unsuccessful ADR can, therefore, increase the costs and time involved. That said, even if unsuccessful, ADR can serve to clarify the issues in dispute between

the parties and help to streamline subsequent arbitral proceedings.

ADR may not always be feasible or acceptable to the host country, depending on the nature of the policy measure challenged by an investor, e.g. where the case relates to legislative measures. Moreover, given the consensual nature of ADR, a mediated outcome of the dispute that has not been endorsed by both parties cannot be enforced. Therefore, if one party does not respect the compromise solution proposed by ADR, binding arbitration may still become unavoidable.

The following policy options suggest actions at different levels of governance: the national and the international level (the IIA). Again, implementation of these options can be complementary.

At the *national level*, countries may want to consider ways in which to strengthen dispute prevention and management policies by

- Emphasizing dispute prevention mechanisms through fostering information sharing between State agencies for the monitoring of sensitive sectors/industries for early warning signals of potential disputes.
- Establishing interinstitutional arrangements to address potential and emerging disputes more effectively.
- Empowering a particular agency to act as lead for the pursuit of amicable settlements (and potential subsequent arbitration).
- Creating investment ombuds offices or specific investment agencies to take the lead in resolving conflicts with investors early on.

At the *international level*, IIAs can include provisions on dispute prevention and management and integrate them into the IIA-based dispute settlement mechanism. Although a significant number of IIAs include the possibility of conciliation proceedings, policymakers may consider the need to strengthen existing mechanisms or add new ones (e.g. mediation). This can include

- Adding an ADR provision.
- Strengthening the use of existing ADR as a dispute prevention mechanism by making it a compulsory step before the commencement of investment arbitration, e.g. through establishing “negotiation periods” (specified time periods during which consultations and negotiations must be pursued).

- Providing for institutional State-State mediation and conciliation efforts prior to investor-State dispute settlement.
- Formulating new provisions for ADR and dispute prevention and management, as e.g. set out by Brazil in its recently concluded CFAs.

Replacing the existing ISDS system with other dispute resolution mechanisms

The options below would abolish the existing system of ad hoc investor-State arbitration and replace it with other mechanisms for settling investment disputes. Potential replacements include (1) the creation of a standing international investment court, (2) State-State dispute settlement, and/or (3) reliance on domestic judicial systems of the host State.

The replacement options differ in the extent of change they bring. States can focus on one of the options or can pursue them in parallel or in combination. For example, option (3) can be combined with option (2) or option (1), which would preserve the possibility of some sort of international legal proceedings.

The option of replacing the ISDS has been recently pursued in the Australia–Japan Economic Partnership Agreement (EPA) (2014), the Australia–Malaysia FTA 2012, the Australia–New Zealand CEPA (2011), the Japan–Philippines EPA 2006, the Australia–United States FTA 2004, and the recently concluded CFAs by Brazil with Angola and Mozambique. These treaties leave investment disputes subject to domestic courts but complement this process with the possibility of State-State proceedings under the treaty.

1. Standing international investment court

This option retains investors' right to bring claims against host States but replaces the system of multiple ad hoc arbitral tribunals with a single institutional structure, a standing international investment court. Such a court would consist of judges appointed or elected by States on a permanent basis; it would be competent for all investment disputes arising from IIAs made subject to its jurisdiction and could also have an appeals chamber.

A standing investment court would be a public institution serving the interests of investors, States and other stakeholders and, more broadly, strengthening

the legitimacy of the investor-State regime. A standing court could contribute to enhancing consistency and predictability in the interpretation of international treaties. It could also strengthen the perceived and actual independence and impartiality of adjudicators, by establishing them as judges with security of tenure and exclusivity of function, i.e. judges, unlike arbitrators in the present regime, would not be permitted to continue serving as counsel or expert witnesses. Moreover, a court could be competent for all investment disputes under an IIA, i.e. both investor-State and State-State proceedings. It has also been suggested, that the competence of the court be broadened, depending upon the content of the IIAs made subject to its jurisdiction, in particular by giving legal standing or procedural rights to other stakeholders (Bernasconi, 2015).

Clearly, establishing such a court raises a number of important legal and political challenges, and, in its very nature, would constitute a long-term project. As countries move in this direction, they need to consider a number of key issues (see also appeals facility):

- *Issues regarding the establishment of such a court*, such as the need to build consensus among a critical mass of countries around a convention establishing such a court.
- *Issues regarding organization and institutional set-up*, such as the location, financing and staffing of the court.
- *Issues around the participation of countries* in the court, namely how to transition from a possible bilateral court established between key trading blocks, as recently proposed by the European Union (European Commission, 2015), to a more universal structure serving the needs of developing and least developed countries.
- *Issues around the competence of the court*, such as the type of IIAs and cases it is competent to address.

Multilateral consensus-building would help respond to the perception that such a court would work best in a plurilateral or multilateral context. It could help seek solutions for making a new court fit the fragmented global IIA regime, which consists of thousands of mostly bilateral IIAs. Similarly, multilateral consensus building would respond to the fact that a standing investment court may well start at a smaller scale, with an opt-in mechanism for those States wishing to join.

Table IV.7.

Summary of arguments put forward in favour and against State-State arbitration

Main arguments made in favour of State-State dispute settlement	Main arguments made against State-State dispute settlement
<ul style="list-style-type: none"> • Could avoid broader legitimacy concerns that have been raised in respect of ISDS. • Could help to filter out frivolous claims. • Only States can bring claims under international law as they are the principal subjects of the system. • May help to avoid controversial legal issues related to challenges to public policies. • States would not make certain types of legal arguments that could be used against them in the future. • Does away with the privileges that ISDS bestows on foreign investors. 	<ul style="list-style-type: none"> • Could politicize investment disputes-commercial dispute would become a matter of State-State diplomatic confrontation. • Investor interests could become a bargaining chip in international relationships. • May be more cumbersome and lengthy for investors due to bureaucracy in either or both disputing States. • May disadvantage SMEs vis-à-vis larger companies. • Raises challenges for States in terms of costs of proceedings and legal remedies. • Has implications for States in terms of administrative and institutional resources.

Source: UNCTAD.

2. Replacing ISDS with State-State dispute settlement

State-State arbitration is included in virtually all existing IIAs, and it is also the approach taken by the WTO for resolving international trade disputes.

Unlike the fostering of State-State dispute resolution as a complement to ISDS, this option presupposes that State-State proceedings would be the only way of settling investment disputes at the international level. The home State would have discretion on whether to bring a claim. States would need to decide on the court that should hear a case; options include the International Court of Justice, ad hoc tribunals or an international court as envisaged above.

State-State arbitration has a number of pros and cons (table IV.7).

Replacing ISDS with State-State dispute settlement could be one way to reinstate countries' confidence in the IIA regime, address the legitimacy concerns raised with ISDS – by filtering out frivolous claims and avoiding controversial legal issues related to challenges to public policies; issues that could also be addressed by reforming the ISDS system (see above). More generally, this option would do away with the privileges that ISDS bestows on foreign investors; relying on State-State dispute settlement would be in line with the principle that only States can bring claims under international law. Also, States may be less likely to make certain types of legal arguments that could be used against them in the future.

However, a number of challenges arise with this option. The main one relates to a possible politicization of investment disputes, with all that this could entail (e.g. State discretion to pursue claims, elevating commercial disputes to the sphere of international relations, corporate lobbying). State-State dispute settlement could also be more cumbersome and lengthy for investors because of bureaucracy in either or both of the disputing States. It could also place SMEs at a disadvantage vis-à-vis larger companies as regards having their case heard. There are also implications for States' administrative and institutional resources. Furthermore, there are questions about how rulings would be implemented, what kind of remedies would be appropriate, how these could be enforced, and who would bear the costs of the proceedings. One important implication to take into consideration is that State-State dispute settlement could lead to the losing party being asked to bring a domestic measure into compliance with treaty obligations, not merely compensate for it (as is the case with ISDS), which implies a far greater intrusion into States' right to regulate.

There are also two other considerations to keep in mind. First, this option requires an identifiable home State, which in the case of complex multinational corporations, with affiliates in numerous countries and multiple ownerships, may be difficult to ascertain. Second, host States may wish to avoid being confronted with diplomatic protection by investors' home States.

Given that there are so far only four known cases to date, it is difficult to draw lessons from State-State arbitration in IIAs.⁷ Experience with State-State dispute settlement in the WTO or in the context of regional agreements (including with respect to the remedies used, i.e. pecuniary vs. non-pecuniary) can help offer insights regarding the pros and cons of this option, but one needs to bear in mind the specific characteristics of investment disputes.

Overall, although the option of replacing ISDS with State-State dispute settlement can help to address some of the concerns with regard to ISDS, it also raises a number of difficult challenges that would need to be addressed before taking this route.

3. Exclusive reliance on domestic dispute resolution

This option abolishes investors' right to bring claims against host States in international tribunals and limits their options for dispute resolution to domestic courts. Unlike the promotion of domestic resolution as a step preceding investor claims at the international level (e.g. exhaustion of local remedies, local litigation requirement), under this option, domestic judicial institutions would be the only and final mechanism for settling investor-State disputes. This option, it has been noted, has merits mainly in countries where reliance on ISDS is less important because of their sound legal systems, good governance and local courts' expertise.

As stated above, this option entails a number of pros and cons.

Arguments made in favour include that it treats foreign investors equally than domestic investors, and that it would help establish a level playing field among foreign investors. It may also support fostering sound and well-working legal and judicial institutions in host States through domestic reform, and could therefore help address some of the host-State institutional deficiencies which the IIA and the ISDS mechanism were designed to address. This would also respond to the increasing argument that rather than focusing exclusively on ISDS, domestic reforms aimed at fostering sound and well-working legal and judicial institutions in host States are important.

Arguments against this option rest on the concerns with regard to the independence, neutrality, efficiency,

and enforceability of local court rulings, especially in governance weak countries. In addition, there are concerns that local courts may take a long time to settle a dispute (including because of delaying tactics). In the end, this could render the IIA non-enforceable. Moreover, local courts may not have the legal competence to apply international law, since many jurisdictions do not allow for the direct applicability of IIAs (see above).

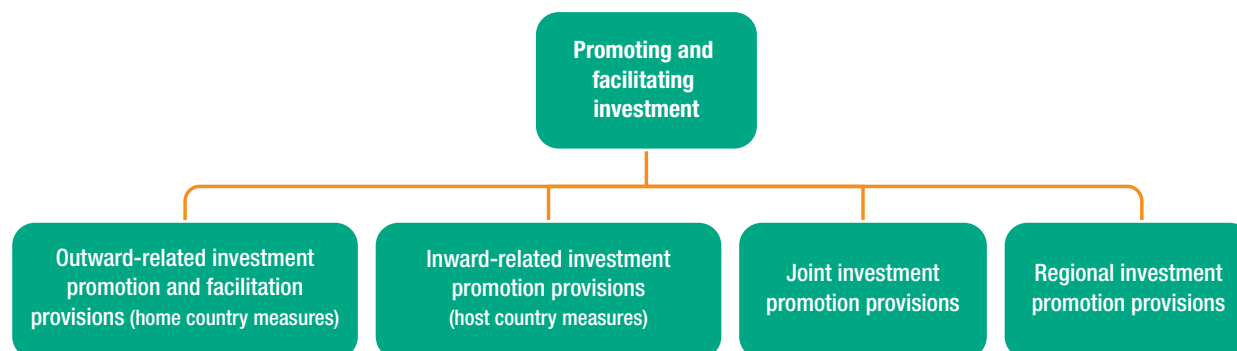
ISDS offers benefits for foreign investors and potential benefits for home and host States, but in its present incarnation the system suffers from significant drawbacks in its substance, procedure and functioning. There is thus a strong case for a systematic reform of investment dispute settlement. However, there are no quick and easy solutions. Reform options have their pros and cons, and pose their own specific challenges.

Some of the reform options discussed in this section, such as clarifying the content of individual IIA provisions or limiting the access of investors to ISDS, are less difficult to implement than others. Some of the reform options can be undertaken through unilateral or bilateral actions, while others require larger, regional, plurilateral or multilateral efforts. Although multilateral options would go furthest in systemically addressing areas of needed reform, they would also face more difficulties in implementation and require agreement between larger numbers of States on a series of important questions (see section C).

In addition, in reforming investment dispute settlement, attention needs to be given not only to the thousands of individual investment treaties, but also to the existing multilateral ISDS-related instruments, such as the ICSID Convention and the widely used UNCITRAL Arbitration Rules. In this context, it has to be noted that terminating membership in one arbitral institution (e.g. ICSID), depending on the language used in the treaty, may have the effect that investors bring cases in other arbitration forums or under other arbitral rules (UNCTAD, 2010a). Hence, this option would not only fall short of preventing State liability, but, depending on the circumstances, could also entail exposing the State to less favourable procedures.

Finally, ISDS is an enforcement mechanism for the substantive provisions of IIAs. Hence, ISDS cannot

Figure IV.7. Promoting and facilitating investment



Source: UNCTAD.

be looked at in isolation, but only together with the substantive investment protection rules embodied in IIAs. Without a comprehensive package that addresses both the substantive content of IIAs and ISDS, any reform attempt risks achieving only piecemeal change and potentially creating new forms of fragmentation and uncertainty.

c. Promoting and facilitating investment

Options include adding inward and outward investment promotion provisions, and joint and regional investment promotion provisions.

States generally conclude IIAs with a view to attracting investment and benefitting from it. However, IIAs rarely include proactive investment promotion or facilitation provisions that effectively encourage outward or inward foreign investment. Instead, IIAs only indirectly promote investment – by protecting it. And IIAs lack the provisions to ensure a certain “quality” of the investment attracted (i.e. investment that delivers concrete and measurable sustainable development benefits to the host country). Given that fostering investment and ensuring its quality is crucial for bridging the financing gap for the SDGs (*WIR14*), this is an important element of IIA reform.

This *WIR* offers a number of policy options for countries wishing to pursue this reform objective (figure IV.7). None of the options envisages a binding commitment for any of the contracting parties that would be enforceable through dispute settlement procedures. Most of the

options require a certain financial and institutional capacity to implement them and therefore would need to be complemented with technical assistance (on a non-reciprocal basis) or special and differential treatment, particularly where the agreement involves structurally weak and vulnerable economies. Finally, there is some doubt about the value added of including such provisions in IIAs, given that actual investment promotion and facilitation measures are largely undertaken at the national level. At the same time, regional initiatives have set best practices in this regard.

- **Outward-related investment promotion and facilitation provisions (home-country measures)**

Usually, IIAs regulate the behaviour of host countries. However, they can also include provisions directed at home countries. These options can, for example, emphasize the importance of specific home-country measures for promoting investment and/or stress home countries’ endeavours to undertake such measures.

A first option is to refer to home-country promotion measures and encourage countries to proactively implement them. Such measures can include granting financial support; e.g. loans, grants (including R&D funding), providing investment guarantees (i.e. to protect investors against certain political risks in the host country) or holding equity participation in investment projects.

A second option is to refer to home-country technical assistance. Such assistance can aim at improving host

countries' regulatory regimes and investment facilitation measures (e.g. help to simplify/streamline admission, registration or licensing procedures; to set up one-stop shops for registering an investment or a business; or to make available information on admission and establishment requirements, as well as on investment opportunities). Assistance can also aim at building institutional structures (e.g. judicial institutions, dispute prevention capacities, investment promotion agencies), at strengthening linkages between parties' research and academic centres or at facilitating feasibility studies for large investment projects.

A third option is to foster the sustainable development dimension of home-country investment promotion measures. Such provisions can state that the granting of outward incentives or investment insurance can be conditioned on the sustainable development impact or good governance record of the benefitting investment. The sustainable development impact can be specified, for example, by reference to specific sustainable development criteria (including for a specifically targeted region/community) or by reference to environmental and social standards (including (international) CSR standards). The United States' Overseas Private Investment Corporation (OPIC) uses about 30 development indicators to evaluate proposed projects. They include (i) job creation and human capacity-building (number of new jobs created, training and employee benefits); (ii) demonstration effects (e.g. technology and knowledge transfer, adoption of internationally recognized quality or performance standards); (iii) host-country impact (local procurement, and fiscal and foreign exchange impacts); (iv) environmental and community benefits (improvement of the environment and benefits to the local community); and (v) development reach (impact on basic infrastructure and/or its potential benefits to the poor and other underserved populations) (OPIC, 2012).

- **Inward-related investment promotion provisions (host-country measures)**

An IIA can identify actions by host countries. Similar to the outward-related provisions, such clauses can stress the importance of these measures and/or aim to link them to specific sustainable development outcomes. An option is to condition host-country incentives on the sustainable development impact of the benefitting investment and that these incentives are in line with other policy areas such as industrial development strategies and regional economic cooperation. A variant

is to condition the granting of investment incentives on the fulfilment of certain performance requirements, if this is permitted by the treaty.

Another variant is the establishment of an investment ombudsperson/facilitator in each contracting party. By monitoring and addressing investor concerns related to bureaucratic obstacles to doing business (e.g. business visas, obstacles to investment generally or to a specific investment project) an ombudsperson/facilitator can help ensure a business-friendly environment, and indirectly, affect a company's investment prospects and decisions. The ombudsperson/facilitator can be tasked with a number of activities, including addressing suggestions or complaints by investors and their home States; taking action to prevent, manage and resolve disputes; providing information on relevant legislative and regulatory issues; or promoting greater awareness and transparency.

Although such an ombudsperson/facilitator would mainly act at the national level, it can be mandated to report to and cooperate with the institutional mechanisms set up under the IIA. Some recent agreements, such as the CFAs signed by Brazil and Mozambique and by Angola and Brazil (2015), have such an ombudsperson/facilitator as one of their key features. The Foreign Investment Ombudsman in the Republic of Korea, which since 1999 has found solutions for grievances filed by foreign companies can also provide insights into the functioning of such a service.

- **Joint investment promotion provisions**

An IIA may also establish mechanisms, institutions and/or processes by which both home and host countries cooperate on investment promotion.

A first option is to establish a joint council or committee on investment promotion. Such a body can be part of the overall institutional framework between the contracting parties or be a self-standing specific element; it can be permanent or ad hoc. Such a body could meet regularly to oversee the implementation of the agreement and its investment promotion effect; to assess investment relations and identify new investment opportunities; to organize joint seminars, conferences, workshops or fairs; to monitor the implementation of specifically listed investment promotion and facilitation measures (e.g. related to the granting of business visas); to address specific concerns of investors (e.g. based on a report by an ombudsperson); or to design, implement and monitor progress on a thematic work

plan (e.g. on green investment, promotion of linkages, issues related to small and medium-sized enterprises (SMEs), global value chains (GVCs)).

A second option relates to linkages. For example, an IIA can seek to foster linkages and stimulate joint ventures, in particular with SMEs, by calling for the sharing of expertise on entrepreneurship and management, and by encouraging the publication of documents on SMEs and the exchange of information and know-how on topics such as taxes, finances and other conditions necessary for the setting up and expansion of SMEs.

A third option for joint investment promotion measures is to foster cooperation between national investment promotion agencies (IPAs). The IIA can provide a platform for IPAs to exchange experiences and best practices in investment promotion, to share information on concrete investment needs and opportunities (e.g. a pipeline of SDG-related investment projects), and to jointly present and prepare large investment projects identified as bilateral investment priorities. Again, all of this work can have a thematic focus. A related option is to expand such cooperation beyond IPAs and also include trade promotion organizations, including, for example, *joint trade and investment promotion missions*. This would respond to the emergence of GVCs where ever-intensifying trade and investment links call for closer coordination between domestic trade and investment promotion agencies.

Another option is cooperation and partnerships between outward investment agencies (OIAs) in home countries and IPAs in host countries, including for example, for the development and marketing of pipelines of bankable SDG investment projects (WIR14). Stimulating such OIA-IPA partnerships can bring information sharing, technical assistance and exchanges, the marketing, financing and facilitation of SDG investment projects as well as joint monitoring and impact assessment.

- **Regional investment promotion provisions**

IAs could also harness the potential of regional cooperation. Building on the promotion-related experiences of regional economic cooperation initiatives, a regional IIA could call for facilitating investment and for establishing joint investment promotion mechanisms and institutions for regional infrastructure projects (e.g. regional development corridors) and regional industrial

zones. This can also take the form of regional SDG investment compacts (WIR14).

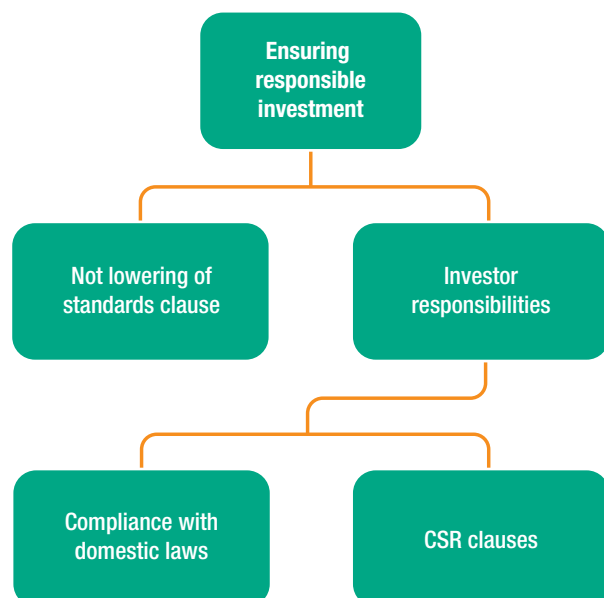
Regional investment promotion initiatives exist around the globe. The ASEAN Investment Agreement (2009) refers to the joint promotion of the region as an integrated investment area, offering special and differential treatment to new ASEAN members (technical assistance to strengthen their capacity for investment promotion) and tasking the AIA Council to provide policy guidance on investment promotion. Investment promotion is also included in the ASEAN–India Investment Agreement (2014) and the ASEAN–China Investment Agreement (2009). The COMESA Treaty (1993) establishes a centre for the promotion of industrial development that works closely and exchanges information with the investment promotion centres in the member States. The COMESA Investment Agreement (2007) obliges member States to strengthen the process of investment promotion, and the COMESA Coordinating Committee on Investment includes chief executives of IPAs. The SADC Investment Protocol (2006) sets out the activities of IPAs, e.g. to proactively identify business opportunities for investments, to encourage the expansion of existing investments, to develop a favourable investment image of their countries, to make recommendations for improvements of their countries as investment destinations, to keep track of all investors entering and leaving the country for the purpose of analysis in terms of investment performance, or to advise investors upon request on the availability, choice or sustainability of partners in joint venture projects. Finally, the Central American Common Market (CMA) Agreement on Investment and Trade Services (2002) provides for the promotion of investments within the region. For example, parties are mandated to provide, upon request, available information on investment opportunities (e.g. information on prospective strategic alliances among investors, and information on investment opportunities in specific economic sectors of interest to the parties), and to exchange information concerning foreign investment trends and available investment opportunities.

d. Ensuring responsible investment

Options include not lowering of standards clauses and provisions on investor responsibilities, such as clauses on compliance with domestic laws and on corporate social responsibility.

Figure IV.8.

Ensuring responsible investment



Source: UNCTAD.

Ensuring responsible investment has several dimensions. First, this reform objective may refer to maximizing the positive contribution that investors can bring to societies and/or to avoiding investors' negative impacts (e.g. on the environment, human rights, public health). Second, this reform objective may relate to investors' obligation to do what is required by law and/or to investors' response to societies' expectations that businesses comply with voluntary standards, i.e. that they do more than what is required by the law. The relevance and suitability of the policy options below differ depending on which of these aspects is the prime objective (figure IV.8).

Not lowering of standards clause

There is a concern that international competition for foreign investment may lead some countries to lower their environmental, human rights and other laws and regulations, and that this could result in a "race to the bottom" in terms of regulatory standards.

There are a number of options to address this concern.

A first option is to explicitly reaffirm parties' commitments under international agreements that they have concluded (e.g. in human rights, core labour rights or the environment). Doing so would not only help address

concerns about a "race to the bottom", but also help foster overall coherence and synergy between different bodies of international law (systemic policy challenge).

A second option is to include a "not lowering of standards" clause in the IIA. The normative intensity of the clause may be increased by stating that each contracting Party "shall ensure" (instead of "shall strive to ensure") that it does not waive or derogate from environmental, labour or other laws (United States model BIT (2012)). This option has similar benefits as the explicit reaffirmation option, as it can (partly) respond to concerns regarding a potential race to the bottom and help manage the interaction between IIAs and national policies.

Both of these options move the IIA regime beyond its traditional role of focusing solely on investment protection, and towards the goal of establishing and maintaining a regulatory framework that is conducive to sustainable development. By helping maintain – and build – a sound regulatory framework, these options can help promote responsible behaviour by investors and better manage the interaction between IIAs and domestic laws – and, possibly, help tip the balance in an ISDS case. However, there is a concern that such clauses, while constituting commitments of the contracting parties, are not enforceable in the traditional sense through ISDS and may have little concrete impact. Moreover, much of their impact depends on the quality of the host country's regulatory framework and its implementation.

A third option is to complement the above with a follow-up mechanism. This can include a mechanism for reporting on issues related to the implementation of the clause (including reporting on improvements of investment-related social, environmental or other laws and regulation).

Investor responsibilities

Most IIAs are asymmetrical in that they set out obligations only for States and not for investors. To correct this asymmetry, an IIA can also include provisions on investor responsibilities, as a few recent IIAs have done.

Although ensuring the responsible conduct of investors is a key objective of IIA reform, there are different views on the role of IIAs (in addition to, for example, national legal frameworks) in ensuring such conduct. Given the

wide recognition of investors' responsibility to respect human rights and to conduct business in a responsible manner (e.g. as set out in the UN Guiding Principles on Business and Human Rights), the recognition of a need to rebalance IIAs, including as part of IIA reform, is gaining prominence.⁹

Noting the evolving views on the capacity of international law to impose obligations on private parties, there are two broad sets of options: raising the obligations to comply with domestic laws to the international level and designing CSR clauses.

- **Compliance with domestic laws**

Numerous IIAs include a requirement for investors to comply with laws of the host State when making an investment. This general obligation could be further specified in the IIA; for instance, by stipulating that the investment can be held legally responsible for damage caused to human health or the environment. The potential impact of this stipulation would be even more relevant if extended to damages arising in the post-operations stage of an investment; e.g. when foreign investors fail to ensure orderly divestment or environmental clean-up of their activities. This raises the issue under which conditions a parent company could be held responsible for damage caused by its foreign subsidiaries (*WIR13*).

More broadly, countries can strengthen their domestic regulatory frameworks by incorporating international principles and standards related to social, human rights, health, environmental and other risks associated with investment. Again, sharing of experiences and best practices, technical assistance and capacity-building can facilitate efforts in this regard (*WIR11*).

- **CSR clauses**

The last decade has seen the development of corporate social responsibility (CSR) standards as a unique dimension of "soft law" that is rapidly evolving. CSR standards typically focus on the operations of MNEs and, as such, are increasingly significant for international investment.

The current landscape of CSR standards is multilayered, multifaceted, and interconnected. The standards of the UN, the ILO and the OECD serve to define and provide guidance on fundamental CSR issues. In addition, there are dozens of international multi-stakeholder initiatives, hundreds of industry association initiatives and thousands of individual

company codes providing standards for the social and environmental practices of firms at home and abroad (*WIR11*).

In the past, the two universes of international rules affecting investment, CSR standards and IIAs, were largely disconnected. However, strengthening the responsibility dimension of IIAs calls for improving and strengthening the interaction between these two universes of international rules affecting investment.

There are a number of policy options to do so.

A first option is to encourage investors to comply with widely accepted international standards (e.g. the UN Guiding Principles on Business and Human Rights). This can be done either through a general reference, without listing the relevant CSR standards; by giving a list of the relevant standards; or by spelling out the content of relevant CSR standards. Each of these approaches has pros and cons. For example, building on the work done by CSR experts rather than reinventing the wheel saves time, costs and efforts and brings together two different bodies of law and policymaking, fostering coherence and improving systemic interaction. Referring to widely recognized and well-regarded instruments can add legitimacy and secure acceptance by different stakeholders.

A second, related option is to require tribunals to consider an investor's compliance with CSR standards, endorsed by the parties, when deciding an ISDS case. However, this raises the question of what legal consequences non-compliance would have. Furthermore, questions with regard to the cross-fertilization between different bodies of law; the need for arbitrators to familiarize themselves with the relevant, rapidly evolving normative standards; and the importance of managing interaction and coordination with CSR-related compliance processes and institutions arise.

A third option is to include a commitment by the parties to promote agreed best-practice international CSR standards. Parties can also commit to fostering compliance at the national level. Actions can include building local industries' capacity to take up CSR standards, by conditioning the granting of incentives on the observance of CSR standards, or introducing certain minimum standards (e.g. relating to anti-corruption, environmental, health and labour standards) into domestic laws.

A fourth option is to establish cooperation between the parties on CSR issues. Cooperation can involve the work of a special committee set up under the IIA and tasked to discuss CSR-related issues. Cooperation can also include promoting best-practice international CSR standards (e.g. by promoting the observance of applicable CSR standards and helping to implement them, including through specific industry support measures, market incentives and regulation), supporting the development of new voluntary standards (e.g. by cooperating on the above activities, and in the exploration and creation of new CSR standards), or other activities.

A fifth option that is worth considering, and that a number of countries are starting to pursue, is home-country efforts to regulate foreign investment for sustainable development. Whereas past CSR-related initiatives have largely taken a host-country perspective, an emerging policy development has home countries monitor or regulate the foreign activities of their companies, e.g. through export credit agencies and investment insurance (see above). Such an effort can address, among others, issues related to human rights, the environment or corruption.

All of the above options have their pros and cons. They can help support the spread of CSR standards, which are becoming an ever more important feature of the investment policy landscape. They can improve the interaction between different bodies of law and policy (see below), and help strengthen the “responsibility dimension” of IIAs. Although there are concerns that the “softer” approaches are unlikely to have a significant effect, they also carry certain advantages. For example, the softer the approach, the easier it will be to implement it and to make CSR part of the IIA. Moreover, soft approaches can have an important impact by “pushing the envelope” for conceptual debate and innovation in international investment policymaking.

e. Enhancing systemic consistency of the IIA regime

Options include improving the coherence of the IIA regime, consolidating and streamlining the IIA network, managing the interaction between IIAs and other bodies of international law and linking IIA reform to the domestic policy agenda.

In light of the high degree of atomization of the IIA regime, a key reform challenge is to avoid further fragmentation of the system, and to enhance, as far as possible, coherence between individual IIAs, as well as coherence between the IIA regime and other international policies. In addition, there is a need to manage the systemic links between the IIA regime and domestic policies.

Improving coherence of the IIA regime

- **Seeking common IIA reform solutions**

With over 3,200 different agreements concluded over 60 years, reflecting different levels of economic development, different interests and different treaty models, the global IIA universe is known for its systemic complexity, incoherence, gaps in coverage and overlapping commitments.

In terms of content, the main differences in the global IIA regime relate to the policy issues of (i) treaty scope (limited to post-establishment treatment or including the pre-establishment phase); (ii) coverage (only FDI or all kinds of investments); (iii) the degree of investment protection; (iv) the number and degree of treaty exceptions; (v) the inclusion of sustainable development considerations; and (vi) the handling of investment disputes.

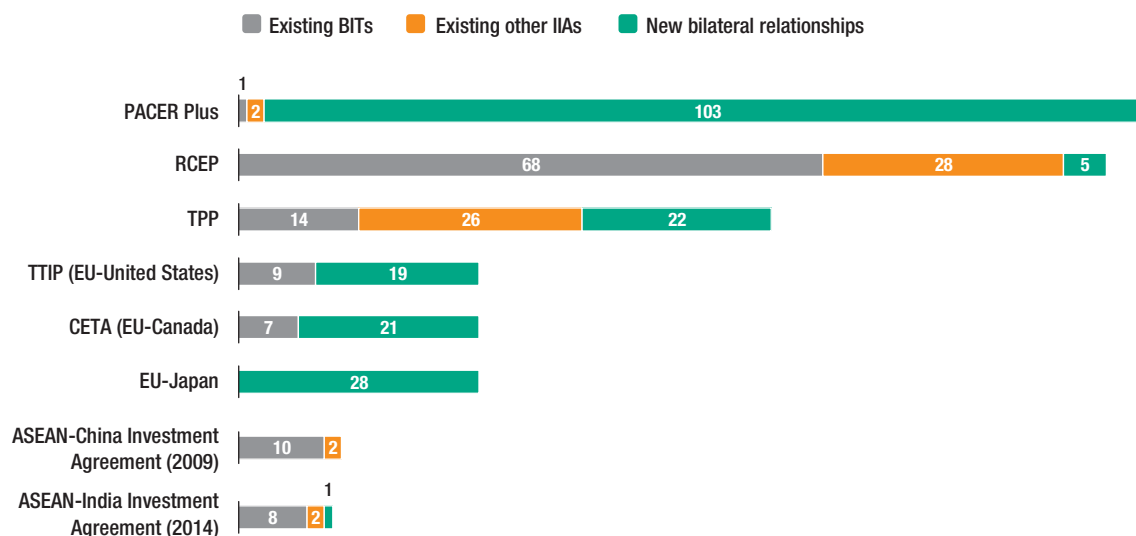
In terms of type, one can distinguish between “pure” investment agreements, such as BITs, on the one hand, and sectoral, regional and plurilateral treaties, or economic cooperation treaties, covering both investment and trade, on the other hand (“other IIAs”).

Differences within the IIA universe can partially be explained by the different “age” of treaties – first-generation IIAs look significantly different from more recent agreements. Variations in content may also derive from the fact that IIAs have been concluded with countries at different levels of economic development, or within the context of regional economic cooperation. Different experiences of countries with ISDS and their reflection in IIAs may be an additional factor. The bargaining power of negotiating parties may play a role as well – the stronger the bargaining strength of a country, the fewer difficulties it will have in ensuring coherent treaty practices.

Working towards more coherence in an IIA regime consisting of thousands of agreements is a global challenge that calls for common responses through

Figure IV.9.

Existing IIAs and new bilateral relationships created, for eight regional agreements concluded or under negotiation (Numbers)



Source: UNCTAD, IIA database.

Note: "New bilateral IIA relationships" refers to the number of new bilateral IIA relationships created between countries upon signature of a megaregional agreement.

a combination of individual, bilateral, regional and multilateral reform steps (see section C). Regional IIA reform, if undertaken properly, can help promote harmonization of investment rules. The backstopping and support function of regional secretariats and international organizations can play a role in this regard.

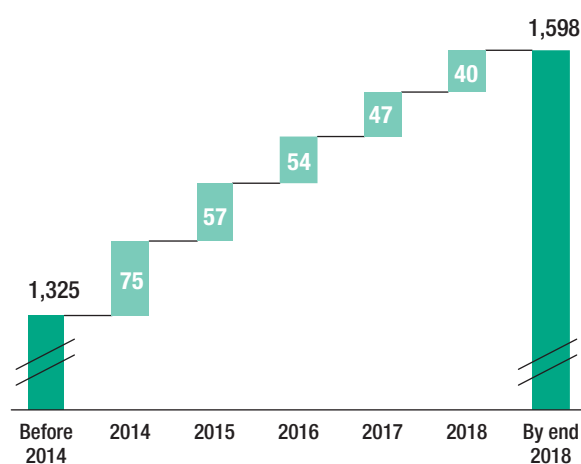
Consolidating and streamlining the IIA network at the regional level

Regional investment policymaking has led to increasing overlaps and inconsistencies within the IIA universe. Most of the regional agreements to date have not phased out pre-existing BITs between members of the regional grouping, which leads to a multiplication of treaty layers. The parallel existence of such prior BITs and the subsequent regional agreements poses a number of systemic legal and policy questions, adds to the "spaghetti bowl" of intertwined treaties and complicates countries' ability to pursue a coherent, focused international engagement on investment policy issues (UNCTAD, 2013b; WIR13).

Although to date parallelism has been the prevalent approach, current regional and megaregional IIA negotiations (e.g. negotiations for the EU–United States Transatlantic Trade and Investment Partnership (TTIP) or for the Trans-Pacific Partnership (TPP)) present an

Figure IV.10.

Cumulative number of BITs that can be terminated or renegotiated at any time



Source: WIR13.

opportunity to consolidate the existing network of BITs. Eight megaregional agreements concluded or under negotiation in which BIT-type provisions are on the agenda overlap with 140 agreements (45 bilateral and regional "other IIAs" and 95 BITs) (figure IV.9; see also WIR14).

If the States that are parties to these forthcoming agreements opted to replace the pre-existing BITs between them, it would be a noticeable step towards streamlining the global IIA regime. A similar approach could be envisaged for existing regional agreements or initiatives with an investment dimension, where the abrogation of the BITs between the respective treaty partners could help consolidate the global IIA regime. Should the underlying BIT provide for desirable features that are absent in the subsequently negotiated regional agreement, such features could be included – if necessary over time – in the region's legal framework for investment. Current discussions in the European Union offer valuable insights in this regard; similar initiatives have also been discussed in other regions with developing-country members. Importantly, any such actions would need to cater to regional specificities. The fact that between 2014 and 2018, more than 1,500 BITs will reach the stage where they could be terminated by a party at any time creates a further opportunity for consolidation and streamlining (figure IV.10). Abrogation could commence with those treaties, in which the initial duration has expired or is soon to expire. In order to use treaty expirations to instigate change in the IIA regime, there is a need to understand how BIT rules on treaty termination work, so as to identify when opportunities arise and what procedural steps are required (UNCTAD, 2013c; *WIR13*).

To this can be added more options on how regional IIA reform can contribute to the streamlining of the IIA regime. For example, a common regional IIA model can serve as the basis for future negotiations with third parties, with the potential to result in treaties that will be similar to each other; regional sharing of experiences and consensus-building can generate common approaches and inform countries' actions at the national, bilateral and multilateral levels, thereby contributing to a more coherent, more harmonious and possibly also more consolidated IIA regime (see also section C).

Managing the interaction between IIAs and other bodies of international law

IIA reform needs to take into account the interaction between investment treaties and other bodies of international law in order to avoid inconsistencies and seek synergies (mutual supportiveness).

First, IIAs interact with other areas of international law, such as international environmental law, labour law, human rights law or trade law. Owing to the fragmentation of international law into different “systems” that pursue their own objectives, past ISDS cases have revealed tensions between IIAs and these other parts of international law. Addressing this relationship in IIA reform can help avoid conflicts and provide arbitral tribunals with guidance on how to interpret such interaction.

In practice, reform efforts may reaffirm, in the IIA, parties' commitments under other relevant international law instruments, such as the ones mentioned above. A variant of this approach is to clarify that the IIA needs to be read in line with parties' obligations under international law in other areas (i.e. States' duty to protect, respect and fulfil human rights). Countries may also include general exceptions in favour of certain public policies covered by such other international law obligations.

Second, reform steps in IIAs would also benefit from parallel reform efforts in other international law instruments dealing with foreign investment. For example, future treaties dealing with policy areas that potentially interact with IIAs could specify that States' efforts to implement these treaties are not constrained by any IIAs they have signed.

A third type of interaction arises in areas where IIA reform efforts and developments in other bodies of law go hand in hand, as is the case with CSR standards. IIAs do not need to establish their own CSR provisions, but instead may refer to other relevant non-binding instruments, such as the ILO Tripartite MNE Declaration, the UN Principles on Business and Human Rights, the FAO/World Bank/UNCTAD/IFID Principles on Responsible Agricultural Investment, or the OECD Guidelines on Multinational Enterprises. This approach avoids lengthy and difficult negotiations on CSR issues in the IIA, and it also allows any potential future reinforcements, updates or subsequent developments of existing CSR principles and guidelines to make their way into the IIAs referring to them. Interaction could also extend to the areas of implementation. And, interaction could extend to encouraging those who design CSR and business and human rights strategies to consider IIAs and investment policymaking when doing so.

A final type of interaction arises with respect to IIA reform in the area of investment dispute settlement. Not only IIAs, but also other international conventions – in particular the ICSID Convention, the UNCITRAL Arbitration Rules and the New York Convention – lay down the rules for investor access to dispute settlement, arbitration procedures, and recognition and enforcement of arbitral awards. To the extent that IIA reform modifies investors' access to ISDS, changes procedural rules or introduces new mechanisms (e.g. an appeals facility or an international court), this might require reform steps not only in the IIA, but also in these other international conventions.

This last aspect also offers opportunities for synergies, because there is the option to translate reform actions at the multilateral level into a great number of existing IIAs, thereby avoiding the need for many time-consuming renegotiations. The recently adopted UNCITRAL Transparency Rules and the UN Transparency Convention provide an example: together they create an opt-in mechanism for countries that wish to incorporate enhanced transparency standards for ISDS proceedings, including in those ISDS cases that are brought pursuant to pre-existing IIAs concluded by these countries.

Linking IIA reform to the domestic policy agenda

IIA reform does not exist in isolation, but has important linkages to the domestic policy agenda. Investment policies interact with numerous other policy areas, including trade, finance, taxation, industrial policy, intellectual property, environmental protection, social and labour policies, human rights, health and cultural policies. It is critical that different government authorities work together in identifying common IIA reform goals and implementing a joint reform strategy.

In particular, IIA reform needs to take into account the following linkages with the domestic policies of host and home countries.

First, it must be re-emphasized that primary conditions for admission and operations of investors,

the legislative framework within which all investors exist, are created at the national level. This internal environment, which includes the ability of domestic institutions to maintain and enforce applicable laws and regulations, is a crucial factor determining investors' decisions about the location of their investments. IIAs act as a complement but do not replace the need for a high-quality domestic policy environment and effective institutions. IIA clauses that emphasize the importance of such a well-functioning regulatory environment, including modern environmental, health or labour standards, can help support States in their efforts in this regard.

Second, the domestic policy framework is key for determining how much regulatory freedom a country requires in order to ensure that its current and future regulatory needs are not inhibited by IIA obligations. This has emerged as a particularly important issue in respect of pre-establishment IIAs. It is important therefore, that IIA negotiations are informed by a proper assessment of its existing, and potential future, domestic regulatory environment.

Third, IIA obligations must be aligned with the relevant domestic laws and regulations. Thus, for example, if IIA reform seeks a clarification of the FET standard or of the concept of indirect expropriation, care needs to be taken in how these principles are dealt with under domestic law in order to avoid differences. This is especially important if the country follows the “no greater rights” philosophy in relation to IIAs. In addition, if IIA reform limits investor access to ISDS, it becomes important to ensure that local remedies are adequate.

Finally, in some cases, IIAs may trigger reform steps at the national level. One case in point is IIA-driven investment liberalization, which may necessitate changes in the host countries' entry policies for foreign investment. Another example is the possible need for modifications in host countries' domestic investment guarantee schemes if IIAs call for environmental or social impact assessments.

C. IIA REFORM: GUIDELINES AND ACTIONS

1. Guidelines for IIA reform

IIA reform should be guided by the goal of harnessing IIAs for sustainable development, focusing on key reform areas, and following a multilevel, systematic and inclusive approach.

Six Guidelines for IIA Reform guide any reform action, be it undertaken at the national, bilateral, regional or multilateral levels (table IV.8). Inspired by the UNCTAD Investment Policy Framework's Core Principles, the lessons learned from 60 years of IIA rule making and the specific reform challenges of today, these six guidelines aim at harnessing IIAs for sustainable development.

2. IIA reform: actions and outcomes

IIA reform actions should be synchronized at the national, bilateral, regional and multilateral levels. In the absence of a multilateral system, the best way to make the IIA regime work for sustainable development is to collectively reform the regime with a global support structure.

Actions for sustainable-development-oriented IIA reform can be and have to be undertaken at all levels – the national, bilateral, regional and multilateral levels

(table IV.9). At each level, the reform process would broadly follow a sequence of steps that include (1) taking stock and identifying the problems, (2) developing a strategic approach and an action plan for reform, and (3) implementing actions and achieving the desired outcomes.

The actions described below differ in their complexity, ease of implementation and impact. It is therefore important for each country to establish some sort of sequencing of reform actions, identifying actions for the near-, medium- and long-term future.

a. Actions at the national level

In its very nature, national-level reform action is unilateral. Accordingly, its potential to create actual change in terms of a new and more sustainable-development-friendly IIA regime is limited. However, national-level action is crucial for preparing proper IIA reform actions at the other (i.e. bilateral, regional and multilateral) levels, and it constitutes the very first step to harness the potential of IIAs for the sustainable development of a country.

National IIA reform needs to be accompanied by domestic reform efforts geared towards improving the regulatory framework for investment.

Table IV.8.

Guidelines for IIA Reform

Description

1. Harness IIAs for sustainable development	The ultimate objective of IIA reform is to ensure that the IIA regime is better geared towards sustainable development objectives while protecting and promoting investment.
2. Focus on critical reform areas	The key areas for reform are (i) safeguarding the right to regulate for public interest, (ii) reforming investment dispute settlement, (iii) strengthening the investment promotion and facilitation function of IIAs, (iv) ensuring investor responsibility, and (v) enhancing systemic coherence.
3. Act at all levels	The reform process should follow a multilevel approach and take place at the national, bilateral, regional, and multilateral levels, with appropriate and mutually supportive action at each level.
4. Sequence properly for concrete solutions	At each level, the reform process should follow a gradual, step-by-step approach, with appropriately sequenced and timed actions based on identifying the facts and problems, formulating a strategic plan, and working towards concrete outcomes that embody the reform effort.
5. Ensure an inclusive and transparent reform process	The reform process should be transparent and inclusive, allowing all stakeholders to voice their opinion and to propose contributions.
6. Strengthen the multilateral supportive structure	The reform process should be supported by universal and inclusive structures that help coordinate reform actions at different levels by offering backstopping, including through policy analysis, technical cooperation, and a platform for exchange of experiences and consensus-building.

Source: UNCTAD.

Table IV.9. Road map for IIA reform

Level	Take stock/identify problem	Strategic approach/action plan	Options for actions and outcomes
National	<ul style="list-style-type: none"> National IIA review Treaty network and content profiles Impact and risk assessment Reform needs 	<ul style="list-style-type: none"> National IIA action plan Design criteria and guidelines Reform areas and entry points Approaches for IIA reform Negotiating strategy 	<ul style="list-style-type: none"> New model treaty Unilateral termination Implementation <ul style="list-style-type: none"> Domestic reform Increased awareness Improved institutions Capacity-building
Bilateral	<ul style="list-style-type: none"> Joint IIA consultations to identify reform needs 	<ul style="list-style-type: none"> Plan for a joint course of action 	<ul style="list-style-type: none"> Joint interpretation Renegotiation/amendment Consensual termination
Regional	<ul style="list-style-type: none"> Collective review Treaty network and content profiles (regional IIA and BIT network) Impact and risk assessment Reform needs 	<ul style="list-style-type: none"> Collective IIA action plan Design criteria and guidelines Reform areas and entry points Approaches for IIA reform and for consolidating and streamlining the IIA network 	<ul style="list-style-type: none"> Consolidation/rationalization of BIT networks Common model Joint interpretation Renegotiation/amendment Implementation/aid facility
Multilateral	<ul style="list-style-type: none"> Global review of the IIA regime (e.g. <i>WIR15</i>) Stocktaking/lessons learned Identification of systemic risks and emerging issues 	<ul style="list-style-type: none"> Multilateral consensus-building on key and emerging issues Shared vision on systemic reform 	<ul style="list-style-type: none"> Multilateral Action Plan <ul style="list-style-type: none"> Multilaterally agreed criteria and guidelines for systemic reform Developing instruments and/or institutions for facilitating reform at all levels Multilateral backstopping <ul style="list-style-type: none"> Research and analysis Coordination, including “bridging” function with other bodies of law Technical assistance Platform/forum for consensus-building and exchange of best practices

Source: UNCTAD.

In other words, IIA reform needs to be accompanied by action regarding those issues that IIAs are supposed to address by overcoming deficiencies and providing guarantees and “insurance”. This is important not only for avoiding the potential negative effects of IIA reform in terms of creating transaction costs, but also for further fine-tuning the role of IIAs in a country’s development strategy. Indeed, one of the arguments for IIA reform is that the domestic regulatory regime of many countries has evolved to such a degree that classical “protection-focused” IIAs are no longer adequate instruments for harnessing investment for sustainable development.

All national level reform actions would benefit from involving all stakeholders, including through interministerial consultations, parliamentary engagement and inputs from academia, civil society and business.

IIA review

The first step for national level IIA reform is an IIA review. Such a review takes stock of the country’s network of IIAs, assesses the impact and risks flowing from these agreements, and identifies concrete reform needs (Poulsen et al., 2013; Tietje et al., 2014).

More specifically, this includes analysing a country’s IIA profile, i.e. reviewing the country’s existing IIAs in terms of partners, coverage, types and content. A subsequent impact and risk assessment looks at the IIAs’ economic and policy impacts. This includes analysing their impact on investment flows and other economic indicators (e.g. trade flows, royalties and license payments flows, tax) and their interrelationship with other policies (e.g. overlaps, inconsistencies with national investment and other policies, with other

international obligations). Such an assessment would also look at the problems the agreements have caused and the risks they give rise to, for example, through ISDS cases (whether withdrawn, settled or decided in favour of the State or the investor). Putting these findings into the context of the country's socioeconomic and political realities (as stipulated in its national development strategy and by today's SDG imperative) enables policymakers to draw lessons learned and to identify concrete reform needs. Although such a risk assessment can never be comprehensive, even if undertaken in a rudimentary manner or in a sector-specific manner, it can offer important insights.

- **National IIA action plan**

The next step is the development of a national IIA action plan. Informed by a number of design criteria and guidelines (e.g. as outlined in the 2012 UNCTAD Policy Framework) and the results of the national IIA review, the country can develop its strategic approach towards IIA reform. Regarding the extent of reform, the country decides whether to comprehensively address all five reform objectives or to single out one or two, such as safeguarding the right to regulate and improving investment dispute settlement. This choice informs the selection of reform areas and entry points to focus on and the policy options best suited for doing so. This last step benefits from comprehensive information about international and/or regional best practice (and state-of-the-art treaty practice). The policy options in UNCTAD's Investment Policy Framework as well as those in this *WIR* serve as examples.

Another key element of the national IIA action plan is the development of a negotiating strategy. Such a strategy sets out the concrete action steps for reforming the different IIA relationships the country maintains. This includes prioritizing certain relationships and setting timelines within which they will be addressed. IIA relationships to be prioritized include those IIAs that have reached the end of their initial duration, those with which major problems have occurred and those that can be rationalized (in the context of regional endeavours).

Determining the best way of reforming these relationships is also important. The country needs to decide whether certain IIA relationships should be terminated, renegotiated or amended, all of this with

concrete timelines, according to which the country approaches its IIA reform agenda with its preferred treaty partners. Finally, also joint interpretation or the negotiation of new IIAs are options to be considered.

- **New IIA model**

In terms of concrete outcomes of national-level IIA reform, this includes first and foremost a new IIA model. The new model will be based on the respective strategic choices (e.g. the extent of reform), selection of reform objectives and areas, and respective policy options. A new model IIA can imply either partial amendments or a complete overhaul of the pre-existing model. By now, at least 50 countries and 4 regional integration organizations have embarked on developing a new model IIA (chapter III). A new model can be accompanied by decisions on which of the new model's elements are priority objectives to be pursued and what fallback options exist if needed.

- **Interpretative statements or treaty termination**

Another set of concrete outcomes of national-level IIA reform action are unilateral actions, such as issuing interpretative statements for a treaty or terminating it. Regarding the latter, rules for treaty termination are typically set out in the BIT itself. Between 2014 and 2018, more than 1,500 BITs will reach the stage where they can be terminated at any time. Countries wishing to terminate their IIAs need to have a clear understanding of the relevant treaty provisions (especially the survival clause) as well as the broader implications of such actions (UNCTAD, 2013c; *WIR11*).

- **Addressing bottlenecks for domestic IIA implementation and IIA reform**

As a third element of the national IIA Action Plan, countries should identify their domestic IIA-implementation and IIA-reform bottlenecks. This could include at least four steps of government action. First, treaty implementation may require administrative actions to fully translate international obligations into national laws and administrative practices. Overall, IIA reform should go hand in hand with domestic regulatory adjustments to ensure coherence and create synergies. Second, the country may wish to create awareness at all levels of government concerning the countries' international IIA-related obligations (even in the absence of disputes). Information campaigns and active training of local officials directly dealing with

foreign investors are examples in point. Third, there may be a need to build the necessary institutions to deal with IIA-related implementation issues. This step could range from establishing early-warning systems or ombuds-like institutional set-ups that are geared towards dispute prevention, to creating dedicated “defence” teams in the ministry charged with dispute settlement, and/or to follow-through on the direct institutional commitments in IIAs, e.g. the establishment of joint committees. Finally, in all of this work governments could identify their technical assistance and capacity-building needs and take actions on their follow-up, through bilateral, regional or multilateral assistance programmes (such as UNCTAD’s IIA work, its Investment Policy Reviews or e-governance programmes). The latter is particularly important for least developed countries and for other small and vulnerable economies.

b. Actions at the bilateral level

Bilateral reform action largely mirrors and builds on national-level actions. Bilateral action will usually create actual change in the legal instruments covering the pertinent bilateral relationship.

A joint IIA review aims at taking stock of the situation and at assessing the impact and the risks of the bilateral IIA relationship, and at identifying reform needs. This time, the review is undertaken jointly, involving the respective actors from the two countries. Such a review can take the form of consultations, possibly making use of joint review committees, and may be in the context of already existing joint economic committees or through a new, institutional set-up, whether ad hoc or permanent. Stakeholder involvement can help to inform the process.

Based on the review, the two countries would proceed to develop a plan for a joint course of action. Such a plan can include options such as (1) joint interpretative statements (in the form of memoranda of understanding) on an existing treaty (UNCTAD, 2011c), (2) amendments to or renegotiation of an existing treaty; (3) the consensual termination of the treaty either upon treaty expiration or if the treaty is superseded by a regional initiative to which both parties are members. The “survival clause” of the terminated treaty would require attention, as it affects how the termination takes effect. To limit the application of the survival clause, treaty partners could agree to amend

the IIA in question by deleting the clause before they terminate the treaty.

c. Actions at the regional level

Regional reform action follows similar steps as national and bilateral actions, but with additional layers of complexity and greater potential for change.

In terms of greater complexity, regional IIA rule making implies overlaps and inconsistencies, particularly given the current practice in which new regional agreements do not provide for the phasing-out of older agreements covering the underlying respective bilateral relationships. At the same time, regional IIA reform provides an opportunity for more efficient and widespread reform as it involves more than two countries, and, if undertaken properly, would harmonize and consolidate existing investment rules. Moreover, regional endeavours may be subject to a different kind of dynamism than bilateral relationships in terms of setting a reform agenda and pursuing it. Regional integration organizations and their secretariats offer the platforms on which regional IIA reform could be pursued.

Again, the first step is an IIA review, this time undertaken collectively by the members of the regional organization/agreement and in a multi-dimensional manner. Similar to the above, such a review would look into the network and content profiles, assess impacts and risks, and identify reform needs, including through stakeholder consultations. In so doing, a collective regional review would consider the different treaty layers and relationships that exist in a regional context. This would be, first and foremost, the regional agreement in question. Second, this would include the existing BITs among the partners to the regional undertaking, internally (i.e. intraregional BITs with the other partners in the regional undertaking). Third, this would include IIAs with third parties, be they between a single member of the regional undertaking and a third, external treaty partner, or between the regional undertaking as such and a third, external treaty partner. When identifying impact and risk, attention would need to be given to the multilayered character of this IIA network, including the overlaps, gaps and inconsistencies, and the attendant risks arising from it.

This special nature of the regional dimension would inform the collective IIA action plan. For example, when defining reform objectives, the fifth one –

promoting systemic consistency – would deserve particular attention, not only in terms of substance of the rules but also in terms of managing the relationship between them. Collective approaches regarding areas for IIA reform and for consolidation and streamlining of IIAs would be particularly important.

Collective approaches will translate into specific, time-bound actions and outcomes. In terms of actions, they range from further discussions and consultations to negotiations, amendments/re negotiations or interpretation of treaties. When it comes to addressing existing treaties, underlying BITs that have reached their expiration dates could be the first to be tackled; however, also other regional undertakings that have long not been updated or modernized are candidates for IIA reform.

In terms of specific results, regional reform efforts could result in a new, common IIA model or a negotiating position for future treaties, a joint interpretation; a renegotiated/amended treaty; the consolidation/streamlining of underlying BITs. Again, the renegotiated treaties can be the regional treaty at issue, or a treaty between the region and third parties. A renegotiated regional treaty can also result in the termination of the underlying bilateral treaties. With this latter outcome, regional IIA reform action can directly support the broader IIA reform effort of streamlining and rationalizing the global IIA regime.

Similar to national-level reform action, regional IIA reform may require regulatory adjustments at the national level to ensure coherence and create synergies. This could be aided by creating new – or improving existing – regional facilities to provide coordination and technical cooperation. The latter could include legal aid and/or training for dispute management and/or prevention, help with translating regional obligations into national laws and administrative practices, follow-through on direct treaty commitments for regionally institutionalized investment promotion and facilitation, and, more broadly, assistance with the implementation of IIA reform at the regional and/or national level (e.g. assistance for conducting a national risk assessment, or the implementation of identified reform action, such as the termination or renegotiation of an existing agreement). Regional technical assistance and capacity-building bodies could serve as counterparts to, and benefit from, international organizations providing such support.

d. Actions at the multilateral level

Reforming an IIA regime consisting of thousands of agreements is a global challenge that calls for common responses from all parties involved. Such a global reform effort, if successful, would be the most efficient way of addressing the sustainable development challenges, inconsistencies and overlaps that characterize the current IIA regime. At the same time, multilateral IIA reform is the most challenging reform option, particularly regarding how to pursue it.

Several levels of multilateral IIA reform, with increasing intensity, depth and character of engagement, can be identified. They interact with the steps and actions undertaken at the other levels of IIA reform actions and, similarly to them, they could benefit from inclusive and transparent multistakeholder engagement.

- **Global IIA review**

First, there is a global review of the IIA regime, aimed at taking stock of experiences and at identifying systemic risks and emerging issues. Such a review could take the form of a series of brainstorming sessions or regular multilateral exchanges of experiences and information (e.g. in the form of consultations or hearings) and be supported by backstopping from a multilateral support structure. Exchanges of experiences would enable governments and other stakeholders to learn from each other's experiences and best practices; this could generate positive feedback on unilateral, bilateral or regional reform steps and lead to a greater harmonization of and coherence in ongoing reform efforts.

In terms of content, a global IIA review could cover the entire range of issues related to IIA reform (e.g. taking stock of all norms contained in IIAs and related instruments). It could also look at novel approaches to be considered for unresolved issues or emerging issues, together with their likely advantages and disadvantages for the sustainable development dimension of the IIA regime. Importantly, a review of the global IIA regime would give attention to issues of systemic importance.

- **Multilateral consensus-building**

Second, following the stocktaking, multilateral consensus-building on areas for improvement could aim at identifying areas of broad consensus and areas of disagreement. In terms of content, consensus-

building can aim to develop a common understanding of the key problems and emerging issues of the IIA reform agenda or go so far as to involve common reform objectives or a road map of steps or guidelines for moving towards such common solutions. Along these lines, the core of multilateral consensus-building could be to identify and consolidate consensus where it already exists, and to explore and seek a more coordinated approach where it does not.

- **Multilateral action plan**

Third, a multilateral action plan could be envisioned that could build on the global IIA review and move multilateral consensus-building towards providing concrete reform elements. This could take the form of multilaterally agreed upon criteria and guidelines for systemic reform. Such criteria and/or guidelines can support reform efforts at the national, bilateral and regional levels. They can also support further multilateral action. Non-binding principles on the reform process could take the form of recommendations addressing member States, international organizations and other stakeholders. Multilaterally agreed criteria and guidelines could provide benchmarks against which certain parameters for IIA reform could be assessed. They could address systemic risks and emerging issues, and guide reform actions in this regard. Guiding principles for the content and implementation of investment policies and IIAs, as contained in UNCTAD's Investment Policy Framework, or for the process of IIA reform, as contained in this *WIR*, are examples in point. Again, an institutional support structure can facilitate the development of such criteria and their adoption.

Such a multilateral action plan could result in the development of a number of *multilateral instruments* that can facilitate reform on all levels. A range of options can be foreseen:

- *A checklist for IIA negotiators*: A checklist would identify those policy issues that IIA negotiators should take into account when negotiating or renegotiating an agreement as part of sustainable-development-oriented IIA reform.
- *Best practices in IIA rule making and/or IIA reform*: A compilation of individual case studies demonstrating how countries have reformed the IIA network to bring it in line with sustainable development considerations, distilling both positive

and negative experiences, can provide lessons for future reform-oriented IIA (re)negotiations.

- *Model provisions (or a model agreement)*: Model texts for IIA clauses in line with certain reform objectives can guide concrete reform actions. If undertaken in a more comprehensive manner covering all possible reform objectives, this could also result in a “new-generation model agreement”. Model provisions or agreements can also address issues related to systemic reform.
- *Guidance for interpreting IIA provisions*: Guidance for interpreting treaties could improve the transparency, predictability and stability of international investment law, and help clarify the substance of key provisions, including their sustainable development dimension.
- *Multilaterally agreed guidelines for investment policymaking*: Multilaterally agreed guidelines or principles for investment policymaking such as UNCTAD's Policy Framework could ensure a coherent, holistic and synergetic approach to IIA reform.

A multilateral action plan could also result in *multilateral institution-building* related to IIA reform, as is already envisioned in the ISDS context – with a possible appeals mechanism or a potential international investment court. Although this is currently considered foremost in the bilateral context (e.g. various United States IIAs provide for the undertaking of an appeals mechanism in the future) and at the regional level (e.g. the European Commission's suggestions for a permanent investment court in future IIAs signed by the European Union (European Commission, 2015)), it could also take on an international dimension. One example is a possible appeals facility under the ICSID Convention. Another is the European Commission's proposal to “multilateralise the [permanent investment] court either as a selfstanding international body or by embedding it into an existing multilateral organization”.⁹ It is important in this context to recall that ISDS is an *enforcement mechanism* as regards the substantive provisions of IIAs and cannot be looked at in isolation. Hence, multilateralizing the enforcement mechanism would greatly benefit from multilateralizing the underlying substantive investment rules as embodied in IIAs.

Multilateral engagement on IIA reform could also result in creating an instrument that would follow the

example of the Convention on Transparency in Treaty-based Investor–State Arbitration developed under the auspices of UNCITRAL; i.e. a multilateral consensus on a clearly defined key IIA reform issue. In this approach, States could sign on to a general statement clarifying the concept of a particular IIA provision and applying it to existing and/or future treaties. This could take the form of a multilateral instrument that would co-exist with the existing IIA network. It would address those provisions (common to most BITs) where need for sustainable-development-oriented reform is deemed most important by the parties, and in the manner agreed upon by the parties. This could allow countries to reform their entire portfolios of investment treaties at once; i.e. parties to the amended multilateral instrument could agree that the revised provision – transparency in case of the UNCITRAL Arbitration Rules – shall apply not only in respect of future IIAs, but also with regard to existing investment treaties. Although it could prove difficult to find consensus among all States on the formulation of controversial substantive provisions (such as FET or indirect expropriation), agreement that takes the form of softer instruments could be envisioned as a first step, thereby progressively moving towards finding common ground.

- **Backstopping**

Any multilateral engagement would benefit from a multilateral support structure that could offer backstopping functions. This includes collecting and disseminating comprehensive up-to-date information about international best practices, state-of-the-art treaty making and the latest developments in adjacent fields of law. It also encompasses acting as repositories of change initiatives, undertaking research and policy analysis on reform options and their pros and cons, coordinating among various processes at different levels and dimensions, and providing the “bridging” function with other bodies of law (e.g. human rights or environmental law) that would ensure two-way coherence and mutually beneficial exchange. Backstopping also entails the provision of technical assistance and capacity-building for implementing IIA reforms, ranging from advisory services and training to awareness-raising work and information dissemination.

Such technical assistance backstopping could take the form of a multilateral aid facility that would

provide legal assistance and/or training for dispute management and/or prevention, along the lines of what the Advisory Centre for WTO Law provides for certain developing-country WTO members. An investment aid facility could build on this by also helping beneficiaries, in particular least developed countries and other small and vulnerable economies, to ensure compliance with international obligations in national laws and administrative practices, provide institutionalized investment promotion and facilitation services on an international level and, more broadly, assist with the implementation of sustainable-development-oriented IIA reform actions.

Finally, backstopping services also include the hosting of a forum for exchange of experiences, lessons learned and discourse on the way forward. Engaging with treaty partners and the broader investment-development community can help ensure a universal, inclusive and transparent discourse and fact-finding and consensus-building. UNCTAD’s World Investment Report, its World Investment Forum and its Expert Meetings are cases in point.

A multilateral support structure could take the form of creating a new international coordination mechanism that would involve several international organizations active in this field of international investment rule making. Built around a core of international organizations that combine expertise in policy analysis, technical assistance and consensus-building on this matter, this could ultimately also include a variety of relevant stakeholder organizations.

IIA reform can take place at various levels of engagement – unilateral, bilateral, regional or multilateral – and countries can select processes and formats in line with their development strategies and needs and their strategic choices about the priority, intensity, depth and character of their engagement in IIA reform. Moreover, the various paths identified are not mutually exclusive. In fact, some options are sequential steps as part of a gradual approach, and most of the actions and options could be pursued in parallel. There is also room for cross-fertilization between different reform paths. However, ultimately collective action is required to ensure that IIA reform is for the benefit of all.

CONCLUSION

The IIA universe is at a crossroads, and many countries and regional groupings are in the process of reviewing, reforming and revising their IIAs and their stances on the issues involved. This chapter takes stock of this ongoing debate, the arguments, the history and lessons learned, and offers an action menu or toolbox for IIA reform. It does not provide a single reform package. Rather, countries are invited to pick and choose which reform option to pursue, at which entry level and with which treaty option, and at what level and intensity of engagement. In other words, countries are invited to formulate their own reform packages.

The chapter advances UNCTAD's earlier work on this matter, in particular its Investment Policy Framework (WIR12), the reform paths for investment dispute settlement (WIR13) and the reform paths for IIA reform (WIR14). Taking into account contributions from other stakeholders, it develops this work further to provide a holistic, coherent and multilevel blueprint for addressing

the five main reform challenges for harnessing IIAs for sustainable development: safeguarding the right to regulate for pursuing sustainable development objectives, reforming investment dispute settlement, promoting and facilitating investment, ensuring responsible investment, and enhancing systemic consistency of the IIA regime.

The chapter stresses that engagement at all levels – national, bilateral, regional and multilateral – is important to achieve the common objective of IIA reform. However, it also underscores that reform needs to be pursued with a common agenda and vision in mind, since any reform step taken without multilateral coordination will only worsen fragmentation. Only a common approach will deliver an IIA regime in which stability, clarity and predictability help achieve the objectives of all stakeholders: effectively harnessing international investment relations for the pursuit of sustainable development.

Notes

¹ One of the first cases was the Anglo-Iranian Oil Co. Case (*United Kingdom v. Iran*) 1951 I.C.J. Rep. 89, 1952 I.C.J. Rep. 93.

² One important difference, however, was that both the Abs-Shawcross Convention (Art. VII(2)) and the OECD Draft Convention (Art. 7(b)) provided for investor-State arbitration (conditioned upon separate advance consent of the contracting party concerned), an idea not taken up in investment treaty practice until the Indonesia–Netherlands BIT of 1968.

³ *Asian Agricultural Products Ltd. (AAPL) v. Republic of Sri Lanka* (ICSID Case No. ARB/87/3, Award, 27 June 1990).

⁴ Some countries also include a list (as described above) without explicitly including a provision entitled “FET”; the SADC model BIT and the draft Indian model BIT are examples.

⁵ To this purpose, IIAs usually stipulate the requirements for a lawful expropriation, i.e. for a public purpose, non-discriminatory, in accordance with due process of law and against compensation.

⁶ Another option is to include a broadly formulated exception for domestic regulatory measures aimed at pursuing legitimate public policy objectives.

⁷ *Mexico v. United States* (2000), *Peru v. Chile* (2003), *Italy v. Cuba*, ad hoc arbitration (2003), *Ecuador v. United States*, PCA (2011).

⁸ In June 2014, the UN Human Rights Council passed a resolution, by majority, that decided to establish an open-ended working group on a legally binding instrument on transnational corporations and other business enterprises with respect to human rights.

⁹ European Commission, 2015, pp. 11–12.

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15

International Tax and Investment Policy Coherence

C H A P T E R V

WORLD



INTRODUCTION: THE TAX AND INVESTMENT POLICY IMPERATIVE

Intense debate and concrete policy work is ongoing in the international community on the fiscal contribution of multinational enterprises (MNEs). The focus is predominantly on tax avoidance – notably in the base erosion and profit shifting (BEPS) project. At the same time, sustained investment is needed in global economic growth and development, especially in light of financing needs for the Sustainable Development Goals (SDGs). The policy imperative is, and should be, to take action against tax avoidance to support domestic resource mobilization and to continue to facilitate productive investment.

The fiscal contribution of MNEs, or the avoidance thereof, has been at the centre of attention for some time. Numerous instances of well-known firms paying little or no taxes in some jurisdictions despite obviously significant business interests have led to public protests, consumer action and intense regulatory scrutiny. Action groups and non-governmental organizations (NGOs) have brought to light cases of abusive fiscal practices of MNEs in some of the poorest developing countries. Broad support in the international community for action against tax avoidance by MNEs has led to a G20 initiative to counter BEPS, led by the Organization for Economic Co-operation and Development (OECD), which is the main (and mainstream) policy action in the international tax arena at the moment.

The formulation of the post-2015 development agenda and the financing needs associated with the SDGs have added to the spotlight on the fiscal contribution of MNEs as an important source of revenue for governments and a crucial element of resource mobilization for sustainable development. Financing the future development agenda will inevitably have to address the eroding tax base of all countries and especially developing countries. MNE tax avoidance is a real challenge. At the same time, the SDG formulation process has also highlighted the need for increased private sector investment. The *World Investment Report 2014 (WIR14)* showed how in developing countries public investment will be insufficient to cover an estimated \$2.5 trillion annual investment gap in productive capacity, infrastructure, agriculture, services, renewables and other sectors. New private investment not only contributes directly

towards progress on the SDGs, but also adds to economic growth and the future tax base.

The key question is thus: how can policymakers take action against tax avoidance to ensure that MNEs pay “the right amount of tax, at the right time, and in the right place” without resorting to measures that might have a negative impact on investment? In other words, how can they maximize immediate tax revenues from international investment while maintaining a sufficiently attractive investment climate to protect the existing and future tax base? If sustainable development requires both public and private investment, the fiscal climate for investors must be balanced for local and foreign companies alike to ensure sufficient *revenues* to support public investment and sufficient *returns* to promote private investment. This is especially pertinent for structurally weak economies and the least developed countries (LDCs), where public investment needs for basic development purposes are often more acute.

The links between cross-border investment¹ and tax policy go in both directions:

- Tax has become a key *investment determinant* influencing the attractiveness of a location or an economy for international investors (box V.1).
- Taxation, tax relief and other *fiscal incentives* have become a key policy tool to attract investors and promote investments.
- Investors, once established, add to economic activity and the tax base of host economies and make a direct and indirect *fiscal contribution*.
- International investors and MNEs, by the nature of their international operations, as well as their human and financial resources, have particular opportunities for tax arbitrage between jurisdictions and *tax avoidance*.

The focus of this chapter is on the latter two links, on the fiscal contribution of MNEs and the extent to which they engage in tax avoidance, as these are at the core of the debate in the international community today. However, any policy action aimed at increasing fiscal contribution and reducing tax avoidance, including the policy actions resulting from the BEPS project, will also

Box V.1.

Tax as a determinant of FDI: what role does tax play in location decisions?

Conventional wisdom has it that tax does not play a fundamental role in investment location decisions. Multinationals make their decisions to enter a particular market mostly on the basis of economic determinants – e.g. the size and growth of a market, access to resources or strategic assets, and the cost of factors of production. Moreover, a host of non-tax policy determinants are generally considered more relevant for location decisions, such as the stability and predictability of the business climate, the strength of commercial law and contract enforcement, trade restrictions, the intellectual property (IP) regime, and many others.

In this view, tax does not so much drive locational decisions as it drives the modality of the investment and the routing of investment flows. Top managers of MNEs decide to enter a given market largely independent of tax considerations, and their tax advisers then structure the investment in the most tax-efficient manner. The fact that a significant share of global investment is routed to its final destination through special purpose entities (SPEs) and tax havens, discussed later in this chapter, lends credence to this view.

The relevance of tax in investment decisions is generally considered low for resource- and strategic asset-seeking investments and for market-seeking investments, and only one of many determinants driving location decisions for efficiency-seeking investments. However, a number of nuances require consideration.

- *Resource-seeking investments* can be highly capital intensive and have very long gestation periods. Calculations of expected returns can be extremely sensitive to cost factors, of which tax is an important one. Investments tend to be subject to long and arduous negotiations over precisely how rents are distributed between investors and states, and through what fiscal mechanisms. The fact that negotiators on both sides make trade-offs between different levying mechanisms (e.g. taxes versus royalties) should not be mistaken for a lack of attention to any one of them. Moreover, stability and predictability in the fiscal treatment of these investments are crucial, given their long-term nature and long payback periods.
- *Market-seeking investments* per se may appear to be less sensitive to tax. But the modus operandi of investors can be strongly influenced by tax. The extent to which MNEs source and produce locally or rely on imported value added, key to the development impact of foreign investments on host economies, is clearly influenced by tax. The common view that market-seeking investments are less sensitive to tax tends to confuse the market-entry decision with actual investment in productive capacity.
- *Efficiency-seeking investments*, through which MNEs look for low-cost locations for parts of their production process, are highly sensitive to tax. Counter-intuitively, for many of these investments low tax *rates* do not actually feature high on the list of locational determinants that MNEs consider, because the expected rate is exceedingly low. Due to the nature of these investments, they tend to be located in special economic zones or fall under special regimes. The differentials across locations in labour costs and productivity, availability and cost of land and other factors of production, and trading costs, tend to be far more important than tax rate differentials at such low levels. However, it is the tax *base* that is really of interest to investors in efficiency-seeking operations, as these are often steps in the global value chains of MNEs, and transfer pricing plays a prominent role. In addition, low taxes on international transactions are obviously a key determinant. Without special regimes, economies are often at a disadvantage for efficiency-seeking investments, confirming the fact that tax can be a key locational determinant.

Thus the importance of tax as a locational determinant risks being generally underestimated. The growth of global value chains, which has increased the relative weight of efficiency-seeking investments in the mix, has served only to make tax an even more important factor in countries' attractiveness and this trend is likely to continue.

It is not only the *level* of taxation that matters in investment decisions. It is also the ease with which tax obligations can be fulfilled that is important. Indicators of the ease of doing business – covering a range of administrative procedures relevant to business operations, including paying taxes – generally feature prominently in location comparisons presented to investors. UNCTAD's Business Facilitation programme, which helps developing countries simplify administrative procedures for investors, prioritizes procedures for paying taxes immediately after procedures for business registration and licensing.

Most important is the stability and predictability of the fiscal environment in host countries. A perceived risk of significant changes in the fiscal regime or in the fiscal treatment of individual investments will tend to be a showstopper. Fiscal authorities that demonstrate the capacity to establish collaborative relationships with investors and provide confidence as to the continuing fiscal treatment of investment operations can help remove a major obstacle to investment.

In summary, tax plays an important role in location decisions, principally in three ways: the fiscal burden, the administrative burden, and long-term stability and predictability.

Source: UNCTAD.

have to bear in mind the first and most important link: that of tax as a determinant of investment.

In addition, in the debate on the public revenue contributions of MNEs, fiscal incentives for investors are also often considered a form of “leakage” or “slippage” of tax revenues for governments, much like tax avoidance schemes (although they are clearly different in that they represent a deliberate policy measure to attract investment). Critical questions have also arisen as to whether MNEs are making adequate contributions for the extraction or exploitation of natural resources. Some of these issues feature in the BEPS discussion where policy action is relevant, for example, to avoid allowing incentives to become part of the tax avoidance toolkit of MNEs, leading them to shift profits to locations with tax holidays. Concerns have been raised about the ability of MNEs to play governments and locations against each other, inducing a “race to the bottom” in tax levies. Incentives and tax avoidance have other parallels – tolerance by authorities of “aggressive” tax minimization schemes can be seen as a (less transparent) alternative to explicitly provided incentives. Nevertheless, this chapter will not attempt to add to the vast body of existing analysis on fiscal incentives and their relative ineffectiveness, but rather focus on key knowledge gaps in the ongoing international debate:

- How much do MNE foreign affiliates contribute to government revenues, especially in developing countries? What is the value at stake, or the baseline, for policy action against tax avoidance?
- How do patterns of international investment flows and stocks drive MNE tax contributions as well as tax avoidance opportunities, and what is the impact on fiscal revenues for developing countries?
- On balance, what is the net fiscal contribution of MNE activity and what are the implications for the links between tax and investment policy, especially in the context of anti-avoidance policy action and BEPS?

As such, the chapter helps lay the foundation for a discussion on harmful tax competition.

The chapter is structured as follows:

Section A looks at the contribution of MNEs to government revenues, especially in developing countries, taking a broad approach including fiscal contributions through corporate income tax as well as other taxes, social contributions and other revenue sources including, critically, royalties on natural resources.

Section B provides the key analytical results on the magnitude and patterns of international corporate investments through offshore investment hubs. It presents an innovative perspective on indirect or transit investment patterns in the global economy – the *Offshore Investment Matrix* – and shows the extent to which investment and tax considerations are inextricably intertwined. The section also describes the root causes behind the outsized role of offshore hubs in global investment and reviews the most relevant MNE tax planning schemes. It specifically highlights those schemes that are most dependent on offshore structures and therefore most visible in global investment patterns.

Section C focuses on the development impact of tax avoidance schemes and estimates the related tax revenue losses for developing economies. It provides estimates that can be considered complementary to existing efforts in the international community, but derived from a new approach based on the *Offshore Investment Matrix*.

Section D draws policy conclusions from taking an investment perspective on MNE tax planning practices and brings them together in a set of guidelines for Coherent International Tax and Investment Policies.

The annexes to this chapter (available online) provide the detailed methodology and approach for the two key analytical contributions: the fiscal contribution of MNEs and the investment perspective on international tax avoidance (including the *Offshore Investment Matrix* and the tax revenue loss calculations). The two technical annexes respond to demand in the international community for new ideas and methods to examine the fiscal impact of MNEs – including an explicit call in the G20 BEPS Action Plan. A third non-technical annex provides an overview of existing countermeasures to tackle tax avoidance and an account of the ongoing debate in the international community.

A. MNEs AS A SOURCE OF GOVERNMENT REVENUES FOR DEVELOPMENT

Policymakers and experts at work on the BEPS project have so far not arrived at a quantification of the value at stake for government revenues. Various research institutes and NGOs have put forward estimates for the amount of taxes avoided by MNEs in developing economies. To date, there is no estimate of a baseline establishing the actual contribution of firms in general and MNEs in particular.

To measure the value at stake at the intersection between international tax and investment policy, and to set a baseline for any discussion on tax avoidance by MNEs, this section examines the overall contribution of foreign affiliates of MNEs to government revenues.

In order to understand the context within which MNEs pay taxes, social contributions, and other levies and fees, the section first provides a broad picture and breakdown of government revenues overall and looks at differences in revenue collection between economies at various levels of development. This initial examination of overall government revenues is instrumental to the approach to estimating MNE contributions developed in this chapter. The approach zooms in from overall government revenues to overall corporate contributions (domestic and foreign), and finally to foreign affiliate contributions. Such an approach ensures that margins of error in estimations are confined along the way. Nevertheless, as available data on foreign operations and tax payments of MNEs are limited and fragmented, the analytical approach has been heuristic, employing a variety of sources and methods to converge towards a meaningful *order of magnitude* for MNE contributions. Annex I describes in detail the data approach and analytical steps.

Looking at the broader backdrop for foreign affiliate contributions to government revenues makes clear that some characteristics of revenue collection in developing economies that might at first glance appear to be a function primarily of the fiscal behaviour of investors are in fact often due largely to structural features of the economy. This is important in the context of the ongoing Financing for Development debate, in which improving domestic resource mobilization is a key pillar under plans to fund progress towards the SDGs. Policy actions focusing on the tax contribution of foreign investors can be an effective way to increase

government revenues but must be seen as part of a broader programme of action addressing domestic resource mobilization.

At the same time, UNCTAD's estimates show that the fiscal impact of MNE foreign affiliates in developing countries is sizable and that their contributions represent an important part of total government revenues. These findings support the need for a balanced approach, through appropriate measures that preserve the financing pool provided by foreign affiliates while at the same time tackling tax avoidance.

It is important to note that the approach taken here assesses not only the pure tax contribution of foreign affiliates (corporate income as well as other taxes) but also other contributions to government revenues, including royalties on natural resources, as well as the corporate share of all other forms of government revenues, in order to provide a full picture of the value at stake. In all cases, data are transparent and clearly distinguish actual tax from other types of contributions.

Finally, the aim in this section is not to arrive at a value *judgement* on the fiscal contribution of MNEs (i.e. whether it is "enough", which is for each government to decide), but only at a rough but objective value *measurement*, as a baseline for the subsequent discussion of tax avoidance.

1. Government revenues and revenue collection in developing countries

In the context of the Financing for Development debate, in which improving domestic resource mobilization is a key pillar under plans to fund progress towards the SDGs, it is important to point out that the level of economic development is generally a more significant driver of variations in revenue collection than natural resource endowment or the presence of MNEs. As a general rule, the lower the level of development of a country, the higher is the share of corporates in government revenue generation and the greater the importance of non-tax revenue streams contributed by firms, including royalties on natural resources, tariffs and other levies.

There are large variations in government revenue collection between countries and regions. Looking at

government revenues as a share of GDP, a key driver for such variations is the level of income of economies (figure V.1). High-income countries collect, on average, about 40 per cent of GDP in taxes, social contributions and other revenues, low-income countries less than 20 per cent.

Looking at economic groupings and regions reveals a mixed picture because of large variations between countries within each region. The weighted average ratio of government revenues to GDP of developing countries is still more than 10 percentage points lower than that of developed countries. The 30 per cent of GDP collected in Africa, which compares favourably with the developing-country average of 27 per cent, is skewed by a few upper-middle-income countries with above-average revenues (mostly due to income from natural resources) that make up for much lower collection ratios in a large group of low-income countries. The lowest levels of revenue collection as a share of GDP are found among the LDCs in Asia.

Overall, the level of economic development and related issues of governance and high degrees of informality are generally more significant drivers of variations in total revenue collection than natural resource endowment or the presence of MNEs. Figure V.2, which focuses specifically on Africa, shows that at

given levels of per capita income, especially at lower income levels, the availability of natural resources and the penetration of FDI do not substantially change revenue collection as a share of GDP.

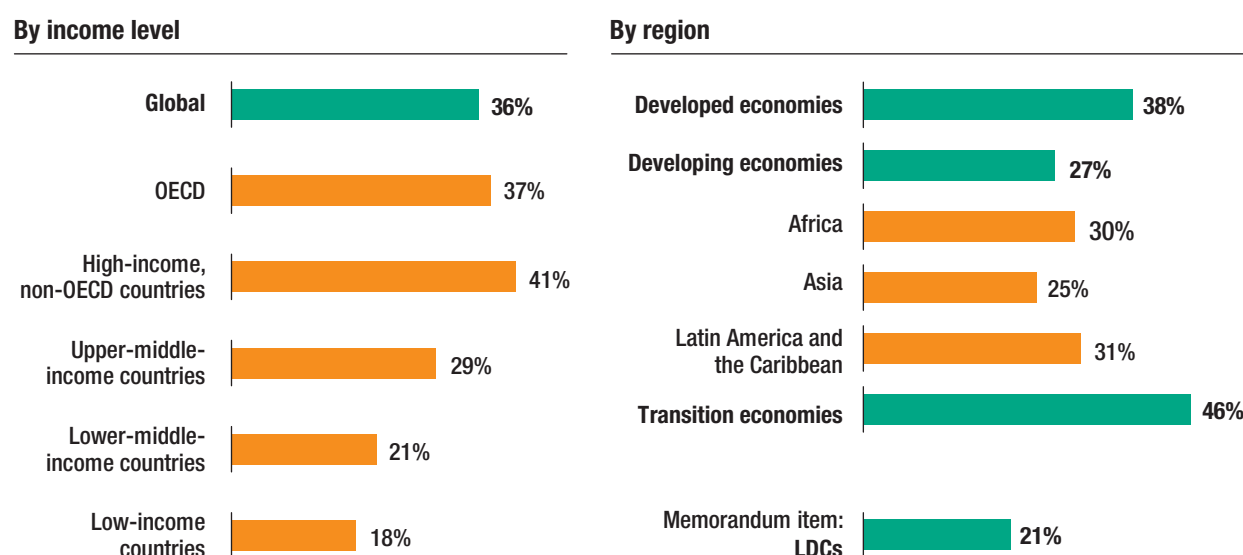
The composition of government revenues (figure V.3) reveals further insights.²

- i. At the first level of disaggregation (left-hand chart in figure V.3), splitting total revenues by taxes, social contributions and other revenues (which include, among others, royalties on natural resources and official development assistance or grants), developed countries show a larger proportion of revenues in the form of social contributions, on average. Developing countries unsurprisingly rely to a much greater extent on other revenues – mostly income from natural resources. The poorest countries tend to rely most on such other revenues: they make up almost half of government revenues in LDCs and in the African region as a whole. There is a clear pattern of shifting revenues from (corporate) income taxation to other revenues related to natural resource endowment. In Africa, at a given level of revenue collection (30 per cent of GDP), resource-driven countries (those with commodity exports representing more than 75 per cent of total exports) exhibit a revenue distribution heavily

Figure V.1.

Differences in government revenue collection

Government revenues as a share of GDP, weighted averages (Per cent)



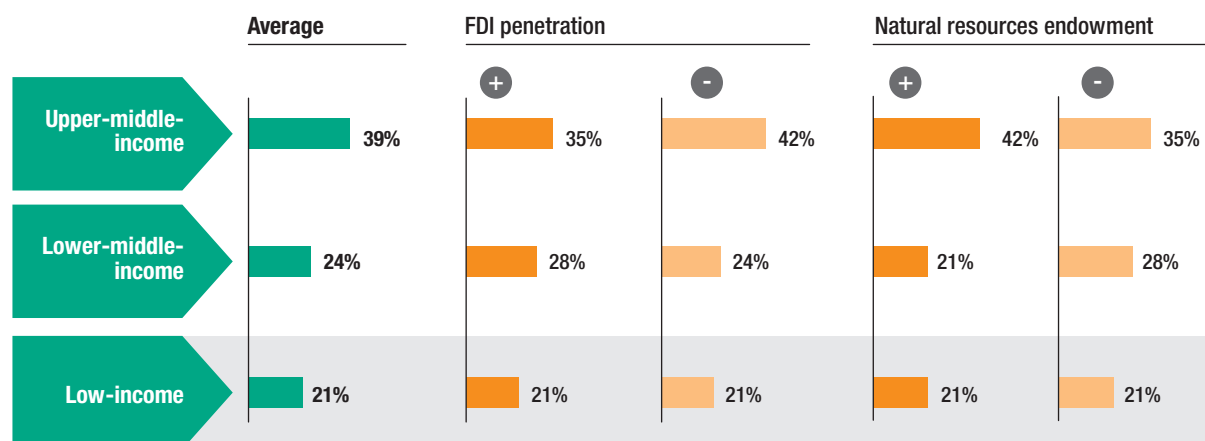
Source: UNCTAD analysis, based on the ICTD Government Revenue Dataset (release September 2014, reference year 2009).

Note: Full details on data sources and methods provided in annex I.

Figure V.2.

Relationship between FDI penetration, resource endowments and government revenues

Government revenues as a share of GDP, weighted averages, Africa (Per cent)



Source: UNCTAD analysis, based on the ICTD Government Revenue Dataset.

Note: For FDI penetration, for each income-level group of countries, "+" is assigned to countries ranking in the top half in terms of the ratio of FDI stock over GDP. For natural resources, "+" is assigned to countries in which the share of commodities in total exports is greater than 75 per cent.

skewed towards other revenues (at about 60 per cent of total revenues), while income taxes account for less than 15 per cent; by contrast, the group of non-resource-driven countries shows income taxes at almost 40 per cent of total revenues and other revenues at 25 per cent. Resource-rich lower-income countries may be making a trade-off in tax collection from corporates between royalties (and export revenues) on the one hand, and corporate income taxes on the other.

- ii. Breaking down the revenue category of taxes one level further (right-hand chart in figure V.3) shows that developed countries rely more heavily on income taxes (50 per cent of taxes) than developing countries (one third of taxes). Other tax components are far more important in developing countries, especially indirect taxes on goods and services (such as value added tax or VAT) at nearly half of total taxes.

It is worth noting that taxes on international trade transactions constitute a sizable component (one fifth) of tax revenues in LDCs, which may be important in the context of ongoing and future trade liberalization processes at regional or multilateral levels.

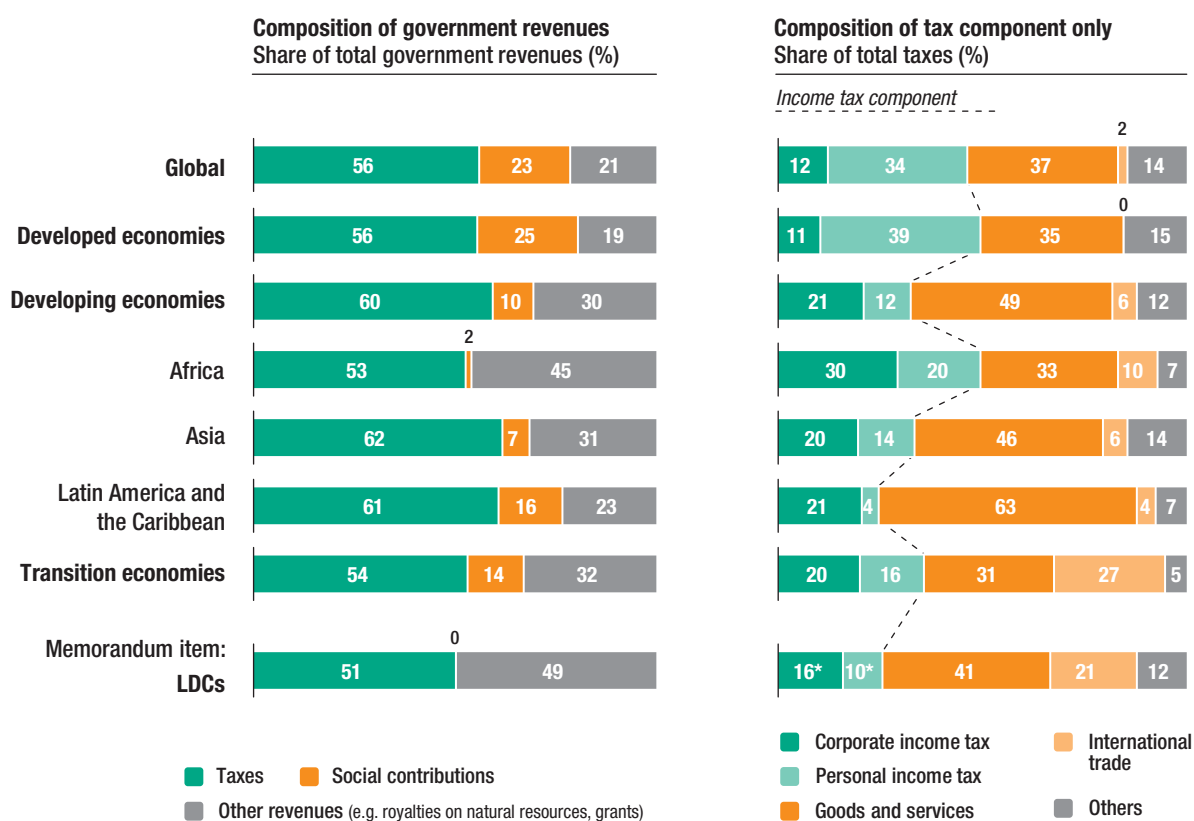
- iii. Corporate income taxes are relatively more important in the composition of taxes for

developing countries than for developed countries: at about 20 per cent of total taxes, they are nearly twice as important. Conversely, the share of personal income taxes is much more limited in developing economies. In developing countries, corporate taxes yield two thirds of all income taxes; in developed countries, only one quarter. Accordingly, as a share of GDP, corporate income tax amounts to almost 4 per cent of GDP in developing economies against 2 per cent in developed economies; by contrast, the share of personal income taxes falls to 2 per cent of GDP in developing economies against 8 per cent in developed economies.

The main patterns, (i), (ii), and (iii), resulting from the regional comparison are fully confirmed (and possibly strengthened) when adopting an income-driven perspective (figure V.4).

It appears that for assessing the relative collection capabilities of economies in different regions the revenue category of social contributions and the tax categories of personal income tax and indirect taxes represent the most useful proxy indicators. Although social contributions and personal income taxes are clearly linked to overall income levels and can thus be expected to amount to less in low-income countries, these categories also require the more sophisticated

Figure V.3. Composition of government revenues, by region (Per cent)



Source: UNCTAD analysis, based on the ICTD Government Revenue Dataset.

Note: The classification is generally based on the standard IMF Government Finance Statistics classification. However, in the left-hand graph the category "other revenues" includes grants (these are very small, at 1.5 per cent of total government revenues in developing economies). In the right-hand graph, income taxes (corporate and personal) reflect the IMF category "taxes on income, profit and capital gains" ("payable by corporations and other enterprises" and "payable by individuals"). The residual category "others" includes taxes on payroll and workforce, taxes on property and other taxes. Data with (*) subject to very limited coverage. Full details on data sources and methods provided in annex I.

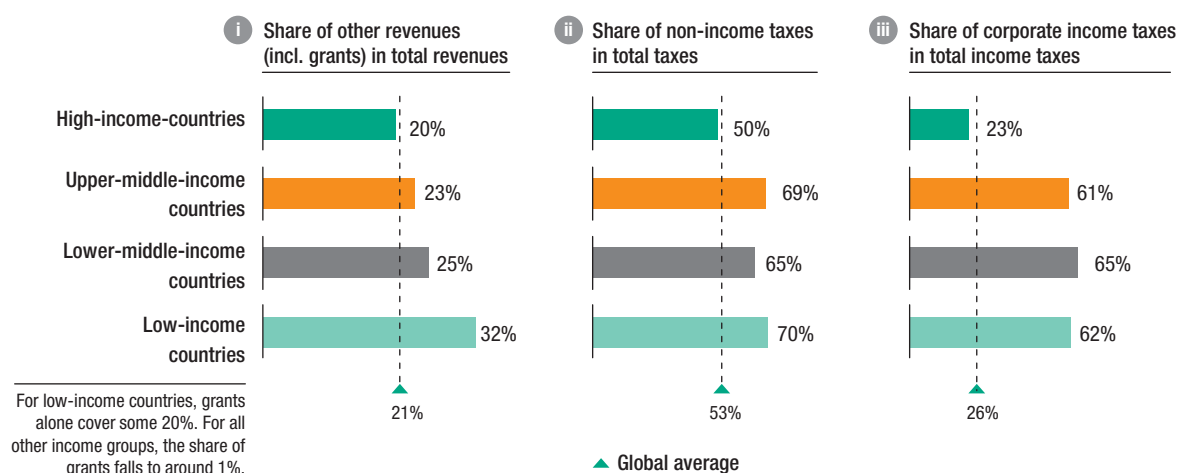
institutional structures and collection capabilities. In contrast, indirect taxes are easier to collect. Lower shares of social contributions and personal income taxes and higher shares of indirect taxes seem to be associated with lower collection capabilities and a greater reliance on corporate income taxes.

Interestingly, corporates are instrumental in collecting all three of these categories. While they do not actually pay personal income taxes and indirect taxes out of their own pockets in theory (leaving aside specific fiscal issues such as non-recoverable VAT) they collect these taxes on behalf of government through their payrolls and from their customers. This role, not explicitly quantified in the assessment of corporate contributions, represents a significant additional

element of fiscal value added – of crucial importance in developing countries with large informal economies.

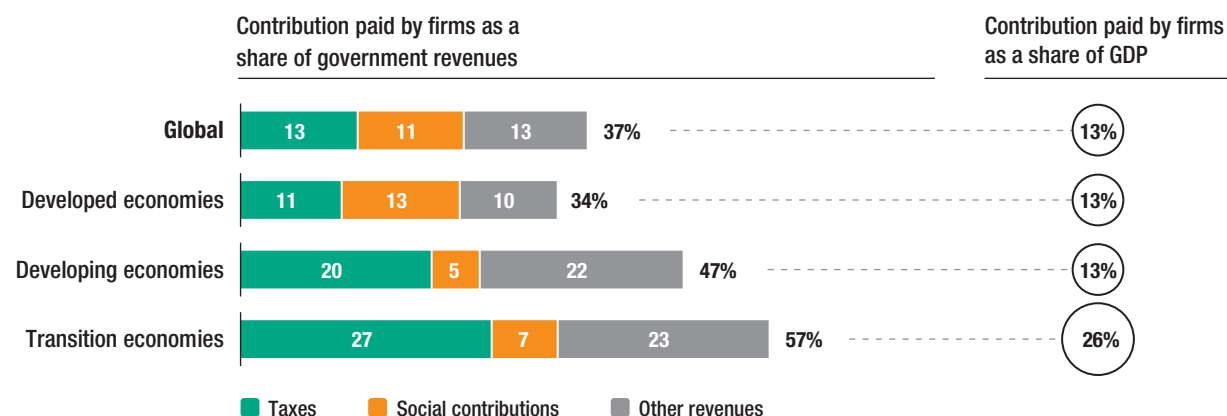
Looking specifically at the (paid) contribution of corporates (domestic and foreign firms) across all three categories of government revenues – taxes, social contributions and other revenues – confirms the significantly higher relative contribution in developing countries (almost half of government revenues) compared with developed countries (one third) (figure V.5). The difference is caused, as noted before, by higher revenues from corporate taxes (income taxes as well as taxes on international trade and other levies) and from relatively higher corporate contributions to other revenues, especially from natural resources and property. Relative to the size of the economies, the

Figure V.4. Key patterns in the composition of government revenues related to income levels (Per cent)



Source: UNCTAD analysis, based on the ICTD Government Revenue Dataset.
 Note: Full details on data sources and methods provided in annex I.

Figure V.5. Contribution to government revenues by firms, domestic and foreign (Per cent)



Source: UNCTAD analysis, based on the ICTD Government Revenue Dataset; IMF Government Financial Statistics database as complementary source.
 Note: Full details on data sources and methods provided in annex I.

corporate contribution to government revenues is practically the same across developed and developing economies at 13 per cent of GDP. The higher relative contribution of firms to government revenues in transition economies is due to relatively high income from natural resources and to the role of state-owned enterprises in the economy.

To sum up, government revenue collection capabilities are largely a function of levels of income and development. At lower levels of development, corporate

contributions to overall revenues and to income taxes are more important due to the low levels of collection of other revenue and tax categories. In addition to taxes paid by corporates, a significant amount of other taxes (especially indirect taxes) depend on collection by corporates. Overall, developing countries rely more on corporates for government revenue collection than do developed countries; as a share of the total economy, fiscal contributions by corporates are at similar levels in developed and developing countries.

2. The contribution of MNEs to government revenues

MNEs are important tax contributors worldwide, and in developing countries in particular. UNCTAD estimates the contribution of foreign affiliates to government budgets in developing countries at about \$730 billion annually. This represents, on average, about 23 per cent of corporate payments and 10 per cent of total government revenues. (In developed countries these shares are lower, at roughly 15 per cent and 5 per cent, respectively, underlining the higher dependence of developing countries on foreign corporate contributions). African countries show the highest relative contribution of foreign affiliates, at more than a quarter of corporate contributions and at 14 per cent of total government revenues. Overall, contributions through royalties on natural resources, tariffs, payroll taxes and social contributions, and other types of taxes and levies are on average more than twice as important as corporate income taxes.

The previous section looked at the level and composition of overall government revenues and at the contribution made by corporates (domestic and foreign firms). This section zooms in on foreign affiliates³ specifically. In order to do so, two new approaches to estimating MNE fiscal contributions have been developed:

1. *Contribution Method.* This approach is based on the economic contribution of foreign affiliates to host economies. It estimates the share of economic activity generated by foreign affiliates (profits, employment, value added, exports) and applies it to relevant components of the corporate contribution.
2. *FDI-Income Method.* This approach is based on country-by-country balance-of-payments data on FDI income. For the main developing regions it estimates the corporate income taxes paid by foreign affiliates by applying a suitable average effective income tax rate to the equity component of FDI income. It then calculates the contribution items other than income taxes based on the estimated weight of income tax in the total contribution paid by the average corporation operating in the region.

The two approaches should not necessarily lead to the same result. In fact, the FDI-income method should in theory yield a lower-bound estimate, given that it can take into account only the income on the foreign-

owned part of directly invested enterprises, rather than the full income of foreign affiliates (although the difference should not be large). Nevertheless, the estimates are broadly consistent, putting the total contribution of MNE foreign affiliates to developing-country government revenues at around \$730 billion annually, representing the midpoint of a range, including a lower bound of about \$650 billion and an upper bound of about \$800 billion. Apart from serving as a cross-check, the two independent approaches allow for different perspectives and provide different insights, discussed below. Comprehensive details on data and statistical methods are contained in annex I; box V.2 provides a brief summary of limitations of the approach and alternative assumptions.

Figure V.6, based on the contribution method, provides the relevant orders of magnitude and shares for developing economies, from total government revenues to the total contribution of foreign affiliates and the breakdown across the main contribution items. Out of total government revenues of \$6.9 trillion (27 per cent of 2012 GDP, see figure V.1), 47 per cent is paid by the corporate sector (see figure V.5), corresponding to some \$3.2 trillion. The share of the corporate contribution pertinent to foreign affiliates is about one quarter (23 per cent), corresponding to \$725 billion or 10 per cent of total government revenues. This contribution includes 60 per cent (\$430 billion) of taxes and social contributions and 40 per cent (\$295 billion) of other revenues. The bulk of these other revenues represents royalties on natural resources.

Within taxes, the subcategories show a slightly different pattern than for corporates as a whole (including domestic firms). While the corporate income tax component is similar, at half of total taxes and social contributions, the share of taxes on international trade transactions is relatively higher for foreign affiliates, at 20 per cent, due to the large share of exports accounted for by foreign affiliates in many developing countries (see *WIR13*). In contrast, the share of payroll taxes and social contributions paid by foreign affiliates is relatively low compared with that paid by domestic firms due to the more capital-intensive nature of many of their operations. Clearly this is an aggregate developing-country picture, with large variations for individual countries and regions, explored below.

As discussed in the previous section, in addition to taxes *paid* by foreign affiliates, which include not

only corporate income taxes but also payroll taxes and social contributions, taxes on international transactions, and a host of other taxes, levies and fees, MNEs contribute to government revenues by *collecting* income taxes from employees, as well as indirect taxes. These taxes are not borne by the MNE; they represent only a compliance cost. In economies with large informal sectors or with relatively limited collection capabilities in the tax authorities, this role can be very important. The collection of taxes on goods and services (e.g. VAT) is especially relevant, as it represents the largest component of developing countries' total tax revenues (at about 50 per cent). As a consequence, tax collection contributions by MNEs are also relevant, covering another 6-plus per cent of government revenues.

Leveraging the FDI-income method to look at the pattern by region (figure V.7), the average 10 per cent foreign affiliate contribution to government revenues becomes 14 per cent in Africa and 9 per

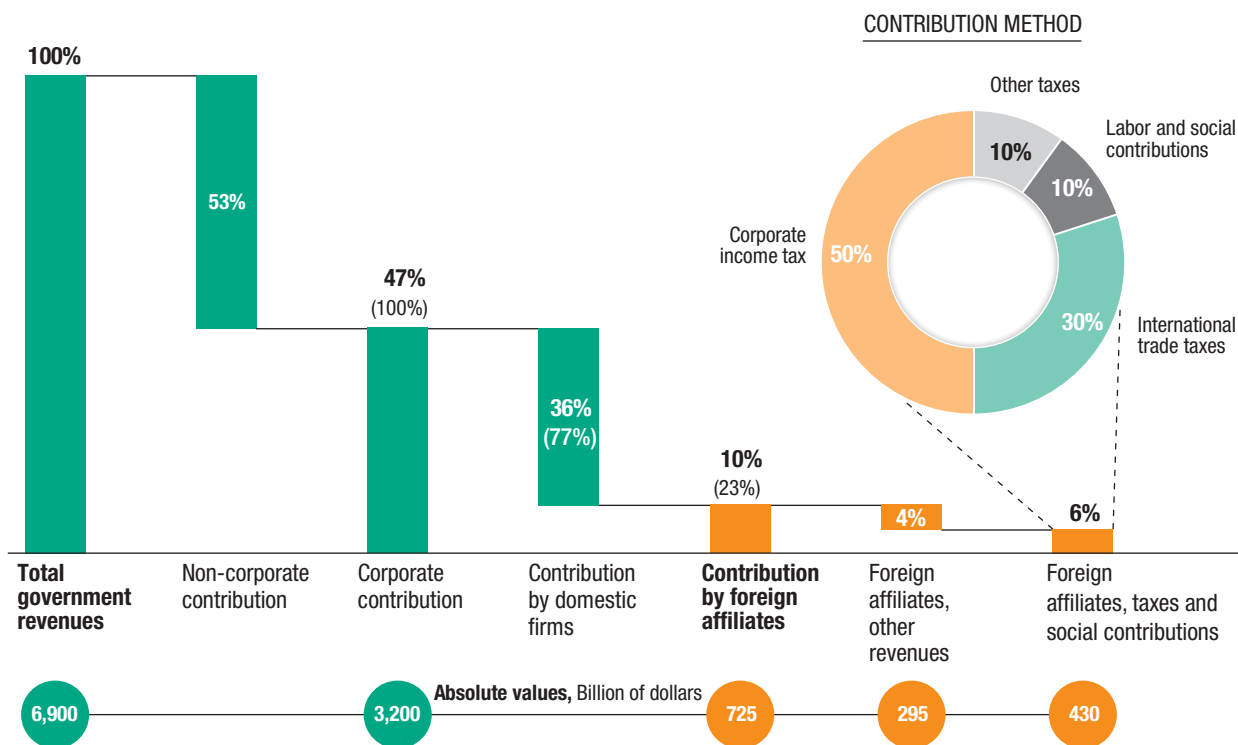
cent in Latin America and the Caribbean (down to 5 to 7 per cent in South America, compensated by higher shares in the Caribbean), with developing Asia representing the average as well as the bulk of overall absolute contributions. The regional variation reflects in part the relative importance of foreign affiliates in the economy of each region, and in part the foreign affiliate contribution to other revenues – in particular to royalties on natural resources. The relative shares of tax and social contributions seem comparable across regions, although when considering South America separately, the relative share of other revenues (resource-related) increases. Summing foreign affiliates' fiscal contributions across regions leads to a global contribution of \$730 billion, in line with the value reported in figure V.6 through the contribution method.

The methodology developed in this chapter not only provides inputs relevant to the international discussion on MNE taxation and development, especially through the establishment of a baseline for the actual

Figure V.6.

Government revenues contributed by foreign affiliates of MNEs

Share of government revenues, developing countries, reference year 2012
(Per cent and billions of dollars)



Sources: UNCTAD estimates, based on the ICTD Government Revenue Dataset; IMF Government Financial Statistics database; United Nations System of National Accounts; Eurostat; U.S. Bureau of Economic Analysis; International Labour Organization; literature review.
Note: Estimates represent range midpoints. Details on data and methods contained in annex I.

Box V.2.

Limitations, alternative assumptions and further research

The analysis of the contribution of MNE foreign affiliates to government revenues presented in this section aims to arrive at meaningful “order of magnitude” estimates. Both the economic contribution and the FDI-income methods developed for this analysis rely on assumptions and approximations to overcome the paucity of relevant data available. The following are some of the most important limitations and assumptions. Full details can be found in annex I.

A meaningful estimate of the actual contribution of foreign affiliates must be calculated net of any profit shifting. The contribution method, however, cannot exclude one form of profit shifting, thin capitalization, because it relies on the national accounts concept of operating surplus to derive profit ratios. A simulation of the impact of this limitation, using extreme assumptions, would bring down the overall contribution from \$730 billion to about \$650 billion – the lower bound of the estimation range. The separate FDI-income method does not present this problem.

The contribution method has another limitation. It does not separate corporate and non-corporate business income in the baseline for the calculation of foreign affiliates’ contribution to corporate income. Removing non-corporate business income, which would be unlikely to contain any foreign affiliate contribution, would have the effect of increasing the foreign affiliate share in the remaining corporate income part, thereby increasing the share paid by foreign affiliates in total corporate income taxes. Simulation of this effect yields the upper-bound estimate for the total foreign affiliate contribution of about \$800 billion. Again, the FDI-income method does not present this problem.

Assumptions regarding the average effective tax rate (ETR) paid by foreign affiliates play an important role, in particular in the FDI-income method. In that method, the ETRs for the developing regions, ranging between 20 and 25 per cent, are based on external studies and confirmed by UNCTAD’s own firm-level analysis, which also finds that ETRs for foreign affiliates and domestic firms are substantially aligned. Other studies have also found no evidence of a substantial difference in ETR between domestic companies and MNEs. The contribution method does not use a specific ETR but, consistent with the empirical findings, it uses the assumption that rates are the same for foreign affiliates and domestic firms.

As uniform ETRs for foreign affiliates and domestic firms may appear counter-intuitive, two important points should be made:

- The fact that domestic firms and foreign affiliates are found to have similar ETRs does not preclude that MNEs, at the consolidated level, may have significantly lower ETRs due to base erosion and profit shifting. (ETRs are calculated on the tax base that remains in foreign affiliates after profit shifting.)
- Many developing countries provide fiscal incentives to MNEs, which (insofar as they lower the tax *rate* rather than the base) would normally imply lower ETRs for foreign affiliates than for domestic firms. While incentives may have a significant impact at the individual country level, at the aggregate level the empirical evidence does not clearly show this. Better and more disaggregated data and further research will be needed to quantify the effect of fiscal incentives.

Finally, a number of assumptions have been made regarding the corporate shares of government revenues across individual revenue categories. These ultimately feed into both the contribution and the FDI-income methods. For each revenue category, the estimation approach determines whether the contribution is made by corporates, made partly by corporates, or not made by corporates. Varying allocations are of course possible and may lead to a wider range of estimates. However, the allocation criteria used here reflect the formal definition and the default application of each revenue category. Different criteria would require the introduction of additional assumptions.

To date, the methods and estimates presented here represent the most comprehensive and systematic picture of the total fiscal contribution of MNE foreign affiliates. Future research efforts may build on the approach developed in this section, experiment with different assumptions, explore methods to reduce approximation errors and, most useful of all, seek ways to disaggregate data at the country level.

Source: UNCTAD. Full details are provided in annex I.

value at stake, but *from the business perspective* it also provides an indication of the *fiscal burden* for the average foreign affiliate. Adopting an approach similar to the World Bank’s *Paying Taxes* study, the fiscal burden for foreign affiliates is measured as the ratio between the fiscal contribution and an adjusted measure of profits (“commercial profits” in the *Paying Taxes* terminology), gross of all relevant contribution items (including above-the-line contribution items).

The resulting fiscal burden on MNE foreign affiliates – taking into account taxes and social contributions only – represents approximately 35 per cent of commercial profits (figure V.8). The inclusion of “other revenues” (in both the numerator and the denominator of the ratio) significantly increases the estimate of the fiscal burden compared with that found using the more standard approach of considering only taxes and social contributions. The total contribution to government

revenues represents about 50 per cent of foreign affiliate commercial profits, with minor variations by region.

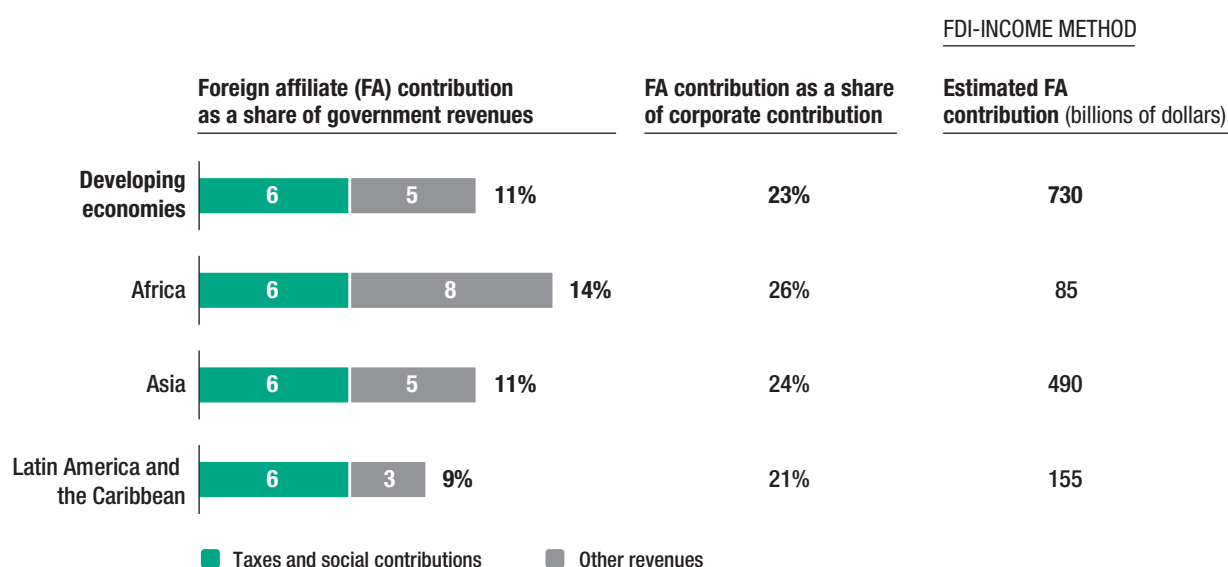
Comparison with the same calculation for developed economies reveals that the fiscal burden based only on taxes and social contributions is lower in developing

economies (35 per cent of commercial profits against 56 per cent in developed economies); however, including other revenues in the equation leads to a partial convergence of the ratios (50 per cent in developing economies against 65 per cent in developed economies).

Figure V.7.

Government revenues contributed by foreign affiliates of MNEs, by developing region

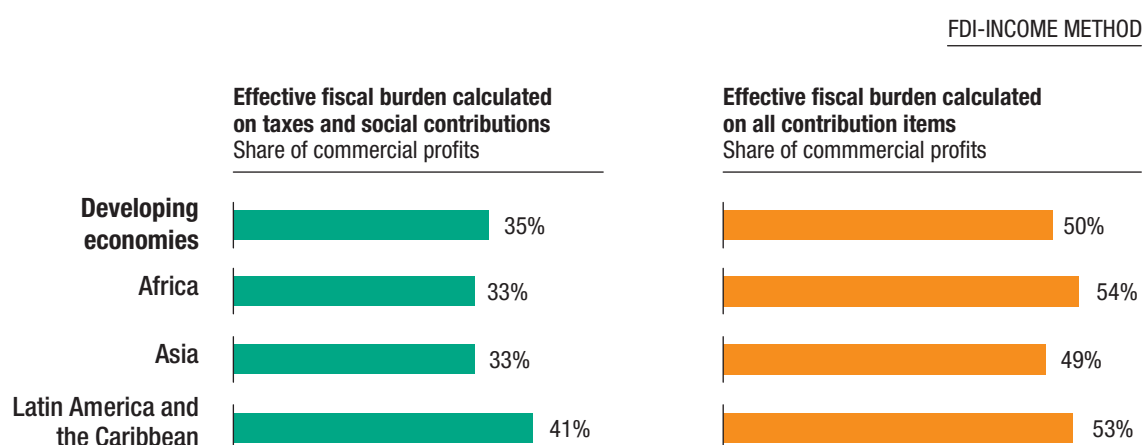
Reference year 2012 (Per cent and billions of dollars)



Sources: UNCTAD estimates, based on the ICTD Government Revenue Dataset; IMF Government Financial Statistics database; IMF Balance of Payments Statistics.
Note: Details on data and methods contained in annex I.

Figure V.8.

The fiscal burden on foreign affiliates of MNEs (Per cent)



Sources: UNCTAD estimates, based on the ICTD Government Revenue Dataset; IMF Government Financial Statistics database; IMF Balance of Payments Statistics.
Note: Details on data and methods contained in annex I.

B. AN INVESTMENT PERSPECTIVE ON INTERNATIONAL TAXATION

MNEs build their corporate structures through cross-border investment. They will construct those corporate structures in the most tax-efficient manner possible, within the constraints of their business and operational needs. The size and direction of FDI flows are thus often influenced by MNE tax considerations, because the structure and modality of investments enable tax avoidance opportunities on subsequent investment income. In tackling tax avoidance, most notably in the BEPS approach, the attention of policymakers focuses naturally on tax rules, company law and transparency principles – i.e. on accounting for income. The fundamental role of investment as the enabler of tax avoidance warrants a complementary perspective.

This section aims to provide a new perspective on corporate international taxation and MNE tax avoidance schemes. It integrates the mainstream approach of the BEPS project with an investment-based approach emphasizing the relevance of corporate structures set up by channelling FDI through offshore investment hubs and OFCs, notably *tax havens* and jurisdictions offering so-called *special purpose entities* (SPEs),⁴ as these are the *enablers* of most BEPS schemes.⁵ In essence, corporate structures built through FDI can be considered “the engine” and profit shifting “the fuel” of MNE tax avoidance schemes.

In order to analyse the scope, dimensions and effects of tax-efficient corporate structures (“fuel-efficient engines”), the section looks at FDI flowing through OFCs or conduit jurisdictions (transit FDI). It is important to emphasize from the outset that the notion of transit FDI does not equate with non-productive FDI. FDI designed as part of tax planning strategies of MNEs may or may not have a real economic impact on the countries involved. For example, an investment from a North American firm in Asia to start a new production plant may be channelled through Europe for tax reasons (potentially penalizing tax revenues in both home and host countries) but still carry the productive-asset-creating effects of a greenfield investment. By contrast, transit FDI tends to have very little real economic impact in countries acting as investment hubs in MNE tax planning schemes.

For the purpose of the analysis in this section, a simple (and conservative) approach has been taken

to identifying offshore investment hubs, limiting the scope to tax havens and a few jurisdictions that (at the time of analysis for this chapter) explicitly publish directional SPE investment data.⁶ Other countries host SPEs and various types of entities that facilitate transit investments. Alternative approaches and perimeters for offshore investment hubs, combining generally accepted tax-based criteria with criteria based on objective FDI data, are discussed in annex II.

It should be noted that the conduit countries discussed in this section are not alone in offering certain tax benefits to foreign investors; a degree of tax competition has led many other countries to adopt similar policies. *No policy implications are implied by the scope of the perimeter for offshore investment hubs used in this section.* In fact, the analysis will show that any action on tax avoidance practices needs to address policies across all jurisdictions – in base (home) countries, conduit (transit) countries and source (host) countries alike.

1. The importance of offshore investment hubs and transit FDI

Offshore investment hubs play a major role in global investment. Some 30 per cent of cross-border corporate investment stocks (FDI, plus investments through SPEs) have been routed through conduit countries before reaching their destination as productive assets. The growth of transit investment saw a sharp acceleration during the second half of the 2000s.

In 2012, the British Virgin Islands were the fifth largest FDI recipient globally with inflows at \$72 billion, higher than those of the United Kingdom (\$46 billion), which has an economy almost 3,000 times larger. Similarly, outflows from the British Virgin Islands, at \$64 billion, were disproportionately high compared with the size of the economy. The British Virgin Islands are only one example of an economy with such unusual FDI behaviour. Such very different economies as the Netherlands and Luxembourg also exhibit amplified investment patterns.⁷ Despite their heterogeneity, all these countries act as offshore investment hubs for MNEs. Many of these hubs display some degree of the following characteristics: (i) no or low taxes;

(ii) lack of effective exchange of information; (iii) lack of transparency; (iv) no requirement of substantial activity.⁸

The investment analysis in this section, which provides a comprehensive map of corporate investment to and from offshore hubs, covers a set of 42 hubs differentiated in two groups:

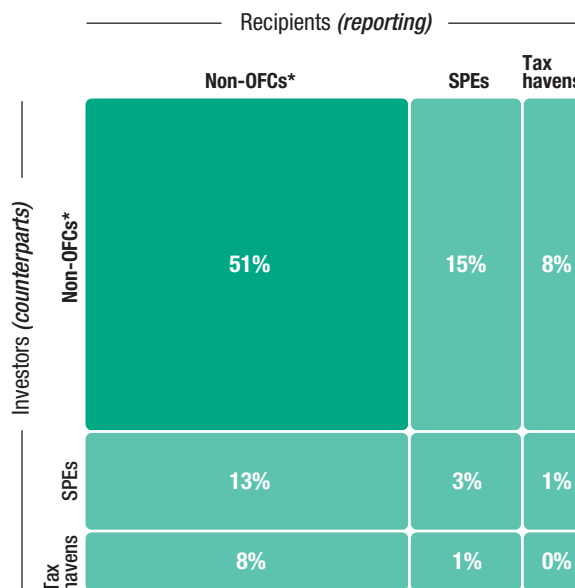
- *Jurisdictions identified as tax havens.* Small jurisdictions whose economy is entirely, or almost entirely, dedicated to the provision of offshore financial services.
- *Jurisdictions (not identified as tax havens) offering SPEs or other entities that facilitate transit investment.* Larger jurisdictions with substantial real economic activity that act as major global investment hubs for MNEs due to their favourable tax and investment conditions.

In the absence of any universally agreed approach to classifying offshore investments and investment hub activity, this chapter has opted for a narrow and conservative perimeter of analysis based on a list of tax havens originally proposed by the OECD⁹ and a limited set of SPE jurisdictions, which are those that have a long-standing record of published SPE data, with the Netherlands and Luxembourg accounting for the lion's share. It should be noted that many other economies facilitate transit FDI in various ways. Annex II provides alternative options and results.

The Offshore Investment Matrix (figure V.9) provides a comprehensive mapping of corporate international investments through offshore investment hubs. For each "unit" of MNE international investment stock, bilateral data provide a pairing of direct investor and recipient jurisdictions, which are grouped under the categories *Non-OFCs*, *SPEs* or *Tax Havens*. When the investor/recipient is a jurisdiction that offers SPEs, only part of the outward/inward investment is allocated to transit investment activity (the *SPE component*) while the remaining part is allocated to the *Non-OFC component*. Full methodological details on the construction of the Offshore Investment Matrix are provided in annex II.

The matrix shows the pervasive role of offshore investment hubs in the international investment structures of MNEs, as already envisaged in *WIR13* and hinted at by other studies.¹⁰ In 2012, out of an estimated \$21 trillion¹¹ of international corporate

Figure V.9. The Offshore Investment Matrix, 2012
Bilateral investment stocks by type of investor and recipient, share of total (Per cent share of FDI stock)



* Non-OFCs are stocks based in or coming from non-tax havens and non-SPE jurisdictions, and include the (FDI-) part of investment stocks in or from SPE jurisdictions not associated with SPEs.

Σ = 100% ≈ \$ 29 trillion
(2012 TOTAL INWARD FDI STOCK plus investment into SPEs)

Source: IMF Coordinated Direct Investment Survey 2012 and 2011; national statistics; UNCTAD estimates.

Note: Full details on the methodology provided in annex II.

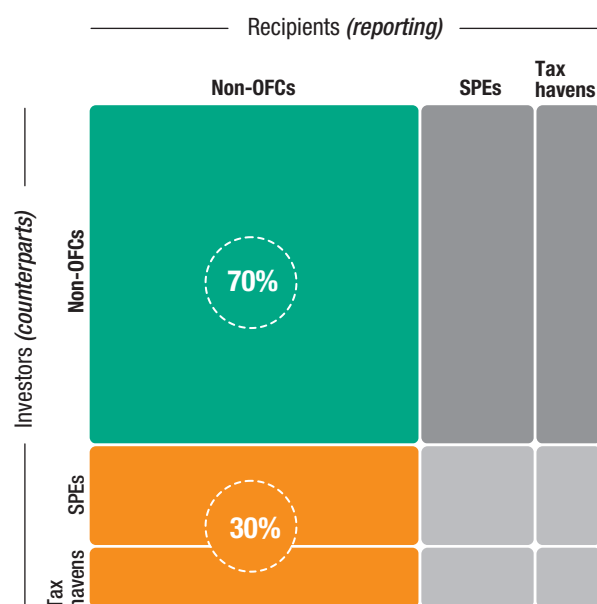
investment stock in *Non-OFC* recipient countries (the coloured area in figure V.10), more than 30 per cent, or some \$6.5 trillion, was channelled through offshore hubs (the orange area). The contribution of SPEs to investments from conduit locations is far more relevant than the contribution of tax havens. The largest offshore investment players are SPE jurisdictions.

A mirror analysis of the inward investment into offshore hubs (the dark grey area in figure V.10 on the next page) reveals that 28 per cent of the total amount of cross-border corporate investment stock is invested into intermediary entities based in hubs. In some cases, these entities may undertake some economic activity on behalf of related companies in higher tax jurisdictions, such as management services, asset administration or financial services (*base companies*). However, often they are equivalent

Figure V.10.

Non-OFC inward investment stocks, by type of investor

Vertical view of the Offshore Investment Matrix (Per cent)



Source: IMF Coordinated Direct Investment Survey 2012 and 2011; national statistics; UNCTAD estimates.

Note: Full details on the methodology provided in annex II.

to letterbox companies, legal constructions conceived for tax optimization purposes (*conduit companies*) and potentially to benefit from other advantages associated with intermediate legal entities. The prominent *pass-through* role of these entities in financing MNE operations causes a degree of *double counting* in global corporate investment figures, represented by the dark grey area in the Offshore Investment Matrix (inward investments into offshore hubs), which broadly mirrors the orange area (outward investments from hubs).¹² In UNCTAD FDI statistics this double-counting effect is largely removed by subtracting the SPE component from reported FDI data.

The share of stock *between* hubs (light grey area) is also relevant, at 5 per cent of global investment stock. This confirms that offshore investment hubs tend to be highly interconnected within complex multilayered tax avoidance schemes. The “*Double Irish-Dutch Sandwich*” employed by IT multinationals is a relevant example of such structures.

An analysis of the Offshore Investment Matrix by the two investment components, *Equity* and *Debt*,

reveals additional dynamics. The picture for the debt component (figure V.11.b) show a significantly larger role for hubs (and especially SPEs) compared with the general pattern. This captures a typical tax avoidance mechanism whereby an SPE channels funds through intracompany loans to third-country affiliates. The basic rationale of this practice is to generate an erosion of the tax base in the recipient (high-tax) jurisdiction, with profit shifted to low-tax locations in the form of deductible interest payments.¹³

The scenario represented in figures V.9 through V.11 is the result of a boom in the use of offshore structures in cross-border corporate investment. Between the start and end of the 2000s, the average share of investment flows to non-OFC countries routed through offshore hubs increased from 19 to 27 per cent (figure V.12). More recently, greater international efforts to tackle tax avoidance practices have managed to reduce the share of offshore investments in developed countries, but the exposure of developing economies to such investments is still on the rise (see also section C).

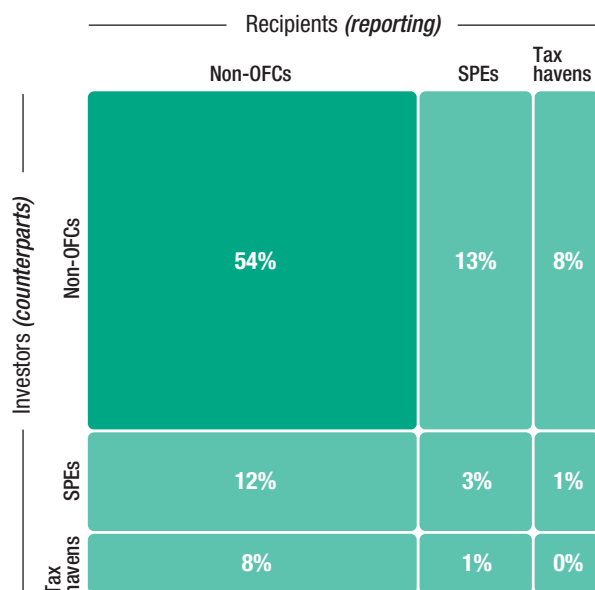
2. The root causes of the outsized role of offshore hubs in global investments

The root cause of the outsized role of offshore hubs in global corporate investments is tax planning, although other factors can play a supporting role. MNEs employ a wide range of tax avoidance levers, enabled by tax rate differentials between jurisdictions, legislative mismatches and gaps, and tax treaties. MNE tax planning involves complex multilayered corporate structures. From an investment perspective, two archetypal categories stand out: (i) intangibles-based transfer pricing schemes and (ii) financing schemes. Both schemes, which are representative of a relevant part of tax avoidance practices, make use of investment structures involving entities in offshore investment hubs.

The investment data and the results of the analyses depicted in the previous section highlight the massive and still growing use of offshore investment hubs by MNEs. Offshore investment structures are an integral part of MNE tax planning strategies aimed at shifting profits from high-tax to low-tax jurisdictions in order to reduce corporate tax bills. What makes them attractive for tax optimization purposes is usually a mix of features. Corporate tax is often reduced to minimal levels through preferential regimes. Some

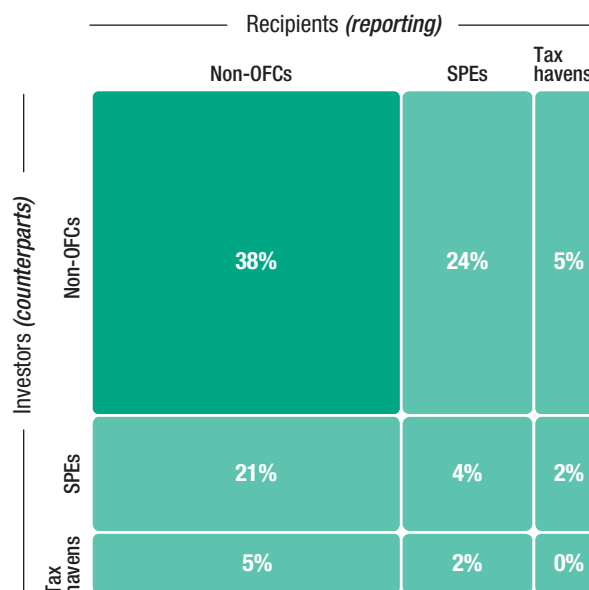
Figure V.11. The Offshore Investment Matrix, by investment component
(Per cent share of FDI stock)

a. Equity



∑ = 100% ≈ \$24 trillion (corresponding to 82% of total FDI stock)

b. Debt instruments



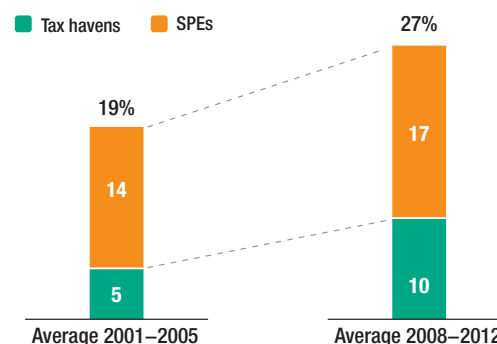
∑ = 100% ≈ \$5 trillion (corresponding to 18% of total FDI stock)

Source: IMF Coordinated Direct Investment Survey 2012 and 2011; national statistics; UNCTAD estimates.
Note: The methodology follows directly from the general case illustrated in figure V.9 and explained in annex II.

of these jurisdictions offer the option to negotiate tax rates or obtain favourable tax rulings from tax authorities. In addition, they may offer special vehicles (special types of entities such as holding structures, foundations, cooperatives, etc.), which result in both tax and operational advantages. Offshore hubs are usually effective in circumventing withholding taxes. For instance, most SPE jurisdictions do not apply withholding taxes on outflows and ensure that withholding tax on inflows is limited through the application of tax treaties. SPE jurisdictions tend to have extensive treaty networks, making them ideal intermediary or regional headquarter locations.

An objective discussion on the root causes of the role of offshore investment hubs, and in particular SPE jurisdictions, in international investment should take into account other factors. Some jurisdictions count on extensive networks of investment treaties providing investor protection and access to international arbitration. In addition, offshore hubs tend to require

Figure V.12. Trend in the share of investment inflows from offshore hubs, 2001–2012 (Per cent)



Source: UNCTAD FDI database; national statistics; UNCTAD estimates.
Note: Elaboration of UNCTAD bilateral flow statistics. The target sample of (recipient) reporting countries includes all countries reporting bilateral investments flows with the exclusion of offshore hub countries (tax havens and the selected countries reporting SPEs). This approach makes it possible to describe the trend in the penetration of offshore investments in "real" economies while removing the (distorting) effects of investments between hubs. In the context of flow analysis, averaging across multiple years is helpful to mitigate the volatility of the offshore component and capture the underlying trend. For the countries reporting SPEs, the share of SPEs in total outflows is derived from central bank data.

relatively few formalities for the set-up of investment vehicles and offer attractive business climates. Countries providing homes to SPEs generally have strong legal and regulatory frameworks, good in-country infrastructure and sophisticated banking environments and are stable from an economic and political perspective. They also offer other advantages such as a skilled labour force and an established business services industry. Geographical location and language are other important factors. However, the relative importance of non-tax factors in making SPE jurisdictions successful investment hubs should not be overestimated. For example, only one third of investment channelled through SPEs in the Netherlands goes to countries with a bilateral investment protection treaty in place.¹⁴

There is significant anecdotal evidence of the occurrence of profit shifting through offshore investment hubs. Google achieved an effective tax rate of 2.4 per cent on its non-United States profits in 2009 by routing profits to Bermuda, with Ireland and the Netherlands playing a key role in the structure. Many examples of multinational corporations that achieved similar results or utilized similar structures have appeared in the media in recent years and will be familiar to the public.

A more systematic, not anecdotal, assessment of BEPS practices at the *firm level* is difficult. MNEs have very limited interest in disclosing tax-relevant information, especially on their cross-border operations. Figure V.13 shows some basic firm-level evidence confirming the special role of offshore hubs in MNE investment structures based on United States

data. Box V.3, at the end of this section, outlines promising directions of future research using firm-level data at the subsidiary level.

MNEs resort to a large number of tax avoidance levers. Table V.1 lists the main ones, categorized according to three enabling factors: tax rate differentials, legislative mismatches or gaps, and double taxation treaties.

The tax avoidance levers listed in table V.1 are rarely used alone. They synergize in complex multilayered schemes in which one or more layers involve an offshore hub as a *facilitator*. According to the OECD (2013a), optimized schemes typically minimize taxes under four different aspects:

- a. *Minimization of taxation in a foreign operating or source country* (which is often a medium- to high-tax jurisdiction) either by shifting gross profits via trading structures or reducing net profit by maximizing deductions at the level of the payer.
- b. *Low or no withholding tax at source.*
- c. *Low or no taxation at the level of the recipient* (which can be achieved through low-tax jurisdictions, preferential regimes or hybrid mismatch arrangements) with entitlement to substantial non-routine profits often built up through intragroup arrangements.
- d. *No taxation of the low-taxed profits at the level of the ultimate parent.*

In practice there may be innumerable combinations of tax avoidance levers to achieve tax minimization. A consolidated approach found in the empirical literature is to focus on two archetypal categories

Table V.1.

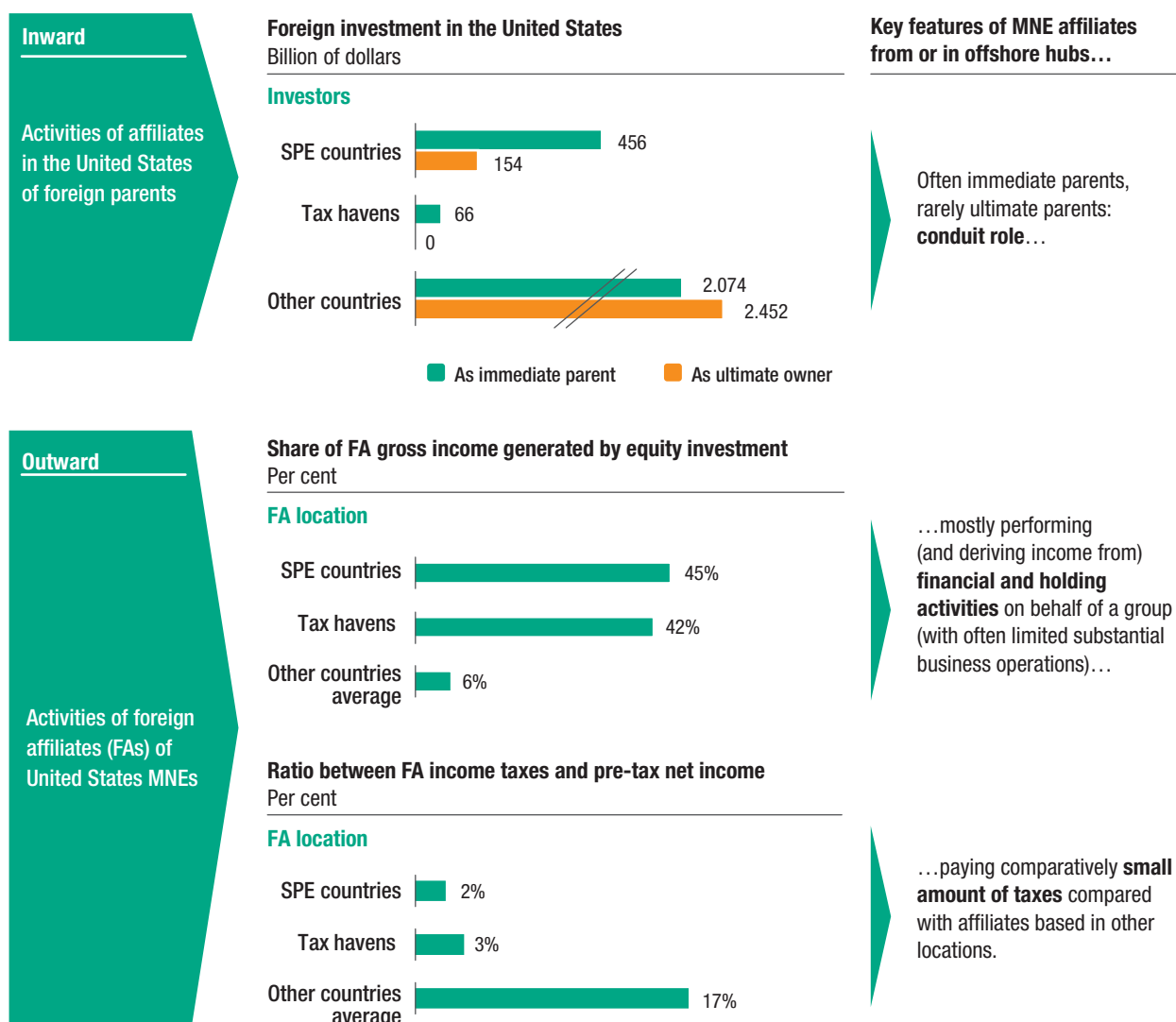
Overview of the main tax avoidance levers

Enabling factor	Specific levers
Tax rate differentials	<ul style="list-style-type: none"> • Transfer pricing manipulation (trade mispricing, use of intangible/IP, commissionaire structures) • Excessive debt financing • Others (e.g. location planning, loss utilization)
Legislative mismatches and/or gaps	<ul style="list-style-type: none"> • Hybrid mismatches • Derivative transactions • Disguised domestic investments • Deferred repatriation
Double taxation treaties	<ul style="list-style-type: none"> • Treaty shopping • Triangular structures • Circumvention of treaty thresholds

Source: UNCTAD.

Figure V.13.

Selected firm-level evidence on the special role played by tax havens and SPEs in MNE investment structures, 2012



Source: United States Bureau of Economic Analysis (BEA); UNCTAD analysis.

Note: Statistics for the group of "SPE countries" are based on Luxembourg and the Netherlands; for the group of "tax havens" on British Virgin Islands.

addressing the most relevant tax avoidance schemes: first, *intangibles-based transfer pricing* schemes and, second, *financing* schemes.¹⁵ Although the precise separating line between the two is not always clear, both conceptually and empirically,¹⁶ it is still valuable to analyse their distinctive features.

(i) Archetype 1: Intangibles-based transfer pricing schemes

The essence of these schemes is to transfer profit to low-tax jurisdictions through transfer pricing

manipulation on intangibles (and associated royalties and licensing fees), generating a divergence between where value is created and where taxes are paid. The higher the intangible component of value creation (IP rights, brands, business services, risks), the higher the profit-shifting opportunities. With the very high share of profits of large MNEs based on what they know rather than what they make, the relevance of this type of scheme is clear, as witnessed also by the continuing trend to introduce so-called IP boxes, where the income on intangibles is taxed at low rates.

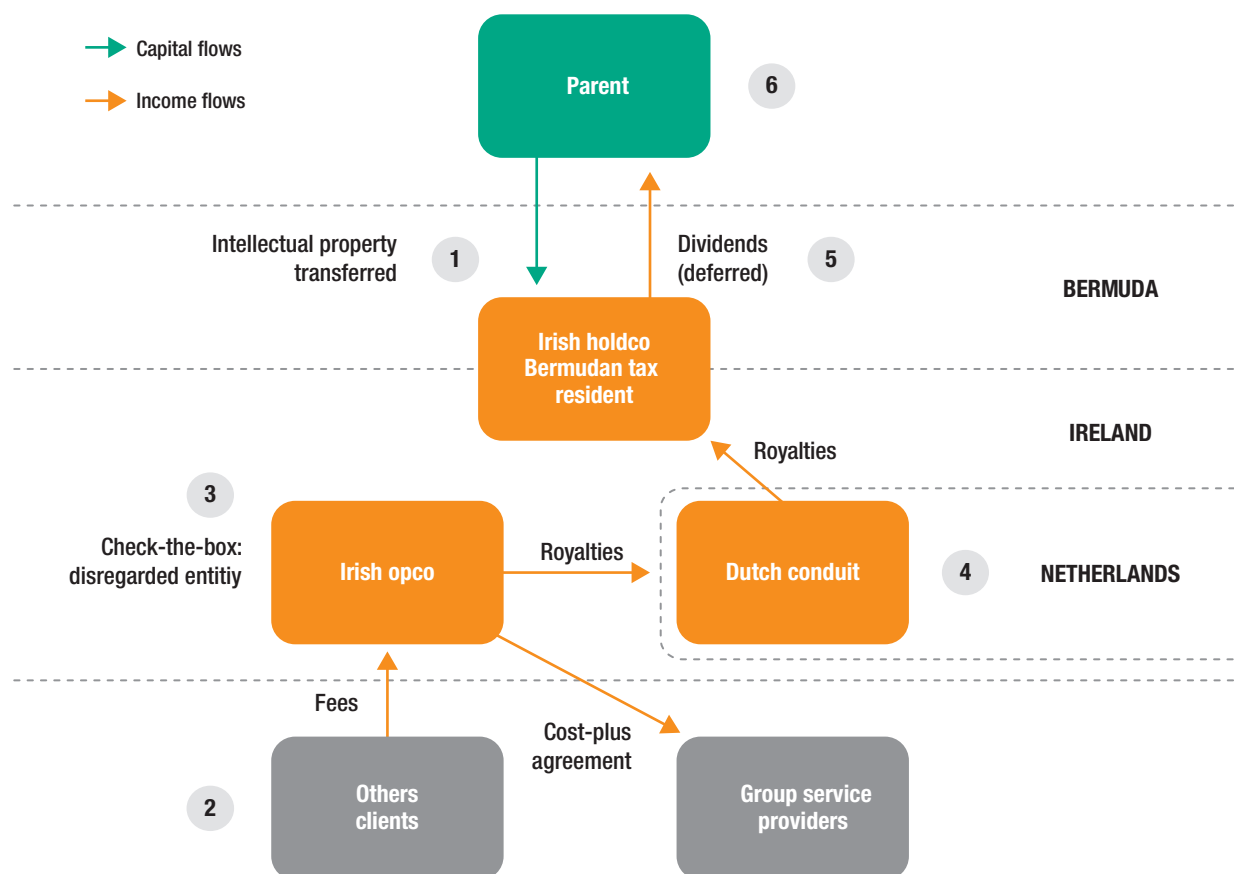
It should be noted that, although intangibles-based schemes are increasingly relevant at the global level, transfer pricing manipulation related to intra-firm trade (trade mispricing) of tangible goods is also common, especially to the detriment of developing economies where basic expertise and instruments to detect transfer pricing abuses are missing.¹⁷ For a broader discussion of issues related to abusive transfer pricing by MNEs and possible policy directions to reform the current arm's-length standards, see Eden (2014).

Typical examples of intangibles-based transfer pricing schemes are in the IT sector where the high-value share of the IP rights (with base erosion opportunities related to high royalty payments) and the digitalization of business operations (with the possibility to separate physical presence from value creation) create a

formidable synergy to minimize taxes. OECD countries where IT firms generate most of their value have been particularly exposed to these types of schemes. The case between the United Kingdom and Google has become exemplary¹⁸ but it is not the only one. Governments around the world, especially in OECD countries, are stepping up scrutiny of tax affairs of the major multinational players in the digital economy. It is not surprising that transfer pricing in the digital economy stands out as a top priority in the OECD/G20 Action Plan.¹⁹ Figure V.14 illustrates the “Double Irish-Dutch Sandwich”, a structure that has become infamous after the Google case.

Although MNEs in the IT sector do not necessarily all use exactly the same technique, the strategies they use follow very similar patterns. The scheme

Figure V.14. Example: Double Irish-Dutch Sandwich



consists of a main tax avoidance lever (transfer pricing manipulation through the use of intangibles) and a number of ancillary tax avoidance levers (including treaty shopping, hybrids, deferred repatriation and commissionaire structures) that in combination achieve the four objectives (a)-(d) listed above, as described in the following example.

a. Minimization of taxation in a foreign operating or source country.

(1) IP is transferred by a United States parent company (high-tax jurisdiction) to an Irish-incorporated subsidiary that is tax resident in a low-tax jurisdiction (Bermuda). The transfer is usually done under a cost-sharing agreement when the IP is not yet fully developed and hence still has a fairly low value. The price can therefore be manipulated. The transfer value is further obscured by the fact that only the non-United States rights attached to the IP are transferred.

(2) The IP is sublicensed by the Irish IP Holding Company to an Irish Operating Company (incorporated and tax resident in Ireland). The Irish Operating Company exploits the IP and usually earns high revenues. Sales-supporting entities in the country of consumption are disguised as low-risk service providers operating under a cost-plus agreement, minimizing the tax base.

(3) The Irish Operating Company pays high tax-deductible royalties for the use of the IP held by the Irish IP Holding Company, offsetting the high revenues from sales and achieving significant erosion of the tax base.

b. Low or no withholding tax at source.

(4) The Irish Operating Company does not pay royalties to the IP Holding Company directly but through an intermediate company in the Netherlands. The intermediate company is an SPE without any substantial activity, interposed between the Irish Operating Company and the Irish IP Holding Company to avoid the payment of the withholding fees (withholding taxes would otherwise apply because the Irish IP Holding Company is a Bermuda tax resident and Ireland levies withholding taxes on royalty payments to Bermuda). Through interposition of the Dutch conduit, withholding taxes are fully circumvented. No withholding tax is levied on the royalty fees

through use of the EU interest and royalties directive, and the Netherlands does not impose withholding tax on royalty payments, irrespective of the residence state of the receiving company.

c. Low or no taxation at the level of the recipient.

(5) The Irish Holding Company, being a Bermuda tax resident, does not pay tax on its income in Ireland, and Bermuda does not levy corporate tax. The income is retained in the Irish Holding Company (i.e. not repatriated to the United States) to avoid United States tax.

d. No taxation of the low-taxed profits at the level of the ultimate parent.

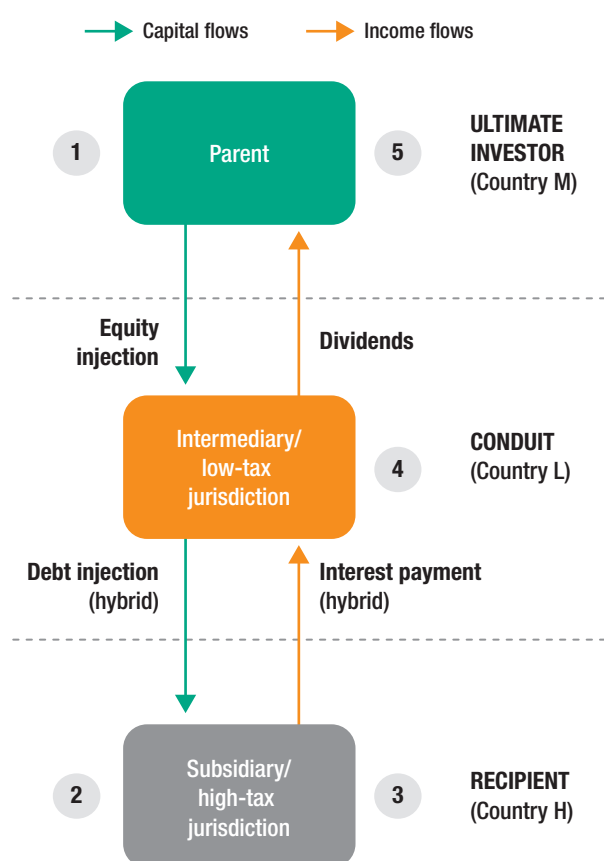
(6) The Irish Operating Company and Dutch conduit are elected in the United States as 'check-the-box' entities (transparent for United States tax purposes) and are hence disregarded by the United States. Thus no United States tax is levied on their income.

(ii) Archetype 2: Financing schemes

The underlying idea of financing schemes is to use loans from an offshore-based entity to maximize the payments of passive interests at the level of the (high-tax jurisdiction) loan recipient. This category can be generalized to include schemes involving all financing operations through offshore intermediate entities in order to reduce the tax bill. In addition to debt financing, other financial operations conveniently manageable through offshore investment hubs may include merger and acquisition operations where the sale of assets is managed through an affiliate in an offshore hub to reduce taxes on capital gains, or leasing operations managed through intermediate entities in offshore hubs to maximize payments at the level of the operating company and thus to erode the tax base. Unlike the transfer pricing schemes described above, these schemes can be employed also in the presence of tangible assets and are particularly suitable for highly capital-intensive industries (such as the extractive industry). Furthermore, while transfer pricing schemes mostly penalize the country of consumption, this type of scheme hits the investment recipient country where operations take place (often developing countries). Although this type of scheme has had less visibility in the media than transfer pricing schemes, they are not less relevant.²⁰ NGOs are also increasingly recognizing the importance of this type of scheme.²¹

Figure V.15.

Example: Debt-financing structure using intermediate holding company and hybrid instrument



Source: UNCTAD based on OECD (2013a).

From an investment perspective, this archetypal scheme is particularly interesting as it is directly visible in FDI data, as illustrated by the debt versus equity analysis in the Offshore Investment Matrix.

Also for this category it is possible to identify some notable examples, as illustrated in figure V.15. As in the case of the Double Irish-Dutch Sandwich, the scheme is founded on a basic concept built around the use of debt financing for base erosion, and combined with further levers, including treaty shopping and hybrids, in order to optimize the tax planning strategy along the four objectives explained above, as described in the following example.

a. Minimization of taxation in a foreign operating or source country.

(1) Parent Company located in Country M (which could be a medium- or high-tax jurisdiction) injects equity funding into its intermediary in Country L, a low-tax jurisdiction.

(2) Intermediary Company injects funding into its subsidiary in Country H, a high-tax jurisdiction. It uses a hybrid instrument to do this; hence the funding is seen as an equity injection by Country L and debt funding by Country H. The funding may be either excessive or unnecessary from an economic perspective and also in relation to the real equity in the subsidiary; however Country H does not have any thin capitalization or similar rules.

(3) Subsidiary Company pays interest to Intermediary Company, which it deducts for its own tax purposes, thereby paying lower taxes in Country H.

b. Low or no withholding tax at source.

(3) The interest is not subject to withholding tax in Country H due to treaty application.

(4) Similarly, no withholding tax is levied on the interest – which is considered a dividend – in Country L due to treaty application.

c. Low or no taxation at the level of the recipient.

(4) The interest is seen as a dividend in Country L, and Country L does not tax dividends.

d. No current taxation of the low-taxed profits at the level of the ultimate parent.

(5) If a dividend is declared to the Parent, no tax is levied on the dividend in Country M due to a dividend exemption. Country M does not have CFC (controlled foreign company) or similar legislation in place.

Table V.2 summarizes the key features of the two types of schemes.

In conclusion, although some of the individual levers employed by MNEs to avoid tax, such as trade mispricing, may not necessarily involve offshore investment hubs, these levers are rarely deployed on their own. The archetypal schemes that are representative of the bulk of tax avoidance practices all make use of investment structures involving entities in offshore hubs.

Table V.2.

Comparison of the two archetypal tax avoidance schemes

	Archetype 1: Intangible based transfer pricing schemes	Archetype 2: Financing schemes
Objective	<ul style="list-style-type: none"> Transfer profit to low tax jurisdictions via transfer pricing manipulation on the intangibles 	<ul style="list-style-type: none"> Erode the taxable base at the level of the financing recipient through deductibles on interest payments
Notable examples	<ul style="list-style-type: none"> Double Irish-Dutch Sandwich 	<ul style="list-style-type: none"> Financing structure using an intermediate holding company and a hybrid instrument
Tax avoidance levers	<ul style="list-style-type: none"> Main: transfer pricing manipulation (use of intangibles/IP) Ancillary: treaty shopping, hybrids, deferred repatriation, commissionaire structures 	<ul style="list-style-type: none"> Main: debt financing Ancillary: treaty shopping, hybrids, deferred repatriation
Business implications	<ul style="list-style-type: none"> Intangible businesses, digital economy Service sector Higher impact on (mostly developed) economies where customers reside 	<ul style="list-style-type: none"> Tangible, capital intensive businesses Primary and secondary sector Higher impact on (mostly developing) economies where investments are made and operations take place

Source: UNCTAD.

Box V.3.

Investigating MNE tax avoidance practices at the firm level: possible research directions

Detailed balance sheet data and profit and loss account data on the affiliates of MNEs may enable further investigation of profit shifting and tax planning strategies. Financial information relevant for the analysis of MNE tax avoidance includes long-term loans, equity balances, revenues, gross profit, operating profit, financing costs, net profit and taxation. Asset values (especially fixed assets) and employee numbers are also important indicators.

Financial data inform a number of metrics that can be used as *tax avoidance signals*:

- Loan and equity balances* can be used to compare debt-equity ratios within peer groups in order to provide an indication of potentially excessive debt funding. The ratio of debt to (non-current) assets can also be used for this purpose. For debt-asset ratios, industry-specific analyses are needed to allow for differences between asset-intensive businesses and others. Financing costs as a percentage of interest-bearing debt can be used as a test on artificial inflation of the interest rate (related to transfer pricing abuses).
- Gross margins and operating margins* (i.e. gross profit and operating profit as a percentage of revenues) could be used to identify potential base erosion, with carefully selected peer group samples to reduce industry variations or factors.
- Tax-specific ratios* include tax as a percentage of revenues, gross profit or operating profit, which may provide insight into excessive deductions that are taking place in a company. Effective tax rates between domestic- and foreign-owned companies can also be compared, e.g. tax (current and deferred tax) over net profit (before tax).

Different approaches are feasible. For a target country, the expectation that foreign-owned companies are more prone than national ones to tax planning techniques can be tested. For a target *group of MNEs* (e.g. the top 100 global MNEs), the comparison could take place across subsidiaries of the same multinational corporate group with the purpose of identifying differences in profit levels, taxation and debt across countries in accordance with tax arbitrage strategies. In all cases, in addition to firm-level financials, complete visibility of the MNE ownership structure is necessary, which can be provided (with limitations on coverage and depth) by databases such as Orbis, maintained by Bureau van Dijk. UNCTAD aims to explore these options further in future work in this area.

Source: UNCTAD; Fuest and Riedel (2010).

C. MNE TAX AVOIDANCE AND DEVELOPING COUNTRIES

The process of formulating the SDGs and the related Financing for Development discussion have raised the political profile and public awareness of the role of taxation as a source of development financing and focused attention on the detrimental impact of tax avoidance schemes on developing economies.

Tax is a major component of the development financing pool. Concord (2013) estimates the total amount of domestic sources of development financing at some 60 per cent of the aggregate GDP of developing economies against 5 per cent for external sources, with taxation at 15 to 30 per cent of GDP, representing a significant share of domestic sources.²² The OECD²³ calculated in 2011 that at the aggregate global level up to half of annual additional resources needed to achieve the (first six) Millennium Development Goals (MDGs) could be recovered just by improving tax revenue collection in developing economies. The situation will be similar for the SDGs.

The concerns of development organizations and NGOs related to BEPS practices in developing countries centre on two issues: (i) developing economies are less equipped than developed economies to counter corporate tax avoidance, so therefore their *exposure* may be greater; and (ii) the *impact* in terms of resource losses for developing economies is significant, especially against the background of the scarcity of available local resources and the development financing gap.

The FDI-based analytical toolkit introduced in this section provides a methodology both to assess the exposure of developing economies to FDI from offshore investment hubs, and to estimate the resulting tax revenue losses. The distinctive feature and to some extent also the limitation of the approach is to focus specifically on the role and the impact of offshore hubs as immediate investors into developing economies. It is important to point out that a direct investment link to an offshore hub is not a prerequisite for profit shifting. However, such links enable some important forms of profit shifting and they are usually part of the tax planning strategy of MNEs. In particular, although transfer pricing-based structures (Archetype 1) may or may not entail direct investment exposure to hubs, financing schemes (Archetype 2) typically leverage

FDI links to create a *direct channel* for profits to easily reach offshore locations.

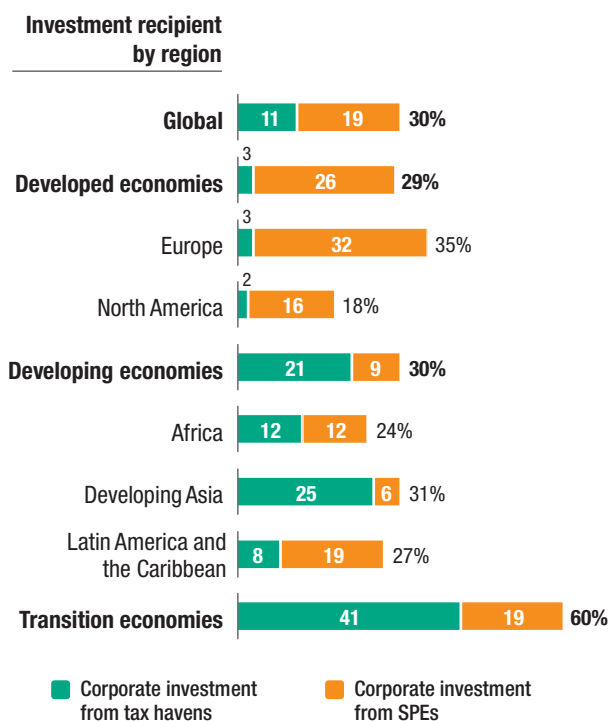
1. Exposure of developing economies to corporate investments from offshore hubs

Tax avoidance practices by MNEs are a global issue relevant to all countries: the exposure to investments from offshore hubs is broadly similar for developing and developed countries. However, profit shifting out of developing countries can have a significant negative impact on their sustainable development prospects. Developing countries are often less equipped to deal with highly complex tax avoidance practices because of resource constraints and/or lack of technical expertise.

The share of inward investment stocks originating from offshore hubs provides an indication of the level of exposure of developing economies to BEPS practices. Figure V.16 on the next page shows the share of investment from offshore hubs (tax havens and SPEs) in total productive investment into non-OFC countries across different regions. The shares for developing and developed regions are substantially aligned, at around 30 per cent of total investment stock.

While the *scale* of the exposure is similar, the relative weight of tax havens and SPEs differs between developed and developing countries, with tax havens much more relevant for developing countries (at two thirds of total offshore hub exposure against only one tenth for developed economies). Regional patterns reflect the fact that specific jurisdictions tend to act as preferential investment hubs for their entire region. For developed economies, in particular for Europe, SPEs in Luxembourg and the Netherlands cover the lion's share. For developing economies the picture is more differentiated. Latin America and the Caribbean also receive a significant share of investment from Dutch SPEs. However, investment in Africa heavily relies on Mauritius, while the British Virgin Islands represent the reference offshore hub for investment in Asia. Finally, the picture for transition economies is skewed by very large investment from Cyprus to the Russian Federation.

Figure V.16. Exposure to investments from offshore investment hubs, by region, 2012
Share of corporate investment stock from offshore hubs (Per cent)

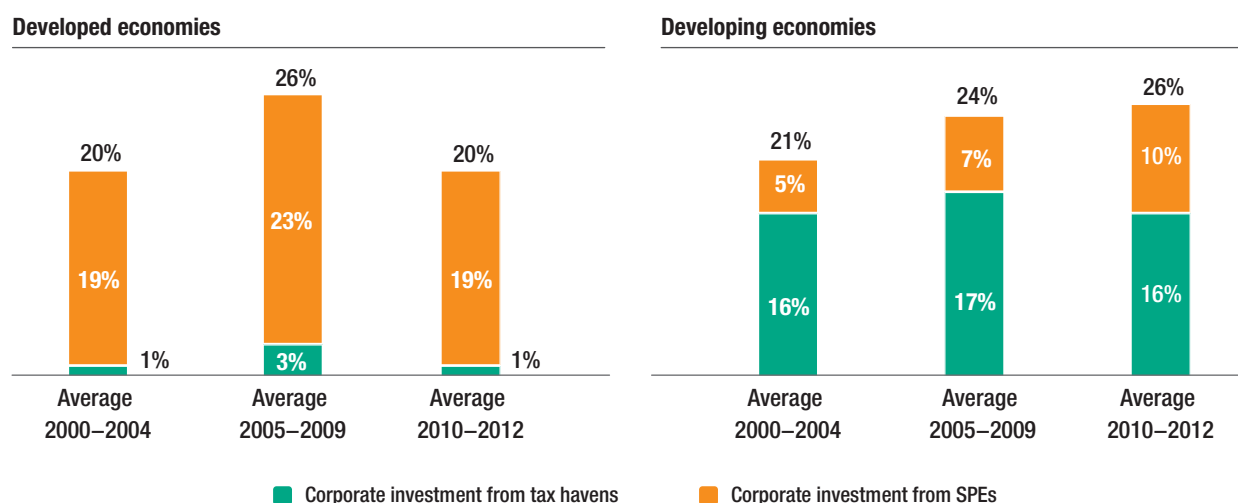


Source: UNCTAD estimates based on IMF Coordinated Direct Investment Survey 2012 and 2011; central banks for SPE investments.
Note: The set of recipient countries includes only non-OFCs. Analysis based on the Offshore Investment Matrix, one-sided perspective. See annex II for further details.

The share of investment in Africa from offshore hubs, at 24 per cent, is lower than in other developing regions. This seems in contrast with other empirical evidence and studies suggesting that Africa faces more severe tax avoidance issues. Africa may face tax avoidance practices that do not require direct investment links to offshore hubs. Also, the average for the continent disguises tax avoidance issues in individual countries – especially the poorest countries, which weigh less in the aggregate picture. Furthermore, the perception of low MNE fiscal contributions in Africa may also be due to high levels of tax competition in individual countries resulting in low effective tax rates, rather than erosion of the tax base.²⁴

While the analysis based on the Offshore Investment Matrix, which is based on stocks, shows a snapshot of the current situation, a look at offshore links in investment flows reveals how exposure to hubs has evolved over time. This perspective highlights a negative trend for developing economies. It shows that their exposure to investments from offshore hubs is on the rise, while that in developed countries has started shrinking in recent years. In particular, although historically developing economies have been more vulnerable to investments from tax havens (as the stock analysis confirms), between 2000 and 2012, the share of inflows from SPEs steadily increased and in fact doubled (figure V.17).

Figure V.17. Evolution of exposure to offshore investment hubs, by level of development
Share of corporate investment flows from offshore hubs, multiyear averages (Per cent)



Source: UNCTAD FDI database; national statistics; UNCTAD estimates.
Note: See figure V.12, also based on flows.

2. Tax revenue losses for developing economies from hub-based tax avoidance schemes

Tax avoidance practices are responsible for a significant leakage of development financing resources. An estimated \$100 billion annual tax revenue loss for developing countries is related to inward investment stocks directly linked to offshore investment hubs. There is a clear relationship between the share of offshore investment in host countries' inward FDI stock and the reported (taxable) rate of return on FDI. The more investment is routed through offshore hubs, the less taxable profits accrue. On average, across developing economies, every 10 percentage points of offshore investment is associated with a 1 percentage point lower rate of return. The average effects disguise country-specific impacts.

The quantification of profit shifting is a challenging exercise. First, tax avoidance options can be numerous. MNEs employ highly sophisticated and creative combinations of individual tax avoidance levers. Second, by the nature of the phenomenon, the available data and information is limited. The profits shifted to offshore locations are difficult to track as they typically do not appear in any official reporting: not, obviously, in the financial reporting of the foreign affiliates where the value is generated and not in that of the foreign affiliates to which it is shifted due to often lax reporting requirements. Given the complexity of the issue, studies aim to quantify specific aspects of corporate profit shifting rather than attempt a holistic approach. The effort is still valuable, as integrating the different approaches provides an order of magnitude of the losses caused by international corporate tax avoidance.

Annex II provides an overview of the main approaches developed for estimating profit shifting and tax revenue losses due to cross-border corporate tax avoidance. The FDI-driven approach used in this section stands at the intersection of some of those approaches.

The methodology proposed builds on the assumption of a negative relationship at the country level between the share of inward investment stock from offshore hubs and the rate of return on the total inward FDI stock. The underlying assumption is that the portion of income generated by FDI from offshore hubs is subject to profit shifting, with the effect of artificially deflating

the average rate of return on foreign investments (computed as the ratio between return on investment and inward investment stock). Thus, all things being equal, the higher the share of inward investment stocks from offshore hubs, the lower the rate of return.

The relationship is supported by country data that confirm a negative and significant linear relationship between the two variables. To capture the full impact of exposure to offshore hubs on investment profitability, and to ensure greater statistical validity of the relationship identified between offshore hub investment links and rates of return on investment, the econometric analysis is based on a greater number of offshore investment hubs than employed in section B. Full details on the different options are described in annex II.

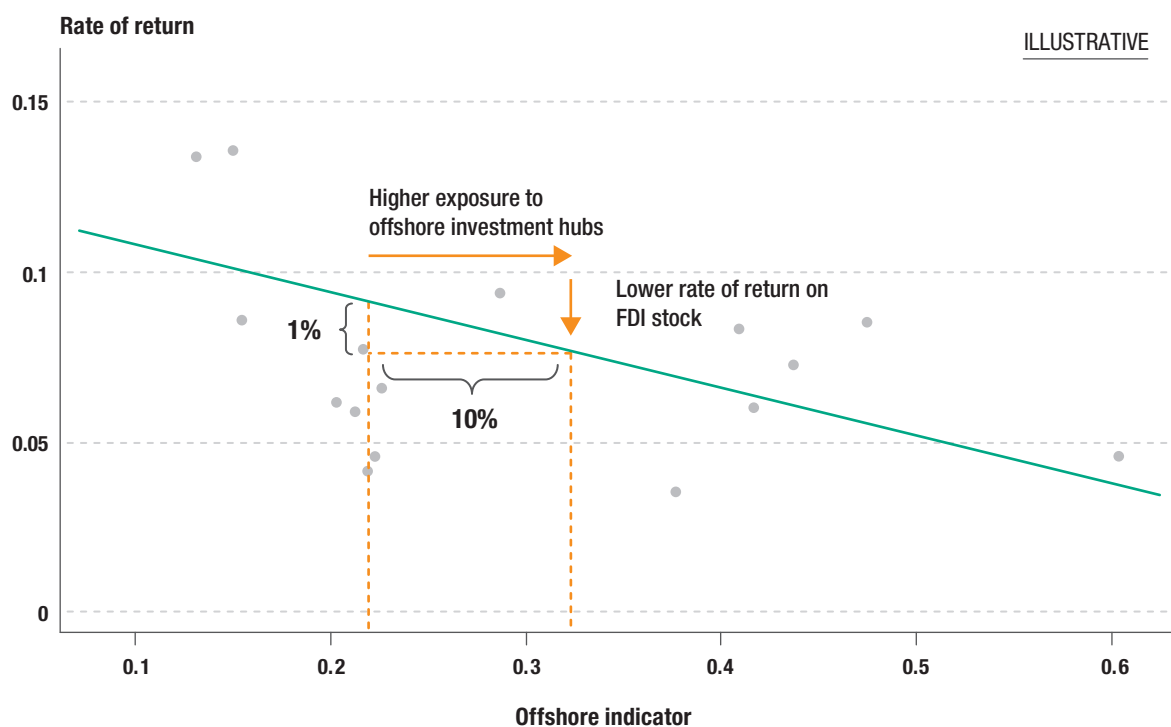
Econometric analysis suggests that on average, across developing economies, an additional 10 per cent share of inward investment stock originating from offshore investment hubs is associated with a decrease in the rate of return of 1 to 1.5 percentage points (figure V.18 illustrates this relationship).

Although it is challenging to irrefutably prove a direct causal relationship between exposure to offshore hubs and reduced profitability of FDI,²⁵ this analysis provides some empirical underpinning to widespread evidence that MNEs leverage direct investment links to offshore investment hubs to enable profit-shifting practices that ultimately result in artificially low FDI income. More importantly, the quantification of the responsiveness of the rate of return to offshore hub exposure allows a *simulation* of the potential impact of these practices on tax revenues.

Once a significant relationship between the exposure to offshore hubs (*Offshore Indicator* in figure V.18) and the rate of return of the FDI income (*Rate of Return* in the figure) has been established, the tax revenue losses can be calculated through appropriate assumptions on the *profitability gap* (how much FDI income is missing due to investments from offshore investment hubs) and on the average corporate tax rate.

UNCTAD's simulation indicates that the amount of corporate profits shifted from developing economies is about \$450 billion – implying, at a weighted average effective tax rate across developing countries at 20 per cent, annual tax revenue losses of some \$90 billion. Annex II shows the parameters of the simulation and the outcomes; it includes a sensitivity analysis employing

Figure V.18. Illustration of the relationship between the share of inward investment from offshore investment hubs and the rate of return on inward investment



Source: UNCTAD analysis based on data from the IMF Balance of Payments database and IMF Coordinated Direct Investment Survey.

Note: Scatterplot representing the relationship between offshore hub exposure (*Offshore Indicator*) and rate of return on investment stock (*Rate of Return*) for developing countries. "Conservative" case with beta coefficient at -10 per cent. The fitted line is merely illustrative and does not reflect the econometric modelling behind the estimation of the beta coefficient (the econometrics rely on a larger sample of data points, including four years, and accounts for regional fixed effects and time fixed effects; see annex II for details).

two formulations of the dependent variable (total rate of return on FDI income versus rate of return on the equity component of the FDI income) and two definitions of tax rates (effective tax rate versus statutory tax rate), with results ranging from \$70 billion to \$120 billion.

Notably, the negative relationship between the exposure to offshore investment hubs and the rate of return on FDI also holds (and remains statistically significant) for developed economies. However, its relative impact on profit shifting and tax revenue losses is proportionally smaller. This is due to a number of reasons, including the lower responsiveness of the rate of return to offshore exposure; in the case of developed economies, an additional 10 per cent share of exposure to offshore investment hubs corresponds to a decrease in the rate of return of 0.5 to 1.0 percentage point.²⁶ As a result, despite the larger size of developed-country economies, the simulation of tax revenue losses resulting from direct offshore

investment links for developed countries yields an estimate similar to that of developing countries, in the order of \$100 billion.

The profit shifting and tax revenue losses estimated here are mostly confined to those associated with tax avoidance schemes that exploit a direct investment relationship through equity or debt. Financing schemes (Archetype 2) are the most obvious example, but other schemes also rely on offshore hubs and financing schemes cannot account for the entirety of the estimated revenue loss.

Trade mispricing does not require a direct investment link: MNEs can shift profits between any two affiliates based in jurisdictions with different tax rates. Especially in the context of the digitalized economy, a significant share of transfer pricing practices exploits schemes similar to Archetype 1 – intangibles-based transfer pricing schemes. Although these schemes also involve

offshore hubs, they do not necessarily appear in host-country FDI inflows; it is enough that the corporate network includes an affiliate based in an offshore location, even if the investment to the particular host country is not channelled through it. (Figure V.19 illustrates two approaches to estimating profit shifting and revenue losses).

Therefore, the results presented here do not necessarily capture the full extent of MNE tax avoidance. They complement findings from other relevant studies focusing on the revenue losses for developing economies generated by corporate trade mispricing schemes, such as Christian Aid (2008) (\$120 billion–\$160 billion). It is important to note that the different types of tax avoidance schemes in practice are often used in combination and generally hard to disentangle. The different methods for the calculation

of revenue losses therefore provide only alternative approaches and arrive at overlapping estimates.

Leaving aside the estimates for overall government revenue losses, the *Offshore Indicator* presented here provides intrinsic value to policymakers as a “signal indicator” for BEPS, and as a rule-of-thumb method for country-level BEPS impact.²⁷

Thus, even based only on the analysis presented here and disregarding potentially significant additional revenue losses from tax avoidance schemes not dependent on direct investment links with offshore hubs, revenue leakage due to tax avoidance practices is substantial. Recovering some or all of these losses could significantly contribute to domestic resource mobilization in developing countries.

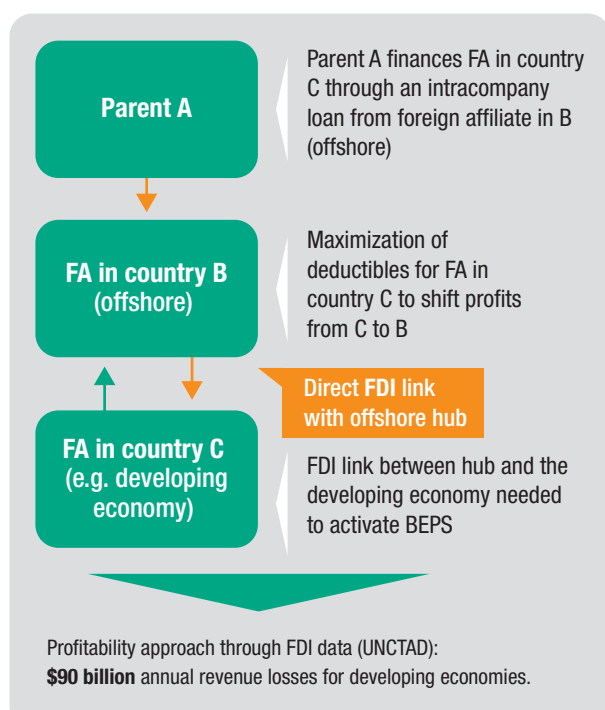
Figure V.19. Two approaches to estimating profit shifting compared

→ Income flow → Investment flow ■ Focus

ILLUSTRATIVE, SIMPLIFIED

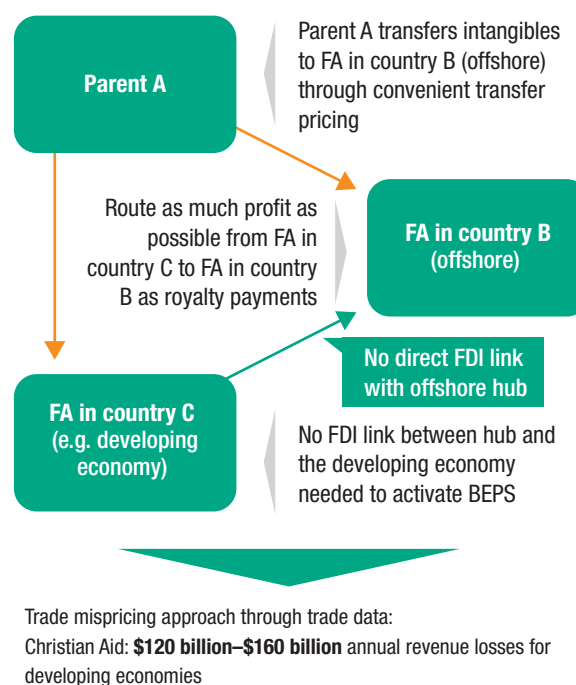
Direct FDI link with offshore hub

Example: Financing scheme (Archetype 2)



No direct FDI link with offshore hub

Example: Transfer pricing scheme (Archetype 1)



In addition, losses caused by MNE tax avoidance practices are not the only form of revenue leakage for governments. As noted in the introduction, an additional form of “slippage” is caused by fiscal incentives actively provided by governments to attract investment. Estimates from external sources – e.g. ActionAid²⁸ – reach as high as \$140 billion, although further empirical investigation, using firm-level data, is needed to better qualify the magnitude of the phenomenon.

The direct investment present in developing countries does contribute to government revenues. Section A

estimated the total contribution of foreign affiliates at some \$730 billion. Between a quarter and one third of that amount relates to corporate income taxes, which is the part mostly affected by BEPS practices. The remainder relates to other revenues, especially royalties on natural resources, and other taxes, especially those on international transactions.

Finally, attracting new investment in productive capacity and infrastructure in developing countries remains important for their sustainable development prospects.

D. TAX AND INVESTMENT POLICYMAKING: A PROPOSAL FOR GREATER COHERENCE

Tax avoidance practices by MNEs lead to loss of revenue for governments in both host and home countries of investors and to basic issues of fairness in the distribution of tax revenues between jurisdictions that must be addressed. In tackling tax avoidance, it is important to take into account the overall contribution to government revenues by MNEs and the existing tax base, as well as new productive investments by MNEs and the future tax base.

The degree to which MNEs engage in tax avoidance varies by industry and home country (among other factors), but tax avoidance practices are widespread. They cause significant tax revenue losses worldwide – in both host and home countries of international investors. Not only do they cause economic and financial damage to countries, they also raise a basic issue of *fairness*. In almost all cases, the shift in profits through the use of offshore investment hubs does not reflect actual business operations (i.e. the profits reported and taxes paid in a jurisdiction are disproportionate to the activities that take place there). The shifting of profits between jurisdictions results in an unfair distribution of tax revenues between jurisdictions.

The practice is especially unfair to developing countries that face certain tax related challenges.

- *Limited tax collection capabilities.* Accurately identifying tax planning practices requires an analysis of global operations for individual MNEs,

an unrealistic task for most countries, and especially developing ones. There is a clear case for technical assistance to developing-country tax authorities.

- *Greater reliance on tax revenues from corporate investors.* Developing economies tend to rely relatively more on tax revenues from a smaller number of large corporations. In India, 41 of the largest companies contribute just over 16 per cent of all corporate tax receipts and almost 5 per cent of the government’s total tax receipts. In South Africa, close to 24 per cent of all corporate tax receipts, approximately 6 per cent of total government tax receipts, is contributed by 35 of the biggest companies.²⁹
- *Growing exposure to harmful tax practices and tax avoidance by MNEs.* Developing countries have seen the share of investment stock originating from offshore locations increase in the last decade. The share of their investments from tax havens was already higher than in developed countries, and the share originating from SPEs is rapidly catching up.

Furthermore, at the business level, the low taxes paid and higher net after-tax profits can provide MNEs with an unfair advantage compared with domestic firms. This directly impacts market competition and suppresses the survival and growth of the small and medium-sized businesses that are vital for development. (In fact, the

BEPS project is not driven by revenue considerations alone, but also by the need to reduce distortions between MNEs and domestic companies, and between those MNEs prepared to engage in aggressive tax planning and those that are not – levelling the playing field.)

At the same time, it is fair to note that tax avoidance (as opposed to tax evasion) is not *per se* illegal – although often there is no “bright line”.³⁰ A full perspective on corporate behaviour warrants these observations:

- Corporate representatives have in the past often used their obligation towards shareholders to manage finances efficiently as a shield. More recently, many MNEs are increasingly acknowledging a wider set of obligations and corporate social responsibilities (CSR) and, more importantly, recognizing reputational risks, leading them to engage in more open dialogue with tax authorities.³¹ They are also recognizing that aggressive tax planning can lead to greater fluctuation of effective tax rates, and that it increases the risk of challenges by tax authorities, with associated financial liabilities.
- There is an intense ongoing debate, at the level of basic taxation principles, on the fairness of some taxes, especially withholding taxes, which are normally levied on gross fees or royalties and which can have effects equivalent to double taxation, thus inducing MNEs to engage in some avoidance practices.
- The BEPS debate focuses largely on corporate income tax (and a few other taxes) yet MNEs pay many other taxes, including taxes on labour, assets, use of resources, indirect taxes, levies and duties. As demonstrated in the first section of this chapter, in developing countries the direct and induced fiscal contributions of MNEs constitute a relatively high share of total government revenues.

These observations do not diminish the clear imperative to tackle tax avoidance practices and to ensure that MNEs “pay the right amount of tax, at the right time, and in the right place”. But they provide a broader context for the actions required to do so, taking into consideration the full contribution that MNEs make to economic growth and development, as well as to government revenues, and taking into account the need for countries worldwide, and especially

developing economies, to attract new investment, especially in productive capacities and infrastructure.³²

1. The tax-investment policy link and the need for a synergistic approach

While taking action against tax avoidance is imperative and urgent, including to meet the financing needs of the post-2015 agenda, the risk of negative effects on investment flows, especially to developing countries, must also be considered carefully. Insufficiently calibrated measures may deter necessary investment for development that might otherwise have taken place. Offshore investment hubs have come to play a systemic role in international investment flows: they are part of the global FDI financing infrastructure. Measures at the international level that might affect the investment facilitation role of these hubs, or that might affect key investment facilitation levers (such as tax treaties), need to take into account the potential impact on global investment and incorporate an investment policy perspective.

The investment data and the results of the analyses in this chapter show the massive and still growing use of offshore investment hubs by MNEs. As a result of growing international scrutiny, a number of hubs, and especially SPE jurisdictions, are becoming more aware of their role in international investment schemes and the potential negative effects on other jurisdictions, and are taking steps to address the situation. There is increasing cooperation, transparency and exchange of information. SPE jurisdictions are also gradually tightening requirements related to substance, or including stronger anti-abuse and denial of benefits clauses in their tax treaties. The Netherlands, for example, has offered its treaty partners the option to renegotiate existing treaties in order to include anti-abuse measures. Ireland is proposing amendments to tax residence rules to prevent “stateless” entities.

Moreover, while some cases can be described as harmful tax competition and “beggar-thy-neighbour” policies, underlining the need for concerted action, the role of offshore hubs in global investment cannot be explained and addressed only in terms of the characteristics and “responsibilities” of individual hub jurisdictions. The scale of the phenomenon clearly indicates that it is a *systemic issue*; i.e. offshore investment hubs play a systemic role in the current international investment environment. They

have become, in the current environment, standard and widely adopted tools for MNE tax and financial optimization, used by all competitors on a level playing field for MNEs, if not for domestic firms. Their systemic nature is clear when considering the fact that they are even used at times by development finance institutions – although, for example, the World Bank and the EBRD have developed a set of internal guidelines to ensure they are used responsibly.

Responsibility for the widespread use (and abuse) of hub-based corporate structures and tax avoidance schemes by MNEs should be widely shared. Home countries of investors often do not have effective legislation in place to prevent the use of hub-based structures or even unintentionally encourage the use of such structures by their MNEs. The “tick-the-box” practice applied in United States CFC (controlled foreign company) legislation is often pointed out as facilitating the use of umbrella entities based in favourable locations. Host countries are often complicit as well, as their focus is on attracting investment, if necessary at the cost of engaging in harmful tax competition.³³ A degree of tolerance for tax avoidance schemes by MNEs may have been considered by some countries as a way to reduce the visible component of such tax competition.

The acknowledgement of the systemic nature of the issue carries two important consequences with critical implications for policymaking. First, the past “*naming and shaming*” approach targeting offshore investment hubs may have been too restrictive, as it left untouched many of the largest hub jurisdictions. Second, any measures aimed at limiting the role of offshore hubs in order to counter tax avoidance and profit shifting should consider the potential impact on global investment.

Policy action aimed at reducing the use of offshore locations as investment hubs by MNEs must start from the basic questions of what makes offshore hubs attractive and what drives their outsized role in global investment. Offshore hubs, in particular SPE jurisdictions, are attractive as conduits for investment because they often provide large networks of tax treaties and investment protection treaties. In their domestic legislation they provide low (or sometimes negotiated) tax rates; their company law allows for the set-up of legal entities that are useful in international investment structures and tax schemes; and they offer a favourable business climate and other locational

advantages. Many of these features are not exclusive to these jurisdictions. They are already offered by an increasing number of other countries, motivated often by a level of tax competition. Any policy action addressing offshore hubs must therefore be of a *systemic nature*, not aimed at individual jurisdictions or a small group of countries, because corporate structures will adapt to new realities and find alternative conduits, and investment flows will take new routes to continue exploiting regulatory arbitrage opportunities.

Some of the uses of offshore investment hubs and offshore vehicles by international investors are not motivated primarily by tax considerations. For example, in mergers or joint ventures between partners from different countries with different legal and tax systems, offshore hubs may provide an attractive neutral location for the entity. They can also help firms from countries with weak institutions set up international businesses more easily and gain access to international capital markets and legal systems (a key driver of the phenomenon of round-tripping FDI).³⁴ Lower transaction costs and economies of scale also likely play a role: once a vehicle has been set up to manage an MNE’s overseas holdings, whether actively or purely administratively, it is easier to route any new investments or reinvestments through the same vehicle.

Whether for tax avoidance or other purposes, it is the reality today that offshore investment hubs are playing a facilitating role in international investment. Diminishing that role is likely to have two types of effects on global investment flows:

- (i) Investments will take a *different route* from their origin or home country to their destination or host country. Existing investments will be re-routed, leading to a likely amplified initial impact of any policy action. Assuming effective policy action, investments should take a more direct route, leading to clearer investment links between host countries and countries of the ultimate beneficial owners of the investment.
- (ii) *Overall international investment levels may be reduced.* Higher transaction costs could make some investments less attractive, and higher taxes on international operations could cause the after-tax returns of some investments to drop below investor hurdle rates (the rate of return below which they will not invest).

Higher transaction costs and higher taxes on international operations could diminish overall investment levels at a time when such investment is sorely needed for economic growth and development.

On the one hand, where investments are desirable for development or other public policy purposes but unattractive for international investors, it could be argued that artificially increasing investor returns through tolerance of tax avoidance is the wrong tool and would lead to an incorrect distribution of the costs of public policy objectives. Direct support to such investments, or public-private partnerships to share risks and change the risk-return picture, would be more appropriate.

On the other hand, policymakers engaged in international discussions on BEPS would do well to assess not only the impact on the level and distribution of fiscal revenues of any proposed intervention, but also the impact on investment. The Offshore Investment Matrix is a helpful tool to start such an assessment, as it provides insights into the share of investments from and to countries affected by offshore hubs, and indications on the relative importance of archetypal schemes.

2. Towards guidelines for Coherent International Tax and Investment Policies

Coherent international tax and investment policies should protect the government revenue base and promote investment. A set of guidelines may help realize the synergies between investment policy and initiatives to counter tax avoidance. Key objectives of the guidelines proposed for discussion in this section include: removing aggressive tax planning opportunities as investment promotion levers; considering the potential impact on investment of anti-avoidance measures; taking a partnership approach in recognition of shared responsibilities between investor host, home and conduit countries; managing the interaction between international investment and tax agreements; and strengthening the role of both investment and fiscal revenues in sustainable development as well as the capabilities of developing countries to address tax avoidance issues.

Recognizing the growing significance of tax avoidance by MNEs, the international community – policymakers in the G20 and beyond, international organizations such as the OECD, the World Bank, the IMF and the United Nations, NGOs and business itself – is engaged in debate and working on concrete initiatives

to counter the phenomenon. The focus of attention is largely on tax policy, accounting rules and company law, and on initiatives to improve information exchange and to increase pressure on tax havens. However, given the fundamental role of investment in building the corporate structures that enable tax avoidance, investment policy should form an integral part of any solution. Conversely, any policy initiative tackling tax avoidance by international investors is likely to affect national and international investment policies.

In considering the interdependence and potential synergies between investment policy and anti-tax-avoidance initiatives, policymakers at both the national and international levels may be helped by a set of guidelines for synergistic international tax and investment policies. These guidelines may be considered design criteria for any action by the UN and/or G20, and common-sense suggestions for national investment policymakers and tax authorities.

The policy guidance for coherent international tax and investment policies proposed below is based on the following three *fundamental principles*.

- *Promoting sustainable development.* A core objective of both international tax and investment policies is financing sustainable development. Investment policies promote private investment, and tax policies enable public investment in sustainable development.
- *Tackling tax avoidance.* MNEs should pay tax where economic activity takes place and value is created. Undue distortions should be minimized to ensure a fair distribution of revenues across countries and a level playing field for domestic and foreign firms.
- *Facilitating productive investment.* The international tax framework should protect the tax base and ensure fair sharing of the tax base among jurisdictions, and promote future investment for development.

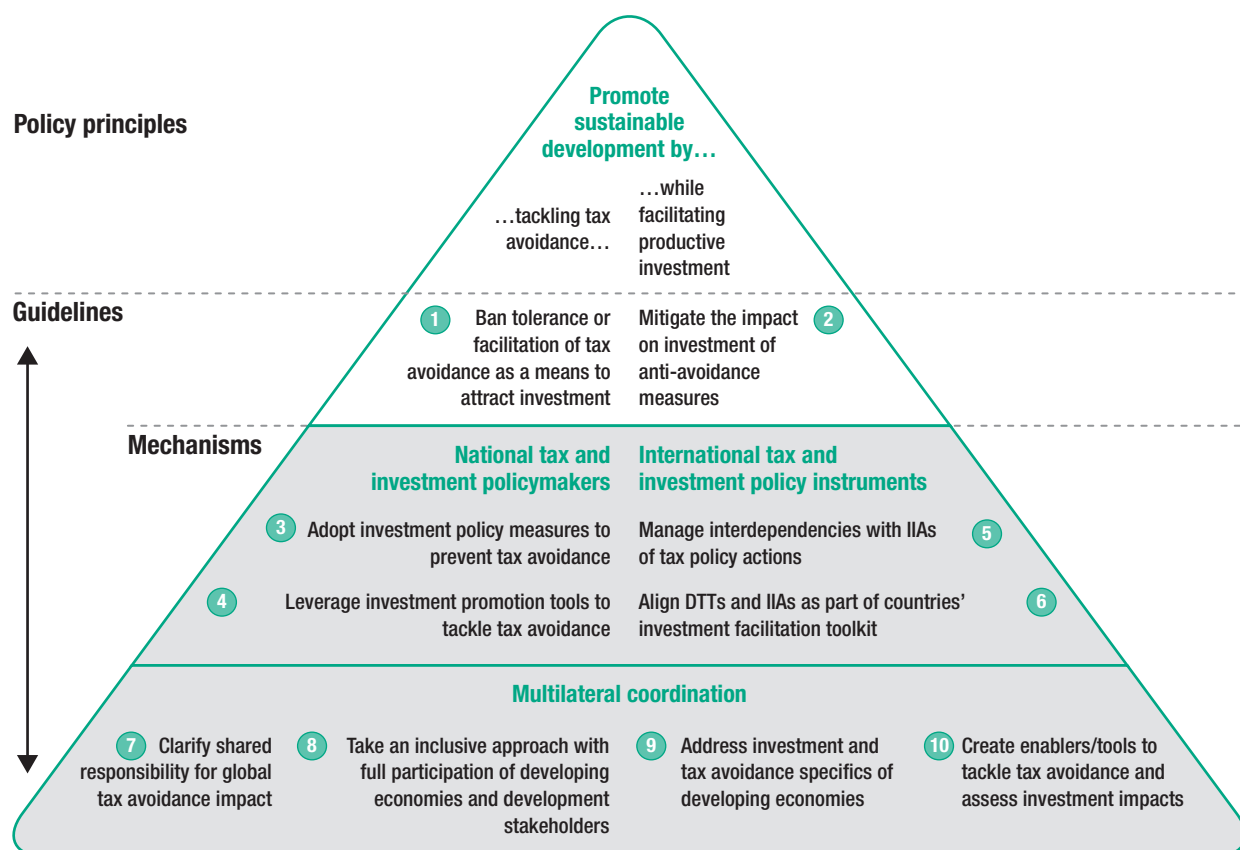
In addition, the guidelines are structured around the following key mechanisms for action:

- Action through national tax and investment policymakers.
- Action through international tax and investment policy architectures and instruments.
- Action through multilateral coordination.

Figure V.20 illustrates the concept, and the guidelines are further elaborated in the subsequent numbered text.

Figure V.20.

Guidelines for Coherent International Tax and Investment Policies



Source: UNCTAD.

Possible guidelines for Coherent International Tax and Investment Policies

1. Tolerance or facilitation of tax avoidance should not be considered an instrument either to attract inward investment or to support the competitiveness of multinational enterprises (MNEs) abroad.

Where countries wish to provide fiscal advantages to attract investors or to support investment overseas, such advantages should be extended through appropriately designed and administered incentives schemes – which should be sector specific, time-bound, transparent and conditional (e.g. on sustainable development contributions), within the boundaries of existing international commitments. See also box V.4 (on the next page) on the role of incentives.

Similarly, where countries feel compelled to attract specific investments to pursue public policy objectives,

increasing investor returns through tolerance or facilitation of tax avoidance will tend to lead to an incorrect distribution of costs; if any support is required (which must be carefully evaluated), direct support to such investments or risk-sharing arrangements would be more appropriate.

2. Measures to address tax avoidance by MNEs should carefully assess the potential impact on investment for development.

Policymakers engaged in international discussions on base erosion and profit shifting (BEPS) should assess – and scenario-test – not only the impact on the level and distribution of fiscal revenues of any proposed intervention, but also the impact on investment, especially to developing countries.

Box V.4.**Is there still a role for fiscal incentives?**

The importance of tax in location decisions (see box V.1) implies that fiscal incentives are an important tool to attract investment. In fact, those developing countries that have been most successful in industrial development over the past decades have made use of various forms of incentives schemes to attract the foreign investment they needed to kick-start economic activities and to bring in the necessary technology and know-how. The success of export-processing and special economic zones in those countries – forms of incentives scheme – is proof of their effectiveness.

Despite the evidence, policy advisors in international organizations have long warned against the dangers and downsides associated with incentives. Ongoing work by the IMF, OECD and WTO on incentives for the G20 adds to the negative policy advice on incentives. The World Bank's research and advisory work has long focused on the cost of incentives and on the redundancy of many schemes for attracting investment – with good reasons: many schemes have indeed been found to be inefficient and ineffective.

However, almost all the arguments against the use of incentives are based on the way incentives are granted or administered, not on incentives per se. Thus, investment authorities worldwide have continued to include incentives in their investment promotion toolbox, fully aware of the important role tax plays in investment decisions, and unwilling to renounce one of the few available tools that can help overcome specific locational disadvantages, or that can help steer investment to priority areas for growth and development.

UNCTAD's advice on incentives, in its Investment Policy Framework and in its technical assistance work (Investment Policy Reviews) is (i) to ensure that incentives schemes are based on an overall sustainable development strategy and investment priorities, and (ii) to administer incentives in such a way as to minimize and mitigate the risks of inefficiency and ineffectiveness, as well as the risk of administrative improprieties.

Key to maximizing the *strategic value of incentives* is focusing schemes on priority activities for development and on underdeveloped regions, and associating them with sustainable development impacts. These may include economic impacts, such as employment generation, training and capacity building, and technology and know-how transfer; social impacts, such as better availability and accessibility of services, the advancement of disadvantaged groups in society, or food security; and environmental impacts, such as the reduction of emissions or the generation of renewable energy.

It is important to tailor schemes to the needs of specific economic activities and associated risk-return profiles. For example, R&D-intensive activities display different profiles of capital investment and payback over time than labour-intensive activities; fiscal incentives schemes must be tailored accordingly. The same holds when schemes are reoriented towards sectors that are central to sustainable development, such as agriculture, education, health and infrastructure.

Key to ensuring the *efficiency and effectiveness of incentives schemes* is establishing clearly defined and transparent criteria and conditions, granting incentives as much as possible automatically on the basis of those criteria and conditions, and administering the process through competent authorities, preferably independent from investment promotion authorities, with the ultimate say for the ministry of finance.

Such a move away from location-based incentives schemes aimed purely at increasing the competitiveness of a location to schemes aimed at advancing sustainable development, and adherence to common-sense good practices for the administration of incentives schemes go a long way towards ensuring consistency with WTO rules on subsidies. The WTO rules on subsidies and countervailing measures, and the gradual expiry of exceptions, have somewhat blunted the incentive tool for developing countries, making it less suitable as an instrument of industrial development (at least for export-oriented industrial development). But as an instrument for the promotion of sustainable development, and for the attraction of investment in the Sustainable Development Goals, their relevance will increase (see *WIR14*).

Source: UNCTAD.

Policy measures to tackle international tax avoidance must inevitably address the role played by offshore financial centres (OFCs). They have to mitigate the harmful tax avoidance effects of global investment hubs, but be mindful of the investment facilitation role of hubs to avoid disruptions of investment flows, especially to developing countries. Where measures might diminish the facilitation role of hubs,

policymakers might consider alternative investment facilitation measures.

A formally agreed list of acceptable uses of offshore investment hubs – e.g. as neutral ground for cross-border mergers or joint ventures – could be a starting point for international action on hubs (see also *WIR13*); policymakers should consider objectively whether tax benefits are an essential ingredient for such acceptable

applications, considering their negative side-effects and potential to escalate into harmful tax competition. In considering these measures, the international community should also take into account the potential economic impact of tax avoidance countermeasures on some developing OFCs that have adopted development strategies based on financial services.

3. National investment policymakers should consider options at the entry and establishment levels to prevent tax avoidance.

Where entry and establishment of investors is subject to approval, investment authorities could require information from prospective investors that would attest to the responsible fiscal behaviour of investors and facilitate tax collection on future revenue streams, such as disclosure of financial information and planning, and country-by-country reporting, while respecting confidential business information.

Investment authorities may even apply (within the constraints posed by international commitments and standards) stricter tax compliance or transparency conditions and rules for entry and establishment. This could be feasible in particular in a number of specific situations, e.g. privatization of state assets, concession in extractive industries, or investments related to government procurement.

Promoting adherence to corporate social responsibility (CSR) and governance standards may also be an effective tool to foster good taxpayer behaviour and transparent reporting on fiscal contributions.

4. Investment promotion and facilitation options and constructive relationship management with investors can be leveraged to reduce the motivation and opportunity for tax avoidance.

Foreign direct investment (FDI) incentives schemes should be designed and structured in such a way that they do not provide additional avenues for tax avoidance. They should not create an additional low-tax location in MNE corporate structures. If fiscal incentives are provided, they should be specific and time-bound, and ideally geared towards promoting investment in sustainable development.

Conversely, it may be possible to design and administer some fiscal incentives schemes in such a way that they remove the motivation to shift profits. For example, where tax breaks are given they could be provided for earnings

reinvested in productive assets; tax incentives could focus on capital goods (e.g. rollover relief). Incentives could also be made conditional upon pre-defined or agreed tax behaviour and on disclosure criteria.

Tax incentives and award processes, if applied, should be made more transparent, integrated into the normal budgetary process, and subject to greater accountability. Investment authorities should coordinate with tax authorities, promote good taxpayer service and foster constructive and transparent dialogue between tax authorities and taxpayers.

5. Any national or international action to tackle tax avoidance should consider interdependencies with international investment agreements (IIAs).

The interaction between international tax policy and IIAs is evident from the fact that the value proposition of the major global investment hubs that are at the heart of many tax avoidance schemes relies not only on their domestic company law and tax rules and on extensive networks of double taxation treaties (DTTs), but also on equally extensive – and often matching – networks of investment protection treaties (IIAs).

There is interaction between international tax policies (and DTTs) on the one hand and IIAs on the other. For example, the dispute settlement mechanism of bilateral investment protection treaties (BITs) has been used for tax disputes. More than 40 ISDS cases to date have involved tax-related issues.

As tax avoidance countermeasures can be interpreted as a change for the worse for investors, reducing the value of the investment, or be applied selectively on foreign investors, IIAs may pose limits on countries' right to regulate. Therefore, in negotiating IIAs, policymakers may wish to safeguard policy space on tax issues and possibly strengthen denial of benefits provisions. Beyond avoiding conflicting effects between international tax policies and IIAs, policymakers could consider how the two could mutually reinforce each other (see Epilogue).

6. IIAs and double taxation treaties (DTTs) are both part of countries' investment facilitation toolkit; these instruments should be aligned.

At the strategic level, just as countries need to consider whether and how to engage in IIAs, they need to apply the same considerations to DTTs and

to specific provisions in DTTs. At the substantive level, IIAs and DTTs have not evolved on the basis of consistent design criteria (see box V.5). For example, it is conceivable that investors may avoid permanent establishment status as defined in DTTs but are covered under IIAs due to their generally broader definition of investment.

Policy action on DTTs to harmonize and/or consolidate the treaty regime needs to consider impacts on and from the international investment policy regime, avoid conflict between the two and make them mutually reinforcing as and where appropriate. Given the importance of regional investment flows (and the competition for investment that often occurs at regional levels), regional cooperation approaches covering tax avoidance may also be fruitful.

IIAs aim to address weaknesses in countries' regulatory and institutional environment for investment. For DTTs this is not an explicit objective (also because DTTs are equally relevant between developed economies). However, in developing countries the effect of DTTs is often to necessitate increased collection capabilities on the part of tax authorities, if only because DTTs put limits on withholding taxes, an effective collection mechanism for countries with weak collection capabilities. Therefore, both IIAs and DTTs – and efforts to reform the two systems at the international level – could be accompanied by development assistance to reduce those weaknesses (e.g. technical assistance to investment and tax authorities).

7. Policymakers should recognize the role in cross-border corporate tax avoidance played by different types of offshore investment hubs as well as by home and host countries; clarify shared responsibility; and take comprehensive action.

National and international action on offshore investment links should address both tax havens and special purpose entities (SPEs) in other countries through which significant international investments are routed. Comprehensive action is needed, as partial solutions will lead only to re-routing and alternative solutions for investors.

Cross-border corporate tax avoidance and the routing of investment through offshore hubs are systemic issues, part of the global FDI financing infrastructure. The phenomenon is not driven solely by tax rules in offshore hubs, but enabled by tax rules in home and

host countries. Policymakers in non-OFC jurisdictions should address features in their own tax rules that support or incentivize the use of offshore hubs by their own MNEs abroad or by foreign investors.

8. Tax avoidance and the lack of transparency in international financial transactions are global issues that require a multilateral approach, with adequate developing-country participation.

Effective action against tax avoidance requires international cooperation; a commitment to strengthen the United Nations committee of experts on taxation is instrumental to a full participatory approach.

International cooperation is fundamental to prevent harmful tax competition; competition to attract investment should not lead to a race to the bottom.

International cooperation is also important for the success of transparency initiatives, such as the Extractive Industries Transparency Initiative (EITI). Such initiatives should ideally not focus only on governments, but also on companies. International cooperation can help improve monitoring, auditing and accountability, and it can support institutional development and capacity-building.³⁵

Effective exchange of information between tax authorities is a fundamental part of international cooperation. It is crucial to efforts to counter tax avoidance, and to counter illicit financial transactions (information exchange should include law enforcement agencies). The effect on good governance would indirectly benefit the investment climate.

Given the growing importance of tax avoidance in developing countries, the proportionately greater impact of tax avoidance on their budgets, and their greater needs to attract international investment for development, they should be adequately represented in discussions on international action on tax avoidance – particularly the low-income countries.

9. Policymakers should consider the importance of both international investment and tax revenues for sustainable development financing, and the specific features of tax avoidance in developing countries.

Given the lower tax collection capabilities of developing countries, rulemaking at the international level should take into account transition or other special and differential treatment options, as well as technical

assistance to deal with greater complexity that may result from new anti-avoidance measures. Some tax avoidance schemes are comparatively more relevant for developing countries; some countermeasures are more difficult to implement in developing countries; and the role of incentives is often greater in developing countries, with implications for the effectiveness of some countermeasures: one size does not fit all.

DTTs often have the effect of reducing or removing an effective means to collect taxes (withholding taxes) in developing countries that may have limited alternative tax collection capabilities; international measures related to DTTs should not hurt developing countries.

10. Investment and ownership information is key to analysing tax avoidance schemes and should be prioritized, together with other tools to enable anti-avoidance measures and to foster good tax behaviour.

Measurement of BEPS is critical to designing and implementing effective anti-avoidance measures. FDI data can be an effective signalling indicator for BEPS.

Collection of FDI data at the macro level (balance of payments, at country level) should be further improved (extended) to show transit FDI through offshore hubs and matching FDI income streams.

At the micro level, transparency and disclosure of investment and ownership information is indispensable. Ultimately, full transparency can only be achieved if governments (tax authorities, financial intelligence units and other regulatory agencies) can get behind the corporate veil and behind trusts to identify ultimate beneficial owners. This would complement the move towards country-by-country reporting, which enables tax authorities to have a more global view of the operations of MNEs.

Sharing of country-by-country reporting information should effectively facilitate host-country tax collection and take into account lower collection capabilities in some developing economies. CSR and integrated reporting requirements for firms could also play a supporting role, by strengthening documentation of fiscal behaviour.

Box V.5.

IIAs and DTTs

International investment agreements (IIAs) for the protection and promotion of investment, and treaties governing the fiscal treatment of investment operations between home and host countries (DTTs) are both part of the international policy environment for investors. Together they address the risk-return profile of cross-border investments, with IIAs providing an “insurance policy” to mitigate investor risk, and DTTs protecting investor returns from fiscal erosion. They are two sides of the same coin.

The systems of IIAs and DTTs naturally developed together. As FDI became an increasingly important phenomenon in the globalizing economy, investment partner countries concluded mostly bilateral investment protection treaties (BITs) and DTTs in parallel. Both types of treaties were often negotiated between the same partner countries, simultaneously or in short succession. Where countries have both a BIT and a DTT, in around a quarter of cases the treaties entered into force in the same year; about one third within a two-year period. As a result, in countries with significant outward investment stocks and large treaty networks, and especially in investment hubs, BIT and DTT network coverage often matches.

Conversely, the piecemeal growth of both systems – BIT by BIT, DTT by DTT – has also resulted in gaps in coverage and inconsistencies in treaty substance. This is compounded by the fact that the competency for negotiating BITs and DTTs generally lies with different ministries; for BITs it tends to be national investment agencies (such as Boards of Investment) or Ministries of Trade and Industry or Foreign Affairs who lead the process, whereas with DTTs Ministries of Finance take the lead, with some expertise supplied by tax administrations.

As to *coverage*, DTTs at first glance appear to be more efficient. Although the number of DTTs and BITs is roughly similar (around 3,000 DTTs are currently in force and around 2,300 BITs), DTTs cover 90 per cent of global FDI stock while BITs cover less than 15 per cent. In part this is due to the fact that the fiscal treatment of cross-border investment is equally relevant in developed countries, while the original purpose of BITs was to provide investment protection mostly in developing countries. Looking only at developing-country FDI stock, BIT coverage increases to 30 per cent, with higher shares among the LDCs. The higher apparent coverage of DTTs also reflects the fact that investment protection and promotion issues are dealt with in a host of other agreements.

As to *substance*, inconsistencies include differences in covered investments, with the concept of permanent establishment in DTTs substantially differing from the definition of “investment” in BITs; differences in dispute settlement mechanisms, with the mutual agreement procedure in DTTs considered weaker from an investor perspective than the investor-State dispute settlement system in IIAs; and varying approaches to managing the interaction between IIAs and DTTs, with only 10 per cent of BITs excluding tax issues from their scope (although 80 per cent exclude tax issues from most-favoured-nation treatment).

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Box V.5.

IIAs and DTTs (concluded)

Both the IIA and the DTT regimes are an important part of the investment promotion and facilitation toolkit of the global economy as a whole and of individual countries. Global investment hubs tend to have relatively large treaty networks of both types, with the treaty coverage of their outward investment increasing to near 100 per cent in individual cases. Host economies in some developing regions and in transition economies rarely receive investment that is not covered by DTTs or BITs, and often both.

The treaty networks evolved in parallel and for the same overarching purpose of promoting cross-border investment in productive assets (box table V.5.1). Along the way, they have come to face similar challenges. Unintended consequences and side effects have increasingly surfaced. IIAs have led to some policymakers feeling more constrained in regulating for the public good, and they have resulted in often costly claims against host states on grounds that were not anticipated in the early development phase of IIAs. DTTs designed to avoid or to mitigate the effect of double taxation have resulted in many instances of double non-taxation, and many developing countries with weak tax collection capabilities have seen limits imposed on the use of a relatively effective tax collection mechanism (withholding taxes). In both situations, to obtain treaty benefits, investors have resorted to treaty shopping and the indirect routing of investments through conduits. About one third of global FDI stock has been routed through investment hubs before arriving at its destination.

Box table V.5.1. | Common and specific themes in IIAs and DTTs

IIA-specific themes	Shared themes	DTT-specific themes
<ul style="list-style-type: none"> • Ensure fair and equitable treatment of foreign investors • Provide for adequate compensation for expropriations • Cover the operation, expansion, management and - potentially - establishment an investment • Ensure funds can be transferred out of the host country without delay 	<ul style="list-style-type: none"> • Promote economic growth and development in contracting states by facilitating cross-border investment • Prevent discriminatory treatment of foreign investors/taxpayers and provide a level playing field • Provide more certainty to taxpayers/investors • Provide a dispute resolution mechanism 	<ul style="list-style-type: none"> • Allocate taxing rights between the contracting states • Establish methods for relief from double taxation and double non-taxation • Exchange tax information and in some cases provide assistance in tax collection • Establish treatment of certain categories of taxpayer or income

Source: UNCTAD, based on ITIC (2014).

Over time, efforts to address some of these challenges – in model treaties and in negotiations – have led to some common (or directionally similar) trends in IIAs and DTTs. In IIAs, more attention is slowly being paid to sustainable development issues. Analogously, in DTTs, clauses favouring developing countries are becoming more common; for example, countries are increasingly retaining taxing rights on services. IIA negotiators are looking for a better balance between rights and obligations. DTT negotiators are starting to balance lower withholding tax rates with more expansive definitions of permanent establishments, widening the tax base.

In both the IIA and DTT regimes, progress in dealing with challenges is held back by the large inventory of existing treaties. A significant share of global FDI stock, and especially FDI stock in developing countries, is covered by treaties that were signed more than a decade (often decades) ago. These treaties do not yet reflect the gradual changes in treaty norms that have taken place, often in favour of developing countries. Only systemic reform efforts can overcome this problem.

A useful starting point will be to bridge an existing knowledge gap: to date, the interaction between DTTs and IIAs remains largely unexamined. Experts in international taxation and international investment agreements rarely have an occasion to exchange views and learn from each other. UNCTAD will aim to provide such an occasion in its regular expert meetings.

Source: UNCTAD.

EPILOGUE

REFORMING INTERNATIONAL INVESTMENT GOVERNANCE

Investment in productive assets, infrastructure and knowledge is a necessary prerequisite and the foundation for economic growth and sustainable development in all countries. Foreign direct investment plays an important role in financing for development and in supporting progress towards the Sustainable Development Goals (SDGs). The *World Investment Report 2014* presented an action plan to bridge the SDG investment gap. It argued for a concerted push by policymakers to mobilize investment, channel it to where it is most needed and ensure its positive impacts. Part of this concerted push must be the strengthening of the regulatory policy environment for investment, by *reforming international investment governance* – the topic of this year’s Report.

The international policy environment for investment is not exclusively made up of international investment agreements (IIAs). A host of related policy areas are also important, including trade, taxation, competition, and social and environment issues, as identified in UNCTAD’s comprehensive Investment Policy Framework for Sustainable Development. International governance varies across these policy areas. Some have a global governance framework, some are fragmented; some are overseen by global institutions and have hard enforcement mechanisms, some are governed by soft-law standards or private initiatives.

This WIR focuses on two core areas of international investment governance that are at the center of today’s debate: IIAs and international taxation. Both are the object of significant reform efforts.

In IIAs, a shared view is emerging that reform is needed and that it should be guided by the goal of harnessing IIAs for sustainable development, focusing on key reform areas and following a multilevel, systematic and inclusive approach. Chapter IV of this report offers an action menu for such reform.

In taxation, attention is focusing on coordinated action against base erosion and profit shifting (BEPS), notably in the OECD/G20 BEPS project. Chapter V of this report places the tax avoidance debate in the context of the contribution of MNEs to government revenues, estimates revenue losses associated with BEPS, and

explains the links between investment and tax and the consequent need for policy coherence.

The international investment and tax policy regimes are closely interrelated. The two have *the same ultimate objective*: promoting and facilitating cross-border investment. They have a *similar architecture*, with both made up of a “spaghetti bowl” of mostly bilateral agreements. The two systems face *similar challenges*, for example, in strengthening their sustainable development dimension and maintaining their legitimacy. They *interact*, with potential consequences in both directions; and *both are the object of reform efforts*.

Reform efforts must ensure the continued effectiveness of both policy regimes to maintain confidence in and support for both. The policy imperative is to continue to facilitate cross-border productive investment and to take action against tax avoidance to support domestic resource mobilization for the pursuit of sustainable development.

Each regime will have its own specific reform priorities related to its specific area of competence. But there may be merit in greater *coherence between the two reform processes*, with better-managed interaction not only avoiding conflict between the regimes (e.g. by carving out taxation from BITs) but making them mutually supporting. The guidelines for coherent international tax and investment policies set out in chapter V are a starting point.

Ensuring that international tax and investment policies are mutually reinforcing is fundamental to building and maintaining an enabling environment for investment, maximizing the chances of reaching financing for development targets (to be discussed at the third international conference on financing for development in Addis Ababa, in mid-July 2015), and supporting the integration in the global economy of developing countries.

To that end, the international investment and development community should, and can, eventually build a common framework for global investment cooperation. UNCTAD can facilitate such a process for the benefit of all.

Notes

- ¹ The term “investment” in this chapter is used as commonly understood and refers to direct private investment in productive assets. The focus is naturally on foreign direct investment (FDI), although policy implications may occasionally extend to, or be equally relevant for, domestic investment.
- ² For a discussion on the relevance of the composition of taxes for development, see UNCTAD’s *TDR14*.
- ³ The term “foreign affiliates” covers direct investment enterprises outside the home country of the investor in which the investor owns at least 10 per cent of voting power. It includes both branches and subsidiaries.
- ⁴ According to the IMF, “SPEs are autonomous legal entities, directly or indirectly wholly foreign owned, that are part of a group company, without substantial real economic links with the host economy, engaged in a variety of cross-border financial activities, which are aimed at the passing through of all types of financial and non-financial assets, liabilities and related income to third countries”.
- ⁵ This chapter groups tax havens and jurisdictions that offer SPEs where doing so is useful to explain the conduit nature of investment structures located there. *Tax haven* refers to small jurisdictions with economies almost entirely dedicated to offshore financial activities; typical examples are the British Virgin Islands and the Cayman Islands. In contrast, jurisdictions offering *SPEs* often have substantial real economic activity, but they also act as financial centres for MNEs owing to their favourable tax conditions and other benefits for investors. The terminology is consistent with the *WIR13* (chapter 1, section A.1.d).
- ⁶ These include Austria, Hungary, Luxembourg and the Netherlands, with the latter two accounting for the bulk of transit FDI discussed here. The number of jurisdictions publishing SPE investment data is currently increasing rapidly as more countries are aligning with the OECD *Benchmark Definition* (edition 4th) and IMF *Balance of Payments and International Investment Position Manual* (edition 6th). The countries used here have a long record of publishing SPE data and (especially through the Netherlands and Luxembourg) account for the bulk of global SPE investment.
- ⁷ Note that for the Netherlands and Luxembourg such amplified FDI patterns do not affect official FDI statistics. For these countries, UNCTAD removes flows to/from SPEs from reported inflows/outflows. This treatment of the data allows segregating the *transit* component.
- ⁸ This characterization was first introduced by OECD (1998), p. 23.
- ⁹ This list of 38 jurisdictions is a revision of the original OECD list (2000) of 41 jurisdictions meeting the four characteristics (i)-(iv) to qualify as *tax havens*. Jurisdictions included are Anguilla, Antigua and Barbuda, Aruba, Bahamas, Bahrain, Belize, Bermuda, the British Virgin Islands, the Cayman Islands, Cook Islands, Cyprus, Dominica, Gibraltar, Grenada, Guernsey, the Isle of Man, Jersey, Liberia, Liechtenstein, Malta, Marshall Islands, Mauritius, Monaco, Montserrat, Nauru, the Netherlands Antilles, Niue, Panama, Saint Kitts and Nevis, Saint Lucia, Saint Vincent and the Grenadines, Samoa, San Marino, Seychelles, Turks and Caicos Islands, the United States Virgin Islands and Vanuatu. More recently, the OECD has increasingly focused on transparency standards and information exchange. The 38-jurisdiction list is still published on the OECD website as “Jurisdictions Committed to Improving Transparency and Establishing Effective Exchange of Information in Tax Matters”. This list has also been referred to by other studies, including Tax Justice Network (2007), U.S. Government Accountability Office (2008) and Gravelle (2013). Note that the 38-jurisdiction list employed in this chapter differs slightly from the list of 35 tax havens used in UNCTAD’s *WIR13* (p. 36, note 4), based on a more restricted set of countries published in OECD (2000) excluding some *advance commitment jurisdictions* even if they met the tax haven criteria.
- ¹⁰ UNCTAD’s *WIR13* estimates the total amount of inflows to OFCs and conduits in 2011 at over \$700 billion, consisting of \$600 billion of inflows to the SPEs in three jurisdictions Hungary, Luxembourg and the Netherlands and \$90 billion of inflows to tax havens. Of the estimated \$700 billion, only the inflows to tax havens are included in the reported FDI statistics (but excluded from analyses in the *WIR*). Other studies that look at the phenomenon of offshore FDI include Christian Aid (2013) and ActionAid (2013).
- ¹¹ The baseline for the calculation of the absolute values (given the shares provided by the Offshore Investment Matrix) is \$29 trillion, resulting from the sum of the total inward stock reported by UNCTAD’s *WIR13* (\$23 trillion) and the (unreported) SPE component (\$6 trillion).
- ¹² Also, tax havens display inward/outward symmetry; however, in the derivation of the Offshore Investment Matrix, symmetry in the case of tax havens applies by construction (see annex II).
- ¹³ There may be reasons other than base erosion for injecting debt funding as opposed to equity funding. In some cases, ease of repatriation can be an additional motivation. There are generally no or minimal restrictions on the repatriation of the principal amount of debt injected, whereas in some jurisdictions difficulties may arise with respect to repatriation of equity capital.
- ¹⁴ Analysis based on UNCTAD’s bilateral FDI and IIA databases. Less than 15 per cent of non-SPE outward FDI from the Netherlands is covered by bilateral investment treaties (BITs), implying that SPE flows have a higher relative preference for BIT coverage. More than 90 per cent of all outward investment (SPE and non-SPE) is covered by DTTs, indicating that tax is the most important motivation for Netherlands SPE use. Note that for investments to developing countries alone the distinction is less clear, with BIT coverage increasing significantly.
- ¹⁵ For a recent discussion of the two types of schemes in the context of developing economies, see e.g. Fuest et al. (2013b) for transfer pricing schemes and Fuest et al. (2013a) for financing schemes.
- ¹⁶ Conceptually, there may be transfer pricing aspects in financing schemes and financing aspects in transfer pricing schemes. The defining terminology is more conventional than substantive. Empirically, often the schemes are used in combination by MNEs. Nevertheless substantive differences between the two types emerge in the mechanics of the schemes (figures V.14 and V.15) as well as in the business implications (see also table V.2).
- ¹⁷ ActionAid reports some cases (www.actionaid.org.uk/tax-justice).
- ¹⁸ In 2012 Google paid only £11.6 million of corporate income taxes on £3.4 billion of revenues generated in the United Kingdom. This practice put Google under the scrutiny of the country’s tax authority.
- ¹⁹ Action 1 of the OECD Action Plan for the G20 (OECD, 2013b) is dedicated to “Addressing the tax challenge of the digital economy”.
- ²⁰ Recent empirical work by Dharmapala and Riedel (2013) suggests that *financial* income shifting due to debt interest payment is even more relevant than *operating* income shifting (driven by transfer pricing schemes). The work analyses how exogenous earnings shocks at the parent firm propagate across low-tax and high-tax multinational subsidiaries. The central result is that parents’ positive earnings shocks are associated with a significantly positive increase in pre-tax profits at low-tax affiliates, relative to the effect on the pre-tax profits of high-tax affiliates, signalling a profit-shifting effect. Interestingly the estimated effect is attributable primarily to the strategic use of debt across affiliates.
- ²¹ ActionAid (2013) proposes some case examples of harmful financing schemes perpetrated by MNEs in developing economies.
- ²² On the basis of Concord estimates, public domestic sources represent on average 30 per cent of GDP (including in addition to taxation, social security contributions and other revenues such as fines and income from property); the remaining part of domestic sources (28 per cent) consists of domestic private sector investments. Domestic taxation ranges from 15 per cent of GDP for low-income countries to 30 per cent for high-income countries. External sources at 5.4 per cent of GDP include loans (1.8 per cent), remittances (1.5 per cent), FDI (1.3 per cent), official development assistance (0.6 per cent) and others (1.5 per cent).
- ²³ See Atisophon et al. (2011).

- ²⁴ Existing studies tend to capture the effect of tax competition rather than that of profit shifting. In empirical studies, individual African countries commonly exhibit low effective tax rates, in part due to the abuse of tax incentives and special regimes to attract investment. However, the effective tax rate assesses tax revenue collection against a baseline (pre-tax corporate profits) that is already depressed by profit shifting. Thus it is more suitable for addressing the impact of tax incentives (leading to cuts of the tax payments, given the taxable base) rather than of profit-shifting schemes (designed instead to erode the taxable base itself).
- ²⁵ As the relationship between offshore hub investment links and rates of return on investment holds across countries, it is not possible to exclude compositional effects of specific countries driving the results. Annex II reports the results of the analysis and discusses methodological and analytical issues, including robustness tests.
- ²⁶ In addition to a lower coefficient, there are also features of developed economies that reduce the baseline on which the simulation of the impact takes place. This has a further “mitigating” effect on the aggregate estimate of profit shifting and tax revenue losses. These issues are discussed in more detail in annex II.
- ²⁷ The *Offshore Investment Matrix* and the *Offshore Indicator* developed by UNCTAD are being considered by Working Group 2 of the OECD Fiscal Committee and the Action 11 Focus Group of the OECD/G20 BEPS Project for inclusion in the deliverable for Action 11 as signal indicators.
- ²⁸ On the basis of tax expenditure data for a sample of 20 developing countries, M. Hearson in 2013 estimated the revenue loss related to tax incentives granted on corporate income taxation at a half percentage point of GDP (0.6 per cent simple average; 0.47 per cent weighted average). Using the 2012 GDP for developing economies, at \$25.5 trillion, leads to total losses of around \$140 billion. See the ActionAid website for more details: www.actionaid.org/2013/07/tax-incentives-cost-138-billion.
- ²⁹ See PwC (2008) and PwC (2013a).
- ³⁰ The very concept of “anti-avoidance rules”, which obviously make a targeted type of avoidance illegal, blurs the definitional distinction. The distinction also does not address the possibility of retrospective measures that would change the characterization of actions over time.
- ³¹ For a discussion on the importance of constructive and transparent dialogue between tax authorities and taxpayers, see Owens (2013).
- ³² For a discussion on tax policy as an investment determinant, see Owens (2012b).
- ³³ For a discussion on positive and negative effects of tax competition, see, for example, Owens (2012a).
- ³⁴ See UNCTAD *WIR13* on FDI and offshore finance, p. 17.
- ³⁵ See also UNCTAD *TDR14* (pp. 194–195) for further recommendations specifically regarding EITI.

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Annex table 1. FDI flows, by region and economy, 2009–2014 (Millions of dollars)

Region/economy	FDI inflows						FDI outflows					
	2009	2010	2011	2012	2013	2014	2009	2010	2011	2012	2013	2014
World^a	1 186 432	1 328 102	1 563 749	1 402 887	1 467 233	1 228 263	1 101 335	1 366 070	1 587 448	1 283 675	1 305 910	1 354 046
Developed economies	652 306	673 199	827 351	678 730	696 854	498 762	819 605	963 210	1 156 137	872 861	833 630	822 826
Europe	437 075	404 843	489 657	400 723	325 533	288 766	400 223	565 949	586 793	376 402	316 819	315 921
European Union	391 285	358 644	444 824	364 767	333 084	257 567	352 388	459 366	519 862	316 726	285 133	280 124
Austria	9 268	2 575	10 616	3 989	10 376	4 675	10 998	9 585	21 913	13 109	16 216	7 690
Belgium	75 169	60 635	78 258	9 308	23 396	- 4 957	15 251	9 092	46 371	33 985	17 940	8 534
Bulgaria	3 385	1 525	1 849	1 467	1 920	1 710	- 95	230	163	347	240	215
Croatia	3 077 ^b	1 133 ^b	1 682 ^b	1 451 ^b	955 ^b	3 451 ^b	1 260 ^b	- 91 ^b	42 ^b	- 56 ^b	- 180 ^b	1 886 ^b
Cyprus	3 472	766	2 384	1 257	3 497	679 ^c	383	679	2 201	- 281	3 473	2 176 ^b
Czech Republic	2 927	6 141	2 318	7 984	3 639	5 909	949	1 167	- 327	1 790	4 019	- 529
Denmark	392	- 9 163	11 463	418	- 742	3 652	3 688	1 381	11 254	7 355	9 537	10 952
Estonia	1 839	1 024	974	1 569	553	983	1 375	156	- 1 488	1 030	375	236
Finland	718	7 359	2 550	4 158	- 5 165 ^c	18 625 ^c	5 681	10 167	5 011	7 543	- 7 519 ^c	574 ^c
France	30 733	13 889	31 642	16 979	42 892	15 191	100 865	48 156	51 415	31 639	24 997	42 869
Germany	23 805 ^b	65 642 ^b	67 515 ^b	20 316 ^b	18 193 ^b	1 831 ^b	68 541 ^b	125 451 ^b	77 930 ^b	66 089 ^b	30 109 ^b	112 227 ^b
Greece	2 436	330	1 144	1 740	2 818	2 172	2 055	1 557	1 772	678	- 785	856
Hungary	1 995	2 193	6 300	14 375	3 097	4 039	1 849	1 172	4 702	11 678	1 868	3 381
Ireland	25 715	42 804	23 545	45 207	37 033	7 698	26 616	22 348	- 1 165	15 286	23 975	31 795
Italy	20 077	9 178	34 324	93	25 004	11 451 ^b	21 275	32 655	53 629	7 980	30 759	23 451 ^b
Latvia	94	379	1 453	1 109	903	474	- 62	19	61	192	411	137
Lithuania	- 14	800	1 448	700	469	217	198	- 6	55	392	192	- 36
Luxembourg	27 313 ^c	38 588 ^c	9 748 ^c	79 645 ^c	23 248 ^c	7 087 ^c	8 201 ^c	23 243 ^c	10 737 ^c	68 428 ^c	34 555 ^c	- 4 307 ^c
Malta	- 8 645	929	15 510	12 061	9 575	9 279	- 7 059	1 921	922	2 574	2 603	2 335
Netherlands	38 752	- 7 184	24 369	17 655	32 039	30 253	26 273	68 358	34 789	5 235	56 926	40 809
Poland	11 889	12 796	18 258	7 120	120 ^c	13 883 ^c	3 656	6 147	3 671	- 2 656	- 3 299 ^c	5 204 ^c
Portugal	1 611	2 424	7 428	8 242	2 234	8 807	- 367	- 9 782	16 495	- 9 157	- 90	6 664
Romania	4 665	3 041	2 363	3 199	3 602	3 234	- 96	6	- 28	- 114	- 281	- 77
Slovakia	- 6	1 770	3 491	2 982	591	479	904	946	713	8	- 423	- 123
Slovenia	- 476	105	1 087	339	- 144	1 564	214	- 18	198	- 259	- 223	- 9
Spain	10 407	39 873	28 379	25 696	41 733 ^c	22 904 ^c	13 070	37 844	41 164	- 3 982	25 829 ^c	30 688 ^c
Sweden	10 093	140	12 923	16 334	3 571	10 036	26 202	20 349	29 861	28 952	28 879	12 156
United Kingdom	90 591	58 954	41 803	59 375	47 675	72 241	20 562	46 633	107 801	28 939	- 14 972	- 59 628
Other developed Europe	45 791	46 199	44 833	35 956	- 7 551	31 199	47 835	106 582	66 932	59 676	31 686	35 797
Gibraltar	172 ^d	165 ^d	166 ^d	168 ^d	166 ^d	167 ^d	-	-	-	-	-	-
Iceland	86	246	1 108	1 025	397	436	2 292	- 2 357	23	- 3 206	460	- 247
Norway	16 641	17 044	15 250	18 774	14 441	8 682	19 165	23 239	18 763	19 561	20 987	19 247
Switzerland	28 891	28 744	28 309	15 989	- 22 555 ^c	21 914 ^c	26 378	85 701	48 145	43 321	10 238 ^c	16 798 ^c
North America	166 304	226 449	269 531	208 946	301 333	146 261	327 502	312 502	448 717	365 285	378 879	389 563
Canada	22 700	28 400	39 669	39 266	70 565	53 864	39 601	34 723	52 148	53 938	50 536	52 620
United States	143 604	198 049	229 862	169 680	230 768	92 397	287 901	277 779	396 569	311 347	328 343	336 943
Other developed economies	48 927	41 906	68 162	69 061	69 987	63 735	91 879	84 759	120 627	131 174	137 931	117 343
Australia	31 667	36 443	57 050	55 802	54 239	51 854	16 409	19 804	1 669	5 583	- 3 063	- 351
Bermuda	- 70 ^c	231 ^c	- 258 ^c	48 ^c	55 ^c	- 32 ^c	21 ^c	- 33 ^c	- 337 ^c	241 ^c	50 ^c	93 ^c
Israel	4 607	5 458	9 095	8 055	11 804	6 432	1 751	8 010	9 166	3 258	4 671	3 975
Japan	11 938	- 1 252	- 1 758	1 732	2 304	2 090	74 699	56 263	107 599	122 549	135 749	113 629
New Zealand	785	1 026	4 034	3 424	1 585	3 391	- 1 001	716	2 530	- 456	525	- 4
Developing economies^a	463 637	579 891	639 135	639 022	670 790	681 387	234 522	340 876	357 570	357 249	380 784	468 148
Africa	54 379	44 072	47 705	56 435	53 969	53 912	6 225	9 264	6 500	12 386	15 951	13 073
North Africa	18 134	15 745	7 548	17 151	13 580	11 541	2 498	4 781	1 491	3 332	951	1 672
Algeria	2 746	2 300	2 580	3 052	2 661	1 488 ^d	214	220	534	193	117	..
Egypt	6 712	6 386	- 483	6 031	4 192	4 783	571	1 176	626	211	301	253
Libya	3 310	1 909	-	1 425	702	50 ^d	1 165	2 722	131	2 509	180	940 ^d
Morocco	1 952 ^c	1 574 ^c	2 568 ^c	2 728 ^c	3 298 ^c	3 582 ^c	470 ^c	589 ^c	179 ^c	406 ^c	332 ^c	444 ^c
South Sudan	-	-	-	-	- 78 ^d	- 700 ^d	-	-	-	-	-	-
Sudan	1 726	2 064	1 734	2 311	1 688	1 277	-	-	-	-	-	-
Tunisia	1 688	1 513	1 148	1 603	1 117	1 060	77	74	21	13	22	39
Other Africa	36 246	28 327	40 157	39 284	40 388	42 371	3 727	4 483	5 009	9 053	14 999	11 401
West Africa	14 725	12 008	18 956	16 322	14 208	12 763	2 120	1 292	2 526	3 501	2 166	2 255
Benin	134	177	161	230	360	377	31	- 18	60	19	59	31
Burkina Faso	101	35	144	329	490	342	8	- 4	102	73	58	59
Cabo Verde	174	159	155	70	70	78	1	0	1	- 3	- 5	- 5
Côte d'Ivoire	377	339	302	330	407	462	- 9	25	15	14	- 6	9
Gambia	1	20	66	93	38	28	-	-	-	-	-	-
Ghana	2 897	2 527	3 237	3 293 ^d	3 226 ^d	3 357 ^d	7	-	25	1	9 ^d	12 ^d

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Annex table 1. FDI flows, by region and economy, 2009–2014 (continued)

Region/economy	FDI inflows						FDI outflows					
	2009	2010	2011	2012	2013	2014	2009	2010	2011	2012	2013	2014
Guinea	141 ^d	101 ^d	956 ^d	606 ^d	135 ^d	566 ^d	-	-	1 ^d	2 ^d	- 0 ^d	1 ^d
Guinea-Bissau	17	33	25	7	20	21	- 0	6	1	- 0	0	0
Liberia	218	450	785	985	1 061	302 ^d	364	369	372	1 354 ^d	698 ^d	..
Mali	748	406	556	398	308	199	- 1	7	4	16	3	8
Mauritania	- 3 ^d	131 ^d	589 ^d	1 389 ^d	1 126 ^d	492 ^d	4 ^d	4 ^d	4 ^d	4 ^d	4 ^d	4 ^d
Niger	791	940	1 066	841	719	769	59	- 60	9	2	101	21
Nigeria	8 650	6 099	8 915	7 127	5 608	4 694	1 542	923	824	1 543	1 238	1 614
Senegal	320	266	338	276	311	343	77	2	47	56	33	37
Sierra Leone	110 ^d	238 ^d	951 ^d	225 ^d	144 ^d	440 ^d	- 0 ^d	- 0 ^d	-	- 0 ^d	- 4 ^d	- 2 ^d
Togo	49	86	711	122	184	292	37	37	1 060	420	- 21	464
Central Africa	5 639	8 315	7 664	9 528	9 035	12 056	48	595	419	191	120	278
Burundi	0	1	3	1	7	32	-	-	-	-	0	0
Cameroon	740 ^d	538 ^d	652 ^d	526 ^d	326 ^d	501 ^d	- 69 ^d	503 ^d	187 ^d	- 284 ^d	- 379 ^d	- 159 ^d
Central African Republic	42	62	37	70	2	3	-	-	-	-	-	-
Chad	375 ^d	313 ^d	282 ^d	343 ^d	538 ^d	761 ^d	-	-	-	-	-	-
Congo	1 274	928	2 180	2 152	2 914	5 502	- 5 ^d	4 ^d	53 ^d	- 31 ^d	- 0 ^d	7 ^d
Congo, Democratic Republic of the	864	2 939	1 687	3 312	2 098	2 063	35	7	91	421	401	344
Equatorial Guinea	1 636 ^d	2 734 ^d	1 975 ^d	2 015 ^d	1 914 ^d	1 933 ^d	-	-	-	-	-	-
Gabon	573 ^d	499 ^d	696 ^d	832 ^d	968 ^d	973 ^d	87 ^d	81 ^d	88 ^d	85 ^d	85 ^d	86 ^d
Rwanda	119	251	119	255	258	268	-	-	-	-	14	-
Sao Tome and Principe	16	51	32	23	11	20	0	0	0	0	0	0
East Africa	3 903	4 520	4 779	5 473	6 127	6 794	118	174	163	251	101	99
Comoros	14	8	23	10	9	14 ^d	-	-	-	-	-	-
Djibouti	75	37	79	110	286	153	-	-	-	-	-	-
Eritrea	91 ^d	91 ^d	39 ^d	41 ^d	44 ^d	47 ^d	-	-	-	-	-	-
Ethiopia	221 ^d	288 ^d	627 ^d	279 ^d	953 ^d	1 200 ^d	-	-	-	-	-	-
Kenya	115	178	335	259	505 ^d	989 ^d	46	2	9	16	6 ^d	-
Madagascar	1 066	808	810	812	567	351	-	-	-	-	-	-
Mauritius	248	430	433	589	259	418	37	129	158	180	135	91
Seychelles	171	211	207	260	170	229	5	6	8	9	8	8
Somalia	108 ^d	112 ^d	102 ^d	107 ^d	107 ^d	106 ^d	-	-	-	-	-	-
Uganda	842	544	894	1 205	1 096	1 147	29	37	- 12	46	- 47	0
United Republic of Tanzania	953	1 813	1 229	1 800	2 131	2 142 ^d	-	-	-	-	-	-
Southern Africa	11 978	3 485	8 758	7 961	11 018	10 758	1 441	2 423	1 901	5 110	12 613	8 769
Angola	2 205 ^c	- 3 227 ^c	- 3 024 ^c	- 6 898 ^c	- 7 120 ^c	- 3 881 ^d	7 ^c	1 340 ^c	2 093 ^c	2 741 ^c	6 044 ^c	2 131 ^d
Botswana	129	218	1 371	487	398	393	6	- 1	10	- 8	- 85	- 43
Lesotho	92	30	61	57	50	46	2	- 21	- 41	- 38	- 34	- 31
Malawi	49	97	129	129	120	130	- 1	42	50	50	- 46	- 50
Mozambique	898	1 018	3 559	5 629	6 175	4 902	3	2	3	3	-	-
Namibia	506	793	816	1 133	801	414	- 3	4	5	- 11	- 13	- 34
South Africa	7 502 ^c	3 636 ^c	4 243 ^c	4 559 ^c	8 300 ^c	5 712 ^c	1 151 ^c	- 76 ^c	- 257 ^c	2 988 ^c	6 649 ^c	6 938 ^c
Swaziland	66	120	107	32	84	13	7	- 8	- 2	39	4	- 1
Zambia	426	634	1 110	2 433	1 810	2 484	270	1 095	- 2	- 702	66	- 213 ^d
Zimbabwe	105	166	387	400	400	545	-	43	43	49	27	72
Asia	323 793	401 851	425 308	400 840	427 879	465 285	214 942	284 078	313 648	299 424	335 318	431 591
East and South-East Asia	209 974	306 975	327 413	320 563	347 537	381 047	180 620	250 008	268 534	266 214	292 427	382 581
East Asia	163 840	201 825	233 878	212 428	221 450	248 180	139 088	194 532	213 680	215 497	225 254	302 520
China	95 000	114 734	123 985	121 080	123 911	128 500	56 530	68 811	74 654	87 804	101 000	116 000
Hong Kong, China	55 535	70 541	96 581	70 180	74 294	103 254 ^b	59 202	86 247	96 341	83 411	80 773	142 700 ^b
Korea, Democratic People's Republic of	2 ^d	38 ^d	56 ^d	120 ^d	227 ^d	134 ^d	-	-	-	-	-	-
Korea, Republic of	9 022 ^c	9 497 ^c	9 773 ^c	9 496 ^c	12 767 ^c	9 899 ^c	17 436 ^c	28 280 ^c	29 705 ^c	30 632 ^c	28 360	30 558 ^c
Macao, China	852	2 831	726	3 894	4 513	3 046 ^d	- 11	- 441	120	469	795	462 ^d
Mongolia	624	1 691	4 715	4 452	2 140	508	54	62	94	44	41	103
Taiwan Province of China	2 805 ^c	2 492 ^c	- 1 957 ^c	3 207 ^c	3 598 ^c	2 839 ^c	5 877 ^c	11 574 ^c	12 766 ^c	13 137 ^c	14 285 ^c	12 697 ^c
South-East Asia	46 134	105 151	93 535	108 135	126 087	132 867	41 533	55 476	54 854	50 717	67 172	80 061
Brunei Darussalam	370	481	691	865	776	568	9	6	10	- 422 ^d	- 135 ^d	-
Cambodia	928	1 342	1 372	1 835	1 872	1 730	19	21	29	36	46	32
Indonesia	4 877	13 771	19 241	19 138	18 817	22 580	2 249	2 664	7 713	5 422	6 647	7 077
Lao People's Democratic Republic	190	279	301	294	427	721 ^d	1 ^d	- 1 ^d	1 ^d	- 0 ^d	- 44 ^d	2 ^d
Malaysia	1 453	9 060	12 198	9 239	12 115	10 799	7 784	13 399	15 249	17 143	14 107	16 445
Myanmar	27	6 669	1 118	497	584	946	-	-	-	-	-	-
Philippines	1 963	1 298	1 852	2 033	3 737 ^c	6 201 ^c	359	616	339	1 692	3 647 ^c	6 990 ^c

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Annex table 1. FDI flows, by region and economy, 2009–2014 (continued)

Region/economy	FDI inflows						FDI outflows					
	2009	2010	2011	2012	2013	2014	2009	2010	2011	2012	2013	2014
Singapore	23 821 ^a	55 076 ^c	48 002 ^c	56 659 ^c	64 793 ^c	67 523 ^c	26 239 ^c	33 377 ^c	24 490 ^c	15 147 ^c	28 814 ^c	40 660 ^c
Thailand	4 854	9 147	1 195	9 168	14 016	12 566	4 172	4 467	6 106	10 487	12 122	7 692
Timor-Leste	50	29	47	39	50	34	-	26	- 33	13	13	13
Viet Nam	7 600	8 000	7 519	8 368	8 900	9 200	700	900	950	1 200	1 956	1 150
South Asia	42 403	35 024	44 539	32 415	35 624	41 192	16 349	16 298	12 888	10 181	2 135	10 684
Afghanistan	76	211	83	94	69	54 ^a	81 ^d	72 ^d	70 ^d	65 ^d	-	-
Bangladesh	700	913	1 136	1 293	1 599	1 527	29	15	13	43	34	48
Bhutan	72 ^c	31 ^c	26 ^c	51 ^c	9 ^c	6 ^c	-	-	-	-	-	-
India	35 634	27 417	36 190	24 196	28 199	34 417	16 058	15 947	12 456	8 486	1 679	9 848
Iran, Islamic Republic of	2 983	3 649	4 277	4 662	3 050	2 105	90 ^d	174 ^d	227 ^d	1 441 ^d	146 ^d	605 ^d
Maldives	158 ^a	216 ^d	424 ^d	228 ^d	361 ^d	363 ^a	-	-	-	-	-	-
Nepal	39	87	95	92 ^d	71 ^d	30 ^a	-	-	-	-	-	-
Pakistan	2 338	2 022	1 326	859	1 333	1 747	71	47	62	82	212	116
Sri Lanka	404	478	981	941	933	944	20	43	60	64	65	67
West Asia	71 415	59 852	53 356	47 862	44 718	43 046	17 973	17 771	32 225	23 028	40 756	38 326
Bahrain	257	156	781	891	989	957	- 1 791	334	894	922	1 052	- 80
Iraq	1 598	1 396	1 882	3 400	5 131	4 782	72	125	366	490	227	242
Jordan	2 413	1 651	1 474	1 497	1 747	1 760	72	28	31	5	16	83
Kuwait	1 114	1 305	3 259	2 873	1 434	486	8 582	5 890	10 773	6 741	16 648	13 108
Lebanon	4 379	3 748	3 390	3 170	2 880	3 070 ^a	1 126	487	934	1 009	1 962	1 893 ^d
Oman	1 485 ^c	1 243 ^c	874 ^c	1 040 ^c	1 626 ^c	1 180 ^d	109 ^c	1 498 ^c	1 233 ^c	877 ^c	1 384 ^c	1 164 ^d
Qatar	8 125	4 670	939	396	- 840	1 040	3 215	1 863	10 109	1 840	8 021	6 748
Saudi Arabia	36 458	29 233	16 308	12 182	8 865	8 012 ^a	2 177	3 907	3 430	4 402	4 943	5 396 ^d
State of Palestine	300	206	349	58	176	124	69	84	- 128	29	- 48	- 32
Syrian Arab Republic	2 570	1 469	804	-	-	-	-	-	-	-	-	-
Turkey	8 585	9 086	16 136	13 283	12 357	12 146	1 553	1 469	2 330	4 106	3 527	6 658
United Arab Emirates	4 003	5 500	7 679	9 602	10 488	10 066	2 723	2 015	2 178	2 536	2 952 ^d	3 072 ^d
Yemen	129	189	- 518	- 531	- 134	- 578 ^a	66 ^d	70 ^d	77 ^d	71 ^d	73 ^d	73 ^d
Latin America and the Caribbean ^a	83 514	131 727	163 868	178 049	186 151	159 405	13 284	46 879	36 490	43 847	28 466	23 326
South America	57 740	96 345	127 426	143 881	125 987	120 708	3 501	31 370	22 420	19 164	13 861	16 652
Argentina	4 017	11 333	10 840	15 324	11 301	6 612	712	965	1 488	1 055	1 097	2 117
Bolivia, Plurinational State of	423	643	859	1 060	1 750	648	- 3	- 29	-	-	-	-
Brazil	25 949	48 506	66 660	65 272	63 996	62 495	- 10 084	11 588	- 1 029	- 2 821	- 3 495	- 3 540
Chile	11 868	16 789	16 930	25 021	16 577	22 949	6 213	10 524	13 738	17 120	7 621	12 999
Colombia	8 035	6 430	14 648	15 039	16 199	16 054	3 505	5 483	8 420	- 606	7 652	3 899
Ecuador	308	166	644	585	731	774	47 ^d	134 ^d	63 ^d	- 6 ^d	42 ^d	33 ^d
Guyana	164	198	247	294	214	255	-	-	-	-	-	-
Paraguay	95	210	619	738	72	236	54 ^d	7 ^d	- 34 ^d	56 ^d	49 ^d	24 ^d
Peru	6 431	8 455	7 665	11 918	9 298	7 607	411	266	147	78	137	84
Suriname	- 93	- 248	70	121	138	4	-	-	3	- 1	-	-
Uruguay	1 529	2 289	2 504	2 536	3 032	2 755	16	- 60	- 7	- 3	5	13
Venezuela, Bolivarian Republic of	- 983	1 574	5 740	5 973	2 680	320	2 630	2 492	- 370	4 294	752	1 024
Central America	22 302	32 404	31 998	28 004	55 399	33 416	9 612	15 426	12 897	22 922	13 922	5 929
Belize	109 ^a	97 ^c	95 ^c	189 ^a	92 ^c	141 ^c	0 ^c	1 ^c	1 ^c	1 ^c	1 ^c	3 ^c
Costa Rica	1 347	1 466	2 178	2 332	2 677	2 106	7	25	58	428	290	218
El Salvador	366	- 230	219	482	179	275	-	- 5	0	- 2	3	1
Guatemala	600	806	1 026	1 245	1 295	1 396	26	24	17	39	34	31
Honduras	509	969	1 014	1 059	1 060	1 144	4	- 1	2	208	68	24
Mexico	17 679	26 083	23 376	18 951	44 627	22 795	9 604	15 050	12 636	22 470	13 138	5 201
Nicaragua	434	490	936	768	816	840	- 29	16	7	52	107	84
Panama	1 259	2 723	3 153	2 980	4 654	4 719	-	317	176	- 274	281	368
Caribbean ^a	3 471	2 979	4 445	6 164	4 764	5 281	171	83	1 174	1 761	683	744
Anguilla	44	11	39	44	42	39	0	0	0	0	-	-
Antigua and Barbuda	85	101	68	138	101	167	4	5	3	4	6	6
Aruba	- 11	190	488	- 319	225	244	1	6	3	3	4	9
Bahamas	873	1 148	1 533	1 073	1 111	1 596	216	150	524	132	277	398
Barbados	247	290	384	436	5	275	- 56	- 54	301	- 129	106	93
Curaçao	55	89	69	57	17	183 ^d	5	15	- 30	12	- 17	27 ^d
Dominica	58	58	51	57	39	41	1	1	0	0	2	2
Dominican Republic	2 165	2 024	2 277	3 142	1 991	2 208	110 ^d	25 ^d	39 ^d	77 ^d	- 55 ^d	20 ^d
Grenada	104	64	45	34	114	40	1	3	3	3	1	1
Haiti	55	178	119	156	186	99	-	-	-	-	-	-

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Annex table 1. FDI flows, by region and economy, 2009–2014 (concluded)

Region/economy	FDI inflows						FDI outflows					
	2009	2010	2011	2012	2013	2014	2009	2010	2011	2012	2013	2014
Jamaica	541 ^c	228 ^c	218 ^c	413 ^c	593 ^c	551 ^c	61 ^c	58 ^c	75 ^c	3 ^c	- 87 ^c	- 2 ^c
Montserrat	3	4	2	3	4	6	0	0	0	0	0	0
Saint Kitts and Nevis	136	119	112	110	139	120	5	3	2	2	2	2
Saint Lucia	152	127	100	78	95	75	6	5	4	4	3	3
Saint Vincent and the Grenadines	111	97	86	115	160	139	1	0	0	0	0	0
Sint Maarten	40	33	- 48	14	34	67 ^d	1	3	1	- 4	4	4 ^d
Trinidad and Tobago	709	549	1 831	2 453	1 994	2 423 ^d	-	-	1 060	1 681	824	726 ^d
Oceania	1 952	2 240	2 254	3 697	2 791	2 784	71	655	932	1 593	1 050	158
Cook Islands	- 6 ^d	-	-	-	-	-	13 ^d	540 ^d	814 ^d	1 307 ^d	887 ^d	..
Fiji	164	350	403	376	272	279 ^d	3	6	1	2	4	1 ^d
French Polynesia	22	64	131	155	101	129 ^d	8	38	27	43	66	46 ^d
Kiribati	3	- 0 ^d	0 ^d	1 ^d	9 ^d	1 ^d	- 1	- 0	-	- 0 ^d	- 0 ^d	- 0 ^d
Marshall Islands	- 11 ^d	27 ^d	34 ^d	27 ^d	23 ^d	28 ^d	- 25 ^d	- 11 ^d	29 ^d	24 ^d	19 ^d	24 ^d
Micronesia, Federated States of	1 ^d	1 ^d	1 ^d	1 ^d	1 ^d	1 ^d	-	-	-	-	-	-
Nauru	1 ^d	-	-	-	-	-	-	-	-	-	-	-
New Caledonia	1 182	1 439	1 715	2 887	2 261	2 288 ^d	58	76	40	109	63	70 ^d
Niue	-	-	-	-	-	-	- 0 ^d	-	- 1 ^d	-	-	-
Palau	- 10	- 7	6	9	2	6 ^d	-	-	-	-	-	-
Papua New Guinea	423	29	- 310	25	18	- 30	4	0	1	89	-	-
Samoa	10	1	15	21	24	23	1	-	1	9	0	4
Solomon Islands	120	238	146	80	43	24	3	2	4	3	3	1
Tonga	20 ^d	25 ^d	44 ^d	31 ^d	51 ^d	56 ^d	5 ^d	3 ^d	16 ^d	7 ^d	7 ^d	11 ^d
Vanuatu	32 ^c	59 ^c	70 ^c	78 ^c	- 19 ^c	- 22 ^c	1 ^c	1 ^c	1 ^c	1 ^c	0 ^c	1 ^c
Transition economies	70 489	75 013	97 263	85 135	99 590	48 114	47 208	61 984	73 740	53 565	91 496	63 072
South-East Europe	6 270	4 600	7 890	3 562	4 740	4 698	140	317	403	410	380	430
Albania	996	1 051	876	855	1 266	1 093	39	6	30	23	40	30
Bosnia and Herzegovina	250	406	496	351	283	564	6	46	18	16	- 15	2
Montenegro	1 527	760	558	620	447	497	46	29	17	27	17	27
Serbia	2 896	1 686	4 932	1 299	2 053	1 996	24	185	318	331	329	356
The former Yugoslav Republic of Macedonia	201	213	479	143	335	348	11	5	- 0	- 8	- 15	- 21
CIS	63 560	69 599	88 324	80 662	93 901	42 137	47 087	61 532	73 190	52 858	90 997	62 440
Armenia	760	529	515	489	370	383 ^c	50	8	78	16	19	18 ^c
Azerbaijan	473	563	1 465	2 005	2 632	4 430	326	232	533	1 192	1 490	2 209
Belarus	1 877	1 393	4 002	1 429	2 230	1 798	102	51	126	121	246	- 1
Kazakhstan	13 243	11 551	13 973	13 337	10 221	9 562	3 159	7 885	5 390	1 481	2 287	3 624
Kyrgyzstan	189	438	694	293	626	211	- 0	0	0	- 0	- 0	0
Moldova, Republic of	208	208	288	195	236	207	7	4	21	20	29	41
Russian Federation	36 583 ^c	43 168 ^c	55 084 ^c	50 588 ^c	69 219 ^c	20 958 ^c	43 281 ^c	52 616 ^c	66 851 ^c	48 822 ^c	86 507 ^c	56 438 ^c
Tajikistan	16	- 15	70	233	105	263	-	-	-	-	-	-
Turkmenistan	4 553 ^d	3 632 ^d	3 391 ^d	3 130 ^d	3 076 ^d	3 164 ^d	-	-	-	-	-	-
Ukraine	4 816	6 495	7 207	8 401	4 499	410	162	736	192	1 206	420	111
Uzbekistan	842 ^d	1 636 ^d	1 635 ^d	563 ^d	686 ^d	751 ^d	-	-	-	-	-	-
Georgia	659	814	1 048	911	949	1 279	- 19	135	147	297	120	202
Memorandum												
Least developed countries (LDCs) ^e	16 865	23 774	21 852	23 524	22 327	23 239	1 123	3 055	4 003	4 698	7 454	2 975
Landlocked developing countries (LLDCs) ^f	26 108	26 011	36 101	34 426	29 980	29 151	4 119	9 378	6 314	2 393	3 917	5 822
Small island developing states (SIDS) ^g	4 599	4 606	6 160	6 776	5 703	6 948	275	332	2 158	2 032	1 319	1 377

Source: UNCTAD, FDI-MNE Information System, FDI database (www.unctad.org/fdistatistics).

^a Excluding the financial centres in the Caribbean (Anguilla, Antigua and Barbuda, Aruba, the Bahamas, Barbados, the British Virgin Islands, the Cayman Islands, Curaçao, Dominica, Grenada, Montserrat, Saint Kitts and Nevis, Saint Lucia, Saint Vincent and the Grenadines, Sint Maarten and Turks and Caicos Islands).

^b Directional basis calculated from asset/liability basis.

^c Asset/liability basis.

^d Estimates.

^e Least developed countries include Afghanistan, Angola, Bangladesh, Benin, Bhutan, Burkina Faso, Burundi, Cambodia, the Central African Republic, Chad, the Comoros, the Democratic Republic of the Congo, Djibouti, Equatorial Guinea, Eritrea, Ethiopia, the Gambia, Guinea, Guinea-Bissau, Haiti, Kiribati, the Lao People's Democratic Republic, Lesotho, Liberia, Madagascar, Malawi, Mali, Mauritania, Mozambique, Myanmar, Nepal, the Niger, Rwanda, Sao Tome and Principe, Senegal, Sierra Leone, Solomon Islands, Somalia, South Sudan, the Sudan, Timor-Leste, Togo, Tuvalu, Uganda, the United Republic of Tanzania, Vanuatu, Yemen and Zambia.

^f Landlocked developing countries include Afghanistan, Armenia, Azerbaijan, Bhutan, the Plurinational State of Bolivia, Botswana, Burkina Faso, Burundi, the Central African Republic, Chad, Ethiopia, Kazakhstan, Kyrgyzstan, the Lao People's Democratic Republic, Lesotho, the former Yugoslav Republic of Macedonia, Malawi, Mali, the Republic of Moldova, Mongolia, Nepal, the Niger, Paraguay, Rwanda, South Sudan, Swaziland, Tajikistan, Turkmenistan, Uganda, Uzbekistan, Zambia and Zimbabwe.

^g Small island developing States include Antigua and Barbuda, the Bahamas, Barbados, Cabo Verde, the Comoros, Dominica, Fiji, Grenada, Jamaica, Kiribati, Maldives, the Marshall Islands, Mauritius, Federated States of Micronesia, Nauru, Palau, Papua New Guinea, Saint Kitts and Nevis, Saint Lucia, Saint Vincent and the Grenadines, Samoa, Sao Tome and Principe, Seychelles, Solomon Islands, Timor-Leste, Tonga, Trinidad and Tobago, Tuvalu and Vanuatu.

Annex table 2. FDI stock, by region and economy, 1990, 2000, 2014 (Millions of dollars)

Region/economy	FDI inward stock			FDI outward stock		
	1990	2000	2014	1990	2000	2014
World^a	2 197 768	7 202 348	26 038 824	2 253 944	7 298 188	25 874 757
Developed economies	1 687 652	5 476 613	17 003 802	2 114 508	6 535 722	20 554 819
Europe	932 579	2 263 007	10 049 259	1 053 382	3 215 429	11 787 347
European Union	885 533	2 144 798	9 171 795	976 336	2 948 579	10 434 829
Austria	11 606	31 165	180 824	5 021	24 821	223 246
Belgium	-	-	525 612	-	-	450 178
Belgium and Luxembourg	58 388	195 219	-	40 636	179 773	-
Bulgaria	112	2 704	46 539	124	67	2 195
Croatia	-	2 664 ^b	29 761 ^b	-	760 ^b	5 444 ^b
Cyprus	.. ^{c,d}	2 846	58 145 ^b	8 ^d	557	41 913 ^b
Czech Republic	1 363 ^d	21 644	121 530	-	738	19 041
Denmark	9 192	73 574	82 922 ^d	7 342	73 100	183 025 ^d
Estonia	-	2 645	19 298	-	259	6 319
Finland	4 277	24 273	133 116 ^e	9 355	52 109	164 554 ^e
France	104 268	184 215	729 147	119 860	365 871	1 279 089
Germany	226 552	271 613	743 512 ^b	308 736	541 866	1 583 279 ^b
Greece	5 681	14 113	20 181	2 882	6 094	33 939
Hungary	570	22 870	98 360	159 ^d	1 280	39 641
Ireland	37 989 ^d	127 089	369 168	14 942 ^d	27 925	628 026
Italy	59 998	122 533	373 738 ^b	60 184	169 957	548 416 ^b
Latvia	-	1 692	14 567	-	20	1 170
Lithuania	-	2 334	14 691	-	29	2 683
Luxembourg	-	-	161 311 ^e	-	-	149 892 ^e
Malta	465 ^d	2 263	172 358	-	193	44 493
Netherlands	71 828	243 733	664 442	109 870	305 461	985 256
Poland	109	33 477	245 161 ^e	95 ^d	268	65 217 ^e
Portugal	9 604	32 043	108 515	818	19 794	58 355
Romania	0	6 953	74 732	66	136	696
Slovakia	282 ^d	6 970	53 216	-	555	2 975
Slovenia	1 643 ^d	2 894	12 743	560 ^d	768	6 193
Spain	65 916	156 348	721 879 ^e	15 652	129 194	673 989 ^e
Sweden	12 636	93 791	321 103	50 720	123 618	379 528
United Kingdom	203 905	463 134	1 662 858	229 307	923 367	1 584 147
Other developed Europe	47 045	118 209	877 464	77 047	266 850	1 352 518
Gibraltar	263 ^d	642 ^d	2 569 ^d	-	-	-
Iceland	147	497	7 425	75	663	7 955
Norway	12 391	30 265	185 620 ^d	10 884	34 026	213 948 ^d
Switzerland	34 245	86 804	681 849 ^d	66 087	232 161	1 130 615 ^d
North America	652 444	2 995 951	6 041 200	816 569	2 931 653	7 033 195
Canada	112 843	212 716	631 316	84 807	237 639	714 555
United States	539 601	2 783 235	5 409 884	731 762	2 694 014	6 318 640
Other developed economies	102 629	217 655	913 343	244 556	388 640	1 734 278
Australia	80 364	121 686	564 608	37 505	92 508	443 519
Bermuda	-	265 ^d	2 632 ^d	-	108 ^d	928 ^d
Israel	4 476	20 426	98 697	1 188	9 091	78 016
Japan	9 850	50 322	170 615	201 441	278 442	1 193 137
New Zealand	7 938	24 957	76 791	4 422 ^d	8 491	18 678
Developing economies ^a	510 107	1 669 812	8 310 055	139 436	741 924	4 833 046
Africa	60 678	153 745	709 174	20 252	38 888	213 486
North Africa	23 962	45 590	239 076	1 836	3 199	33 446
Algeria	1 561 ^d	3 379 ^d	26 786 ^d	183 ^d	205 ^d	1 733 ^d
Egypt	11 043 ^d	19 955	87 882	163 ^d	655	6 839
Libya	678 ^d	471	18 511 ^d	1 321 ^d	1 903	20 375 ^d
Morocco	3 011 ^d	8 842 ^d	51 664 ^e	155 ^d	402 ^d	4 194 ^e
Sudan	55 ^d	1 398 ^d	22 693	-	-	-
Tunisia	7 615	11 545	31 540	15	33	305
Other Africa	36 716	108 156	470 098	18 416	35 689	180 040
West Africa	14 013	33 010	151 897	2 202	6 381	17 821
Benin	- 173 ^d	213	1 581	2 ^d	11	172
Burkina Faso	39 ^d	28	1 679	4 ^d	0	276
Cabo Verde	4 ^d	192 ^d	1 474	-	-	.. ^c
Côte d'Ivoire	975 ^d	2 483	7 711	6 ^d	9	114
Gambia	157 ^d	216	340 ^d	-	-	-

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Annex table 2. FDI stock, by region and economy, 1990, 2000, 2014 (continued)

Region/economy	FDI inward stock			FDI outward stock		
	1990	2000	2014	1990	2000	2014
Ghana	319 ^d	1 554 ^d	23 205 ^d	-	-	130 ^d
Guinea	69 ^d	263 ^d	2 584 ^d	-	12 ^d	68 ^d
Guinea-Bissau	8 ^d	38	123	-	-	5
Liberia	2 732 ^d	3 247 ^d	6 569 ^d	846 ^d	2 188 ^d	4 345 ^d
Mali	229 ^d	132	3 109	22 ^d	1	45
Mauritania	59 ^d	146 ^d	5 968 ^d	3 ^d	4 ^d	48 ^d
Niger	286 ^d	45	5 133	54 ^d	1	130
Nigeria	8 539 ^d	23 786	86 671	1 219 ^d	4 144	10 259
Senegal	258 ^d	295	2 699	47 ^d	22	397
Sierra Leone	243 ^d	284 ^d	1 365 ^d	-	-	-
Togo	268 ^d	87	1 685	-	.. ^c	1 843
Central Africa	3 808	5 736	67 425	390	721	2 776
Burundi	30 ^d	47 ^d	48 ^d	0 ^d	2 ^d	1 ^d
Cameroon	1 044 ^d	1 600 ^d	6 493 ^d	150 ^d	254 ^d	43 ^d
Central African Republic	95 ^d	104	623	18 ^d	43	43
Chad	250 ^d	576 ^d	5 518 ^d	37 ^d	70 ^d	70 ^d
Congo	575 ^d	1 893 ^d	22 010 ^d	18 ^d	40 ^d	94 ^d
Congo, Democratic Republic of the	546 ^d	617	7 694 ^d	-	34	1 480 ^d
Equatorial Guinea	25 ^d	1 060 ^d	17 250 ^d	0 ^d	.. ^{c,d}	3 ^d
Gabon	1 208 ^d	.. ^{c,d}	6 339 ^d	167 ^d	280 ^d	1 006
Rwanda	33 ^d	55	1 105 ^d	-	-	13 ^d
Sao Tome and Principe	0 ^d	11 ^d	345 ^d	-	-	22 ^d
East Africa	1 701	7 202	55 447	165	387	2 139
Comoros	17 ^d	21 ^d	121 ^d	-	-	-
Djibouti	13 ^d	40	1 505 ^d	-	-	-
Eritrea	0 ^d	337 ^d	837 ^d	-	-	-
Ethiopia	124 ^d	941 ^d	7 264 ^d	-	-	-
Kenya	668 ^d	932 ^d	4 370 ^d	99 ^d	115 ^d	321 ^d
Madagascar	107 ^d	141	6 277	1 ^d	10 ^d	6 ^d
Mauritius	168 ^d	683 ^d	4 586 ^d	1 ^d	132 ^d	1 482 ^d
Seychelles	213	515	2 567	64	130	280
Somalia	.. ^{c,d}	4 ^d	988 ^d	-	-	-
Uganda	6 ^d	807	9 917	-	-	50
United Republic of Tanzania	388 ^d	2 781	17 013 ^d	-	-	-
Southern Africa	17 194	62 208	195 328	15 658	28 200	157 304
Angola	1 025 ^d	7 977 ^d	.. ^{c,d}	1 ^d	.. ^{c,d}	19 218 ^d
Botswana	1 309	1 827	4 367	447	517	795
Lesotho	83 ^d	330	586	0 ^d	2	253
Malawi	228 ^d	358	1 239 ^d	-	.. ^c	24
Mozambique	25	1 249	25 577	2 ^d	1	10
Namibia	2 047	1 276	3 722	80	45	60
South Africa	9 210	43 451 ^e	145 384 ^e	15 010	27 328 ^e	133 936 ^e
Swaziland	336	536	759 ^d	38	87	103 ^d
Zambia	2 655 ^d	3 966 ^d	15 009	-	-	2 417 ^d
Zimbabwe	277 ^d	1 238	3 546	80 ^d	234	487
Asia	340 242	1 052 754	5 679 670	67 066	597 220	3 948 830
East and South-East Asia	302 285	953 635	4 618 719	58 504	579 768	3 555 214
East Asia	240 645	696 032	2 931 267	49 032	495 206	2 709 546
China	20 691 ^d	193 348	1 085 293 ^d	4 455 ^d	27 768 ^d	729 585 ^d
Hong Kong, China	201 653 ^d	435 417	1 549 849 ^b	11 920 ^d	379 285	1 459 947 ^b
Korea, Democratic People's Republic of	572 ^d	1 044 ^d	2 012 ^d	-	-	-
Korea, Republic of	5 186	43 738 ^e	182 037 ^e	2 301 ^d	21 497 ^e	258 553 ^e
Macao, China	2 809 ^d	2 801 ^d	26 747 ^d	-	-	2 277 ^d
Mongolia	0 ^d	182	16 693	-	-	355
Taiwan Province of China	9 735 ^d	19 502 ^e	68 636 ^d	30 356 ^d	66 655 ^e	258 829 ^d
South-East Asia	61 640	257 603	1 687 452	9 471	84 563	845 669
Brunei Darussalam	33 ^d	3 868 ^b	6 219	0 ^d	512 ^d	134 ^d
Cambodia	38 ^d	1 580	13 035	0 ^d	193	484
Indonesia	8 732 ^d	25 060 ^d	253 082	86 ^d	6 940 ^d	24 052
Lao People's Democratic Republic	13 ^d	588 ^d	3 630 ^d	1 ^d	20 ^d	.. ^{c,d}
Malaysia	10 318	52 747 ^d	133 767	753 ^d	15 878 ^d	135 685
Myanmar	285 ^d	3 752 ^d	17 652 ^d	-	-	-
Philippines	3 268 ^d	13 762 ^d	57 093 ^e	405 ^d	1 032 ^d	35 603 ^e

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Annex table 2. FDI stock, by region and economy, 1990, 2000, 2014 (Millions of dollars)

Region/economy	FDI inward stock			FDI outward stock		
	1990	2000	2014	1990	2000	2014
Singapore	30 468	110 570	912 355 ^e	7 808	56 755	576 396 ^e
Thailand	8 242	30 944	199 311	418	3 232	65 769
Timor-Leste	-	-	316	-	-	86
Viet Nam	243 ^d	14 730 ^d	90 991 ^d	-	-	7 490 ^d
South Asia	6 795	29 834	350 971	478	2 791	136 106
Afghanistan	12 ^d	17 ^d	1 692 ^d	-	-	-
Bangladesh	477 ^d	2 162	9 355	45 ^d	69	130
Bhutan	2 ^d	4 ^d	112 ^a	-	-	-
India	1 657 ^d	16 339	252 331	124 ^d	1 733	129 578
Iran, Islamic Republic of	2 039 ^d	2 597 ^d	43 047	56 ^d	414 ^d	4 096 ^d
Maldives	25 ^d	128 ^d	2 490 ^d	-	-	-
Nepal	12 ^d	72 ^d	541 ^d	-	-	-
Pakistan	1 892 ^d	6 919	30 892	245 ^d	489	1 695
Sri Lanka	679 ^d	1 596	10 511	8 ^d	86	607
West Asia	31 161	69 286	709 981	8 084	14 661	257 510
Bahrain	552	5 906	18 771	719	1 752	10 672
Iraq	.. ^{c,d}	.. ^{c,d}	23 161 ^d	-	-	1 956 ^d
Jordan	1 368 ^d	3 135	28 734	158 ^d	44	608
Kuwait	37 ^d	608	15 362	3 662 ^d	1 428	36 531
Lebanon	53 ^d	14 233	56 834 ^d	43 ^d	352	12 629 ^d
Oman	1 723 ^d	2 577 ^e	19 707 ^d	-	-	7 453 ^d
Qatar	63 ^d	1 912	31 004 ^d	-	74	35 182 ^d
Saudi Arabia	15 193 ^d	17 577	215 909	2 328 ^d	5 285 ^d	44 699
State of Palestine	-	1 418 ^d	2 453	-	-	167
Syrian Arab Republic	154 ^d	1 244 ^d	10 743 ^d	4 ^d	107 ^d	421 ^d
Turkey	11 150 ^d	18 812	168 645	1 150 ^d	3 668	40 088
United Arab Emirates	751 ^d	1 069 ^d	115 561 ^d	14 ^d	1 938 ^d	66 298 ^d
Yemen	180 ^d	843 ^d	3 097 ^d	5 ^d	12 ^d	806 ^d
Latin America and the Caribbean ^a	107 187	460 991	1 893 554	52 050	105 533	663 970
South America	74 815	308 952	1 384 301	49 201	95 861	518 205
Argentina	9 085 ^d	67 601	114 076	6 057 ^d	21 141	35 938
Bolivia, Plurinational State of	1 026	5 188	11 206	7 ^d	29	52
Brazil	37 143	122 250	754 769	41 044	51 946	316 339
Chile	16 107 ^d	45 753	207 678	154 ^d	11 154	89 733
Colombia	3 500	11 157	141 667	402	2 989	43 082
Ecuador	1 626	6 337	14 591	18 ^d	252 ^d	697 ^d
Falkland Islands (Malvinas)	0 ^d	58 ^d	75 ^d	-	-	-
Guyana	45 ^d	756	1 960	-	1	2
Paraguay	418 ^d	1 221	5 381	.. ^{c,d}	29 ^d	379 ^d
Peru	1 330	11 062	79 429	122	505	4 205 ^d
Suriname	-	-	1 012	-	-	-
Uruguay	671 ^d	2 088	22 318 ^d	186 ^d	138	428 ^d
Venezuela, Bolivarian Republic of	3 865	35 480	30 139	1 221	7 676	27 349
Central America	28 496	139 675	439 838	2 793	8 600	138 868
Belize	89 ^d	301 ^e	1 765 ^a	20 ^d	43 ^a	54 ^e
Costa Rica	1 324 ^d	2 709	24 309	44 ^d	86	2 049
El Salvador	212 ^d	1 973	8 504	56 ^d	104	3
Guatemala	1 734	3 420	12 102	0	93	503
Honduras	293	1 392	11 228	-	-	393
Mexico	22 424	121 691	337 974	2 672 ^d	8 273	131 246
Nicaragua	145 ^d	1 414	8 040	-	-	375
Panama	2 275 ^d	6 775 ^d	35 917	-	-	4 246
Caribbean ^a	3 876	12 365	69 415	56	1 072	6 897
Anguilla	11 ^d	231 ^d	1 131 ^d	-	5 ^d	31 ^d
Antigua and Barbuda	290 ^d	619 ^d	2 845 ^d	-	5 ^d	112 ^d
Aruba	145 ^d	1 161	3 941	-	675	698
Bahamas	586 ^d	3 278 ^d	18 751 ^d	-	452 ^d	3 868 ^d
Barbados	171	308	5 248	23	41	3 840
Curaçao	-	-	890 ^d	-	-	86 ^d
Dominica	66 ^d	275 ^d	846 ^d	-	3 ^d	38 ^d
Dominican Republic	572	1 673	28 757 ^d	-	68 ^d	171 ^d
Grenada	70 ^d	348 ^d	1 506 ^d	-	2 ^d	51 ^d
Haiti	149 ^d	95	1 209 ^d	-	2 ^d	2 ^d

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Annex table 2. FDI stock, by region and economy, 1990, 2000, 2014 (Millions of dollars)

Region/economy	FDI inward stock			FDI outward stock		
	1990	2000	2014	1990	2000	2014
Jamaica	790 ^d	3 317	13 324	42 ^d	709	314
Montserrat	40 ^d	83 ^d	140 ^d	-	0 ^d	1 ^d
Netherlands Antilles ^f	408 ^d	277	-	21 ^d	6	- ^d
Saint Kitts and Nevis	160 ^d	487 ^d	2 078 ^d	-	3 ^d	59 ^d
Saint Lucia	316 ^d	807 ^d	2 510 ^d	-	4 ^d	67 ^d
Saint Vincent and the Grenadines	48 ^d	499 ^d	1 814 ^d	-	0 ^d	6 ^d
Sint Maarten	-	-	321 ^d	-	-	13 ^d
Trinidad and Tobago	2 365 ^d	7 280 ^d	26 125 ^d	21 ^d	293 ^d	6 411 ^d
Oceania	2 001	2 321	27 657	68	283	6 759
Cook Islands	1 ^d	218 ^d	836 ^d	-	.. ^{c,d}	5 037 ^d
Fiji	284	356	3 713 ^d	25 ^d	39	51 ^d
French Polynesia	69 ^d	139 ^d	908 ^d	-	-	327 ^d
Kiribati	-	-	15 ^d	-	-	1 ^d
Marshall Islands	1 ^d	218 ^d	1 057 ^d	-	.. ^{c,d}	205 ^d
Nauru	.. ^{c,d}	.. ^{c,d}	.. ^{c,d}	18 ^d	22 ^d	22 ^d
New Caledonia	70 ^d	67 ^d	15 051 ^d	-	2 ^d	582 ^d
Niue	-	6 ^d	.. ^{c,d}	-	10 ^d	22 ^d
Palau	2 ^d	126	177 ^d	-	-	-
Papua New Guinea	1 582 ^d	935	3 877 ^d	26 ^d	210 ^d	315 ^d
Samoa	9 ^d	51 ^d	235 ^d	-	-	25 ^d
Solomon Islands	-	106 ^d	781	-	-	48
Tonga	1 ^d	19 ^d	403 ^d	0 ^d	14 ^d	100 ^d
Vanuatu	-	61 ^d	503 ^e	-	-	23 ^e
Transition economies	..	55 924	724 967	..	20 541	486 892
South-East Europe	..	787	55 114	..	16	3 995
Albania	-	247	4 466 ^d	-	-	239 ^d
Bosnia and Herzegovina	-	-	7 383 ^d	-	-	208 ^d
Montenegro	-	-	4 983 ^d	-	-	422 ^d
Serbia	-	-	29 564	-	-	2 819
The former Yugoslav Republic of Macedonia	-	540	5 140	-	16	112
CIS	..	54 375	657 612	..	20 408	481 382
Armenia	9 ^d	513	5 831 ^d	-	0	206 ^d
Azerbaijan	-	3 735	18 180 ^d	-	1	11 214 ^d
Belarus	-	1 306	17 730	-	24	588
Kazakhstan	-	10 078	129 244	-	16	27 200
Kyrgyzstan	-	432	3 520	-	33	427
Moldova, Republic of	-	449	3 647	-	23	178
Russian Federation	-	32 204	378 543 ^e	-	20 141	431 865 ^e
Tajikistan	-	136	1 887 ^d	-	-	-
Turkmenistan	-	949 ^d	26 203 ^d	-	-	-
Ukraine	-	3 875	63 825	-	170	9 705
Uzbekistan	-	698 ^d	9 002 ^d	-	-	-
Georgia	..	762	12 241	..	118	1 514
Memorandum						
Least developed countries (LDCs) ^g	11 046	37 095	221 524	1 089	2 673	32 490
Landlocked developing countries (LLDCs) ^h	7 471	35 793	301 812	699	1 120	44 799
Small island developing states (SIDS) ⁱ	7 136	20 611	97 692	220	2 048	17 416

Source: UNCTAD, FDI/MNE database (www.unctad.org/fdistatistics).

^a Excluding the financial centers in the Caribbean (Anguilla, Antigua and Barbuda, Aruba, the Bahamas, Barbados, the British Virgin Islands, the Cayman Islands, Curaçao, Dominica, Grenada, Montserrat, Saint Kitts and Nevis, Saint Lucia, Saint Vincent and the Grenadines, Sint Maarten and Turks and Caicos Islands).

^b Directional basis calculated from asset/liability basis.

^c Negative stock value. However, this value is included in the regional and global total.

^d Estimates.

^e Asset/liability basis.

^f This economy dissolved on 10 October 2010.

^g Least developed countries include Afghanistan, Angola, Bangladesh, Benin, Bhutan, Burkina Faso, Burundi, Cambodia, the Central African Republic, Chad, the Comoros, the Democratic Republic of the Congo, Djibouti, Equatorial Guinea, Eritrea, Ethiopia, the Gambia, Guinea, Guinea-Bissau, Haiti, Kiribati, the Lao People's Democratic Republic, Lesotho, Liberia, Madagascar, Malawi, Mali, Mauritania, Mozambique, Myanmar, Nepal, the Niger, Rwanda, Sao Tome and Principe, Senegal, Sierra Leone, Solomon Islands, Somalia, South Sudan, the Sudan, Timor-Leste, Togo, Tuvalu, Uganda, the United Republic of Tanzania, Vanuatu, Yemen and Zambia.

^h Landlocked developing countries include Afghanistan, Armenia, Azerbaijan, Bhutan, the Plurinational State of Bolivia, Botswana, Burkina Faso, Burundi, the Central African Republic, Chad, Ethiopia, Kazakhstan, Kyrgyzstan, the Lao People's Democratic Republic, Lesotho, the former Yugoslav Republic of Macedonia, Malawi, Mali, the Republic of Moldova, Mongolia, Nepal, the Niger, Paraguay, Rwanda, South Sudan, Swaziland, Tajikistan, Turkmenistan, Uganda, Uzbekistan, Zambia and Zimbabwe.

ⁱ Small island developing States include Antigua and Barbuda, the Bahamas, Barbados, Cabo Verde, the Comoros, Dominica, Fiji, Grenada, Jamaica, Kiribati, Maldives, the Marshall Islands, Mauritius, Federated States of Micronesia, Nauru, Palau, Papua New Guinea, Saint Kitts and Nevis, Saint Lucia, Saint Vincent and the Grenadines, Samoa, Sao Tome and Principe, Seychelles, Solomon Islands, Timor-Leste, Tonga, Trinidad and Tobago, Tuvalu and Vanuatu.

Annex table 3. Value of cross-border M&As, by region/economy of seller/purchaser, 2008–2014 (continued)

Region/economy	Net sales ^a							Net purchases ^b						
	2008	2009	2010	2011	2012	2013	2014	2008	2009	2010	2011	2012	2013	2014
Mauritania	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Mauritius	26	37	176	6	13	-	75	136	16	433	- 173	- 418	65	1 219
Mozambique	-	-	35	27	3	2	2 758	-	-	-	-	-	-	-
Namibia	15	59	104	40	15	6	-	-	-	-	-	-	-	-
Niger	-	-	-	-	-	-	-	-	-	-	-	-	185	-
Nigeria	- 597	- 197	476	539	- 159	537	997	418	25	-	1	40	241	2 104
Rwanda	6	9	-	-	69	2	1	-	-	-	-	-	-	-
Senegal	-	-	457	-	-	-	-	-	-	-	-	-	-	-
Seychelles	49	-	19	-	-	-	-	66	13	5	- 78	189	1	-
Sierra Leone	40	-	13	52	-	-	-	-	-	-	-	-	-	-
South Africa	6 815	3 860	3 653	6 673	- 968	195	379	2 873	1 497	1 619	4 291	825	2 246	1 867
Swaziland	-	-	-	-	-	-	- 101	-	-	6	-	-	-	-
Togo	-	-	-	-	-	-	529	20	-	-	353	- 5	-	2
Uganda	1	-	-	-	-	15	- 86	-	-	257	-	-	-	-
United Republic of Tanzania	-	2	60	0	36	-	18	-	-	-	-	-	-	-
Zambia	1	11	272	-	8	-	-	-	-	2	-	-	-	-
Zimbabwe	7	6	-	27	- 296	5	22	1	- 1	-	-	-	-	1
Asia	84 683	38 903	37 723	55 967	33 360	40 183	89 337	102 475	69 556	79 865	80 499	92 819	100 707	137 059
East and South-East Asia	54 553	29 197	27 128	31 714	22 320	33 344	80 653	59 601	41 135	67 218	67 641	78 440	91 009	125 250
East Asia	29 933	16 437	17 855	14 072	11 944	26 914	73 135	40 687	36 520	52 810	51 100	61 861	70 276	103 857
China	17 475	11 017	6 758	11 501	9 524	26 404	52 415	35 878	23 402	29 828	36 364	37 908	50 148	39 580
Hong Kong, China	8 651	3 530	12 684	2 125	2 912	433	17 070	493	6 217	13 318	9 916	16 009	16 459	58 959
Korea, Republic of	1 107	1 962	- 2 063	2 537	- 1 528	- 616	3 843	5 052	6 601	9 952	4 574	5 714	3 765	3 928
Macao, China	593	- 57	33	34	30	213	0	0	- 580	52	-	10	-	3
Mongolia	-	344	57	88	82	- 77	- 80	106	- 24	-	-	-	-	-
Taiwan Province of China	2 106	- 360	385	- 2 212	925	558	- 112	- 843	904	- 339	247	2 221	- 96	1 387
South-East Asia	24 620	12 759	9 273	17 642	10 376	6 429	7 517	18 914	4 615	14 407	16 541	16 579	20 733	21 393
Brunei Darussalam	-	3	-	-	-	0	0	-	10	-	-	-	-	- 1
Cambodia	30	- 336	5	50	- 100	12	31	-	-	-	-	-	-	-
Indonesia	2 744	747	1 384	6 828	477	844	814	757	- 2 402	186	165	315	2 923	1 176
Lao People's Democratic Republic	-	-	110	6	-	-	-	-	-	-	-	-	-	-
Malaysia	2 905	354	2 837	4 429	721	- 749	472	9 111	3 292	2 372	3 380	9 105	2 144	1 056
Myanmar	-	0	-	-	-	-	-	-	-	-	-	-	-	-
Philippines	3 988	1 476	329	2 586	411	890	922	- 150	57	19	479	682	71	3 211
Singapore	13 883	9 871	3 859	1 615	8 023	4 147	4 736	7 832	2 793	8 963	7 948	795	5 986	16 674
Thailand	150	351	461	954	- 65	40	448	1 339	865	2 810	4 569	5 659	9 602	- 721
Viet Nam	921	293	289	1 175	908	1 245	94	25	-	57	-	21	7	- 0
South Asia	12 532	5 931	5 634	13 090	2 821	4 784	5 955	13 376	456	26 626	6 288	2 989	1 621	1 105
Bangladesh	-	10	13	-	-	13	-	-	-	1	-	-	-	- 4
Iran, Islamic Republic of	765	-	-	-	16	-	-	-	-	-	-	-	-	-
India	10 303	5 877	5 613	12 795	2 805	4 763	5 892	13 370	456	26 642	6 282	2 988	1 619	1 084
Maldives	3	-	-	-	-	-	0	-	-	- 3	-	-	-	-
Nepal	13	-	-	4	-	-	-	-	-	-	-	-	-	-
Pakistan	1 377	-	0	247	- 153	8	- 8	-	-	- 13	-	-	2	-
Sri Lanka	71	44	9	44	153	- 0	70	6	-	-	6	1	-	25
West Asia	17 598	3 775	4 961	11 163	8 219	2 055	2 729	29 499	27 965	- 13 979	6 571	11 390	8 077	10 705
Bahrain	335	-	452	30	-	111	-	3 451	155	- 3 674	- 2 723	527	317	- 2 131
Iraq	34	-	11	717	1 727	324	-	-	-	-	-	- 14	8	-
Jordan	877	30	- 99	183	22	- 5	35	322	-	- 29	37	- 2	-	-
Kuwait	506	- 55	460	16	2 230	414	629	3 688	441	- 10 793	2 078	376	258	1 414
Lebanon	108	-	642	46	317	-	-	- 233	253	26	836	80	-	63
Oman	10	-	388	-	- 774	-	-	601	893	- 530	222	354	- 20	0
Qatar	124	298	12	28	169	-	-	6 028	10 276	626	- 790	7 971	3 078	3 796
Saudi Arabia	330	42	297	657	1 429	291	235	1 518	121	2 165	107	294	520	- 674
Syrian Arab Republic	-	2	66	-	-	-	-	-	-	-	-	-	-	-
Turkey	13 982	3 159	1 958	8 930	2 690	857	2 045	1 495	-	- 38	908	2 012	590	398
United Arab Emirates	1 292	299	755	556	366	286	- 215	12 629	15 825	- 1 732	5 896	- 207	3 326	7 964
Yemen	-	-	20	-	44	-	-	-	-	-	-	-	-	-
Latin America and the Caribbean ^c	9 233	- 911	29 013	18 927	22 586	34 797	25 457	2 761	8 160	16 725	16 385	30 735	16 239	8 440
South America	4 205	- 1 680	18 585	15 535	19 471	17 260	20 567	5 980	4 763	13 698	10 312	23 728	12 501	2 386
Argentina	- 1 757	97	3 457	- 295	343	- 76	- 5 334	259	- 80	514	102	2 754	99	42
Bolivia, Plurinational State of	24	- 4	- 16	-	1	74	312	-	-	-	-	2	-	-
Brazil	1 900	84	10 115	15 107	17 316	9 996	14 204	5 480	2 518	9 030	5 541	7 401	2 956	- 2 449
Chile	3 252	1 534	826	514	- 78	2 513	8 662	60	1 701	867	628	10 257	2 771	746
Colombia	- 46	- 1 633	- 1 370	- 1 220	1 974	3 864	681	16	209	3 210	5 085	3 007	6 406	1 629
Ecuador	0	6	357	167	140	108	109	0	-	-	40	-	-	-
Falkland Islands (Malvinas)	48	-	-	-	-	-	-	-	-	-	-	-	-	-
Guyana	1	1	-	3	-	-	-	-	-	-	0	3	-	-
Paraguay	4	- 60	- 1	0	-	-	6	-	-	-	-	-	-	-
Peru	430	34	612	512	- 67	618	1 819	623	417	71	171	319	225	1 041
Suriname	-	-	-	-	3	-	-	-	-	-	-	-	-	-
Uruguay	20	2	448	747	89	162	108	-	-	7	13	0	8	4
Venezuela, Bolivarian Republic of	329	- 1 740	4 158	-	- 249	-	-	- 458	- 2	-	- 1 268	- 16	35	1 372
Central America	2 900	182	8 853	1 157	1 747	16 845	3 711	- 780	3 354	2 949	4 736	6 887	3 577	5 880
Belize	0	-	1	-	-	-	-	-	2	-	-	-	-	-
Costa Rica	405	-	5	17	120	191	3	-	-	-	-	354	50	-
El Salvador	-	30	43	103	- 1	-	-	-	-	-	-	12	-	-
Guatemala	145	-	650	100	- 213	411	15	-	-	-	-	-	-	-
Honduras	-	-	1	23	-	-	-	-	-	-	-	-	104	-

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Annex table 3. Value of cross-border M&As, by region/economy of seller/purchaser, 2008–2014 (concluded)

Region/economy	Net sales ^a							Net purchases ^b						
	2008	2009	2010	2011	2012	2013	2014	2008	2009	2010	2011	2012	2013	2014
Mexico	2 306	129	7 989	1 143	1 116	15 896	3 652	- 190	3 187	2 896	4 274	6 504	3 845	5 372
Nicaragua	-	- 1	-	6	0	130	-	-	-	-	-	-	-	-
Panama	44	23	164	- 235	725	216	41	- 590	165	53	462	18	- 421	509
Caribbean ^c	2 128	588	1 575	2 235	1 368	693	1 179	- 2 440	44	78	1 337	120	162	174
Anguilla	-	-	-	-	-	-	-	- 2	-	- 10	-	-	-	-
Bahamas	-	-	-	-	-	-	-	514	- 254	- 6	- 558	-	- 123	- 374
Barbados	-	-	-	-	-	-	-	-	-	-	-	-	-	- 11
British Virgin Islands	-	-	-	-	-	-	-	- 2 632	- 2 882	- 298	511	444	- 142	- 429
Cayman Islands	-	-	-	-	-	-	-	35	- 2 615	167	1 079	- 174	- 625	- 160
Dominican Republic	- 108	0	7	39	1 264	213	-	-	-	-	-	-	-	-
Haiti	-	1	59	-	-	-	4	-	-	-	-	-	-	-
Jamaica	-	-	-	9	-	-	-	14	28	1	-	-	15	26
Netherlands Antilles ^d	-	-	-	-	-	-	-	14	- 30	- 156	35	- 158	-	-
Puerto Rico	-	587	1 037	1 214	88	1 079	-	- 2 454	22	77	202	120	- 9	- 20
Saint Kitts and Nevis	-	-	-	-	-	-	-	-	-	- 0	-	-	-	-
Trinidad and Tobago	2 236	-	-	973	16	- 600	1 175	-	- 10	-	- 15	-	- 244	168
U.S. Virgin Islands	-	-	473	-	-	-	-	-	4	-	1 150	-	400	-
Oceania	- 742	4	8 844	23	- 67	4	278	906	174	- 4	-	15	78	1 160
American Samoa	-	-	-	-	11	-	26	-	-	-	-	- 29	86	123
Fiji	2	-	1	-	-	0	- 2	-	-	-	-	-	-	-
French Polynesia	-	-	-	-	-	-	-	-	1	-	-	44	-	-
Marshall Islands	-	-	-	-	-	-	258	136	0	-	-	-	3	- 79
Micronesia, Federated States of	-	-	-	-	-	-	-	-	-	-	-	-	4	-
Nauru	-	-	-	-	-	-	-	-	172	-	-	-	-	-
Norfolk Island	-	-	-	-	-	-	-	-	-	-	-	0	-	-
Papua New Guinea	- 758	0	8 843	5	- 78	-	- 2	1 051	-	- 4	-	-	-	1 116
Samoa	13	-	-	-	-	-	-	- 324	-	-	-	-	- 14	-
Solomon Islands	-	-	-	19	-	-	-	-	-	-	-	-	-	-
Tokelau	-	-	-	-	-	-	-	-	1	-	-	-	-	-
Tuvalu	-	-	-	-	-	-	-	43	-	-	-	-	-	-
Vanuatu	-	4	-	-	-	3	-	-	-	-	-	-	-	-
Transition economies	25 868	6 934	4 095	32 966	6 825	- 3 820	4 220	11 005	7 789	5 378	13 108	9 296	3 054	1 831
South-East Europe	587	529	65	1 367	3	16	20	- 9	- 174	-	51	2	-	-
Albania	3	146	-	-	-	-	-	-	-	-	-	-	-	-
Bosnia and Herzegovina	9	8	-	-	1	6	10	-	-	-	-	1	-	-
The former Yugoslav Republic of Macedonia	67	-	46	27	-	-	-	-	-	-	-	-	-	-
Serbia and Montenegro	7	3	-	-	-	-	-	- 3	-	-	-	-	-	-
Serbia	501	10	19	1 340	2	9	10	- 7	- 174	-	51	1	-	-
Montenegro	-	362	-	-	-	-	-	-	-	-	-	-	-	-
Yugoslavia (former)	-	-	-	-	-	-	-	-	-	-	-	-	-	-
CIS	25 177	6 391	4 001	31 599	6 822	- 3 838	4 189	11 014	7 963	5 378	12 869	9 294	3 054	1 831
Armenia	204	-	-	26	23	-	30	-	-	-	-	0	-	-
Azerbaijan	2	-	0	-	-	-	-	519	-	-	2	748	-	256
Belarus	16	-	649	10	-	13	- 51	-	-	-	-	-	215	-
Kazakhstan	398	1 621	101	293	- 831	217	- 1 321	1 634	-	1 462	8 088	- 32	-	- 1
Kyrgyzstan	-	-	44	6	- 5	-	-	-	-	-	-	-	-	-
Moldova, Republic of	4	-	-	- 9	-	-	-	-	-	-	-	-	-	14
Russian Federation	18 596	4 620	2 882	29 859	7 201	- 3 901	5 525	7 869	7 957	3 875	4 673	8 302	2 242	1 685
Tajikistan	-	-	-	14	-	-	-	-	-	-	-	-	-	-
Ukraine	5 931	145	322	1 400	434	- 169	7	993	6	40	106	276	597	- 122
Uzbekistan	25	4	1	-	-	3	-	-	-	-	-	-	-	-
Georgia	104	14	30	-	1	2	11	-	-	- 0	188	-	-	-
Unspecified	-	-	-	-	-	-	-	12 645	8 170	16 580	7 158	10 872	10 541	16 573
Memorandum														
Least developed countries (LDCs) ^e	- 2 565	- 765	2 204	501	374	26	3 734	63	-	259	353	- 102	2	23
Landlocked developing countries (LLDCs) ^f	778	1 983	615	634	- 574	258	- 1 062	2 262	- 25	1 727	8 076	544	6	270
Small island developing States (SIDS) ^g	1 571	41	9 038	1 011	- 48	- 596	1 503	1 637	- 35	424	- 824	- 230	- 294	2 065

Source: UNCTAD, cross-border M&A database (www.unctad.org/fdistatistics).

^a Net sales by the region/economy of the immediate acquired company.

^b Net purchases by region/economy of the ultimate acquiring company.

^c Excluding the financial centers in the Caribbean (Anguilla, Antigua and Barbuda, Aruba, the Bahamas, Barbados, the British Virgin Islands, the Cayman Islands, Curaçao, Dominica, Grenada, Montserrat, Saint Kitts and Nevis, Saint Lucia, Saint Vincent and the Grenadines, Sint Maarten and Turks and Caicos Islands).

^d This economy dissolved on 10 October 2010.

^e Least developed countries include Afghanistan, Angola, Bangladesh, Benin, Bhutan, Burkina Faso, Burundi, Cambodia, the Central African Republic, Chad, the Comoros, the Democratic Republic of the Congo, Djibouti, Equatorial Guinea, Eritrea, Ethiopia, the Gambia, Guinea, Guinea-Bissau, Haiti, Kiribati, the Lao People's Democratic Republic, Lesotho, Liberia, Madagascar, Malawi, Mali, Mauritania, Mozambique, Myanmar, Nepal, the Niger, Rwanda, Sao Tome and Principe, Senegal, Sierra Leone, Solomon Islands, Somalia, South Sudan, the Sudan, Timor-Leste, Togo, Tuvalu, Uganda, United Republic of Tanzania, Vanuatu, Yemen and Zambia.

^f Landlocked developing countries include Afghanistan, Armenia, Azerbaijan, Bhutan, Bolivia, Botswana, Burkina Faso, Burundi, the Central African Republic, Chad, Ethiopia, Kazakhstan, Kyrgyzstan, the Lao People's Democratic Republic, Lesotho, The former Yugoslav Republic of Macedonia, Malawi, Mali, Republic of Moldova, Mongolia, Nepal, the Niger, Paraguay, Rwanda, South Sudan, Swaziland, Tajikistan, Turkmenistan, Uganda, Uzbekistan, Zambia and Zimbabwe.

^g Small island developing States include Antigua and Barbuda, the Bahamas, Barbados, Cabo Verde, the Comoros, Dominica, Fiji, Grenada, Jamaica, Kiribati, Maldives, Marshall Islands, Mauritius, Federated States of Micronesia, Nauru, Palau, Papua New Guinea, Saint Kitts and Nevis, Saint Lucia, Saint Vincent and the Grenadines, Samoa, Sao Tome and Principe, Seychelles, Solomon Islands, Timor-Leste, Tonga, Trinidad and Tobago, Tuvalu and Vanuatu.

Annex table 4. Value of cross-border M&As, by sector/industry, 2008–2014 (Millions of dollars)

Sector/industry	Net sales ^a					Net purchases ^b								
	2008	2009	2010	2011	2012	2013	2014	2008	2009	2010	2011	2012	2013	2014
Total	617 649	287 617	347 094	553 442	328 224	312 509	398 899	617 649	287 617	347 094	553 442	328 224	312 509	398 899
Primary	89 495	52 808	67 509	148 857	51 290	40 792	39 948	47 927	27 914	46 838	93 254	3 309	892	14 191
Agriculture, hunting, forestry and fisheries	2 920	730	2 524	1 426	7 585	7 422	581	2 173	1 784	408	366	-1 423	318	-214
Mining, quarrying and petroleum	86 574	52 078	64 985	147 431	43 705	33 370	39 367	45 754	26 130	46 400	92 888	4 732	574	14 405
Manufacturing	193 617	74 408	133 155	202 289	112 211	116 044	145 911	133 981	38 142	127 792	222 833	137 818	96 238	174 312
Food, beverages and tobacco	10 608	5 079	34 762	48 340	18 509	46 041	30 994	-43 041	-467	33 620	31 541	31 671	35 837	33 863
Textiles, clothing and leather	3 831	425	546	4 199	2 233	4 535	2 891	-51	546	2 963	2 449	2 508	1 747	929
Wood and wood products	1 022	612	720	5 060	4 516	2 802	1 368	408	1 425	8 388	3 748	3 589	3 018	2 955
Publishing and printing	-347	-	-8	-223	31	20	194	-284	30	906	-112	65	16	47
Coke, petroleum products and nuclear fuel	90	1 506	1 964	-1 479	-1 307	-663	-9 368	-3 333	-844	-6 802	-2 673	-3 748	-2 003	-16 065
Chemicals and chemical products	76 384	27 752	33 693	77 075	38 524	32 049	72 914	60 802	26 416	46 874	89 702	41 485	28 339	72 428
Rubber and plastic products	925	0	5 471	2 223	1 718	760	824	461	-285	127	1 367	570	368	2 335
Non-metallic mineral products	27 103	2 247	6 549	927	1 619	5 733	1 681	23 126	-567	5 198	1 663	755	3 609	2 251
Metals and metal products	19 507	-972	6 635	5 687	8 891	9 490	3 072	21 660	2 746	5 075	18 375	9 705	649	46 114
Machinery and equipment	8 505	2 180	6 349	14 251	1 285	5 296	12 474	7 837	1 814	5 910	14 564	12 836	6 804	7 179
Electrical and electronic equipment	21 477	19 763	21 278	27 525	22 231	7 516	20 343	47 336	4 713	11 758	39 440	26 821	13 567	16 502
Motor vehicles and other transport equipment	13 569	12 539	8 644	4 299	6 913	1 234	508	9 221	73	6 737	10 899	4 902	1 058	-897
Other manufacturing	10 943	3 277	6 551	14 406	7 048	1 592	8 017	9 839	2 540	7 040	11 870	6 661	3 229	6 671
Services	334 536	160 401	146 430	202 296	164 723	155 312	213 040	435 741	221 562	172 464	237 355	187 097	215 378	210 396
Electricity, gas and water	48 087	59 048	-6 784	21 100	11 923	9 988	17 636	26 510	44 246	-14 841	6 758	3 128	7 739	16 877
Construction	4 568	11 646	10 642	3 062	2 253	3 174	2 345	-2 890	-2 561	-2 001	-1 575	2 774	4 823	992
Trade	29 132	3 554	7 195	15 285	12 730	-4 165	24 579	18 866	3 821	6 104	6 412	23 188	-1 591	28 496
Accommodation and food service activities	6 402	794	1 907	1 494	-501	4 537	16 825	3 507	354	867	684	-1 847	925	16 792
Transportation and storage	14 789	5 456	10 690	16 009	10 401	5 708	10 381	6 993	3 651	7 637	6 595	9 129	3 461	4 944
Information and communication	28 441	45 074	19 213	24 934	34 875	31 079	-61 969	49 461	38 880	19 306	22 954	17 417	26 874	-78 695
Finance	103 585	17 126	58 480	64 698	37 717	49 575	134 861	312 975	125 835	138 016	168 033	113 475	145 893	184 132
Business services	88 408	14 483	30 609	48 283	43 707	43 807	51 630	32 050	7 773	16 864	26 423	18 839	26 593	33 388
Public administration and defence	4 209	1 271	1 380	2 910	3 602	4 078	4 322	-11 118	-594	-4 303	-288	-1 165	-1 049	-4 523
Education	1 225	509	881	685	213	76	1 256	155	51	112	112	317	-1 040	125
Health and social services	2 944	653	9 936	2 947	6 636	4 085	1 892	-730	187	3 815	729	964	2 315	2 652
Arts, entertainment and recreation	1 956	525	1 565	726	971	1 591	6 312	1 116	-77	635	526	275	406	4 923
Other service activities	793	263	715	164	196	1 780	2 769	-1 154	-3	55	-9	615	29	292

Source: UNCTAD, cross-border M&A database (www.unctad.org/fdistatistics).

^a Net sales in the industry of the acquired company.

^b Net purchases by the industry of the acquiring company.

Note: Cross-border M&A sales and purchases are calculated on a net basis as follows: Net cross-border M&As sales by sector/industry = Sales of companies in the industry of the acquired company to foreign MNEs (-) Sales of foreign affiliates in the industry of the acquired company; net cross-border M&A purchases by sector/industry = Purchases of companies abroad by home-based MNEs, in the industry of the acquiring company (-) Sales of foreign affiliates of home-based MNEs, in the industry of the acquiring company. The data cover only those deals that involved an acquisition of an equity stake of more than 10 per cent.

Annex table 5. Cross-border M&A deals worth over \$3 billion completed in 2014

Rank	Value (\$ billion)	Acquired company	Host economy ^a	Industry of the acquired company	Acquiring company	Home economy ^a	Industry of the acquiring company	Shares acquired
1	130.3	Verizon Wireless Inc	United States	Radiotelephone communications	Verizon Communications Inc	United States	Telephone communications, except radiotelephone	45
2	42.2	CITIC Ltd	China	Investment advice	CITIC Pacific Ltd	Hong Kong, China	Steel works, blast furnaces and rolling mills	100
3	23.1	Société Française de Radiotéléphone SA	France	Telephone communications, except radiotelephone	Numericable Group SA	France	Cable and other pay television services	100
4	15.3	Alliance Boots GmbH	Switzerland	Drug stores and proprietary stores	Walgreen Co	United States	Drug stores and proprietary stores	55
5	14.2	Merck & Co Inc-Consumer Care Business	United States	Pharmaceutical preparations	Bayer AG	Germany	Chemicals and chemical preparations, nec	100
6	13.9	Beam Inc	United States	Wines, brandy and brandy spirits	Suntory Holdings Ltd	Japan	Malt beverages	100
7	13.4	Tim Hortons Inc	Canada	Eating places	Burger King Worldwide Inc	United States	Eating places	100
8	11.2	E-Plus Mobilfunk GmbH & Co KG	Germany	Radiotelephone communications	Telefonica Deutschland Holding AG	Germany	Telephone communications, except radiotelephone	100
9	10.0	Grupo Corporativo ONO SA	Spain	Telephone communications, except radiotelephone	Vodafone Holdings Europe SLU	Spain	Radiotelephone communications	100
10	9.1	Concur Technologies Inc	United States	Prepackaged software	SAP America Inc	United States	Prepackaged software	100
11	9.1	Scania AB	Sweden	Motor vehicles and passenger car bodies	Volkswagen AG	Germany	Motor vehicles and passenger car bodies	37
12	8.3	InterMine Inc	United States	Biological products, except diagnostic substances	Roche Holding AG	Switzerland	Pharmaceutical preparations	100
13	7.0	Xstrata Peru SA	Peru	Copper ores	MMG South America Management Co Ltd	Hong Kong, China	Investment offices, nec	100
14	6.8	Athlon Energy Inc	United States	Crude petroleum and natural gas	Encana Corp	Canada	Crude petroleum and natural gas	100
15	6.8	Ziggo NV	Netherlands	Cable and other pay television services	Liberty Global PLC	United Kingdom	Cable and other pay television services	72
16	5.8	Oriental Brewery Co Ltd	Korea, Republic of	Malt beverages	Anheuser-Busch Inbev	Belgium	Malt beverages	100
17	5.7	AS Watson Holdings Ltd	United States	Retail stores, nec	Mayon Investments Pte Ltd	Singapore	Investors, nec	25
18	5.7	Itissalat Al Maghrib SA	Morocco	Telephone communications, except radiotelephone	Emirates Telecommunications Corp	United Arab Emirates	Telephone communications, except radiotelephone	53
19	5.6	Questor Pharmaceuticals Inc	United States	Pharmaceutical preparations	Mallinckrodt PLC	Ireland	Pharmaceutical preparations	100
20	5.4	International Lease Finance Corp	United States	Equipment rental and leasing, nec	AerCap Holdings NV	Netherlands	Equipment rental and leasing, nec	100
21	5.4	Gates Corp	United States	Rubber and plastics hose and belting	Blackstone Group LP	United States	Investors, nec	100
22	5.3	YPF SA	Argentina	Petroleum refining	Argentina	Argentina	National government	51
23	5.2	Brookfield Office Properties Inc	Canada	Operators of nonresidential buildings	Brookfield Property Partners LP	Bermuda	Real estate investment trusts	51
24	5.0	Invensys PLC	United Kingdom	Process control instruments	Schneider Electric SA	France	Power, distribution and specialty transformers	100
25	5.0	Nokia Oyj-Devices & Services Business	Finland	Radio and TV broadcasting and communications equipment	Microsoft Corp	United States	Prepackaged software	100
26	4.9	Oldford Group Ltd	Isle of Man	Amusement and recreation svcs	Amaya Gaming Group Inc	Canada	Amusement and recreation svcs	100
27	4.9	Sky Deutschland AG	Germany	Cable and other pay television services	Kronen Tausend985 GmbH	Germany	Cable and other pay television services	57
28	4.8	Wing Hang Bank Ltd	Hong Kong, China	Banks	OCBC Pearl Ltd	Singapore	Banks	98
29	4.8	Celesto AG	Germany	Drugs, drug proprietaries and druggists' sundries	Dragonfly GmbH & Co KgaA	Germany	Drugs, drug proprietaries and druggists' sundries	74
30	4.7	OAD RN Holding	Russian Federation	Crude petroleum and natural gas	Novy Investments Ltd	Cyprus	Investors, nec	12
31	4.6	Oilanking Partners LP	United States	Natural gas transmission and distribution	Enterprise Products Partners LP	United States	Natural gas transmission	66
32	4.6	TUI Travel PLC	United Kingdom	Travel agencies	TUI AG	Germany	Travel agencies	54
33	4.6	Repsol SA-Liquefied Natural Gas Business	Peru	Natural gas liquids	Royal Dutch Shell PLC	Netherlands	Crude petroleum and natural gas	100
34	4.5	UNS Energy Corp	United States	Electric services	Fortis Inc	Canada	Electric services	100
35	4.3	Bristol-Myers Squibb Co-Diabetes Business	United States	Pharmaceutical preparations	Astrazeneca AB	Sweden	Pharmaceutical preparations	100
36	4.2	ViroPharma Inc	United States	Pharmaceutical preparations	Shire PLC	Ireland	Pharmaceutical preparations	88
37	4.2	Sky Italia Capital	Italy	Cable and other pay television services	Sky Italian Holdings	Italy	Investment offices, nec	100
38	4.0	Noble Agri Ltd	Hong Kong, China	Grain and field beans	Investor Group	China	Investors, nec	51
39	4.0	Grohe AG	Germany	Plastics plumbing fixtures	Investor Group	Japan	Investors, nec	88
40	3.7	Chrysler Group LLC	United States	Motor vehicles and passenger car bodies	Fiat North America LLC	United States	Automobiles and other motor vehicles	41
41	3.5	JPMorgan Chase & Co-Physical Commodities Business	United States	National commercial banks	Mercuria Energy Group Ltd	Switzerland	Petroleum and petroleum products wholesalers, nec	100
42	3.4	Engine Holding GmbH	Germany	Motor vehicle parts and accessories	Rolls-Royce Holdings PLC	United Kingdom	Turbines and turbine generator sets	50
43	3.3	CFR Pharmaceutical SA	Chile	Pharmaceutical preparations	Abbott Laboratories	United States	Pharmaceutical preparations	100
44	3.3	Telefonica Czech Republic as	Czech Republic	Radiotelephone communications	PPF Group NV	United States	Investors, nec	66
45	3.3	Banco Santander(Brasil)SA	Brazil	Banks	Banco Santander SA	Netherlands	Banks	7
46	3.2	Lindorff Group AB	Norway	Adjustment and collection services	Lindorff Group AB SPV	Sweden	Investment offices, nec	100
47	3.2	Cia General de Electricidad SA	Chile	Electric services	Gas Natural Fenosa Chile SpA	Chile	Natural gas transmission	97
48	3.2	Neis Holding A/S	Denmark	Functions related to depository banking, nec	Investor Group	United States	Investors, nec	100
49	3.1	Motorola Mobility Holdings Inc	United States	Radio and TV broadcasting and communications equipment	Lenovo Group Ltd	Hong Kong, China	Electronic computers	100
50	3.1	WILD Flavors GmbH	Switzerland	Flavoring extracts and flavoring syrups, nec	Archer Daniels Midland Co	United States	Cottonseed oil mills	100
51	3.1	Freeport-MoMoRan Oil & Gas LLC-Eagle Ford Shale Assets	United States	Crude petroleum and natural gas	EnCana Oil & Gas(USA)Inc	United States	Crude petroleum and natural gas	100
52	3.1	Castle Peak Power Co Ltd	Hong Kong, China	Electric services	Investor Group	China	Investors, nec	60
53	3.1	Rottapharm SpA	Italy	Pharmaceutical preparations	Meda AB	Sweden	Pharmaceutical preparations	100
54	3.0	Firth Rixson Ltd	United Kingdom	Aluminum rolling and drawing, nec	Alcoa Inc	United States	Rolling, drawing and extruding of nonferrous metals	100

Source: UNCTAD, cross-border M&A database (www.unctad.org/fdistatistics).

a Immediate country.

Note: As long as the ultimate host economy is different from the ultimate home economy, M&A deals that were undertaken within the same economy are still considered cross-border M&As, nec = not elsewhere classified.

Annex table 6. Value of announced greenfield FDI projects, by source/destination, 2008–2014 (continued)

Partner region/economy	World ^a as destination							World ^a as investors						
	2008	2009	2010	2011	2012	2013	2014	2008	2009	2010	2011	2012	2013	2014
	By source							By destination						
Guinea	-	-	-	-	-	-	-	-	67	1 417	556	29	33	6
Guinea-Bissau	-	-	-	-	-	-	-	-	22	-	-	-	-	321
Kenya	494	326	3 552	471	532	585	421	597	1 315	912	2 364	1 017	3 635	2 305
Lesotho	-	-	-	-	-	-	-	12	26	56	512	4	-	-
Liberia	-	-	-	-	-	-	-	2 600	824	5 103	281	53	558	22
Madagascar	-	-	-	-	-	-	-	1 337	164	-	104	216	211	358
Malawi	11	11	-	-	2	-	-	22	710	316	206	23	559	29
Mali	22	11	22	-	-	-	22	400	58	15	0	792	25	52
Mauritania	-	-	-	-	-	-	-	270	-	46	274	350	22	1 312
Mauritius	334	764	2 534	1 577	298	3 273	1 752	323	108	63	1 389	140	51	341
Mozambique	-	-	-	-	58	-	-	6 590	785	3 200	8 928	3 207	6 281	8 801
Namibia	15	-	-	-	289	402	-	1 799	1 501	378	886	764	1 066	184
Niger	-	-	-	-	-	-	-	3 141	-	100	277	-	350	19
Nigeria	671	724	654	1 012	636	2 812	641	28 402	7 807	9 272	3 789	6 277	6 320	10 800
Reunion	-	-	-	-	-	-	-	-	-	-	-	-	-	150
Rwanda	-	15	-	-	22	-	-	265	315	1 663	591	1 202	434	496
Sao Tome and Principe	-	-	-	-	-	-	-	280	-	-	-	150	150	6
Senegal	-	-	-	2	6	389	14	1 324	532	801	81	1 159	1 312	377
Seychelles	-	-	-	-	-	-	-	141	1	130	11	37	156	37
Sierra Leone	-	-	-	-	-	-	-	78	260	230	218	110	611	-
Somalia	-	-	-	-	-	-	-	161	-	34	-	40	378	165
South Africa	4 526	7 503	4 563	28 533	1 982	6 666	5 564	12 199	5 847	5 951	10 845	4 604	5 765	3 833
Swaziland	-	-	-	-	-	-	-	21	11	-	439	7	150	67
Togo	110	151	48	280	55	199	80	146	15	-	-	410	370	22
Uganda	39	44	11	-	-	7	-	2 935	1 431	7 830	2 393	421	816	426
United Republic of Tanzania	11	55	52	51	22	138	297	2 120	431	837	3 112	1 064	782	569
Zambia	-	9	-	-	46	33	-	1 305	2 229	1 206	2 398	747	1 075	2 990
Zimbabwe	670	33	12	-	-	6	556	1 020	1 000	750	5 432	3 103	473	457
Asia	320 547	218 646	170 813	198 878	170 707	171 595	186 257	558 381	403 869	300 605	332 651	228 966	241 266	268 884
East and South-East Asia	155 819	121 350	122 334	126 226	108 398	117 002	145 108	304 815	236 370	198 409	212 085	148 642	158 851	192 612
East Asia	108 541	83 141	86 211	92 672	71 322	93 154	110 991	144 826	127 203	114 474	126 100	97 124	90 942	96 173
China	47 529	25 757	20 472	41 158	19 467	22 092	63 295	121 661	109 145	96 010	105 106	78 547	75 740	77 411
Hong Kong, China	16 025	16 538	7 389	10 799	11 997	53 614	11 832	6 300	7 943	6 075	6 342	7 285	5 943	5 263
Korea, Democratic People's Republic of	-	-	-	-	-	-	-	606	221	-	59	-	227	2
Korea, Republic of	32 897	28 840	30 025	27 499	29 495	11 139	23 412	11 282	4 784	3 793	9 634	6 201	5 934	10 828
Macao, China	70	-	-	-	-	81	-	689	490	221	483	2 356	257	870
Mongolia	-	-	150	-	-	-	-	335	257	1 655	356	249	657	165
Taiwan Province of China	12 020	12 007	28 176	13 216	10 363	6 229	12 453	3 953	4 363	6 720	4 120	2 486	2 185	1 635
South-East Asia	47 278	38 208	36 123	33 554	37 076	23 848	34 117	159 989	109 167	83 936	85 985	51 518	67 908	96 438
Brunei Darussalam	105	-	-	70	-	-	140	379	434	204	5 928	76	45	134
Cambodia	65	209	-	-	189	184	108	3 372	3 747	1 423	2 109	1 540	2 186	2 250
Indonesia	229	1 097	319	4 998	861	366	856	32 608	26 005	13 062	27 600	15 649	10 579	17 330
Lao People's Democratic Republic	185	-	-	-	-	-	81	1 133	2 074	261	1 254	703	459	1 016
Malaysia	16 102	14 362	20 092	3 639	17 694	3 542	9 676	23 411	11 916	15 379	12 906	6 023	6 982	19 190
Myanmar	-	-	-	71	-	160	-	1 377	1 800	435	590	1 995	13 727	4 456
Philippines	604	1 496	2 044	369	545	530	2 023	13 410	9 960	4 741	4 086	4 124	3 744	7 357
Singapore	19 697	13 656	9 498	13 042	15 084	12 903	16 530	12 023	11 541	16 513	18 278	9 072	8 857	11 999
Thailand	7 672	5 784	3 322	10 036	2 527	5 235	3 962	14 754	6 776	9 258	4 039	6 065	5 634	8 870
Timor-Leste	-	-	-	-	-	-	-	-	-	1 000	-	79	-	10
Viet Nam	2 619	1 605	848	1 330	175	928	741	57 521	34 915	21 661	9 197	6 192	15 695	23 828
South Asia	34 253	23 212	20 323	33 177	28 743	15 955	14 220	83 870	66 607	51 883	57 244	39 296	26 368	38 957
Afghanistan	-	-	-	37	-	13	-	256	2 980	303	308	227	320	-
Bangladesh	104	51	113	101	131	1	48	776	523	2 574	514	2 267	912	2 051
Bhutan	-	-	-	-	-	-	-	-	116	70	91	35	183	-
India	32 402	17 382	19 351	32 156	25 974	14 794	13 274	65 437	52 847	41 472	47 461	31 267	18 917	24 976
Iran, Islamic Republic of	425	5 726	638	515	1 563	-	382	7 880	2 771	2 743	1 744	-	80	1 667
Maldives	-	-	-	-	-	-	-	358	401	2 048	902	279	107	108
Nepal	1	-	3	31	151	243	-	580	356	339	95	-	603	390
Pakistan	1 286	22	146	245	92	739	434	7 353	4 389	1 359	2 325	4 153	3 067	7 858
Sri Lanka	33	32	72	93	832	165	84	1 231	2 225	973	3 805	1 068	2 180	1 906
West Asia	130 476	74 085	28 156	39 475	33 565	38 638	26 929	169 696	100 891	50 313	63 321	41 028	56 047	37 316
Bahrain	15 800	14 758	797	734	1 530	618	467	7 488	2 086	2 408	3 850	3 950	1 166	1 018
Iraq	-	20	-	51	-	53	-	25 813	10 970	4 208	8 731	978	15 020	2 270
Jordan	547	897	598	50	1 015	107	553	11 882	2 518	2 143	2 822	1 459	10 938	1 730
Kuwait	15 779	3 394	2 479	2 824	1 215	9 806	399	2 021	763	572	811	614	2 168	238
Lebanon	518	571	268	220	415	166	220	1 938	2 131	1 274	483	222	106	1 182
Oman	173	3 069	107	220	99	466	269	7 757	7 364	3 534	3 664	4 311	1 662	1 528
Qatar	8 495	13 536	1 583	11 508	7 514	1 496	252	18 543	25 033	4 089	3 796	2 089	1 597	1 215
Saudi Arabia	4 896	5 946	1 435	5 627	2 033	2 701	1 926	37 162	14 581	8 315	16 152	7 859	6 351	9 967
State of Palestine	-	-	-	-	15	-	-	1 050	14	15	-	-	7	20
Syrian Arab Republic	357	61	-	219	0	-	-	5 521	3 638	1 992	1 593	3	-	4
Turkey	4 871	3 883	3 075	3 019	4 139	6 803	2 685	19 499	19 619	9 483	11 185	8 996	9 714	4 779
United Arab Emirates	78 988	27 952	17 744	15 003	15 578	16 402	20 159	28 676	11 264	10 866	10 227	10 245	7 141	12 856
Yemen	52	-	70	-	11	21	-	2 345	910	1 413	6	302	178	510
Latin America and the Caribbean ^a	17 856	12 475	22 462	20 724	10 398	20 499	8 689	132 518	112 792	110 077	125 316	77 808	153 023	89 446
South America	15 397	9 983	19 619	9 726	6 661	14 131	4 592	84 077	76 901	86 723	90 590	55 394	68 031	40 528
Argentina	420	875	1 267	533	1 349	1 368	69	5 870	8 491	6 086	11 590	5 837	4 263	3 273
Bolivia, Plurinational State of	-	-	-	-	-	66	-	747	1 912	776	243	10	1 028	502
Brazil	11 027	5 896	11 703	4 281	3 130	9 159	1 590	41 844	34 992	42 325	50 054	30 081	28 317	18 713

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Annex table 6. Value of announced greenfield FDI projects, by source/destination, 2008–2014 (concluded)

Partner region/economy	World ^a as destination							World ^a as investors						
	2008	2009	2010	2011	2012	2013	2014	2008	2009	2010	2011	2012	2013	2014
	By source							By destination						
Chile	772	1 462	2 217	1 791	1 175	1 600	1 421	6 515	15 847	5 721	14 814	10 903	10 195	6 610
Colombia	600	109	3 384	815	812	1 073	392	8 953	3 167	13 048	7 102	3 258	12 191	3 162
Ecuador	69	368	190	81	41	-	2	529	324	108	619	488	803	562
Guyana	-	-	-	-	-	-	-	1 000	12	159	45	302	38	-
Paraguay	-	-	-	-	-	-	-	280	65	369	111	369	401	326
Peru	16	358	27	265	12	400	376	9 791	10 768	11 320	4 332	3 023	5 688	5 464
Suriname	-	-	-	-	-	-	-	107	-	-	160	31	13	-
Uruguay	2	45	2	5	-	11	-	4 356	248	724	1 027	753	1 075	1 160
Venezuela, Bolivarian Republic of	2 491	870	830	1 955	142	453	741	4 084	1 075	6 086	494	338	4 021	755
Central America	1 566	2 438	2 748	10 790	3 725	6 121	3 678	41 651	32 507	20 931	26 937	20 447	76 074	45 611
Belize	-	-	-	13	-	-	-	-	5	1	-	259	100	4
Costa Rica	5	55	119	11	3	114	84	508	1 403	1 711	2 983	677	762	1 363
El Salvador	-	264	145	20	-	55	-	529	718	252	479	230	858	515
Guatemala	48	116	71	146	205	222	7	992	1 108	892	237	384	1 058	379
Honduras	-	-	-	-	37	373	-	1 062	121	246	483	51	548	1 551
Mexico	1 397	1 923	1 701	10 532	3 474	5 291	3 446	35 217	26 173	16 078	20 531	17 706	30 545	33 319
Nicaragua	62	-	246	3	3	31	2	147	751	265	270	350	40 597	725
Panama	54	81	465	65	4	35	139	3 196	2 228	1 487	1 954	790	1 606	7 755
Caribbean ^a	893	55	95	209	12	247	420	6 790	3 385	2 422	7 788	1 968	8 918	3 307
Antigua and Barbuda	-	-	-	-	-	-	-	69	-	-	-	-	-	2 221
Aruba	-	-	-	-	-	-	-	65	-	6	25	65	-	84
Bahamas	10	35	-	1	8	96	37	70	6	68	479	24	16	221
Barbados	-	-	5	32	21	-	-	-	28	122	227	4	-	240
Cayman Islands	608	987	65	483	295	76	464	310	98	248	282	299	6	298
Cuba	7	-	-	31	-	-	133	2 281	958	1 552	446	221	195	19
Dominica	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Dominican Republic	-	39	25	-	-	-	-	2 861	1 336	253	5 307	603	2 858	1 375
Grenada	-	-	-	-	-	-	-	-	-	4	6	30	0	1
Guadeloupe	-	-	-	-	-	-	-	267	-	-	25	-	-	221
Haiti	-	-	8	-	-	9	-	3	49	59	350	45	434	-
Jamaica	880	13	28	168	12	237	232	245	38	37	458	12	1 363	505
Martinique	-	-	13	-	-	-	13	-	6	-	-	15	-	221
Puerto Rico	5	3	20	10	-	1	42	747	681	497	1 071	952	2 555	965
Saint Kitts and Nevis	-	-	-	-	-	-	-	-	-	-	-	65	-	-
Saint Lucia	-	-	-	-	-	-	-	-	1	145	65	-	65	44
Saint Vincent and the Grenadines	-	-	-	-	-	-	-	-	-	-	-	-	-	31
Trinidad and Tobago	-	-	3	-	-	-	-	387	316	24	131	118	1 513	3
Turks and Caicos Islands	-	-	-	-	-	-	1	65	-	31	-	-	221	-
Oceania	69	86	16	185	-	-	0	4 684	2 283	2 486	3 278	1 388	3 066	923
Fiji	-	70	10	-	-	-	0	111	302	-	159	36	12	48
French Polynesia	-	10	-	-	-	-	-	-	-	70	-	-	-	-
Micronesia, Federated States of	-	-	-	-	-	-	-	-	-	-	-	156	-	35
New Caledonia	-	-	-	35	-	-	-	1 400	18	-	10	-	-	-
Papua New Guinea	67	-	7	150	-	-	-	2 638	1 927	2 195	3 045	1 196	3 054	840
Samoa	2	-	-	-	-	-	-	500	-	-	-	-	-	-
Solomon Islands	-	6	-	-	-	-	-	35	36	221	65	-	-	-
Transition economies	22 495	20 549	19 801	16 827	9 737	18 818	5 801	97 848	49 974	46 169	55 628	37 092	29 345	25 650
South-East Europe	660	325	498	182	75	225	148	16 415	5 589	4 937	6 833	7 736	6 345	6 094
Albania	-	-	105	-	-	3	3	3 324	116	58	317	288	56	53
Bosnia and Herzegovina	7	-	19	3	4	38	4	1 981	1 316	277	1 258	1 349	878	1 006
Montenegro	-	-	7	-	-	9	-	715	120	372	424	350	612	1 143
Serbia	653	316	365	146	71	78	142	7 734	3 262	3 775	3 981	4 633	4 223	2 926
The former Yugoslav Republic of Macedonia	-	9	1	33	-	99	-	2 661	776	454	853	1 117	576	966
CIS	21 761	20 195	19 296	16 464	8 895	18 562	5 653	78 919	40 549	40 185	47 100	28 827	21 707	18 701
Armenia	47	-	13	70	120	-	-	590	878	229	658	486	811	281
Azerbaijan	1 215	3 418	569	422	2 883	220	110	1 530	2 063	646	1 384	1 496	1 006	647
Belarus	1 410	395	2 075	109	75	539	222	974	1 143	1 783	1 012	616	594	348
Kazakhstan	350	700	693	343	137	219	419	16 218	1 743	2 379	7 455	1 188	1 386	2 165
Kyrgyzstan	81	31	-	-	-	-	-	463	45	-	277	60	49	70
Moldova, Republic of	537	-	-	0	-	3	-	153	487	271	346	155	282	115
Russian Federation	15 421	14 890	14 885	14 619	4 251	16 376	4 569	46 149	26 583	29 645	22 416	16 683	12 468	12 974
Tajikistan	82	8	-	-	-	-	-	223	539	2	1 060	587	159	482
Turkmenistan	-	-	-	-	-	-	-	4 024	1 262	300	2 219	7	-	35
Ukraine	2 617	754	1 063	901	1 429	1 206	334	7 644	4 463	4 062	2 869	3 061	4 669	1 090
Uzbekistan	-	-	-	-	0	-	-	952	1 344	867	7 404	4 488	285	495
Georgia	75	29	7	181	766	31	-	2 514	3 836	1 047	1 694	529	1 292	855
Memorandum														
Least developed countries (LDCs) ^b	875	589	861	896	1 131	1 624	1 604	52 569	31 192	37 704	31 629	22 061	40 279	47 680
Landlocked developing countries (LLDCs) ^c	3 258	4 312	1 483	1 213	3 500	1 047	1 220	44 241	23 815	22 271	38 535	18 640	17 712	16 398
Small island developing States (SIDS) ^d	1 292	887	2 585	1 928	3 309	3 605	2 021	5 302	3 163	6 101	7 079	2 456	6 504	4 841

Source: UNCTAD, based on information from the Financial Times Ltd, fDi Markets (www.fDimarkets.com).

^a Excluding the financial centers in the Caribbean (Anguilla, Antigua and Barbuda, Aruba, the Bahamas, Barbados, the British Virgin Islands, the Cayman Islands, Curaçao, Dominica, Grenada, Montserrat, Saint Kitts and Nevis, Saint Lucia, Saint Vincent and the Grenadines, Sint Maarten and Turks and Caicos Islands).

^b Least developed countries include Afghanistan, Angola, Bangladesh, Benin, Bhutan, Burkina Faso, Burundi, Cambodia, the Central African Republic, Chad, Comoros, the Democratic Republic of the Congo, Djibouti, Equatorial Guinea, Eritrea, Ethiopia, the Gambia, Guinea, Guinea-Bissau, Haiti, Kiribati, the Lao People's Democratic Republic, Lesotho, Liberia, Madagascar, Malawi, Mali, Mauritania, Mozambique, Myanmar, Nepal, the Niger, Rwanda, Sao Tome and Principe, Senegal, Sierra Leone, Solomon Islands, Somalia, South Sudan, Sudan, Timor-Leste, Togo, Tuvalu, Uganda, the United Republic of Tanzania, Vanuatu, Yemen and Zambia.

^c Landlocked developing countries include Afghanistan, Armenia, Azerbaijan, Bhutan, Bolivia, Botswana, Burkina Faso, Burundi, the Central African Republic, Chad, Ethiopia, Kazakhstan, Kyrgyzstan, the Lao People's Democratic Republic, Lesotho, The former Yugoslav Republic of Macedonia, Malawi, Mali, the Republic of Moldova, Mongolia, Nepal, the Niger, Paraguay, Rwanda, South Sudan, Swaziland, Republic of Tajikistan, Turkmenistan, Uganda, Uzbekistan, Zambia and Zimbabwe.

^d Small island developing countries include Antigua and Barbuda, the Bahamas, Barbados, Cabo Verde, Comoros, Dominica, Fiji, Grenada, Jamaica, Kiribati, Maldives, the Marshall Islands, Mauritius, Federated States of Micronesia, Nauru, Palau, Papua New Guinea, Saint Kitts and Nevis, Saint Lucia, Saint Vincent and the Grenadines, Samoa, Sao Tome and Principe, Seychelles, Solomon Islands, Timor-Leste, Tonga, Trinidad and Tobago, Tuvalu and Vanuatu.

Note: Data refer to estimated amounts of capital investment.

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