Statement, UNCTAD's Work Related to the Development Dimension of International Investment Agreements

Karl P. Sauvant, Columbia University
UNCTAD's work related to the development dimension of international investment agreements

World Trade Organization, Geneva
16 June 1998

STATEMENT

by

Karl P. Sauvant
Chief
International Investment, Transnationals and Technology Flows Branch
Division on Investment, Technology and Enterprise Development
UNCTAD

15 June 1998
DITE/PPR/1998/6
This note has been prepared in response to a request by the WTO Working Group on the Relationship between Trade and Investment which, at its meeting of 30 and 31 March 1998, expressed interest in knowing more about UNCTAD’s work on the development dimension of international investment agreements.

Introduction

Today, most countries are pursuing national policies aimed at attracting FDI, including through the liberalization of their investment regimes (i.e., the reduction of barriers to FDI; the strengthening of standards of treatment of foreign investors; and the pursuit of policies meant to ensure the proper functioning of markets), the granting of legal protection to foreign investors and the adoption of a host of promotional measures.

These national policies are increasingly complemented by agreements dealing with investment at the bilateral, regional, plurilateral and multilateral levels. In order to ensure tangible benefits, such agreements need to contribute to the promotion of growth and development. It is generally agreed that, in an increasingly liberalized and globalized world economy, investment frameworks at the national and international levels should facilitate the equitable integration of developing countries into the international economic system by facilitating increased FDI flows to a wide range of developing countries; equally important, they need to help countries maximize the positive effects of FDI and minimize any negative effects.

UNCTAD’s work on FDI is geared towards development concerns by providing analytical and policy-oriented inputs on the role and impact of FDI policies and by improving the understanding of the issues involved in international investment frameworks. Discussions in different fora show that investment issues -- by their very nature -- touch on the entire range of issues relating to production and the production process. They concern, therefore, complex aspects of national policy in both developed and developing countries alike. This note, after an overview of the work undertaken in UNCTAD, provides in a succinct manner the main elements of relevant discussions carried out so far in UNCTAD. The note concludes with a few basic remarks regarding approaches for identifying the development friendliness of international investment frameworks.

UNCTAD’s work

The prime objective of UNCTAD’s work on international investment agreements is to assist developing countries, including least developing countries, to participate as effectively as possible in international discussions of investment agreements at all levels. More specifically, and with a view towards consensus building, UNCTAD’s work aims at deepening the understanding of the issues involved, exploring the range of issues that need to be considered, identifying interests, and, in particular, ensuring that the development dimension is adequately addressed in investment agreements.

The Midrand conference (UNCTAD IX) requested UNCTAD to provide a forum for international dialogue on FDI issues. In particular, Midrand called on UNCTAD to identify and analyze the development implications of issues relevant to a possible multilateral framework on investment (MFI), beginning with an examination and review of existing agreements, taking into
account the interests of developing countries and bearing in mind the work undertaken by other organizations.

Pursuant to this mandate, UNCTAD's work involves a two-track process that encompasses (i) work in intergovernmental bodies, especially the Trade and Development Board and the Commission on Investment, Technology and Related Financial Issues and its expert meetings dealing with this subject (for which the secretariat provides substantive support), and (ii) activities carried out by the secretariat.

The principal forum in which intergovernmental discussions on issues relating to a possible MFI take place in UNCTAD is the Commission on Investment, Technology and Related Financial Issues, one of the three subsidiary bodies of the Trade and Development Board. The Commission draws on the findings of expert meetings that serve as a forum for the exchange of experiences and substantive debate on existing investment agreements and their implications for development. The meetings of experts have addressed the nature and implications of these agreements, the range of issues addressed by them, the extent to which the development dimension is taken into account and the extent to which issues arising in the context of these agreements are relevant, from a development perspective, to a possible MFI. Two experts meetings have been held so far: the first, held on 28-30 May 1997, dealt with bilateral investment treaties and their development dimension; the second took place on 1-3 April 1998 and focused on regional and multilateral investment agreements.

The secretariat's work relates to identifying and analyzing implications for development of issues relevant to a possible MFI, and consists of the preparation of issues papers; the organization of seminars and symposia; the organization of public and private sector dialogues; and the provision of training.

The main purpose of the issues papers is to examine key concepts and issues relevant to international investment agreements -- such as "national treatment", "admission", "transparency", "operational measures", "transfer of technology", "dispute settlement", "transfer pricing" and "taxation" -- and to present them in a manner that is easily accessible to delegates and other interested parties. Particular attention is given to the way in which the key issues have been dealt with so far in existing international investment agreements, how individual issues interact and the needs and concerns of developing countries.

Regional symposia for decision-makers focus on key concepts and issues relevant to discussions of a possible MFI. The first regional symposium took place in 1997 in Fèz, and was designed for African countries. Other symposia are planned for Asia (India, 15-16 July 1998), the Caribbean (29-30 September 1998), Latin America, Central and Eastern Europe and Central Asia.

A seminar series for negotiators in Geneva has been launched in cooperation with the WTO. The first Geneva seminar took place on 26-27 February 1998, in Glion-sur-Montreux; the second seminar took place on 8-9 June 1998.
Dialogues in the form of round tables between representatives of the civil society and ambassadors in Geneva provide a forum for the discussion of issues related to international investment agreements. The first such event was organized in Geneva in cooperation with the European Round Table of Industrialists in December 1997; a similar event with NGOs took place on 10 June 1998.

Training courses on FDI are being designed for junior diplomats and government officials from capitals (a pilot training course took place in Turin, Italy, in December 1997). In addition, an intensive training course is being developed that aims at a core group of negotiators from developing countries involved in discussions relating to international investment agreements.

*Expert Meetings: main findings*

As mentioned earlier, two Expert Meetings were convened by the Commission on Investment, Technology and Related Financial Issues to examine and review existing agreements on investment and their development dimensions. Discussion in this area began at a first Expert Meeting (May 1997) with an examination of bilateral investment treaties (BITs), their development dimensions and implications for a possible MFI. The rationale for starting with an examination of BITs was that these treaties have been concluded in great numbers over the past 40 years, and especially in the past ten years -- in fact, more than half of the more than 1,300 BITs in existence at the end of 1996 were concluded since 1990. Moreover, although BITs were initially concluded mostly between developed and developing countries at the suggestion of developed countries, such treaties are now increasingly being negotiated between developing countries and between these countries and economies in transition. Bilateral investment treaties, therefore, constitute an international instrument that is familiar to most countries and thus appeared to be a natural point of departure for the exercise.

The experiences of countries with BITs vary considerably. It is generally agreed, however, that BITs are only one factor contributing to the establishment of a favourable investment climate, and they are important as confidence-building signals to foreign investors. Other, more important determinants in attracting investment include the size and growth of the market accompanied by political and macroeconomic stability of the host country, the availability and cost of resources (such as labour, skills and, increasingly, created assets such as innovation capability and patents), preferably coupled with the existence of an adequate physical and business infrastructure. Typically, no single determinant can explain FDI flows or stocks. Usually, it takes many conditions and determinants for an international investment project to take place. Examples include the following:

- When economic and political stability is in place, and policies allow entry of FDI, it is typically the largest countries among both developed and developing countries which account for the largest amounts of inward FDI. Not surprisingly, the largest host developed country in terms of FDI stock is the United States while the largest host developing countries are China, Brazil and Mexico. However, although the latter countries have always been leaders among developing countries in terms of the market size, their FDI stock was built at a time of political and macroeconomic stability.
Apart from natural resources -- a traditional magnet for FDI -- availability of cheap, unskilled labour has been an important factor attracting FDI to developing countries in labour intensive industries and labour-intensive processes of otherwise-capital and skill-intensive industries (such as electronics). Much of this FDI has been located in export-processing zones of developing countries and has taken the form of non-equity arrangements such as subcontracting or original equipment manufacturing contracts. But, again, the availability and the cost of unskilled labour has been a necessary but not sufficient condition for this FDI to take place: if it were so, most of the FDI of this type would be concentrated in the countries with the cheapest and most abundant unskilled labour, such as India or Bangladesh, which is not the case.

In the global economy, man-made resources -- created assets -- rather than natural resources, have become increasingly a significant determinant of FDI. These assets may be embodied in individuals (e.g., all types of skills, ranging from technical to managerial skills) as well in enterprises (e.g., innovatory capabilities, marketing skills, sales network, research laboratories). These assets are sought by transnational corporations in both developed countries (where they explain a large part of Mergers and Acquisitions, driving FDI in these countries) as well as developing countries (where they explain, for example, large investments by TNCs in the automobile industry in Mexico, for exports to the United States).

These are only selected examples that illustrate some key determinants of inward FDI. On the top of this are countries’ efforts to attract FDI by using an increasingly elaborate set of promotional tools. To help countries understand how these various determinants work and interact, and which of them are more important than others, the World Investment Report 1998 will specifically address this question.

The second Expert Meeting focused on regional and multilateral instruments and in particular, their objectives and the question of definition of investment in existing investment agreements. As regards objectives, it was considered in the deliberations that the ultimate objective of international investment agreements was growth and development. It was recognized that a stable, transparent and predictable investment framework, providing security for investments, helps to attract investment flows which could contribute to employment, technology transfer, the strengthening of domestic capacities and the improvement of efficiency and competitiveness. This could contribute to promoting the integration of developing countries into the world economy, with a view towards sharing in the benefits of globalization and strengthening domestic capacities. There was moreover a general feeling that all stakeholders, including civil society and domestic investors, should be heard through dialogues and other appropriate mechanisms, so as to shed further light on the interrelationships between international investment agreements and economic growth and development. (See UNCTAD (1998), Report of the Expert Meeting on Existing Regional and Multilateral Investment Agreements and their Development Dimensions. (Geneva, 1-3 April 1998). TD/B/C.OM.2/11).

It has been stressed that international investment agreements, and especially those involving developing countries, need to take into account the development needs of developing countries. In this respect, and in order to facilitate discussions, the secretariat has begun to catalogue -- on the basis of the Expert Meetings -- elements that could be used to evaluate the
conditions under which international investment agreements could be conducive to economic
development. The beginning of such a catalogue of “development-friendly elements” are
contained in a very informal and preliminary note that is available to delegations upon request.
These elements are not listed in any particular order, and they do not indicate any preference.
They are merely a listing of points expressed by experts during the Expert Meetings.

Before this work is moved forward, it is necessary to reflect whether this is, indeed, the
best approach to deal with the development-friendliness of international investment agreements.

Development-friendliness of investment agreements

Development is the fundamental objective of developing country governments and of the
international community as a whole. To what extent and how this objective can be served by
international agreements that address specifically investment issues is a matter that is currently
obtaining considerable attention. If international agreements can, indeed, be helpful in this
respect, an important issue is how the concerns of the principal actors in this regard—host
countries, home countries, investors—can be addressed in a mutually beneficial manner. It needs
to be recalled in this context that, to a large extent, an investment-friendly environment is also
a development-friendly environment. The requirements of such an environment need, of course,
to be determined carefully.

Indeed, there are various approaches that could be taken in this respect, and they are not
necessarily mutually exclusive. The ones that are outlined below are illustrations:

• One approach is to establish a catalogue of development-friendly elements of international
investment agreements. Such a catalogue could be a checklist of elements -- without
establishing priorities or a hierarchy among them -- of issues and concerns that can be
consulted when negotiating international investment agreements. It would be compiled
to make sure that, when negotiating agreements, negotiators have, indeed, considered all
relevant issues. Given the congruence, to a large extent, of an investment-friendly
environment and a development-friendly environment, such a catalogue would therefore
include virtually all issues that need to be considered in the context of investment
agreements. A more elaborated version of this approach is to analyse each of these
elements in greater detail, including to determine how they contribute -- singly or
collectively -- to the development objective of host countries. Indeed, this kind of analysis
may be necessary in any event because, in practice, it is possible that one element would
counteract another.

• A second approach begins with the recognition that not only the contents (specific treaty
provisions) of investment agreements need to be development-friendly, but their very
structure (overall design or plan) needs to reflect this objective, as should their
implementation (specific actions by various parties involved). The challenge is, of course,
to spell out in operational detail what “structure” means beyond the statement of
objectives. On the other hand, when it comes to “content”, the catalogue of
development-friendly elements appears, of course, relevant.
A third approach would be to identify a set of development objectives that international investment agreements should serve. Such objectives could include, for example, securing a stable, predictable and transparent investment climate; increasing the level and quality of FDI flows; strengthening domestic entrepreneurship; and recognizing the non-discriminatory exercise of governmental regulatory power in pursuing development objectives.

UNCTAD's efforts at identifying the development dimensions of international investment agreements are still at an early stage. Any ideas, suggestions and feedback from this meeting would help us refine and develop further our work and would, therefore, be most welcome.