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**Promoting investment, trade, entrepreneurship and related development policies to foster sustained economic growth for sustainable and inclusive development**

## UNCTAD XIII Round Table II – Addressing the policy challenges for sustainable development and enterprise development

Issues note prepared by the UNCTAD secretariat

### I. Background

1. At a time of persistent global imbalances and pressing social and environmental challenges, harnessing sustained economic growth for sustainable and inclusive development is more important than ever. Pro-active investment and enterprise development policies at the national and international level can help promote such growth and generate much-needed development benefits. Policymakers around the globe are striving to identify the best possible options in line with their countries' specific levels of development, locational and entrepreneurial potential and, above all, in line with their overarching development strategies.

2. Over the last decade, at least until the advent of the financial crisis, a number of favourable trends in the global economic environment supported a faster pace of growth across most developing regions. Even so, financing productive investment has remained a constraint on sustained and inclusive growth in many countries. With the steady rise in the minimum scale of investment required to operate in a more open and competitive international environment, enterprise development has become an even bigger policy challenge for many developing countries.

3. Where local capacity to undertake large investment projects is weak, foreign direct investment can make a contribution to industrial upgrading and to the progressive establishment of such local capacity, provided appropriate strategies and regulations are in place. The related policy challenge has become more complicated with the dynamic evolution of the global economy, as exemplified by the growing importance of global value chains and the emergence of non-equity modalities of international production (e.g. contract manufacturing, service outsourcing or contract farming) and the increasingly complex

interactions between different areas of policymaking (e.g. between trade and investment policies and environmental or social policies) and different levels of policymaking (e.g. national, regional and international levels).

4. This Round Table, also part of the 2012 World Investment Forum, aims to help address the complexities of harnessing investment and entrepreneurship for development. It will convene government ministers and heads of international organizations to consider how policies at the nexus between investment, trade and enterprise development can be strengthened to facilitate developing countries' productive capacity-building, industrial upgrading and integration into global value chains.

5. This note serves as a background document for the discussion. More specifically, it sets out (a) the sustainable development contribution of investment and enterprise development; (b) the policy challenges arising when striving to ensure these benefits; and (c) possible ways forward, including the role of multilateral cooperation. The note concludes with (d) a set of questions for the Round Table to address.

## **II. Investment and enterprise development offer valuable contributions for sustainable development**

6. Economic development is primarily driven by domestic private and public investment. Mobilizing such investment remains a major challenge for developing countries, particularly for least developed countries (LDCs) and structurally weak economies that have low levels of domestic savings. Given the huge development financing gaps in these countries, foreign investment can provide a necessary complement to domestic investment. As a source of finance for development, foreign investment has numerous potential benefits. While such benefits exist across all sectors of economic activities, there are some areas where the sustainable development contribution potential of foreign investment is most prominent. Infrastructure, agriculture and sectors related to the green economy are cases in point, although these are also areas that require a carefully balanced regulatory framework for the benefits of foreign investment to materialize.

7. Foreign investment can transfer capital, technology and skills across various sectors. It can generate employment and increase fiscal revenues; it can create trade linkages and strengthen export capacities (for example, by linking domestic companies to global value chains); and it can generate business linkages, spillover effects and other development benefits. The growing importance of global value chains and non-equity modalities can also have an important pro-poor dynamic to the extent that marginalized communities and small suppliers can integrate into global or regional value chains as producers, suppliers or goods and service providers. This offers opportunities by fostering the sustainable development contribution of foreign companies, where socially and environmentally responsible behaviour is ensured. In that context, corporate social responsibility standards, which increasingly span the supply chains and integrated production networks of multinational enterprises, can effectively influence the social and environmental practices of businesses worldwide

8. Foreign investment can be particularly beneficial when it interacts in a synergetic way with domestic and public investment. For example, foreign investment may complement or even strengthen the formation of capital by domestically owned firms and be instrumental in mobilizing domestic productive capacities. If domestic investment levels are low, as is particularly the case in LDCs, there are numerous situations under which foreign and local firms can work together to exploit their respective comparative advantages and achieve mutually beneficial outcomes.

9. The important role of public investment as a countercyclical tool and a State's crucial function as an investor of last resort have gained prominence during the recent economic and financial crisis. Aside from this, public investment is of paramount importance for long-term growth and development, notably through its contribution to the expansion of productive capacities, the stimulation of aggregate demand and the allocation of resources across an economy. Again, agriculture, infrastructure and climate-change-

related investments are cases in point for the mutually beneficial interaction between foreign and domestic, and public and private investment.

10. Linked to all of the above issues is entrepreneurship, one of the most powerful drivers of economic growth. Unleashing entrepreneurial capacity and facilitating start-ups can foster the development of a growth-oriented small- and medium-sized business sector, which in turn can spur job creation, innovation, value added and fiscal revenues. It can facilitate structural transformation and industrial upgrading. Encouraging entrepreneurship can enhance productivity growth and help find practical business solutions to social and environmental challenges, such as developing eco-friendly economic activities or employing women, young people or disadvantaged groups. It is a central characteristic of most competitive economies and has the potential to contribute to inclusive and sustainable development objectives.

11. In sum, foreign investment and domestic enterprise development together can spur a virtuous cycle of growth and development.

### **III. Policy action is required**

12. For foreign investment to contribute effectively to sustainable and inclusive development, a number of policy efforts should be made. For example, measures aimed at attracting foreign investment have to be accompanied by measures aimed at strengthening its sustainable development impact (e.g. by ensuring that investors act responsibly), and by policies to achieve the best possible mix between domestic and foreign, and public and private investment.

13. Policies are also needed to realize the development benefits of global value chains and non-equity modalities. For example, the increasing complexity of global value chains requires countries to increase the competitiveness of their domestic producers and the reliability and efficiency of their production processes. Policy responses are also needed to prevent multinational enterprises from crowding out domestic industries, locking local producers into the lower value added segments of the production process and creating undesirable social and environmental impacts.

14. Finally, there is need for pro-active policies to support entrepreneurship. Currently, dedicated policy initiatives that focus on the birth of new businesses and facilitate the development of micro-, small- and medium-sized businesses are lacking in many countries.

### **IV. Investment policies need to be embedded into countries' overall development strategies**

15. Governments face the challenge of choosing the right investment policy instruments and properly incorporating them into their development strategies. They need to do so in the context of a world economy that appears to be entering a new phase of globalization, one in which inclusive and sustainable development is imperative. As a consequence, a new generation of investment policies is emerging, pursuing a broader and more intricate development policy agenda within a framework that seeks to maintain a generally favourable investment climate.

16. At the national policy level, for example, a more proactive steering of economic development by many governments is leading them to consider targeted policies to improve the investment climate and to channel investment to areas most conducive to sustainable development, including infrastructure, agriculture, and the green economy. In order to harness the benefits of non-equity modalities, policy responses should aim at diversifying a country's industrial base (this is particularly important for LDCs and African countries) and at upgrading their industrial capability in the value chain (especially for middle-income countries).

17. Concerns about the negative social and environmental impacts of investment as well as non-equity modalities, especially in developing countries, have spurred calls for the introduction of policies to promote adherence to standards of corporate behaviour and to strengthen State oversight. Responsible corporate behaviour should be encouraged in activities all along the global value chains of multinational enterprises, including in non-equity modalities.

18. With respect to the interaction between foreign and domestic investment, a key policy challenge lies in identifying the optimal balance between the two, avoiding crowding out and realizing the potential of foreign investment for mobilizing domestic productive capacity-building and maximizing potential linkages and synergies at the different levels of the value chain, ranging from research and development to production. With respect to the interaction between private and public investment, policy challenges include identifying investment projects suitable for public-private cooperation, targeting the most promising types of partnerships for the achievement of development objectives – for example, different types of public-private partnerships – and attaining a fair distribution of costs and risks between the public and private sector. In both scenarios, setting the right policy and regulatory frameworks – for example, by strengthening the rule of law or deciding on the extent of openness or liberalization – is crucial.

19. With regard to the international policy level, international investment agreements (IIAs) can make an important contribution to a stable, predictable and transparent international investment policy environment, facilitating cross-border investment flows. At the same time, they pose a number of systemic and substantive challenges for negotiators, policymakers and other stakeholders. With more than 3,000 core investment treaties, numerous ongoing negotiations and multiple dispute-settlement mechanisms, the universe of IIAs has become almost too large for States to handle, too complicated for firms to take advantage of, and too complex for stakeholders at large to monitor. Furthermore, such agreements face growing concerns about their sustainable development dimension. How to re-balance those agreements, including by using IIA mechanisms to preserve policy space, without substantially reducing the level of protection granted to investors, is a key challenge.

20. To help policymakers tackle the above-mentioned challenges, UNCTAD has developed an investment policy framework for sustainable development, addressing both national and international policy dimensions.

## **V. Investment policies should be complemented by policies stimulating entrepreneurship**

21. In the area of enterprise development, the key policy challenge is that the many different policy domains involved – industrial development, infrastructure, human resources, skills and technology development and financial infrastructure – need to be closely coordinated to maximize synergies and impact. Entrepreneurship policies cannot be dissociated from broader national economic development policies and changing realities. This requires a whole-of-government approach with strong government commitment and coordination across ministries, in partnership with the private sector and other civil society stakeholders.

22. Also in this area, a policy framework may provide a valuable point of reference for policymakers. While there is no one-size-fits-all solution, the entrepreneurship policy framework recently developed by UNCTAD has identified six priority areas that have a direct impact on entrepreneurial activity: (a) formulating national entrepreneurship strategies, (b) optimizing the regulatory environment, (c) enhancing entrepreneurship education and skills, (d) facilitating technology exchange and innovation, (e) improving access to finance and (f) promoting awareness and networking.

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## VI. Multilateral cooperation and the way forward

23. Productive investment and enterprise development are key components of a dynamic global economy. While their importance for sustainable development is unquestioned, devising the right policies remains a major challenge.

24. The above investment- and enterprise-related challenges, together with a broader debate about global economic governance, raise the question of whether countries' policy responses – in their current form – are appropriately focused on promoting investment and entrepreneurship, and on ensuring they effectively deliver on their development promise. The ministerial Round Table offers an excellent opportunity to discuss how to strengthen policies on investment and enterprise development with a view to maximizing the benefits they can generate.

25. The comprehensive policy frameworks on investment and enterprise for sustainable development proposed by UNCTAD and introduced in this note aim to provide substantive guidance and advice for setting policies and to serve as a reference for policymaking at the national and international levels. By considering these frameworks through an exchange of experiences and lessons learned with different policy approaches, the Round Table will help foster policy initiatives for sustainable development. In so doing, it will also distil the visions, strategies and experiences that can contribute to a new policy paradigm for investment, trade (via global value chains) and enterprise development.

26. With this in mind, the ministerial Round Table could explore the following questions:

- (a) What are today's crucial policy challenges in harnessing investment and entrepreneurship for sustainable development? What are countries' experiences in this regard?
  - (b) What can be done to ensure responsible and sustainable foreign investment and maximize its role in mobilizing domestic investment and domestic productive capacity-building? What lessons can be learned from countries' experiences?
  - (c) What can be done to better equip the IIA regime to serve its purpose of promoting investment for development?
  - (d) What can be done to integrate enterprise development policies into countries' overall development strategies with a view to maximizing sustainable development benefits?
  - (e) What new initiatives for international cooperation and coordination in this field can be envisaged?
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