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OECD Global Forum on International Investment

GLOBAL FORUM ON INTERNATIONAL INVESTMENT - INAUGURAL CONFERENCE HELD ON 26-27 NOVEMBER 2001 IN MEXICO CITY
NEW HORIZONS AND POLICY CHALLENGES FOR FOREIGN DIRECT INVESTMENT IN THE 21ST CENTURY

SELECTED DOCUMENTATION

Attached for delegates' information and reference are (i) the conference conclusions; (ii) the draft outline of the proceedings to be published in early 2002; (iii) selected presentations; and (iv) the final list of participants.

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PRESS RELEASE ON CONFERENCE CONCLUSIONS

Tuesday, 27 November, 15:00 p.m.

OECD Investment Forum calls for improved enabling policy environment and new partnership for promoting foreign direct investment for development

The OECD Global Forum for International Investment (GFII) "*New Approaches and Policy Challenges for Foreign Direct Investment in the 21st Century*" was launched on 26-27 November in Mexico City, by the Minister of the Economy of Mexico, Luis Ernesto Derbez, and the OECD Deputy Secretary General, Thorvald Moe. This inaugural conference attracted more than 300 experts and representatives from OECD member countries, non-members, multilateral organisations and civil society.

Co-chairs, Juan Antonio García Villa, Vice-Minister of Regulations and Foreign Trade Services, Luis de la Calle Pardo, Vice-Minister of International Trade Negotiations and William Witherell, Director, OECD, summed up the deliberations of the Conference as follows:

FDI is needed more than ever….

We all affirmed the importance of sustained FDI flows in the current juncture of the world economic slowdown. FDI is a powerful engine for achieving the international community's reinvigorated development goals, particularly reducing poverty.

FDI should be strongly linked to local enterprise development and not be confined to small enclaves. An important challenge is to bring in the less developed countries, particularly in parts of Africa and Asia, into the fold of countries, which benefit from FDI inflows.

Policies matter…

We agreed that with the current uncertainty surrounding the short-term economic prospects and FDI, it is all the more necessary to get the conditions right for the forces driving the FDI surge over the last decade to reassert themselves and for reaping the full benefits of existing FDI.

The benefits of FDI do not accrue automatically and are not uniform across sectors and countries. Policies and institutions matter. Experience shows that governments need to go beyond traditional liberal FDI policies. They need to pay more attention to the broad set of regulatory and institutional frameworks conducive to an enabling environment both for foreign investment and domestic entrepreneurship. These include the prevalence of rule of law, more transparent administrative practices, effectively combating corruption, good corporate governance, sound competition policy, as well as protection of labour rights and the environment.

Mexico is a case in point. Its reform efforts are paying off: FDI flows have been very robust, and they have been increasing amid the global economic slowdown.

Forging new partnership for capacity building

Building necessary capacities is key to the coherence of policies and their effective implementation. We all agreed that there was a need to establish strong and new partnerships to contribute to the domestic capacity building efforts in FDI host countries. These partnerships should include host and home countries, multinational enterprises, international organisations and civil society groups. They need to be turned into relevant and effective action. For its part, the OECD remains committed to making this Global Forum on International Investment and its other initiatives open to non-Members and other stakeholders for expertise sharing and broad based dialogue.

Input to UN Financing for Development and other multilateral organisations

The results of the Forum will be shortly published as an input into the preparatory process of the UN Conference on Financing for Development that will take place in Mexico next March. They could also be fed into the investment work taking place in other multilateral organisations.

Contact Persons

For further information, journalists are invited to contact Mehmet Ögütçü, Principal Administrator, OECD Global Forum on International Investment and Non-Members (tel. 33 1 45 24 93 95) or Gabriela Ramos, Head of the OECD Mexico Centre (tel. 52 52 80 03 30 or 52 52 81 38 10). On the Mexican side, the media contact person is Alan Nahum Kain, Director-General of Media Relations at the Mexican Economy Ministry (tel. 52 57 29 91 00 ext. 1200, 1201 or 1202).

All conference documentation including papers, presentations and final list of participants are available the OECD website (http://www.oecd.org/daf/investment) and at Mexico's website (http://www.economia-snci.gob.mx).

NEW HORIZONS AND POLICY CHALLENGES FOR FOREIGN INVESTMENT IN THE 21ST CENTURY

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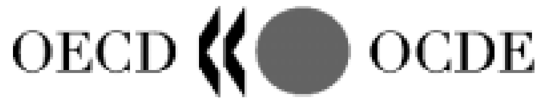


OECD GLOBAL FORUM ON INTERNATIONAL INVESTMENT

NEW HORIZONS AND POLICY CHALLENGES FOR FOREIGN DIRECT INVESTMENT IN THE 21ST CENTURY

Mexico City, 26-27 November 2001

OPENING REMARKS

MR. THORVALD MOE
DEPUTY SECRETARY GENERAL
ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT

Minister Derbez
Ladies and Gentlemen

Introduction
On behalf of the OECD let me warmly welcome all of you to the inaugural conference of the OECD Global Forum on International Investment. I wish to thank our gracious hosts, in particular Minister Derbez, Vice Minister de la Calle and Vice-Minister García Villa, who have contributed to making this event today possible. Our thanks also go to all chairs, speakers, panellists and participants from all over the world, who have come a long way to take part in this gathering.

Many of us in the international investment community feel the need to come together to exchange information, views and ideas on emerging issues in an open and inclusive dialogue. This Forum, which I hope you will consider to be yours, does provide such a platform for all stakeholders and players in the field of international investment.

Objectives
This OECD Global Forum and seven others, created this year, aim at deepening and extending relations with non-OECD members and other dialogue partners in fields where the OECD has particular expertise.

Our aim in doing so has been to create venues for discussing issues that require global solutions. Today's conference represents an important step in this direction.

It is also our hope that the discussions and conclusions of this conference will contribute to the forthcoming UN International Conference on Financing for Development, scheduled to take place in Mexico, next March.

Mexico provides a positive contrast
The growth of international private financial flows, including FDI, in recent decades, has been exceptional, both absolutely and relative to official development aid. This year, however, for the first time in a decade, global FDI flows are expected to shrink. Yet, I believe that, if the right conditions remain in place, the forces that have driven foreign direct investments in the past will soon reassert themselves.

Listening to Minister Derbez's remarks, I could not help but take note of an interesting contrast that Mexico offers. Whereas the worldwide FDI flows are likely to decline this year, Mexico has so far escaped this decline. The preliminary figures for early 2001 show an upbeat trend. This certainly reflects Mexico's efforts to improve its foreign investment regulatory framework and to advance reform in other areas.

The outcome: between 1994 – the first year of NAFTA and the year Mexico acceded to the OECD - and 2000, Mexico received about 85 billion dollars in FDI. This has made Mexico one of the largest recipient countries of FDI in the world.

FDI is needed more than ever
Like Mexico, many other countries are making efforts to attract more FDI. Increasingly, FDI have been recognised as a powerful engine and a major catalyst for achieving development, poverty-reducing growth and global integration process.

Unfortunately, many low-income countries have not benefited from the international investment surge. They have lagged behind in terms of pursuing policies and institutions conducive to their integration in the world economy. Indeed, some areas of the world have been excluded from any of the benefits of globalisation. Intensified efforts are hence needed to foster FDI worldwide. This is especially important for countries and continents such as Africa, which so far have attracted little FDI.

The new technologies, managerial practices and financing techniques of business operations have considerably changed the environment and decision-making process for international investment. At the same time, larger FDI flows also create new challenges to policy makers in host countries, in particular to preserve the capacity to pursue — in a non-protectionist and non-discriminatory way — its own social and environmental objectives.

But we believe that, in general, the best response to this challenge lies in strengthening the environmental and social safeguards, rather than in limiting FDI flows and foregoing the economic benefits that these carry with them. Ensuring that foreign and domestic investment policies, and national environmental and other relevant policies remain mutually supportive raises new challenges for governments. A rethinking of some traditional approaches to FDI is underway.

Governments need to go beyond traditional FDI policies
Today, the vast majority of countries welcomes FDI and have liberalised considerably their rules and regulations. Efforts towards traditional liberal policies (i.e. National Treatment, Most Favoured Nation, investment protection treaties, and market access) are now almost taken for granted. However, while open FDI policies are a necessary pre-condition to attract and maximise the benefits of FDI, they are no longer a sufficient condition. We need to go beyond them.

A wide range of other policies can influence the location and benefits of investment – whether foreign or domestic: strong competition policy, transparency, good corporate governance rules, an efficient public administration, a non-distortionary tax system, adequate standards in the financial sector and in environmental protection. The relevant set of policies also includes government measures that influence institutional effectiveness, infrastructure and skill endowments, macroeconomic and political stability. These and some others are the issues that our speakers and panellists will address in greater detail.

A shared responsibility
Let me stress that the creation of such favourable conditions for maximising the benefits of FDI is largely a shared responsibility of governments in both developing and developed countries, of firms and of international organisations.

With respect to *governments*, it is not enough to preach that developing countries should adopt best policy practices with respect to FDI and improve their governance structures; they need to be assisted by developed countries to build the necessary capacities.

Nearly 80 percent of foreign private investment to the developing world goes to three regions (Asia, Latin America and Central Europe) and twelve countries. For the poorest countries and regions, OECD countries can help in a number of ways. Development assistance is one way. Last year, DAC Members of the OECD gave US$ 53 billion in ODA to developing countries. Though not adequate in current levels, ODA can contribute to raising domestic capacities, and also to leverage private investments in the expansion of essential infrastructure in developing countries.

Providing more adequate and effective level of development assistance would be in the self-interest of OECD Members. Not only is a world with billions of people condemned to poverty unsustainable in the long run, but also expanded investment opportunities for OECD Members will depend upon sustainable economic growth and social stability in every region of the globe.

Multinational enterprises have an equally crucial role to play in promoting development in host countries. Businesses today face an ever-widening circle of expectations . Not only must they satisfy their shareholders, customers and their employees, but also respond to broader environmental and social concerns.

A recent OECD Study, “Corporate Responsibility-Private Initiatives and Public Goals" shows that most large OECD-based multinational enterprises have developed codes of conduct and other voluntary initiatives for corporate responsibility. At the same time, the OECD Study identifies a number of areas where further consideration and action might be particularly useful and relevant.

30 OECD and 5 non-OECD countries have adhered to the OECD Guidelines for Multinational Enterprises. These Guidelines provide a multilaterally endorsed set of comprehensive (and often quite detailed) recommendations for responsible business conduct. The adhering countries want to use them to reinforce the effectiveness of private initiatives for corporate responsibility.

This leads me to the role of the OECD and other international organisations.

Role of OECD and Other International Organisations
International co-operation and the sharing of experience can help all our governments to learn from each other what are the “best practices” in the field of FDI.

For its part, the OECD is actively engaged in open dialogue and experience sharing beyond its membership. Since its creation, the OECD has been at the forefront in developing “rules of the game” for international investment and multinational enterprises.

Today, five non-member countries (Argentina, Brazil, Chile, Estonia and Lithuania) have adhered to the OECD Declaration on International Investment and Multinational Enterprises, a political agreement providing a framework for co-operation on a wide range of investment issues. As a counterpart to their commitments under this instrument, non-member adherents participate in related OECD.

The adherence of Israel, Latvia, Singapore, Slovenia and Venezuela is in process of being negotiated as of this date. Our 2001 Ministerial Council Meeting has called on the OECD to invite other interested non-member countries to adhere to the Declaration.

The need for co-ordination and participation of many donors and international institutions in the field of international investment is particularly important. I am pleased to note that the World Bank, UNCTAD, UNIDO, IMF, Inter-American Development Bank, European Commission are all represented here today. There is a great deal of synergies to be achieved among us in our work on foreign direct investment.

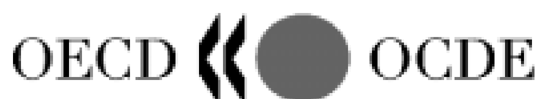
In this respect, the OECD welcomes the results of Doha and pledges its full support for follow-up work at WTO. Together with other international partners, we will contribute to deliberations on how multilateral organisations could help promote FDI in support of sustainable development.

Conclusion

In concluding, let me stress once again that FDI has an important potential to support economic growth, social development and environmental protection, but that its benefits still need to be equally shared and more fully exploited. Capacity building to establish an enabling environment for investment — whether foreign or domestic — is the key. Host countries are not alone in this endeavour. Home countries, companies, multilateral organisations and civil society groups all also share responsibility.

This conference will advance this agenda. I wish you all a fruitful meeting, expressing the hope that each of you will take home new ideas, increased mutual understanding, and even stronger commitment, all of which will benefit the global economy, our economies and our citizens.

Thank you.



OECD GLOBAL FORUM ON INTERNATIONAL INVESTMENT

NEW HORIZONS AND POLICY CHALLENGES FOR FOREIGN DIRECT INVESTMENT IN THE 21ST CENTURY

Mexico City, 26-27 November 2001

OPENING REMARKS FOR THE PLENARY SESSION:
NEW APPROACHES AND OPPORTUNITIES FOR FDI AND DEVELOPMENT

MR. WILLIAM WITHERELL
DIRECTOR, FINANCIAL, FISCAL AND ENTERPRISE AFFAIRS, OECD

The title for this first plenary session is essentially the same as that for the conference – New Horizons and Policy Challenges for Foreign Direct Investment in the 21st Century. This is because this session is meant to help set the scene for the more focussed panel discussions to follow. I hope that as the conference proceeds it will become clear that the word "new" in the title is justified – that the international investment policy scene is a dynamic one, with important developments that need to be taken into account by all interested parties: host and home countries, multinational enterprises and their providers of finance, representatives of the workers, NGOs and the multilateral organizations. We are fortunate to have speakers that are highly qualified to help us identify emerging trends and policy challenges and to evaluate alternative approaches. But it is your active participation in the open discussions that will produce the open and inclusive dialogue that we hope will be the trademark of this and future events of the Global Forum on International Investment.

The high interest in this Forum is evidenced by so many of you making the effort to participate, many traveling long distances to do so. This suggests to me that most if not all present would agree that foreign direct investment (FDI) is now needed more than ever, particularly in the current juncture of the world economic slowdown and the international drive to advance the development and poverty reduction agenda. Indeed, I would argue, FDI is not only a mainstay of development; it also contributes to an environment conducive to international peace and solidarity as well.

As we will hear from Karl Sauvant, for the first time in a decade, global FDI flows are expected to shrink this year for reasons largely related to the global economic slowdown. But I remain optimistic about medium and longer-term economic prospects and I expect that the forces that have driven investments in the past will likely reassert themselves in 2002 and beyond. We should not be satisfied with the prospect of a resumption of global growth in FDI, however, for we still face the important challenge of bringing into the fold the large number of developing and transition economies – particularly the least developed – who have not been able to attract significant FDI flows. While this task can appear daunting in some cases, recent experiences in several African countries demonstrate the positive benefits that can flow from well directed FDI capacity building efforts to establish an enabling environment. As a number of speakers will indicate, it is no long sufficient for a country simple to liberalize its restrictions on FDI - most have already done so. Nor is offering expensive tax and other incentives the key to success. Rather attention should be given to a broader set of policies and institutions, starting with the provision of national treatment, reduction of bureaucratic red tape and a fair and predictable tax system, but including such other policy areas as education, public and corporate governance, the rule of law, anti-corruption, competition policy, property rights, sanctity of contracts, protection of intellectual property, and so on.

A related challenge is how best to maximize the benefits of FDI in ways that do not deter the investment flows in the first place. This requires a better understanding of the various effects of FDI - both positive and negative – and how they work. A number of the speakers will present the latest analyses addressing aspects of this issue. It will be evident from the discussion, I believe, that in developing an enabling environment that will enhance the location's attractiveness to foreign investors, a country will also be adopting those policies and creating those institutions that will help it maximise the net benefits of FDI and of domestic investment as well.

Host countries are not alone in this endeavor of capacity building; home countries, companies, multilateral organizations and civil society groups all share responsibility. As Deputy Secretary General Moe emphasised, there is an acute need to work together in an effective and coherent way towards FDI capacity building in host countries, whether bilaterally, regionally or through multilateral organizations such as the OECD, the World Bank Group, WTO, UNCTAD or other relevant regional/international organizations.

As we enter into this dialogue we should bear in mind several international events to which this meeting could contribute. The first, which is rapidly approaching, is the UN International Conference on Financing for Development that will take place in Mexico next March. Second, the recent Doha Conference has raised the prospect of negotiations on FDI commencing in the WTO in several years if the necessary consensus can be achieved. The issues we will be discussing during the next two days will be very relevant to both of these processes.

OECD GLOBAL FORUM ON INTERNATIONAL INVESTMENT

NEW HORIZONS AND POLICY CHALLENGES FOR FOREIGN DIRECT INVESTMENT IN THE 21ST CENTURY

Mexico City, 26-27 November 2001

THE NEED FOR A BROADER POLICY APPROACH TO FOREIGN DIRECT INVESTMENT

AMBASSADOR MARINO BALDI, SWITZERLAND
AND CHAIRMAN, ADVISORY GROUP ON NON-MEMBERS OF THE
OECD COMMITTEE ON INTERNATIONAL INVESTMENT AND MULTINATIONAL ENTERPRISES

1. Introduction

Foreign Direct Investment (FDI) has long been considered an instrument of exploitation and a threat to national sovereignty in a number of countries. This attitude has considerably changed of late however. Today it is widely recognised that FDI can act as an engine of economic growth. It is, therefore, not astonishing that most countries – whether developed, developing, or in transition – seek to attract FDI to advance their economic development. In particular, developing and transition economies are often in great need of the resources that FDI typically provides: these are, besides capital, intangible resources such as technological know-how and managerial skills.

Home and host countries all have a common interest in maximising the gains from foreign investment and, more generally, from transnational economic activities. They should, therefore, strive for a better understanding of the conditions for increasing the benefits from FDI. The objective of the international community should be to make sure that all countries can benefit from the international division of labour

and the ensuing growth of the world economy. In particular, less developed and transition countries should be supported in their efforts to reap the full benefits of FDI. To achieve this aim, numerous measures have been introduced around the world.

2. Traditional Policies

Let's first look at some of the well-known promotional measures, such as incentives for inward investment by host countries and supporting policies for outward investment by home countries. Afterwards, I should like to discuss what a broader policy approach to FDI, one that would suit the long-term needs of host and home countries in an ever more integrating world economy, could look like.

2.1 Host countries measures

The demand for FDI has sharply increased over the last ten to fifteen years. Governments on all continents now actively compete for FDI. In order to attract their share of the limited FDI supply, host countries apply a variety of measures. These include, on the one hand, fiscal and financial incentives as, for example, a reduction in the base income tax rate, tax holidays or government subsidisation. On the other hand, host countries also adapt their regulatory environment to suit the needs of foreign investors. They may, for example, enhance protection of intellectual property rights; they may, however, also be tempted to relax the enforcement of labour and environmental standards.

Most of these investment incentives have undesirable effects.[1] Fiscal and financial incentives, for example, entail direct costs: expenses of USD 100,000 per expected job are not unusual at all. The indirect costs of such incentives in terms of inefficient resource allocation and market distortions can be even more important. Rent-seeking behaviour by investors, not to mention corruption and bribery, waste scarce resources while investment incentives for foreign investors may lead to discrimination and discouragement of local investors. Such distortions at the expense of domestic enterprises are particularly detrimental in view of the need for many countries to develop a diversified and expanding domestic business sector. For host countries, however, the deployment of local business is key to reaping the full growth potential of FDI.

2.2 Home country measures

Home countries have an interest of their own to promote investment in developing and transition economies, especially in order to foster the internationalisation of their small and medium sized enterprises (SMEs). They support private companies in their endeavours to invest in developing countries by improving awareness of business opportunities in host countries and via financial intermediary instruments such as venture capital, leasing or guarantee funds. In Switzerland, to give a specific example, measures have been designed to meet the needs of investors at the different stages of implementation of a project, from the first draft to its completion. Instruments include a Government sponsored institution that provides information to interested companies, helps them in finding foreign partners and, more generally, offers them assistance during the pre-investment phase; and also a Study Fund that facilitates and financially supports systematic preparation of private investment projects through feasibility studies, pilot projects and

[1] cf. Charles Oman: “Policy Competition for Foreign Direct Investment”, Development Centre Studies, Development Centre of the Organisation for Economic Co-operation and Development, OECD Publications, Paris 2000.

risk-sharing with the promoters. The guiding principle behind this policy is to widen profitable and sustainable investment opportunities in developing and transition countries that are particularly in need of FDI. At the same time, the institutions referred to assume a share of the perceived increased investment risk.

2.3 Bilateral and multilateral instruments

Unlike in the area of trade in goods and services, there exists no global institutional framework governing international investment. International investment is mainly regulated within the scope of regional agreements (integration agreements of different types) and bilateral investment treaties (BITs). Within the OECD, the Codes of Liberalisation of Capital Movements and of Current Invisible Operations together with the Declaration on International Investment and Multinational Enterprises provide a relatively comprehensive and balanced framework for international investment. In terms of investment policy, the guiding principle of these OECD instruments is the concept of National Treatment. This concept reflects the perception that in an economically interdependent world, where countries actively compete for foreign investment, it generally speaking makes no economic sense to treat foreign investors less favourably than domestic ones. All 30 OECD member countries as well as five non-member countries (Argentina, Brazil, Chile, Estonia and Lithuania) already adhere to the Declaration on International Investment, while several other countries are actually undertaking steps to do so.

3. New Approaches

3.1 The concept of ‘functioning markets’

During the 1990s, when FDI flows soared and many of the recipient countries registered amazing growth rates, the various measures taken by host and home countries did in fact seem to be crowned with success. But then, in 1997, the Asian crisis abruptly called traditional policies into question. It suddenly became clear that liberalisation and promotional measures do not by themselves guarantee sustainable economic growth and development. Many economists will argue that this insight was not new. Be that as it may, at least since the Asian crisis, it has widely been accepted that the globalisation of markets and the removal of obstacles to trade and investment can only bear their fruits if the freed market forces are integrated into appropriate national (and international) legal and institutional frameworks. These frameworks should guarantee the rule of law, transparency and accountability of government policies as well as responsible corporate governance: all crucial elements to ensure the long-term ‘functioning of markets’.

The various elements of this concept of ‘functioning markets’ do not as such, i.e., individually, represent new measures. They have to be seen as an ensemble, a coherent set of regulatory and institutional measures that in their interplay are conducive to an enabling environment, both for foreign investment and domestic entrepreneurship. The equal treatment of foreign and domestic investors is, as we have seen, important to no small degree for developing countries. An essential feature of the concept of ‘functioning markets’ is also its long-term orientation, i.e., the inclusion of sustainability concerns. Indeed, ignoring aspects of social and environmental viability in economic policy may, over time, also lead to market failure and disruptions in economic development. Let's now look at some of the key elements of this whole concept:

3.2 Key elements of 'functioning markets'

- The rule of law and good (public) governance

What is most important in order to create and maintain the functioning of markets is the rule of law. This includes, besides basic principles of justice, an efficient judicial system to resolve disputes, and enforcement mechanisms to implement the subsequent decisions. Furthermore, it includes the setting-up of a sound legal framework for business activities in general. Basic economic freedoms, such as property rights, the right to free commercial and industrial activity, and the freedom to enter into private contracts are all essential pillars of such an economic environment based on the rule of law. On an international level, the notion of the rule of law finds its expression, inter alia, in the concept of good (public) governance. Apart from the rule of law, this concept also encompasses responsible government practices and the absence of corruption. There are good reasons for which nowadays the fight against corruption forms an important part of international economic co-operation.

- Corporate governance

Modern economies with numerous transactions involving foreign countries also need sophisticated sets of norms in such fields as company law, capital market law, or contract law and bankruptcy law. The economic rationale of these rules is that they provide transparency and accountability. The Asian crisis has demonstrated how important the observance of such standards is for the stability of economic activities, and that neglecting them can destroy the fruit of otherwise promising prosperity in newly emerging economies practically over night. Some of the principles recommended in this field are generally referred to as corporate governance. They are promoted in various fora, most prominently in the OECD. All stake-holders in companies, be it the shareholders, workers, creditors, suppliers, or the State, are interested in sound business practices in such fields as accounting, managing company finances and dealing with human resources in order to create an environment of confidence and transparency for investment and related economic activities.

- Competition law

An important prerequisite for the 'functioning of markets' is undeniably represented by competition laws. They ensure the contestability of domestic markets, thereby favouring efficiency and dynamism and working against the accumulation of rigidities and harmful oligopolistic rent-seeking behaviour. A state-of-the-art competition law constitutes one of the main pillars to guarantee equal competitive opportunities and to prevent the benefits from liberalized trade and investment from being reduced through collusive practices and abuses of dominant market positions. At an international level, we are far from asking for a harmonized universal competition law, but we recognize the need for convergence of rules and effective international co-operation. The application of multiple and often diverging national antitrust laws on the behaviour of enterprises with transnational activities, i.e., that act in a variety of markets, leads to unwholesome situations which should be avoided in the interest of economic operators as well as of the States involved.

- Core labour standards

Another ingredient that, in my view, should be part of a sustainable economic order is the observance of basic labour standards. By now, this seems to be largely accepted by the participants of the world

economy. In 1998, the International Labour Organization adopted a Declaration on Fundamental Principles and Rights at Work. This instrument calls for freedom of association, effective recognition of the right to collective bargaining, the elimination of all forms of forced and compulsory labour, effective abolition of child labour, and the elimination of discrimination with respect to employment and occupation. I would like to particularly stress the importance of the freedom of association and of the right to collective bargaining. Freedom of association not only creates the basis for a good relationship between employers and employees – which in turn constitutes an important pillar of social stability, but also fosters transparency and accountability, thereby constituting an important prerequisite for public and corporate governance. In addition, freedom of association and the right to collective bargaining guarantee that employees partake in the fruits of economic liberalisation and new technologies, thereby indirectly fostering higher labour productivity.

- Protection of the environment and sustainability

An essential element of long-term ‘functioning markets’ at national and international levels is the protection of our environment and, in particular, our shared global heritage. The fact that we all share the same environment leads to the inevitable need for co-operation among nations to promote sustainable growth and prevent the degradation of the global environment. In this context, let me point to a particular issue in the discussion on international investment. There already exist international instruments that prohibit – or at least discourage – the lowering of environmental standards with a view to attracting FDI. Provisions to that effect would also have been, by the way, an important ingredient of the Multilateral Agreement on Investment (MAI) that was negotiated during the late 1990s. Debates on how such standards can be integrated into existing OECD instruments are continuing.

4. The role of international co-operation

Most of the policies that I just described have to be designed and implemented on a national level; all the more so, since existing international structures would be far too weak to secure their effective enforcement. National policy and lawmakers need, however, the support of the international community. With a view to the integrating world economy, it is crucial that measures be co-ordinated on an international level. This does not imply that national laws have to be identical – nevertheless, a certain functional equivalency of national rules is essential; to achieve this aim, a minimal international consensus on common values is indispensable.

The various issues related to the concept of 'functioning markets' are tackled in many international fora, *inter alia*, the OECD, the Bretton Woods Institutions, the United Nations and the WTO. I would like to take this opportunity to emphasise the pace-setting role of the OECD in the investment field. From its earliest days, member governments have used the Organisation as a mechanism for systematically reducing the extent of their restrictions on international capital flows of all kinds. But, more importantly, the Organisation has never limited its activities to mere liberalisation. The OECD has always adopted a much broader approach. Over the years, it has made a unique contribution to the study and understanding of the economic effects of FDI on the world economy. It has also worked extensively to manage the effects of globalisation through the development of rules and the encouragement of best practices, thereby dealing with important issues such as good public or corporate governance, the behaviour of multinational enterprises, or corruption and bribery. All in all, the OECD has developed a fairly comprehensive and balanced framework to improve the international investment climate and to encourage the positive contributions multinational enterprises can make to economic, social and environmental goals. The various OECD instruments are widely accepted and oftentimes even taken up in other fora, such as the United Nations and the World Bank.

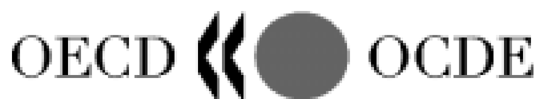
International co-operation should not only involve governments, but also multinational enterprises (MNEs). While governments need to provide an appropriate regulatory framework for investment, it is also important that MNEs conduct themselves as good corporate citizens. Especially in recipient countries, where rules and institutions do not yet allow for long-term sustainable development and stability of liberalized markets, MNEs should make their contribution to 'functioning markets'. They should, for instance, avoid that individual corporations gain undesirable competitive advantages by side-stepping or ignoring international labour or environmental standards. One important instrument towards this goal is the OECD Guidelines for Multinational Enterprises. I could go on talking about the importance of the contributions by MNEs, but will refrain from doing so as the topic is to be discussed in another presentation during this Conference.

5. Final remarks

Traditional policies and measures for attracting or promoting inward investment can, at the utmost, play a complementary role. They do not by themselves attract (sustainable) FDI. We should always bear in mind that investors make their investment decisions on the basis of economic considerations! In other words, FDI tends to flow to countries where investors can expect a reasonable return on capital. And such returns depend primarily on market opportunities, along with sound economic policies and a legal framework that is transparent and predictable. In other words, they depend on 'functioning markets'.

To conclude, let me reiterate that instead of concentrating on measures that are at the most second-best options, countries should focus their endeavours on shaping a pro-business environment in recipient economies and on improving the long-term functioning of markets – a concept that, as we have seen, also takes into account sustainability concerns. How can this concept be turned into effective action? What is needed above all are *new partnerships* between host and home countries – which should possibly also involve multinational enterprises and civil society groups – with a view to contributing to the capacity building efforts in recipient economies.

I hope that this first Conference under the auspices of the OECD Global Forum on International Investment will be a significant step towards this goal.



OECD GLOBAL FORUM ON
INTERNATIONAL INVESTMENT

NEW HORIZONS AND POLICY CHALLENGES FOR FOREIGN DIRECT INVESTMENT IN THE 21ST CENTURY

Mexico City, 26-27 November 2001

GOVERNMENT RESPONSIBILITY: BEYOND TRADITIONAL FDI POLICIES

MR. WESLEY SCHOLZ
DIRECTOR, INVESTMENT AFFAIRS, STATE DEPARTMENT, UNITED STATES
(AND VICE-CHAIRMAN, COMMITTEE ON INTERNATIONAL INVESTMENT AND MULTINATIONAL ENTERPRISES)

- Welcome to Panel B: "*Government Responsibility: Beyond Traditional FDI Policies*."

- This conference and its focus on the policy framework comes at a particularly important time given the slowing global economy and the recent controversy at Doha over the issue of investment rules.

- When I came to my job six years ago, I came as a lawyer masquerading as an economist. As a lawyer I was quite comfortable with the emphasis my office placed on negotiating investment agreements.

- But increasingly I came to understand that the interests of U.S. investors and those countries desirous of their investment were most strongly affected by the policy framework.

- Agreements, whether bilateral investment treaties, regional agreements or multilateral rules could make a contribution, but they were not an end in themselves.

- To often our interlocutors in negotiations came to the table with the view that simply concluding an agreement would cause investment to flow without the need for fundamental changes in policy in key areas.

- Adapting a phrase from the political campaign of our previous President, “It’s the policy stupid.”

- For this reason we should not be too concerned about differences over whether the new Global Trade Round produces comprehensive rules on investment.

- Investment is an area where good policy drives out bad and the competition for investment is the driving force.

- Over aggressiveness in pressing for multilateral rules when there are legitimate concerns among some about their capacity to realize the benefits of existing trade rules can be counterproductive.

- The danger of multilateral negotiations in such an environment is that they tend toward the least common denominator.

- In such circumstances, rulemaking can actually impede the policy reform and liberalization rather than stimulate it.

- All of our governments need to reflect on this as we approach the subject of investment in the New Round. Careful thought will need to be given to how to develop a realistic progressive agenda that will reinforce the reform that is already underway at the national level.

- In particular, proponents of an ambitious negotiating agenda need to modulate their expectations.

- I apologize for this digression, but I believe it does help to put the importance of the issues to be addressed by this panel in perspective.

- Panel B's focus is how governments can adopt and **integrate both traditional and innovative investment policy tools** to fare better in the global competition for investment.

- Earlier speakers have noted the anticipated decline of FDI flows in 2001 and the urgency it brings to **coordinating the broadest possible set of policies** to attract foreign investors.

- As Dept Sec Gen Moe pointed out in his opening remarks, **"traditional liberal FDI policies" i.e. National Treatment, Most Favored Nation, investment protection, and market access**, are only the starting point.

- Although necessary they are **not alone sufficient**.

- They must be complimented by **sound rules on corporate governance, effective public administration, shared responsibility in capacity building, fair and non-distortionary tax policy, effective competition policy an efficient banking and financial sector, and linkages to trade policy.**

- In addition they **must take account** of growing **societal expectations** in home and host countries in other areas such as **environmental protection, improved working standards and respect for human rights**.

- The more effective countries are in integrating policies in all of these areas, the more success they are having in attracting significant flows of foreign investment.

- Economic determinants and locational advantages will remain vital, but increasingly for most countries the competition for foreign investment is being fought and won on the basis of a well integrated policy framework.

- Our **First Speaker, Mr. Vudayagi Balasubramanyam (who kindly introduces himself as "Baloo")** is a Professor of Development Economics, at the Management School of Lancaster University in the United Kingdom. He was educated at the Universities of Mysore, Chicago and Illinois and is a specialist on international trade and investment issues. Widely published, Baloo will be talking to us about the challenges facing policy makers in developing countries -- how best to attract substantial volumes of FDI and utilize it effectively in the promotion of development objectives. Baloo may make a case for multilateral rules for investment and for increased assistance from source countries in much-needed capacity building, especially in the building of government structures.

- Our second speaker, **Ambassador Marino Baldi,** is someone with whom I have had the pleasure of working through the OECD Committee on International Investment and Multinational Enterprises for many years. Ambassador Baldi is a member of the Executive Board of the State Secretariat for Economic Affairs in Switzerland's Ministry of Economic Affairs. He also serves as Chairman of the Advisory Group on Non-Members of the OECD Committee on International Investment and Multinational Enterprises. Ambassador Baldi, in part, responding to some of the points raised by Mr. Baloo, is prepared to speak with us today about the shared responsibility between governments, MNEs, international organizations and other stakeholders, to create favorable conditions for maximizing the benefits of FDI. He will also offer a home (source) country and OECD-member perspective.

- We now turn to our third Panel B presenter, **Mr. Pierre Poret,** another OECD colleague with whom I have had the honor of working over the past years. Mr. Poret is Head of the Capital Movements, International Investment and Services Division in the OECD's Directorate for Financial and Fiscal Affairs. Previously, he served as Deputy Head in the OECD Secretary General's Cabinet. A sound and efficient banking and financial sector is often a key determinant of where investors decide to locate. Mr. Poret will speak to us today about making FDI and financial sector policies mutually supportive.

- **Panel Discussions**

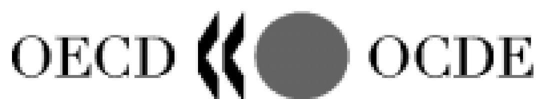
Given the high interest in individual presentations, the conference organizers have given us the opportunity this afternoon to hear from four experts, including OECD Non-Member perspectives.

- To begin this session, I would like to welcome **Ms. Nataliya Yacheistova**, who comes to us from Russia's Ministry for Antimonopoly Policy and Support of Entrepreneurship. She serves as Advisor to the Minister and is a member of the Intergovernmental Council for Competition Policy. Ms. Yacheistova has received training at the European Institute of State Administration, the WTO, the European Commission and at the OECD. The topic of Ms. Yacheistova's talk is "The Russian Experience Regarding the Impact of **Competition Policy on FDI Flows**."

- **Second speaker (TBD)** will address **taxation** issues, focusing on FDI policies regarding tax incentives and transfer pricing. (Will be either a Brazilian or South African speaker.)

- **Mr. Michael Gestrin** comes to us from the OECD Trade Directorate, and in this capacity is excellently positioned to discuss the theoretical and empirical arguments on the proposition that **export-oriented FDI** is better than FDI that is not export oriented. Mr. Gestrin previously served as an economist at UNCTAD where he conducted research on the activities of MNEs and also lectured on international business at the University of Toronto. "Mr. Gestrin, is export-oriented FDI better?"

- Panel B's final panelist comes to us from the world-renowned World Wide Fund for Nature (formerly the World Wildlife Fund). **Ms. Aimee Gonzales** is a Senior Policy Adviser, who will address FDI, the environment and setting a framework for **sustainable development**.



OECD GLOBAL FORUM ON INTERNATIONAL INVESTMENT

NEW HORIZONS AND POLICY CHALLENGES FOR FOREIGN DIRECT INVESTMENT IN THE 21ST CENTURY

Mexico City, 26-27 November 2001

MAKING FDI AND FINANCIAL-SECTOR POLICIES MUTUALLY SUPPORTIVE

PIERRE PORET
HEAD, CAPITAL MOVEMENTS, INTERNATIONAL INVESTMENT AND SERVICES DIVISION, OECD

1. The development of a sound and efficient banking and financial sector is widely recognised as an important ingredient of an effective system of resources allocation and robust growth within national economies. It has also proven to be a key condition for ensuring orderly capital account liberalisation. Finally, a solid domestic infrastructure for banking services and capital markets is among the parameters considered by investors as they decide on the location of their investments.

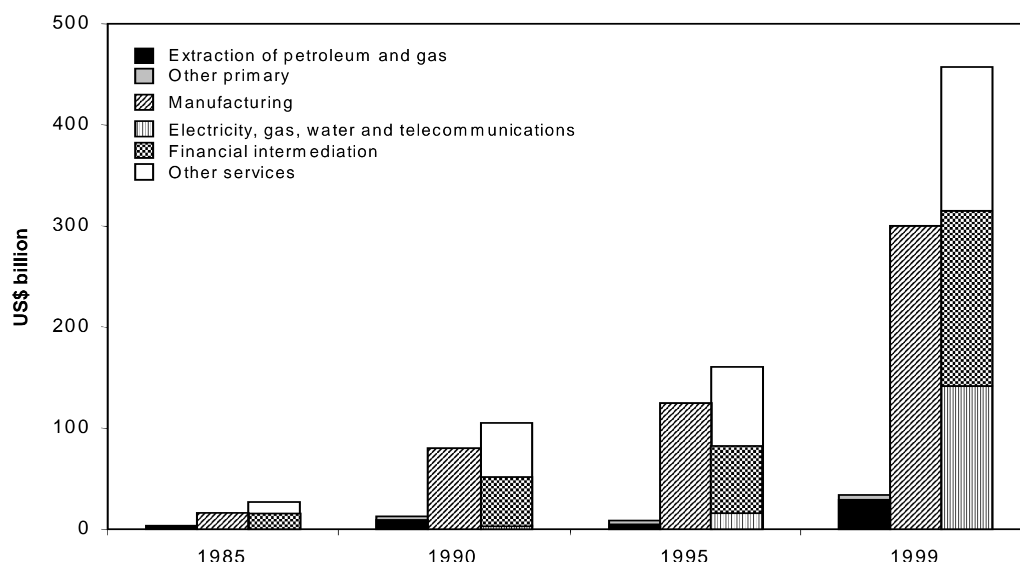
2. This presentation addresses the following question: to what extent can foreign direct investment (FDI) in the banking and financial industry sector support capacity building and more generally enterprise development in this sector?

What are the trends?

3. An important trend in world FDI flows in recent years has been the strong orientation of FDI towards the services sector. More than half of OECD countries' FDI involves the services sector. Banks

and other financial institutions accounted for a very high share of these investments. But only a small part of OECD countries' FDI outflows is directed to developing countries – largely concentrated in a few countries in Latin America and Asia. This suggests that a significant under-exploited potential exist for many other countries around the world to catch up.

Total OECD FDI outflows to selected sectors



Source: Compiled from OECD (2000), International Direct Investment Statistics Yearbook.

4. The orientation of FDI towards services has been accompanied in a number of countries by a significant relaxation of the remaining discriminatory barriers to foreign direct investors' participation in the banking and financial sector. Harmonisation and mutual recognition of regulation has also been an important factor in facilitating FDI in this sector.

5. The experience of some of the former transition and emerging market countries that recently joined the OECD illustrates these policy developments:

-- At the time of their accession to the OECD in 1995-96 OECD Members from Eastern and Central Europe exhibited comparatively few restrictions on FDI in banking and finance. However, the Czech Republic required special approval for foreign ownership of domestic banks, and Poland and Hungary did not allow the establishment of branches by non-resident financial institutions. After the introduction of appropriate non-discriminatory prudential arrangements, these restrictions have now been removed. Slovakia acceded to the OECD in 2000 with no restrictions;

-- When Korea acceded to the OECD in 1996, foreign ownership of domestic financial institutions, as well as other parts of the corporate sector, was subject to discriminatory limitations. While the establishment of foreign bank subsidiaries was not legally forbidden, in practice no licences were given. Formal restrictions existed with respect to certain other categories of foreign institutions. As part of OECD accession commitments toward future liberalisation of FDI, and as a response to the 1997 financial crisis, these restrictions were removed in 1998. The government also announced a policy of ending direct interference in bank management. Promotion and transparent implementation of these measures will be key to their success.

-- Upon accession to the OECD in 1994, Mexico undertook to extend most NAFTA provisions to OECD Member countries, including those fully liberalising the direct establishment of, and direct investment in, several categories of non-bank financial institutions. Mexico also agreed to consider extending the remaining market access benefits accruing to NAFTA-based financial institutions,

which concerned banks, insurance companies and securities dealers. This extension was decided in 1998 and became fully effective in 2001.

What are the potential benefits of FDI in the banking and financial sector?

a) Broadening of the capital base of the banking and financial sector

6. Recent crises in Asia and other countries have revealed the fragility of many national banking sectors. Governments have often had to recapitalise the sector and resolve non-performing loans problems, since they generally had difficulties in finding a sufficient number of large and healthy domestic banks -- or other investors -- to back the failed institutions. Therefore, encouraging take-overs by foreign investors have been used in banking crisis resolution programmes, for example, in the Nordic countries, Hungary, Korea, Mexico and Slovakia. During periods of retrenchment of domestic banks' balance sheets, the entry of foreign institutions may also be needed if the process of credit intermediation is to be maintained, thus paving the way for a faster recovery.

7. Participation by foreign strategic investors in bank privatisation programmes on the basis of transparent and non-discriminatory rules has also proven instrumental in ensuring a timely and effective implementation of these programmes.

b) Transfer of financial know-how and increased efficiency

8. Foreign participation contributes to increased competition between financial service providers. This competition benefits the economy, by providing incentives for adopting improved corporate management standards, reducing overall intermediation costs, improving the quality of risk management and boosting advisory and other services offered to enterprise and household clients. Foreign institutions also allow instant access to key competitive assets such as advanced financial management systems, marketing expertise in retail banking and presence in global markets.

9. In Korea, for instance, increased foreign participation and the resulting enhanced competition are now seen as key to raising managerial skills in local institutions. Another interesting reported example of this is the case of UK commercial banking. When acquiring Midland Bank, HSBC brought with it from Asia a cash-flow method of assessing lending to SMEs, moving away from a traditional collateral approach. This increased possibilities for smaller companies to gain access to bank lending, aligning practice in the UK with that already in place in Thailand and Korea.

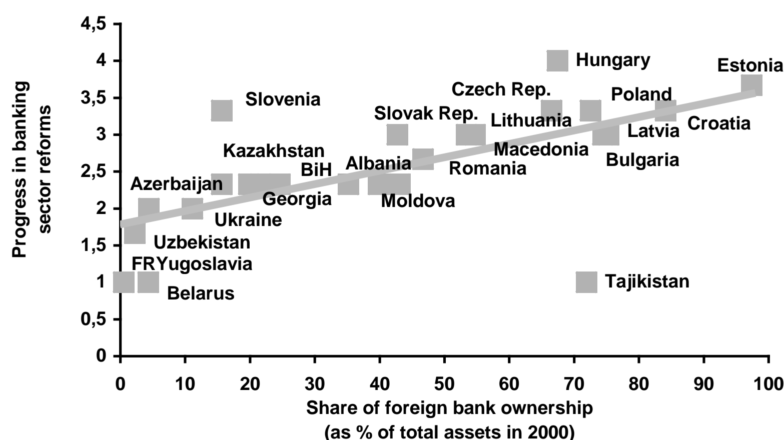
c) Prudential standard upgrading and compliance

10. Local supervisory authorities can enhance prudential standards by opening market access to foreign banks and other financial institutions already subject in their home countries to Basel and to other internationally accepted requirements to capital adequacy, risk management and information disclosure. They are likely to benefit directly from the high standard of prudential surveillance of the entrants, and indirectly to the extent that the entrants promote good standards in the host economy.

11. The presence of foreign financial services competitors, coming from outside established local circles, can also assist the local supervisory authorities as they take steps to limit politically motivated and other connected lending, corruption and other illegal financial activities.

12. In sum, there is broad empirical evidence that foreign involvement helps banking sector development. Using a sample of 21 transition countries, recent findings by EBRD show a clear correlation between the share of foreign bank ownership and a synthetic index of privatisation, interest rate deregulation and other banking sector reform indicators.

Foreign Involvement Helps Banking Sector Reforms



Source: EBRD

Risks of adverse impact

13 The possibility that more efficient foreign financial institutions can crowd out local institutions is real. While the impact in the longer term is beneficial to the industry and the economy as a whole, labour market policies apply to minimise the social costs of adjustment in the short term.

14. Abuse of market position is best combated through appropriate, non-discriminatory competition policy , which, again, is underpinned by a dismantling of entry barriers to the financial services markets. In Hungary, for example, the majority of the banking and financial sector assets are located in institutions originating from other OECD countries. It has been argued that maintaining barriers to cross-border competition in financial services would have amounted to protecting these institutions from overseas competition and depriving the country of the full benefits accruing from the presence of sophisticated foreign-controlled financial institutions

15. It has also been argued that foreign financial institutions are not subject to the same civic spirit and sense of social responsibility as local institutions. In fact, major international banks and other financial institutions are those most often represented in the financial sectors' efforts to develop a reporting framework in support of sustainable development or in the banking sector's initiative for defining good management practice in the fight against money laundering. In addition, while social objectives can be attained by many other means than through the financial sector, nothing should prevent governments from imposing certain non-discriminatory requirements on financial institutions. In the United States, for example, banks are required through the Community Reinvestment Act to recycle a proportion of the deposits they take from poorer regions as loans in those areas.

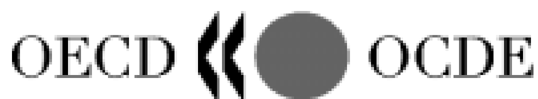
Policy challenges facing governments

16. Maximising the benefits of FDI for financial sector development creates important challenges for governments.

17. The first policy challenge is to establish a broad enabling environment conductive to attracting high quality investors. Such an environment includes *inter alia* transparent regulatory and supervisory practices. Moreover, financial institutions cannot perform efficiently if public governance and other parts of the system work poorly.

18. Once FDI has been attracted to the domestic financial sector, more institutions are therefore in operation. Therefore, a second challenge is to upgrade the regulatory framework and the supervisory authorities' monitoring capacity. In particular, this entails the involvement of host country authorities in bilateral information sharing and other co-operative arrangements with their home country counterparts, as well as active interest in the work undertaken in standard-setting international fora, including the OECD.

19. Thirdly, it must be recognised that the opening up of a domestic financial system to foreign participation has wider structural ramifications. As financial practices become increasingly market based, weak debtors can no longer count on forbearance and evergreening of loans, sectors previously considered as "strategic" lose their special status and financial institutions demand influence on the capital structure of their corporate borrowers. Additional policy measures may be needed in order to deal with the changing environment -- *inter alia* in areas such as improved insolvency rules and foreclosure procedures for the corporate sector. Governments should therefore consider taking steps toward greater financial sector openness in unison with, and as a supplement to, their broader policies toward structural reform in the private sector.



OECD GLOBAL FORUM ON INTERNATIONAL INVESTMENT

NEW HORIZONS AND POLICY CHALLENGES FOR FOREIGN DIRECT INVESTMENT IN THE 21ST CENTURY

Mexico City, 26-27 November 2001

DO CORPORATE RESPONSIBILITY INITIATIVES WORK FOR DEVELOPMENT? AN OECD PERSPECTIVE

PIERRE PORET
HEAD, CAPITAL MOVEMENTS, INTERNATIONAL INVESTMENT AND SERVICES DIVISION, OECD

1. Responsible business conduct by multinational enterprises (MNE) can help countries reap the full benefits of international direct investment for development. The thirty five -- OECD member and non-member -- countries adhering to the Guidelines for Multinational Enterprises wish to work with developing countries in order to strengthen the case that foreign direct investment and corporate responsibility promote economic development and enhances the welfare of citizens around the world.

2. Private initiatives for corporate responsibility are efforts by companies to develop and maintain internal control systems which allow them to comply with market, regulatory and other legitimate expectations. As such they are not new initiatives. Over the last 10 years, however, a major movement of voluntary and often public initiatives among international enterprises has taken place at an unprecedented pace.

3. A recent OECD Study, "*Corporate Responsibility—Private Initiatives and Public Goals*", using databases covering over two thousand organisations in thirty countries shows that most large OECD-based multinational enterprises have participated in this movement in one way or another. These initiatives initially involve the issuance of codes of corporate conduct setting forth commitments in such areas as

labour relations, environmental management, human rights, consumer protection, competition, disclosure and fighting corruption. These codes are often backed up by management systems that help firms respect their commitments in their day-to-day operations. More recent developments include work on management, reporting and auditing standards and the emergence of supporting institutions (for example, professional societies, consulting and auditing services). The OECD Study also identifies a number of areas where further consideration and action might be particularly useful and relevant to Development (e.g. corporate responsibility vis-à-vis the supply chain and issues for extractive industries).

4. The countries adhering to the OECD Guidelines want to use them as a framework to reinforce private initiatives for corporate responsibility. I will not make a detailed presentation of the Guidelines here since the previous speakers have already referred to them – and I understand that the text has been made available to all participants. The text is also available at http://www.oecd.org/daf/investment. The Guidelines, which were first adopted some 25 years ago, provide a multilaterally endorsed set of comprehensive (and often quite detailed) recommendations for responsible business conduct.

5. It is possible to read these Guidelines as an approach to the Development agenda that is now confronting the international community. The approach of the Guidelines is not one of regulation, but rather one that favours co-operation and accumulation of expertise in order to enhance further the benefits of international investment. A few illustrations:

a. In their chapters II, IV and VIII, the Guidelines recommend a series of steps that MNEs should take to facilitate technology diffusion and human capital accumulation in host countries – two areas which have long been recognised as central to growth and productivity increases in less developed countries;

b. In their chapter II and others, MNEs are asked to co-operate with local communities, keeping in mind the distinctive needs of different communities as well as their cultural diversity;

c. The Guidelines also provide that MNEs should refrain from seeking or accepting exemptions from host country regulatory requirements in areas such as environment, labour or financial incentives. This echoes efforts by developing countries to avoid being trapped into some kind of a "race to the bottom" or in a zero sum game of incentive-based competition to attract FDI, which in the long run benefits no country;

d. The Guidelines cover all core labour standards and underline the importance of capacity building in host countries through local employment and training. The recommendations draw on an agreed body of international thought on labour rights, most of it developed in the International Labour Organisation. Far from imposing inappropriate labour standards on developing countries, the Guidelines enhance the positive role that multinational enterprises can play in helping to address the root causes of poverty, through their labour management practices, their creation of high-quality jobs, and their contribution to economic growth.

e. Chapter VI enlists MNEs in the fight against bribery and corruption in host countries – an area which, we know, an increasing number of developing countries' governments now consider central to their reform efforts;

f. Chapter III on disclosure promotes business transparency on the basis of the standards set forth in the OECD Principles of Corporate Governance. Further global dissemination of these standards will promote development by strengthening the effectiveness and robustness of financial systems everywhere.

g. The Guidelines also contain provisions asking MNEs to respect the human rights of all people affected by their operations. While the countries adhering to the Guidelines recognise that governments play the primary role in protecting human rights, companies can help in a number of important ways. Respect of human rights is increasingly viewed as the most fundamental feature of successful market systems. Thus, the business community's assistance in promoting human rights will not only help reduce the suffering caused by human rights abuses, but will promote economic development.

6. The Guidelines have an important complementary role to play in the process of discussion and consensus building. The Guidelines can enhance the visibility and public understanding of private initiatives, thereby making them more effective from companies' point of view and more credible from the point of view of civil society in host and home countries. The Guidelines implementation procedures, which adhering governments are committed to support, can also be used to promote and disseminate management practices that help companies respect appropriate norms for business conduct.

7. At the same time, private initiatives for corporate responsibility raise significant challenges from a developing country perspective.

8. These initiatives can occasionally have "unintended consequences". The background associated with one of the business association codes in the database of the OECD Study shows how problems can inadvertently arise from well-meaning initiatives. The code emerged as a result of what is now an infamous case of unintended consequences of NGO activity -- in this case, in response to the revelation that children were involved in the production of soccer balls in Pakistan. As a result of NGO activity, soccer balls suppliers in Pakistan were instructed to stop employing children immediately, which they did. However, since many of the children had been brought in from surrounding areas to work in factory-type situations, they ended up on the streets without caretakers or family supervision.

9. In a further development of this same episode, soccer ball retailers worked extensively with the ILO and with NGOs to restructure conditions of production in the Pakistani soccer ball industry. Their aim has been the progressive elimination of child labour. This restructuring increased the market share of formal, factory-like production sites ("stitching centres"), while decreasing the market share of "cottage" or home-based production (where it is more difficult to control participation of children). But this shift also undermined the economic autonomy of adult women in the region, who are less involved in factory work than in home-based production. This was another largely unintended consequence.

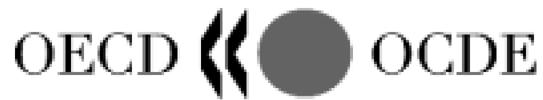
10. These examples underscore the need to proceed carefully with corporate responsibility initiatives and to have adequate knowledge of local conditions. A "one-size-fits-all" approach cannot work.

11. Corporate responsibility raises challenges to host country governments too. More and more, governments' business can no longer be as usual. Private initiatives cannot work if public governance and other parts of the system work poorly. When companies are serious about reputation risk management and their public commitments towards corporate responsibility, they may find situations where they will decide to reduce their investments or even opt for alternative business locations depending on the quality of the governance environment in which they operate. Governments may have to respond to this by adapting and accelerating regulatory reform efforts. However, while regulatory reforms have costs, in the long run they will be beneficial to the country. Experience shows that they are the surest way of attracting and retaining first-class and long-term investors, whether foreign or domestic.

12. Indeed, the notion of corporate social responsibility is not meant to be a substitute to the responsibility of other stakeholders, notably the states themselves. A mutual dependence exists between enterprises and the societies in which they operate: a business sector cannot prosper in a failing society,

and a failing business sector inevitably distracts from general wellbeing. States have the responsibility of ensuring a favourable environment for business, through provision of such services as law enforcement, appropriate regulation, and investment in the many public goods and services used by business. And businesses, beyond their core objective of yielding adequate returns to owners of capital, are expected not only to obey the various laws applicable to them, but also to respond to the societal expectations that are not written down as formal law.

13. Meeting these challenges calls for private-public sector partnership, together with active co-operation among developed and less developed countries – bilaterally or through multilateral institutions, including the OECD. By and large, the Guidelines, with its multi-stakeholder consultation and consensus-building procedures, are the precursor of an emerging global system of governance combining legal requirements, voluntary compliance and co-operative arrangements with a view to ensuring that globalisation works for all.



OECD GLOBAL FORUM ON INTERNATIONAL INVESTMENT

NEW HORIZONS AND POLICY CHALLENGES FOR FOREIGN DIRECT INVESTMENT IN THE 21ST CENTURY

Mexico City, 26-27 November 2001

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