

EREF-2010  
Graz Preparatory Workshop, 23 April 2010

**FDI in Strengthening Regional Knowledge-based  
Competitiveness**

**Recommendations**  
Draft 22/4/2010

Text of Recommendation	EU	Country / Region	Stakeholders
<p><b>1</b> Overall experience shows that FDI can make an <b>important contribution to competitiveness</b> and sustainable development at local, regional and national levels, contingent on the right economic legal and financial conditions at the regional/national level. The general trends indicate that <b>importance of FDI will continue</b> increasing which implies that companies and authorities should pay enhanced and <b>systematic attention to create favourable conditions</b> for incoming and outgoing FDI.</p> <p>FDI can contribute to better international and regional resource allocation, mobilisation of resources in receiving economies, stronger competitive markets, as well as to the development of human capital, employment creation and reduction of poverty.</p> <p>All these positive effects can be achieved only if certain conditions are created and respected, while if this is not the case inward /outward FDI can cause crowding out of local business, unemployment, excessive import/export market dependency, and monopolistic tendencies at domestic market, as well as reduction of local R&amp;D activities or export of jobs</p>	X	X	X
<p><b>2</b> The <b>delicate balance</b> between positive and negative effects of FDI is particularly relevant to <b>economies in transition</b> if motivation of government to sell companies to foreign investors is primarily to obtain liquid capital for filling the budgetary gaps. Equally, this balance can move strongly into negative territory if new private owners of cheaply acquired</p>		X	X

	<p>companies negotiate with foreign investors in less responsible fashion and with limited knowledge and experience in international capital transactions.</p> <p>Authorities in transition economies should therefore <b>develop appropriate FDI strategy and policies, as integral part of the overall regional development strategy</b> in order to secure their genuine national/regional interests. They should protect the existing 'family silver', particularly by retaining competitive manufacturing establishments and lucrative service providers, as well as by not alienating or wasting national/regional RTD potential and engineering skills &amp; experience.</p> <p>This cannot be achieved by discouraging FDI but rather by creating sound economic fundamentals, enhancing competition on the local market and rule of law. Besides improving general infrastructure and business climate for the development of local entrepreneurship, R&amp;D and knowledge creation, engineering skills &amp; experience need to be preserved.</p>			
3	<p>The recent financial and economic crisis had a considerable negative impact on international FDI flows. For the first time ever, developing countries, particularly emerging economies, attracted more FDI than those in the developed world. Despite some protectionist tendencies and backlashes against FDI, it remains an important factor in the regions'/countries' development effort also as part of their exit strategies. Like globalization, FDI is more part of the solution rather than the problem in itself, having proven to be more resilient to the crisis than other forms of international business.</p> <p>Regions/countries should seize the opportunity and <b>use the current crisis as a catalyst to rethink their economic strategies</b> also by making FDI more instrumental for sustainable development.</p>		X	
4	<p>Various studies clearly point out the valuable <b>spillover effects</b> which FDI brings to the region/country, regardless of their type but depending on the local absorptive capacities. Generally, FDI increases the output and competitiveness of the region, even the jobs that may be initially lost in the short term, are often compensated later with an increased demand for new, better skilled and better paid jobs.</p> <p>Geographically disadvantaged regions should put additional efforts in <b>creating the necessary general and political economic environments and policies to attract FDI</b>. The region is responsible to draft a sustainable strategy in order to be able to reap the benefits of FDI, particularly if they are part of an integral, polycentric, national strategy.</p>		X	
5	<p>To optimally benefit from FDI, regions should create appropriate <b>incentive programmes</b> on top of <b>the existing favourable conditions</b> for business investment (sound economic fundamentals, functioning infrastructure, well trained labour force, necessary resources, market access). Overcoming of still persisting <b>attitudinal barriers against FDI</b> (protectionism on the grounds of national interest argument, xenophobia) is the necessary precondition for the effectiveness of such incentives.</p> <p>The incentives programme should <b>aim at foreign investors but should not discriminate against local entrepreneurs</b>. Thus by targeting both foreign and local investors, domestic actors will be able to equally participate in the regional development (i.e spur the development of local clusters, etc). This should lead the way to a more <b>positive and attractive entrepreneurial climate</b>.</p>	X	X	
6	<p><b>Regional incentives programmes and/or regional strategies</b> will often not be sufficient. Ultimately, it is up to the national and regional governments to <b>work together</b> in adopting coherent national/regional development strategies.</p> <p>Most importantly, a <b>decentralized development strategy</b> will provide a much better attraction to FDI than centralized strategies (major FDI are most often found in central/capital and not in peripheral regions).</p>		X	
7	Regional strategies promoting FDI – although being part of regional growth		X	

	strategies/policies – are of limited scope and are only a supplement to national incentive schemes. <b>National programmes are necessary for attracting FDI.</b> National government strategies must give preferential treatment and some priority to <i>underprivileged, remote</i> regions which deserve additional support measures.			
8	<p>According to a World Bank study, FDI incentives offered to foreign investors should be:</p> <ul style="list-style-type: none"> <li>▪ <b>Affordable</b> (<i>forgone income should not severely undermine government revenue streams</i>);</li> <li>▪ <b>Targeted</b> (<i>targets for incentives should be based on research to confirm that they will benefit the country in ways that would not have been possible if there were no incentives, thereby reducing revenue costs</i>), and</li> <li>▪ <b>Simple</b> (<i>incentive administration should permit easy accessibility and determination of eligibility</i>).</li> </ul> <p>FDI incentives should be reviewed and evaluated periodically, and adjusted as necessary. It is recommended that incentives be designed and used with restraint – they should basically address market failures and – to the extent possible – be linked to the FDI results, in terms of generated growth and development. It has also been proven that ‘tax holidays’ are not as instrumental in attracting FDI as originally thought.</p>		X	
9	<p>In line with the above recommendations, a <b>three edge FDI promotion policy</b> has proved to be the most productive:</p> <ul style="list-style-type: none"> <li>▪ Focusing on <b>improving general investment climate</b>, economic fundamentals, infrastructure, coherent (regional) development strategy</li> <li>▪ Policy <b>targeting specific value added activities and tasks oriented incentives</b> aimed at specific development goals of a country/region</li> <li>▪ Targeting <b>specific groups of investors</b> (existing, investment brokers, strategic partners, diasporas, neighbouring countries and promising new actors).</li> </ul>		X	
10	<p>Complementary to the financial/fiscal incentives mentioned above, <b>soft skills such as negotiating and communication skills may prove to be more useful</b> than traditional instruments of attracting FDI.</p> <p>Regions and especially <b>regional investment agencies</b> should therefore recruit staff on the basis of their soft skills, private sector experience and language proficiency.</p>		X	X
11	<p>Instead of general and uniform, more <b>selective discriminatory measures on returnable incentives and fewer grants</b> are recommended; such as those supporting <b>specific functions</b> (application of modern technology, export and R&amp;D promotion, employment generation and ecological projects).</p>		X	
12	<p>In line with previous recommendations, <b>incentives should only be used as icing on the cake</b>, not to substitute sound fundamentals as necessary precondition for sustainable FDI.</p> <p>FDI - which was attracted predominantly by incentives – will often not stay much longer than the period of incentives (subsidisation), specially if they belong to the footloose category of FDI.</p> <p>Giving <b>too much weight on incentives</b> may therefore be <b>counter productive</b>, particularly as sustainability of FDI is a major motive of host country/region. <b>Regions should therefore rely more on other attraction factors in order to enhance sustainable regional development.</b></p>		X	
13	<p><b>There is no one-fit-all strategy</b> for attracting FDI into regions. Promotion programmes are highly idiosyncratic and <b>should be tailored to the specific situation</b> (income per capita, infrastructure, competitive advantages, technological development, knowledge of foreign languages, geographical position, etc) and needs of the regions as well as of the preferred foreign investors.</p>		X	
14	<p>In terms of sectors, FDI in services merit higher priority in the future than manufacturing or extractive industries. Besides finance, tourism, medical services, education and training, <b>off-shoring in general ought to receive greater attention.</b></p>		X	X

	Also, regions should focus on tasks which can be best performed in their specific context (contemporary globalization is increasingly globalization of tasks).			
<b>15</b>	<p>Once foreign investors have established themselves in the region, they <b>should be used as a kind of promoter</b>, characterised by more credibility than conventional promotion campaigns undertaken by official national or regional institutions.</p> <p>FDI should be encouraged to expand its activities, its presence in the region, and effectively <b>climb up the 'value chain'</b> which is also in the interest of the host economy.</p> <p>Therefore, besides attracting new investors <b>after investment service activities should be enhanced</b>.</p>		<b>X</b>	
<b>16</b>	<p>Attention should also be paid to the <b>new types of investors</b> – global in nature – such as the Sovereign Wealth Funds. In part because of different motivations and decision criteria, a different approach is needed to these investors; <b>greater emphasis should be put on economic diplomacy, intergovernmental actions sensitive to cross cultural differences, as well as other noneconomic factors</b>.</p> <p>Even though these factors may well fall under the domain of the country rather than the region, it is up to the <b>regions to address these specific issues when designing its policies and human capital development strategies</b>.</p>		<b>X</b>	