PART THREE

PROMOTING EXPORT-ORIENTED FDI

INTRODUCTION

Part Two highlighted cases of developing countries and economies in transition that have strengthened their export competitiveness over the past decade and a half, increasing their market shares in dynamic export products as well as moving up the technology ladder from exports of natural resources or low-technology products to those embodying higher technologies. It also drew attention to the role of TNCs in the exports of a number of other countries, including countries that have found new niche markets in the export of services, products or fresh agricultural produce. All these countries have, in one way or another, linked up with TNCs to enhance their export competitiveness. While there are different ways to improve the export competitiveness of a country, the pervasive role of TNCs in world trade makes it important for countries to contemplate how to take advantage of TNC activities in terms of enhancing their own development objectives.

What policy challenges face countries that want to attract export-oriented FDI and benefit from it? What lessons can be drawn from their experiences and the successes of countries that have attracted export-oriented TNC activities? The diversity of the group of winner countries studied in Part Two, as well as the experiences of other countries with substantial involvement in their exports, shows that there is no simple, universal prescription for the promotion of export-oriented FDI. Some countries have chosen a highly pro-active approach, whereas others have managed to expand their exports based on less focused efforts. In general, however, successful experiences have shown that macro-economic stability as well as the availability of appropriate skills, technological capabilities and a strong domestic supplier base are key factors in making a location competitive. It goes well beyond the scope of this report to address the range of broad-based policies that are needed to promote development in these areas.[1]

Rather, the purpose of Part Three is to review a variety of policy tools with direct relevance to FDI that can be used to attract, upgrade and benefit from export-oriented FDI to achieve sustained export competitiveness. Although the focus is narrow, it should be understood that a successful policy approach has to be broad-based and in tune with the broader development strategy of a country. Policy-makers also need a good understanding of the corporate strategies driving export decisions and to adjust policies to changing strategies. While the international restructuring of production activities and the search among firms for more cost-efficient configurations undoubtedly open new opportunities for developing countries, the demands on potential locations are also increasing. Even in such low-technology activities as apparel manufacturing, a higher level of productivity and efficiency is now necessary to compete with other exporters. When it comes to more dynamic industries, few locations have the advantages needed to become an integrated part of TNC production systems. Policy-makers need also to take account of the international regulatory framework affecting trade and investment, as international rules in some cases prohibit the use of instruments applied in the past.

In general, the challenge is related to the need for continuous upgrading of domestic resources. Countries with a strong domestic export base and substantial technological capabilities seek to upgrade into higher-value-added exports. With rising incomes and labour costs, efforts to raise productivity are essential to remain competitive. For those that have attracted FDI into low-technology exports, the key priority is to diversify into higher-value products, which also requires an upgrading of capabilities. Countries that have built up sizeable industries behind protective barriers but not made the transition to dynamic export growth need to consider how FDI can support the reorientation and upgrading of existing industries. In countries with weak industrial and export capacity, the question is how to attract FDI that can help create export capacity in any sector with potential (*WIR99*, pp. 251-252).

Part Three consists of two chapters. The first (chapter VII) considers various policies that have a direct bearing on the ability of countries to attract and benefit from export-oriented FDI and thereby strengthen their export-competitiveness. While most of the discussion concentrates on what host-country Governments can do, the chapter starts by looking at an issue that is largely shaped by home-country policies: access to foreign markets. The analysis in Part Two showed that preferential trade arrangements, production-sharing initiatives and regional integration continue to influence the location of export-oriented activities in some industries. While these arrangements can facilitate access to major markets, some of them are limited in time and their advantages are being eroded by progressive liberalization. The recent rise in the use of certain protectionist measures in major markets creates further uncertainty for export-oriented companies and is a legitimate cause for concern for host developing countries.

With more open markets, host-country Governments can consider a range of measures to improve their long-term attractiveness as a base for export-oriented production by TNCs. In the context of an evolving international regulatory framework, a common concern among developing countries is whether sufficient policy space will be available for them to pursue their development-enhancing policies.

Starting from a clear understanding of how their locational advantages can match the requirements of export-oriented TNCs, host-country policies may aim at:

- Improving access to imported inputs and facilitating trade more generally, through trade liberalization and facilitation measures, given that export-oriented activities (especially in non-resource-based industries) often involve a large proportion of imported inputs.

- Inducing more exports by foreign affiliates through export-performance requirements.

- Lowering production costs and risks by offering incentives to induce new or more export-oriented FDI, taking due account of prevailing WTO and other international rules.

- Setting up export-processing zones (EPZs) with a view to providing efficient infrastructure and removing red tape within the confines of a limited area.

- Developing relevant skills, linkages, industrial clusters and the like.

When appropriate, throughout the policy analysis, lessons are drawn from the experience of developing countries and economies in transition that have successfully used inward FDI to enhance their competitiveness. Care must be taken, however, in applying the lessons: a particular policy may work only in a specific economic, historical, geographical, cultural and political context. Policy choices must reflect the specific circumstances of each location and the locational determinants of specific activities.

The last chapter (chapter VIII) turns to the role of investment promotion. Given their position at the interface between business and government, investment promotion agencies (IPAs) can assume several important roles in promoting export-oriented FDI. Promotional strategies are evolving against the background of a changing global environment for FDI, including increasing competition for such FDI. More and more countries are adopting a focused approach to investment promotion, inspired by the successes of such countries as Costa Rica, Ireland and Singapore. In targeted investment promotion, the work of IPAs is an integral component of broader development strategies. The goal is to attract FDI that maximizes the advantages of a given location and contributes to carefully defined development objectives. The first part of the chapter discusses why, what and how IPAs target their efforts to promote export-oriented FDI, as well as some of the risks and pitfalls that are involved in the process.

IPAs also assume important responsibilities in ensuring that new investment projects are handled efficiently. Even though FDI may be allowed into most economic sectors, screening, licensing and other time-consuming requirements can discourage investors, as can corruption. Investors are not without alternatives and may not be patient. The ongoing restructuring of international production systems underlines the need for IPAs to provide after-care services to existing investors. Such efforts can be important to facilitate retention, expansion or upgrading of current activities and can generate important inputs into a longer-term process of improving a location's attractiveness. Given their close links to the private sector, IPAs can be in a unique position to provide relevant information to other branches of government, so that coordinated action to remove obstacles becomes possible.

The conclusion underlines the need for an adequate policy response to arrive at the ultimate objective of attracting export-oriented FDI: to promote development. This essentially implies a need for FDI policies to be well integrated with policies in other related areas. While export-oriented FDI can bring important benefits to a country, it is nonetheless mainly a complement to domestic capital formation, not a substitute for it. Thus, in countries that have successfully leveraged TNC activities to strengthen export competitiveness in line with long-run development objectives, considerable resources were normally invested in strengthening the domestic skills base and the enterprise sector. Strong domestic skills and other capabilities are necessary to expand or upgrade exports and to benefit fully from the FDI that comes in. It is the interplay between domestic and TNC capabilities that determines how countries build competitiveness and move up the value chain.

Note

1 *WIR99* examined the role of TNCs in enhancing technological capacity and strengthening the skills base of host countries, and *WIR01* analyzed policies to promote linkages between foreign affiliates and domestic suppliers.