DRAFT AS OF 13 NOVEMBER 2002

FOREIGN DIRECT INVESTMENT AND REGIONAL DEVELOPMENT: *SHARING EXPERIENCES FROM BRAZIL, CHINA, RUSSIA AND TURKEY*

International Conference on Regional Development and Foreign Investment in Brazil
Fortaleza, Brazil
12-13 December 2002

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1. Overview

Attracting sufficient and "quality"[2] foreign direct investment (FDI) and its efficient utilisation is clearly on top of the agendas of most countries and regions. The strong competition for FDI is in itself a testimony to its ability to promote growth and development. As the much-discussed "global market" has become a reality over the last ten years, all countries find it more difficult to stay competitive without FDI, which sustains growth and brings at least four things of value: financial capital, management skills, technology, and access to export markets -- and therefore enhance a country's or region's competitiveness in the global marketplace.

Long-term economic growth is dependent on the ability of people, firms and institutions in a region to compete against other regions, not just locally but around the world. At the same time, with globalisation of production and distribution, there is a better appreciation of the ways in which business depends as much on co-operation as on competition. For a region to be economically active internationally, its firms, institutions and people would have to make connections and alliances with partners abroad. Rapid technological change, extended markets and a greater demand for knowledge are offering new opportunities for regional development.

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[2] The quality FDI usually comes from OECD-based multinational enterprises (MNEs) and has a strong export orientation along with strong forward and backward links to the domestic sector. It also brings high skills and technology spillovers, which makes a clear difference from the "low quality" FDI having few such linkages and not adding to the competitive strength.

Yet, there should be no illusion: the experience shows that FDI is not a panacea to the development of underdeveloped regions – perhaps complementary to national efforts, depending on the comparative advantages and location of the region. In underdeveloped regions where many of market imperfections prevail, FDI could make a second best policy option. Many countries attach high importance to develop their relatively underdeveloped regions for political or social objectives, but private investment cannot be allocated. It needs to be competed for and won.

In general, foreign investors are influenced by three broad groups of factors: (i) the profitability of the projects, (ii) the ease with which subsidiaries' operations can be integrated into investors' global strategies, and (iii) the overall quality of the host country's enabling environment. FDI, without policy intervention, will likely flow into developed areas (unless they target extractive industries, labour-intensive manufacturing or natural resources in any part of the country) where higher marginal economic return is expected.

As practitioners in the field are well aware, investors are increasingly selective in their choice of locales for investment. They seek, *inter alia,* market opportunities, stability of policies, non-discrimination vis-à-vis local investors and a threshold level of human capital and infrastructure facilities. In the absence of these basic ingredients foreign investors may neither be able to meet their objectives of profit maximisation and market expansion nor would their operations promote development objectives of host countries.

No amount of incentives can be a substitute for a stable economic environment (i.e. stable macro policies including exchange rate policies, stability and transparency of polices towards foreign firms, an open economy free of import tariffs and export subsidies mainly designed to placate sectional interests or pursue the unattainable- so called economic self sufficiency, and policies designed to develop infrastructure and human skills). Therefore, the government intervention in attracting and maximising the benefits of FDI might be deemed necessary for the late starter regions, provided that it should be confined to the minimum level and all other efforts should be made for improving the business environment and competitiveness at a global level.

After a brief overview of global and regional FDI trends, this paper will discuss the role of FDI in regional development by looking at the investment-development nexus in Brazil, China, Russia and Turkey. It will also attempt to draw some policy conclusions that may be relevant to Brazil and other countries facing similar challenges.

2. Global and Regional Trends in FDI

A few countries -- essentially Japan and Korea -- have been able to grow rapidly with minimal reliance on FDI. Many countries have attempted to imitate the Japanese or Korean model, but with limited success. *De facto*, most other fast-growing countries have relied heavily on FDI (for example Chile, China, Malaysia, Singapore, and Thailand). Most astonishingly, Ireland -despite being a relatively advanced country - has managed to grow at some 8 per cent per year for most of the 1990s due in large part to effective attraction and

deployment of foreign investment. This is not to say that FDI is all it takes to achieve rapid growth, but it appears that FDI remains a key ingredient.

Important changes are taking place in the world FDI scene – not only in terms of ups and downs in global FDI flows, but also in scope, structure, and methods of participation and in the composition of its principal actors. The scope of FDI has vastly extended from traditional manufacturing to services including information technology, finance and banking and the media. It is no more a phenomenon of big countries seeking cheap labour and raw materials in developing countries. The scene has altered with new entrants from China, India, Brazil, Russia, Malaysia joining the ranks of the traditional investors from the US, Europe and Japan, although OECD countries still provide the bulk of worldwide FDI flows. The contractual form of foreign enterprise participation has also changed with licensing, joint ventures and franchises assuming importance along with the traditional form of FDI. We need to reflect these changes in our thinking and policies:

- *Country policie*s: More and more countries have continued to liberalise their economic policies over the last decade or two, becoming more open both to trade flows (lower tariffs, fewer quantitative restrictions, currency convertibility) and to FDI flows (fewer restrictions on which sectors are open or percentage of foreign ownership allowed, abandonment of case-by-case approval procedures, etc.). The ones that are not open are experiencing difficulties in maintaining growth.

- *Company behavio*ur: More and more multinational enterprises (MNEs) are adopting integrated regional or even global strategies, using both subsidiaries and strategic allies to locate *interdependent* facilities in various countries so as to maximise their competitive edge world-wide. This is a change from the dominant behaviour of 10 or 20 years ago, when MNE subsidiaries in foreign countries were operated more or less independently of each other and were located anywhere there was a market and without regard to whether the locale offered the conditions necessary for world-competitive price and quality production.

- *Technolog*y: Huge improvements in international transportation and communications, combined with greater use of electronic controls and information storage and transmission, have made the opening of countries, and the change in behaviour of companies, viable and important. Changes in communication technology have drastically reduced many of the costs of locating interdependent activities in more than one location. The changes in technology, behaviour and policies reinforce and validate each other. Because of this, the world is separating into two kinds of countries: (i) those that offer competitive conditions for production, attract FDI, trade, and experience continuing increases in productivity and hence in incomes, and (ii) those that do none of these things and stagnate.

The world FDI inflows, after a record $1.4 trillion in 2000 from just over $200 billion in 1993, fell sharply by around 50percent in 2001 to $0.7 trillion and by 27percent to about $ 534 billion in 2002 (according to preliminary estimates by UNCTAD). Over the past decade, about three-quarters of FDI went to the developed economies whereas the developing countries absorbed about 20 percent of world inflows -- concentrated in a handful of countries such as China, Brazil, Argentina and Mexico (these three Latin American countries hosted 70-

80 percent of FDI inflows in the Western Hemisphere in 1998-2000). As in 2001, the decline this year - about a third of the peak value recorded in 2000 - is again likely to be larger in developed countries[3] (31percent) than in developing countries (23percent). The uncertain economic situation and weak stock market are undermining business confidence, with a sharp impact on cross-border mergers and acquisitions (M&As) and corporate investment expansion plans.

3. FDI inflows in Brazilian Economy

While in 1993 and 1994 portfolio capital represented almost all the net private capital flowing into Latin American, since 1999 nearly 100 percent of the net private capital flows into the region were FDI. Thus, FDI has virtually become the "only game in town". The slowdown in the industrial countries may present an opportunity for Latin America and the Caribbean (LAC) to attract new capital. FDI inflows into Latin America and the Caribbean are expected to fall in 2002 for the third year in a row[4], tumbling 27percent from $ 85 billion to $ 62 billion (UNCTAD preliminary estimates).

Brazil, the region's top FDI destination, has lifted many restrictions in the past several years to encourage foreign investors since 1995, particularly in formerly closed sectors, such as petroleum, telecommunications, mining, power generation, internal transport, and insurance to foreign investors. Brazil's privatisation policies, merger and acquisitions (M&A), investment regulations and ease of project implementation have boosted the country's attractiveness for FDI. From 1996 to 2002, Brazil received nearly $170 billion in FDI ($32.8 billion in 2000, $22.6 billion in 2001 and an estimated $20 billion in 2002). Credit disbursements to Brazil – direct loans, trade credit, bonds and notes – used to be larger than FDI inflows in a proportion of 3:1, up to 1995, but this scenario has changed and nowadays FDI inflows are closer to the value of total credit disbursements.

The "Two Brazils" and Regional Development Challenge

Although Brazil has five regions, it is in practice divided into the two: The "Brazil One" or rich Brazil, (south, south-east regions and the developed part of the middle west) and the "Brazil Two" or poor Brazil (north, north-east, and the state of Mato Grosso in middle west). In the "Brazil Two", the north-east region, including the states of Maranhão, Piauí, Ceará, Pernambuco, Rio Grande do Norte, Alagoas, Sergipe, Paraíba and Bahia, is relatively the poorest largely due to the scarcity of natural resources and its high population at 47 million.

The northeast region, rich in mineral resources, has most of petroleum and natural gas production, as well as mines of granite and precious and semi-precious stones. The San Francisco River provides electricity through several hydroelectric plants and water for

[3] . Among the OECD nations, the UK is expected to suffer the biggest slump from $54 billion last year to just $12 billion in 2002. The US could see its figure plunge from $124 billion in 2001 ($ 295 billion in 1999 and $ 281 billion in 2000) to $44 billion in 2002.

[4]. The decline is concentrated in Mexico, where inflows last year were inflated by Citicorp's acquisition of Banamex; excluding that investment, FDI into Mexico this year ($ 14 billion) would remain at 2001 levels, despite the economic slowdown at home and in the United States, the country's biggest investor. In Argentina, the impact of last year's financial crisis reduced inflows to a minimum during the first six months of 2002. Investments are likely to pick up in the second half of the year - due mainly to Petrobras' $ 1.1 billion acquisition in July of Pérez Compac - to reach some $ 3 billion.

irrigated fruit culture. Another sector, which provides significant boost to the region's development, is tourism -- sandy beaches and a sunny climate most of the year. Still, the economic development level of the region is far below the national average.

As would be expected, most of the FDI inflows are located in the southeast region, which receives 87.5 per cent of all assets of companies with foreign participation. As for other regions, 0.6 per cent of these assets are in the middle west, 3 per cent in the north region, 4.2 per cent in the northeast, and 4.7 per cent in the south region. Although the south and northeast regions have different levels of economic development, the difference in the concentration of enterprises with foreign participation is not very significant. This occurs because the northeast has some comparative advantages in relation to the other regions, in particular, the low costs of labour and generous fiscal incentives. The transfer mechanisms are also important -- through the States and Municipalities Participation Fund and Negotiated Transfers of around 4 per cent of the annual GDP. The north and northeast benefited approximately 50 per cent of these transfers - about 2 per cent of the GDP.

Thus, it has become the destination of traditional industries of intensive natural resources that generates fewer added values. This same tendency can be observed in relation to the enterprises with foreign controlling interest. The south-east received 90.3 per cent of all assets of these enterprises, while the middle west, north-east, north and south regions aggregate 0.6 per cent, 3 per cent, 2 per cent and 3.7 per cent respectively.

Under the 1988 Federal Constitution after the return to democracy, regional development has topped the nation's political and economic agenda, although the country has not been able to pursue a coherent regional development strategy. The new development policies attempt, on the one hand, to reduce the regional inequalities in income and job opportunities, while on the other aiming at improving the efficiency by the implementation of a productive structure capable of competing nationally and internationally. It may be possible to kick off a process aimed at clearly identifying, enhancing the regions' competitiveness and comparative strengths vis-à-vis other regions and neighbouring countries. Rather than well-rehearsed generalities it is important to focus on some specifics, with a particular attention to the characteristics of the region because the lessons learned in this region could be relevant and disseminated to other regions of Brazil.

4. China's Uneven Regional Development and FDI[5]

China's efforts to redress the wide regional imbalance through a set of government policy and funding tools present a striking example. China's growth has been impressive since the 1980s and even conservative projections point to a bright future. However, there may be a weakness: that growth has been very unevenly spread, with the bulk of the investment during 1983-2001 concentrated in the eastern and southern coastal belt. In fact, the eastern coastal region accounted for 86percent of China's total inflows of FDI during this period, but the central region attracted just 8.8percent and the western region little more than 5.2percent.

[5]. For various country experiences, use has been made of the papers from the OECD-China Conference on Foreign Direct Investment in China's Regional Development (October 2001 in Xi'an, China) and the author's earlier papers. Hak-Loh Lee has contributed to this chapter.

Cumulative FDI inflows to East, Central and West China as of 2001

Region	Projects (Number)	Share (%)	Contractual value (US$ million)	Share (%)	Realised value (US$ million)	Share (%)
Total	**390,025**	**100.0**	**745,291**	**100.0**	**395,223**	**100.0**
East	315,053	80.8	643,923	86.4	339,726	86.0
Central	46,713	12.0	56,521	7.6	34,693	8.8
West	28,259	7.2	44,847	6.0	20,804	5.3

Source: MOFTEC FDI Statistics.

During the 1990s China became by far the largest recipient of FDI among developing countries. The second largest was Brazil. The nearest country in population size, India, attracted well below $20 billion during this period, while Indonesia, which experienced sizable disinvestments in 1998-2000, recorded FDI inflows totaling less than $7.6 billion in 1995-2000.

FDI inflows to China and selected developing countries, 1995-2001

(US$ million)

Country or territory	**1995**	**1996**	**1997**	**1998**	**1999**	**2000**	**2001**
China	35,849	40,180	44,237	43,751	38,753	40,710	46,880
Hong Kong, China	-	-	-	14,776	24,587	61,883	22,834
India	2,144	2,426	3,577	2,635	2,169	2,315	N/A
Indonesia	4,346	6,194	4,677	-356	-2,745	-4,550	N/A
Singapore	8,788	10,372	12,967	6,316	7,197	6,390	N/A
Thailand	2,068	2,336	3,895	7,315	6,213	3,366	3,820
South Africa	1,248	816	3,811	550	1,503	969	7,162
Argentina	5,609	6,948	9,160	7,291	23,988	11,657	3,214
Brazil	48,590	11,200	19,650	31,913	28,576	32,779	22,636
Chile	2,957	4,633	5,219	4,638	9,221	3,675	N/A

Source: IMF, International Financial Statistics, October 2002; National Bureau of Statistics, *China Statistical Abstract , 2002* (China figures for 2000 and 2001). Compiled by Kenneth Davies.

However, in terms of FDI inflows per capita, China ($30.1 in 2000) ranks relatively low even among developing countries, receiving far less than the main South American FDI destinations, Argentina ($315), Chile ($242) and Brazil ($195), or its competitors for FDI in South-east Asia (Singapore $1547 and Thailand $54). If FDI totals are divided by population, it is clear that China's FDI per capita was smaller than that received by any OECD member country in 2000 except Turkey. Even Japan, where FDI accounts for a tiny fraction of GDP, received 7.6 times China's GDP per capita, while Ireland absorbed over 200 times as much as China by this measure.

The south-eastern province of Guangdong has received the lion's share of FDI, largely because it is adjacent to Hong Kong, China, the main provider of FDI and China's largest port, and also because it houses three of the Special Economic Zones (SEZ) of Shenzhen, Zhuhai and Shantou, together with the Pearl River Delta open zone. By end-2000 Guangdong, whose population was only 6.8 per cent of the national total and which contributed only 11 per cent of GDP in that year, had absorbed 28.2 per cent of China's cumulative realised FDI. The second largest recipient of cumulative FDI in 2000 was Zhejiang, where the share of national FDI stock was 12.6 per cent, more than double its 5.9 share of population and rather higher than its 9.7 per cent share of GDP.

The whole coastal region was also more attractive to foreign investors than were hinterland provinces because of the government's encouragement of export-oriented FDI, which favoured locations possessing easy access to ports and shipping routes. Another important determinant of high levels of FDI has been state expenditure on infrastructure, notably in the major province-level cities of Beijing, which received 4.1 per cent of cumulative FDI, Tianjin (3.8 per cent) and Shanghai, which, although major construction work and FDI attraction only really took off in the 1990s, received 8.1 per cent of total national realised FDI stock in the two decades up to 2000. Guangdong and Fujian also benefited from revenue-sharing agreements with the central government which allowed them to keep a relatively large share of their tax revenue, which they were able to use to upgrade the inadequate or nonexistent (in places such as Shenzhen) physical infrastructure.

Inland provinces suffered a relative dearth of FDI because of the difficulty and high cost of transporting products to ports for export. As labour has become gradually more mobile, skilled labour has shifted from these areas to the more prosperous coastal zones, raising labour costs, especially in high-technology projects. Whereas foreign-invested enterprises have increasingly been servicing the domestic market in the eastern region, consumer markets in the central and eastern regions remain relatively weak. Consequently, there has been a tendency for foreign investors to adopt a "wait and see" posture towards the hinterland, purchasing land leases for possible future use there while maintaining an eastward bias in the distribution of productive investments.

Western and central Chinese provinces, the latecomers in the hinterland, are certainly in a disadvantageous position with regard to the hosting of FDI. They are farther remote from the world markets, burdened with the remnants of a faltering state owned industry, handicapped by a reform and open door policy that has discriminated against them for at least 15 years, and possessing only a very restricted local market. In addition, there was a substantial brain drain observed during recent years when the Western region's most skilled and entrepreneurial

youth migrated to the coastal regions, where it could expect higher salaries and better living conditions. And contrary to political willingness – but very much in concordance with economic theory – net-capital flows have been moving from the West to the East belt, where much higher earnings could be realised, in such a way further draining the West of important resources for its own economic development.

The heavy geographic concentration of FDI in the coastal provinces leads to aggravation of economic and social disparities with the central and western provinces. The most obvious phenomena are the lack of sufficient industrial linkages between the provinces, the low level of inter-regional co-operation and the weak dissemination of the benefits of FDI in coastal areas to other parts of the country. Moreover, the coastal provinces have been in advantageous positions to accumulate FDI, which only tend to widen the gap with them and the western and central regions by snowballing the FDI inflow into the coastal regions. The central and western regions, which have fewer assets and left behind the rich neighbouring regions, found themselves incapable of luring desirable amount of foreign investment. The situation went worse in the western provinces.

Policy Intervention: "Go West" Strategy

For smaller countries or more advanced larger ones, regional imbalances can be managed. But China is a veritable giant and, despite being bound together by a strong central authority, is a country of several cultures and traditions. One challenge it has to face in this era of globalisation is to prevent its uneven growth pattern from jeopardizing not only cohesion, but long-term economic stability too. The Chinese government is responding with its Great Western Development Strategy, launched in January 2000. This is an ambitious effort to steer state investment, outside expertise, foreign loans and private capital into the regions. In fact, the government channelled $45.5 billion in 2000 to develop the west, and plans are afoot to increase that figure. But it will take more than money to make the strategy work.

World Trade Organization membership offers a chance for these regions to compete for new investment, including from abroad, but they will have to overcome massive infrastructure and employment problems first. On the positive side, the region does have lower costs to offer in the form of an untapped reservoir of skilled labour from former military-managed enterprises, as well as a huge mass of cheap unskilled labour. There are some research institutes and universities in provincial capitals such as Xi'an and Chengdu, abundant natural resources, with oil, gas and minerals in Xinjiang, and a strong agricultural base. In fact, Sichuan province is the main producer of rice in China. There is also great tourist potential to be tapped from such historic sites as the Silk Road, the Tibetan plateau, the archeological digs of Liuzhaigou and the desert oasis of Turpan, where much fruit is grown. But these assets have not been enough to attract foreign investors in today's hard and competitive global economy.

Obviously, given their distance from the coast, the promotion of direct export-oriented industries is hardly an option for these regions; nearby countries like Russia, Kazakhstan, Uzbekistan, Turkmenistan, Pakistan and India, may offer opportunities, not least because of their proximity, though there are one or two political difficulties that could complicate matters, like ethnic questions along some borders. A less bumpy route would be to target resource-seeking FDI from elsewhere in the world market that would integrate western China into the value chains of its eastern coast's export-oriented businesses. This may mean

relocating some investments as well as bringing in new ones and would focus on operations that do not have to be close to the final customer. Services would be an obvious option, such as accounting for the coast's hotel businesses, or call centres and data processing. In manufacturing, attracting producers of spare parts for technology and machinery may be useful.

All of this presupposes a modern information technology (IT) infrastructure, which western China lacks. Moreover, the transport systems would have to be improved and inter-regional trade restrictions removed to give the inner regions a chance to supply the natural resources and labour inputs that eastern-based enterprises currently import from abroad. In the longer term it might be feasible to locate more market-oriented research and development facilities away from the east, where facilities tend to be military related. And more use should be made of the small pool of skilled labour until now absorbed in military and other state enterprises. The massive concentration of funds brought in by the government's "Go West" campaign should greatly improve the region's infrastructure over the medium term, but not so the institutional and regulatory setup.

China knows this well: its Shanghai Investment Promotion Agency and Yantai Investment Development Agency have been very successful out east and are no doubt seen as a model for investment promotion agencies (IPAs) to be created in the various western localities. Given the vastness of China, changing the FDI fortunes of all regions at the same time would be impossible. Rather, the Great Western Development Strategy could concentrate more on establishing focal points of investment, as it has started to do. Industrial districts in Xi'an, Kunming, Luoyang, could be encouraged to become development clusters, for instance, with their greater provision of research and development and networking.

The Chinese government has much to do to correct the widening income disparities between its rich coastal provinces and the sluggish interior. But Premier Zhu Rongji has stressed that the Great Western Development Strategy was a long-term programme with a timeline of 20 to 30 years. This is a realistic assessment. This highly ambitious programme, however, is not undisputed:

- This project alone may not be enough to be able to induce substantial FDI inflows to these provinces. The capacity of a region with regard to FDI inflows is circumscribed by the geographical and historical setting and can only partly be shaped by government interventions. Each region can only try to enhance its particular locational advantages and try to promote development processes corresponding to the endowment. The hinterland provinces of China cannot and should not try to copy the successful development strategies of the coastal regions. Different types of FDI inflows have to be targeted. However, common denominator for promoting FDI should lie at the bottom line. Based on that, different and adaptive strategies should be taken.

- Some critics point out that increased government spending in the west will reduce the amount of money available for current social programs, health, education and welfare, thereby aggravating the problems at another hot spot of China's contemporary development process. In the perception of some foreign enterprises, the programme is not tackling all the main issues at stake for foreign investments in the region.

Alternative measures must therefore be taken to enhance the attractiveness of the other provinces, in particular by investing in infrastructure, as has been done in the coastal provinces, by developing forms of inter-regional co-operation and by fostering domestic economic integration.

- The build up of a physical infrastructure will have to be complemented by an improved institutional set up of the market place. Especially the banking system will have to be modernized and freed of any “fiscal” functions it has still retained from the planned economic system. A greater availability of RMB-loans and an improved bankability of projects would be highly instrumental to attracting foreign investors, which until now shrink back from any engagement as they do not find the support by the financial system they need and are used to from ventures in other regions of the world.

- Today many western enterprises face the problem that they might find personnel willing to move to the metropolitan centers at the eastern coast. But qualified people who are willing to move for two to five years to the central or even western regions are hard to find. Local governments able to create an attractive environment to skilled labor (Chinese and expatriates) will increase the chances of their region to attract FDI.

- The promotion of direct export orientation would run counter to the regional comparative advantages of abundant resources. It rather seems to be more promising to target resource-seeking FDI, which integrate the West into the value chains of the eastern coast’s (export) businesses. This strategy seems skewed and risky. Therefore, complementary strategy, which targets market-seeking investments and bolsters local purchasing power, would be desirable. This approach would be trying to attract investors that intend to produce for the local market and are therefore not predominantly looking at the local factor endowment.

- Government bodies both on the central as well as on the local level will have to become active. The central government is responsible for the integration of particular promotion policies in the context of the macro-economy and the national transformation process. It defines the freedom local governments have in creating their own microenvironment for FDI-attraction. In addition it can direct resources under its control into the central and western provinces in order to improve the local investment environment.

- The wealthier and more developed eastern and coastal provinces are being asked to play a major role. The government expects them to provide special subsidies and establish joint ventures with western entities. They are called upon to develop new markets and bring advanced management and innovative production styles to less-developed western enterprises. Eastern China, most prominently Shanghai, has shown some commitment to funding parts of the western development program by signing 200 co-operative contracts with a total value of over $1.21 billion.

Serious reform measures should be taken against corruption and a lack of business savvy among local officials. It is often mentioned by foreign businesses that a lot more transparency would be of great help to do business in the western regions, not to mention the start up of the business.

- To the extent that the investment incentives available to foreign-invested enterprises are the same as those on offer to domestic enterprises, the policy of attracting capital investment to the Western and Central regions is consistent with the principle of national treatment. However, such incentives do not constitute a sufficient condition for increased investment in those regions. If the Chinese government wishes to redirect investment westward, it may prefer to put the main emphasis on improvements in the business environment there.
- The Chinese authorities are encouraged to continue raising the standard of investment promotion and investment approval in these regions to that prevailing in the open coastal zones, where the authorities are generally much more flexible in their interpretation of FDI laws and regulations.

5. FDI in Russia and Regional Development

Russia is a vast country of 89 regions stretching across Europe and Asia, possessing spectacular wealth in the form of exploitable natural resources, technology, a large, skilled workforce, and nearly 150 million consumers whose needs are endless. It is a country whose goals are to move towards a market system based on private capital investment and enterprise and to integrate rapidly into the world economy. Indeed, it has rapidly privatised the bulk of the assets of former state enterprises (although in many cases with a lack of transparency and fairness that has created an unfortunate legacy). It has also spawned hundreds of thousands of new small and medium-sized private enterprises.

Among the most important reforms so far undertaken to create, not in word but in deed, a democratic rule-of-law state with a modern market economy is the re-engineering of federated relations and reform of local government, as it is virtually impossible to rule the regions from Moscow. Depending on the region investors encounter different conditions for business, different degrees on interference by the authorities. This is due on the none hand to the existing level of lawlessness that was rampant in the country when, in violation of the Constitution and the federal laws, the political leanings and agendas of the heads of regions and municipalities introduced various restrictions[6].

The Russian economy has seen an upturn over the past three years (1999-2001). The State is consolidating its control functions, the economy is expanding, and political and macroeconomic risk factors have been significantly reduced. The economy is displaying considerable resilience and is likely to continue expanding through 2002, despite the worldwide economic downturn and the fall in oil prices. The consolidation of the Federal Government's authority in the regions (via the Presidential Representatives in the Federal

[6] . "Inter-Governmental Relation Reform is priority", Dmitry Kozak, Deputy Head of the Russian President's Administration, in AmCham News, March-April 2002, p.22.

Districts) has regional legislation into line with federal law on most issues, thereby overcoming the fragmentation of the national economic territory while reducing administrative barriers and risks.

However, what has been achieved to date is not in itself enough to guarantee an improvement in the investment climate and a long-term revival of the economy. Despite a general economic recovery, problems of a strategic nature remain. Until Russia sees stable growth in the output of competitive products, it will be too early to speak of a stable economic growth pattern. That applies not only to the raw materials sectors, but also to secondary industries and services, and it will require massive investment into industrial plants and equipment, the widespread deployment of new technologies, and an improvement in economic management in practically all sectors of the economy. That is the real essence of the Government's task of modernising the economy, as laid out in the Gref Program[7].

It will not be enough for Russia merely to achieve high growth rates. It must also modernize the economy, ensure structural changes and actively foster global economic links if it is to enhance the long-term resilience of its economic system. Modernisation of the Russian economy will result first and foremost in stable growth in domestic demand, thereby reducing Russia's dependence on the international raw material and oil markets. However, there is still a long way to go before the country reaches that stage. To that end, Russia must create conditions conducive towards generating revenue and increasing in-bound investment, and make more effective decisions on how it uses resources and promote goods on the market.

Over the past three years, investment growth has outstripped GDP growth in relative terms; but it is difficult to say that Russia is making full use of its investment potential. Its mechanisms for transforming savings into investments are ineffective, resulting in a situation where total savings in Russia significantly exceed total capital. Sector-to-sector capital flow is also at a very low level. In terms of investment resources, there is a clear misbalance in supply and demand between the export-oriented raw materials sectors and the rest of the economy, which is in dire need of capital.

Yet, foreign direct investment has remained a marginal phenomenon in Russia. The cumulative figure for FDI in Russia from 1991 through the end of 2001 amounted to $18.2 billion, or only 5 percent of domestic fixed capital formation. This performance may be compared with FDI in China of $46 billion in 2000 alone and more than $200 billion in the United States in 2001 in a global total of $1,270 billion in 2000. The level of FDI in Russia is very low relative to other transition countries in the region as well, adjusted for population size: on a per capita basis, cumulative FDI in Russia is $15, compared to $84 for Poland, $118 for the Czech Republic and $221 for Hungary.

[7] In 2000, under President Putin, the Government published a Social & Economic Policy Program 2000-2010 (the Gref Program) that demonstrates an understanding of the threats currently facing the country and which offers a development strategy based on a series of social and economic reforms intended to create a liberal market economy, governed by a democratic political system. The Program was widely endorsed by the business community in Russia, and refers to the task of improving the investment climate as one of the most important issues facing Russia today.

One, perhaps cynical, explanation for low level of FDI is that Russia may not really want foreign investment, and has only paid lip-service to the principle in order to gain the backing of foreign governments and international financial institutions[8]. Russia's history, not just in the Soviet period but going back centuries, has been one of isolation from the West and distrust of the outside world. It takes time for attitudes to change. Many members of today's Duma distrust foreigners per se and believe their only purpose in investing in Russia is to “rob the country of its riches by making quick profits and shifting them abroad”. However, there is an enlightened segment of leadership in Russia, which does not share this view, but to the contrary, recognises that there are enormous benefits Russia can and should derive from FDI.

The factors responsible for the comparatively low level of FDI inflows in Russia are on the whole not different from those depressing domestic investment. Impediments to private investment, domestic and foreign alike, are already well diagnosed. So are the remedies to rectify this situation. The key challenge is a political willingness to tackle these problems, build the necessary capacities and move to an effective implementation of the policy reform priorities. It is quite clear that increased levels of FDI could play a crucial role in transforming the industrial configuration still remaining from the period of central planning into a product of competitive forces, reducing the current excessive levels of horizontal and vertical consolidation as well as regional market segmentation.

Federal vs Regional Governments: Implications for Investment

Russia received FDI of only $4.4 bn in 2000, which fell to $4 billion in 2001. Even this small amount of FDI is divided very unevenly between the regions. A survey carried out by the Russian investment bank Troika Dialog last year discovered that 10 regions attracted 83 percent of total FDI[9]. These included obvious places such as Moscow and St Petersburg together with resource rich places such as Sakhalin in the Far East and Khanty-Mansiisk in Western Siberia, which produces 65 percent of Russia’s oil.

Russia lacks a clear strategic vision of how FDI could fuel its growth and modernise some of its antiquated industries. It also needs to have an integrated approach towards investment across the often-disconnected central government departments, the regions, and the municipalities in order to ensure that investors would operate in an enabling environment without arbitrary government hindrance and on the basis of market-based incentives. Significant benefits would flow from exposure to new entrants with advanced organisational and managerial skills, particularly in the infrastructure monopoly sectors, where deregulation is now being considered. The dominance of many large industrial firms, hitherto fairly immune from robust competitive pressures, would also be seriously challenged.

The business in Russia suffers from the absence of a unified economic space and the frequent regulatory changes, contradictory interpretation and discriminatory implementation of existing legislation resulting from unclear and contested separation of powers. There is still a sense of uncertainty in the relations between different levels of power. Participants stressed that what Russia needed was a clear-cut definition of state functions, transparency of official actions and the determination of what every level can and cannot do.

[8] See http://www.iccwbo.org/home/conferences/reports/budapest/book_articles/hertzfeld.asp

[9] “Russian Roulette”, FDI Financial Times, August/September 2002, p.25-27

Among the most important reforms so far undertaken to create, not in word but in deed, a democratic rule-of-law state with a modern market economy is the re-engineering of federated relations in the Russian Federation and reform of local government, as it is virtually impossible to rule the 89 regions from Moscow. Depending on the region investors encounter different conditions for business, different degrees on interference by the authorities. This is due on the none hand to the existing level of lawlessness that was rampant in the country when, in violation of the Constitution and the federal laws, the political leanings and agendas of the heads of regions and municipalities introduced various restrictions.

President Putin is now giving priority to restoring authority to the central government and dismantling power bases and conflicting administrative and other structures at regional level. In May 2000 he announced as a primary task to restore a common legal space in the Russian Federation. Existing federal laws make it very difficult even for a skilled lawyer to determine which body of government has what power and responsibilities, and what relations it can regulate and what the scope of its interference is. If you look at the existing federal laws, they very often use the formula whereby simultaneously three levels of government are responsible for compliance with federal laws: federal, regional and municipal.

A programme of administrative reform is also under way, redefining the powers of the regional authorities. Special presidential representatives in seven newly created federal (supra-regional) districts encompassing varying numbers of subjects of the Federation are to oversee compliance with federal law. This as yet untested new layer of authority will face very specific economic and political challenges. Whether for investors this will result in elimination of some of the differences in interpretation of laws and legislative practices (land ownership and transfer, taxation, foreign investment policy) remains to be seen.

The many unresolved issues in the field of inter-budgetary relations and arrangements for revenue sharing between the federal and regional governments have brought added uncertainty and changeability to the tax environment faced by investors through multiplication of seemingly irrational and incoherent taxes. Although the current policies aim to reclaim and reaffirm federal authority, relying on closed lists of taxes allowed at the different budgetary levels, many regions and local governments continue to introduce taxes that are not provided for in the federal legislation.

Thus, while strong federal presence seems likely to remain necessary in the near future, it should not simply take the form of increasingly rigid federal regulation, which could risk backfiring as sub-national authorities continue to seek loopholes for every restriction. A workable revenue-sharing system clearly requires consensus about its fairness in order to be genuinely effective.

A level playing field and a rule of law require an honest, even-handed and efficient bureaucracy and judicial system, implementing reasonable rules in a consistent and predictable manner. It also requires the evolution of a new business culture in Russia which favours compliance, with rather than avoidance of, the rules and a system of values, which encourages productivity, and efficiency in the workplace. Such a change cannot be achieved overnight, but can be achieved over time. Failure to do so will certainly discourage FDI. However, even more importantly, it will carry a heavy political, social and economic price - continuing decline in the country's economic performance with still lower levels of new

investment, higher rates of unemployment, and a growing percentage of the population living below the poverty level.

Seeking remedies in revisions to the legal and regulatory framework for foreign investment represents an incomplete approach, as deficiencies in this respect only form a minor part of the greater picture. The lags in structural reform and the policy deficiencies that have combined to produce an unfavourable climate for domestic as well as foreign investment need to be analysed as a whole.

While it is no doubt beneficial to encourage some spontaneous innovation and new ideas and approaches stemming from the degree of regional diversity, policy direction should ideally ensure:

- Harmonisation of legislation and implementation practices affecting investors at regional and federal level, including a full review of diverging legislation contravening federal law as well as of existing bilateral treaties and agreements in separate areas;

- Transparency of regional administrative structures for remaining region-specific competencies;

- Transparency in the role and evolution of powers of the newly created supra-regional districts;

- Formulation of region-specific investment policy and development plans to ensure best use of regional and federal programmes and resources, including budgetary transparency of incentive packages and full elimination of extra-budgetary contributions.

The problems faced in Russia are in large part as relevant to most domestic investors as they are to foreign investors in the Russian economy. However, the basic difference between the two is that the domestic entrepreneur is condemned to cope with local conditions while the foreign investor is free to choose from among competing host countries and to decide which one offers the most attractive balance of risk and opportunity for its investment. A country's success in attracting foreign investment is therefore a measure of its domestic success as well. There is today a huge pent-up interest for investment in Russia. As and when positive change occurs, foreign direct investment will dramatically increase and such investment will indeed become a motor for economic growth and prosperity in the coming years.

6. FDI in Development of Turkey’s Southeastern Region

Turkey is the largest economy in Eastern Europe, the Balkans, the Black Sea basin and the Middle East. It is the European Union’s sixth biggest trading partner and one of the world’s largest emerging economies. Yet FDI flows into Turkey have rarely reached $1 billion in any one year - a fraction the level of FDI attracted to countries of comparable size and development like Argentina and Mexico and only one-quarter the level of FDI attracted into Poland.

To understand why Turkey's has under-performed, one should revisit the key factors determining investment location. The location of FDI reflects the match of corporate strategy with three major location determinants: economic; political-institutional; and enabling environment. There is significant evidence that Turkey has a strong competitive position in relation to the economic determinants of investment location. Turkey is particularly well placed compared to competitor locations due to its economic size and dynamism and quality of its labour force. But in terms of the political-institutional determinants of FDI location, Turkey is in a weaker position. Political and economic instability, manifested as chronic inflation, fragile coalition governments, and negative attitudes towards foreign investors are major obstacles to FDI which are compounded by a weak enabling environment for privatisation-related FDI and a total lack of effective investment promotion.

The stock of FDI in Turkey was only $300 million in 1971, and up until 1980 the average annual inflow of FDI was only $90 million. This was far less than other comparable countries, and FDI did not increase significantly for most of the 1980s. It was only with a shift in Turkey from a protectionist trade regime to export-oriented economic liberalisation in the mid-1980s that FDI increased significantly. Annual FDI flows in Turkey grew rapidly from the mid-1980s, reaching $1 billion in 1990. However, FDI flows per annum have not increased for the decade since then. In other words, during the 1990s when global FDI flows accelerated – exceeding the growth in world trade since 1989 – FDI in Turkey remained static.

Turkey's leading competitors for inward investment are developing increasingly sophisticated investment promotion strategies, which are not only helping them to "win" new FDI but are also creating dynamic benefits for their economies. For example, CzechInvest, the investment agency for the Czech Republic, has quickly established high brand awareness and a reputation as a professional agency. The agency has a clear targeted strategy and is investing in initiatives to link foreign investors with domestic suppliers and to promote the upgrading for foreign facilities over time. Turkey needs a detailed review of its organisation and strategy of investment promotion.

Redressing Regional Imbalances and Southeastern Anatolia Project (GAP)

The role of FDI in promoting Turkey's regional development is currently negligible because even the more advanced regions have failed to attract much-needed foreign capital. The only realistic hope for the development of the relatively backward eastern and south-eastern regions of Turkey is the gigantic GAP project, which could produce a booming effect on private capital accumulation and entrepreneurship.

The GAP is the most comprehensive integrated regional development project ever attempted in Turkey in response to the wide disparities in the southeast, and in recognition that strengthening this region socially and economically will benefit all of Turkey. The GAP was initially formulated as individual irrigation and hydropower projects on the Euphrates and the Tigris Rivers[10] in the 1970s, which was later transformed in the early 1980s to a multi-

[10] The project area includes the watersheds of the lower Euphrates and Tigris Rivers and the upper Mesopotamian plains. It covers the nine provinces of Adiyaman, Batman, Diyarbakir, Gaziantep, Kilis, Mardin, Siirt, Sanliurfa and Sirnak.

sectoral, socioeconomic, regional development program. As an integrated project, it is not limited with the dams, hydro electric power plants, irrigation systems only, but it also contains industries and investments for the development of socio-economic sectors such as agricultural, industry, urban and rural infrastructure, communication, education, health, culture, tourism and other social services in a co-ordinated way[11].

The poorest cities of Turkey such as Mus, Agri, Bitlis and Bingol are located in its eastern and southeastern region, where subsistence agriculture is still prevalent, land inequality is at large proportions, the climate is harsh, and where for the past 15 years (1985-2000) an off-and-on civil war was fought. About 15 percent of all families in the nation live in the region, which in turn uses only 10.2percent of national income. In the region, the average income per family is $3,851, 30percent below the national average[12].

GAP's focus on sustainable human development in the region builds upon the concept of integrated regional development of the GAP Master Plan of 1989, which mandated the creation of the GAP Regional Development Administration to co-ordinate the implementation, management, monitoring, and evaluation of development related activities, in a concerted effort to respond to the problems. The subsequent Social Action Plan of 1995 was a major step toward a greater integration of sustainable development with socio-economic and infrastructure projects. Within the scope of a macro economic and social development program, the GAP Master Plan defined small and medium scale investment and socio - economic development projects ranging from educational and health infrastructure to environmental protection, irrigation systems, management development, transportation.

However, investments related to GAP, seen as a partial remedy for economic problems, have so far failed to produce positive effects that spread to the entirety of the region. The civil war that erupted in mid-80s put both lives and property in danger and played a determining role in the region's economic downturn. Yet, investments in manufacturing, electrical power, and mining undertaken by the state did not have a blooming effect on private capital accumulation and entrepreneurship in the region.

Government incentives for underdeveloped regions did not secure the necessary flow of investments into this region. In the 1980s, the reduction in government subsidies and the

[11] Sometimes the GAP is compared with the Cerrado Plain, a savanna area of central Brazil reaching into parts of Colombia. The area is huge, covering an area larger than all of Western Europe. Brazil is already an agricultural powerhouse, the world's largest producer of rice outside Asia, among the top three producers worldwide of corn and soybeans and a leading producer of beef, tobacco and of course coffee, sugar and citrus. Credible Brazilian estimates say the area under cultivation could be expanded by up to 60 million hectares, an area equivalent to the entire plantings in corn and soybeans in the U.S.

[12] There are various historical and social reasons for the disparity in income and development between the East and the West of the country. When choosing the place or sector to make an investment, the alternative with the lowest costs and the highest return is preferred. This is the universal and constant rule of economic behavior. The same rule was applicable to Turkey in the second half of the 19th century as the country was integrating with western capitalism. The Ottoman Empire's process of integration with the world markets began at that time in those areas most accessible to western capitalism, that had better transportation and market followed suit. Some sections of Central Anatolia and the Black Sea regions, and all of Eastern-Southeastern Anatolia were left behind in this capitalist expansion.

freezing of investments by the State Economic Enterprises had a significant effect on the East and the Southeast. In this region, where population growth was much higher than the national average, production and income per capita decreased. Agriculture and husbandry were on decline, and unemployment became the primary problem especially for the youth. This unproductive economy mainly dependent on government spending, while providing nothing more than limited sustenance of daily life for a part of the population, also contributed to the demise of the productive activity in the region.

The difference in prosperity and income between Western and Eastern-Southeastern Turkey continues to cause the flight of manpower and capital. Years of manpower and capital flight hurt the development process. Internal migration data on manpower potential is truly striking. According to the 1990 census, the region's population was 9,365,000. The same data show that there were about 12,000,000 people who were born in eastern cities. This means that 30percent of the region's population, that is 3,607,000 persons have migrated to the west and are living there. Due to both economic and political reasons, this ratio may have increased by 2 to 3 percentage points by 2000. Hence, 1 out of every 3 Easterners is living outside the region[13].

The forward and backward linkages in this sector are almost non-existent. The investments in power generation made in the region fail to create sub-industries and businesses that are related to this sector. Three quarters of the power generated in Turkey is for industrial use. Since industries are established in the west, power generated in the east is consumed in the west. According to Turkish Electricity Authority data, whereas the average power consumption per person in Turkey is 625 kW/h annually, this figure is 349 kW/h in the east. A significant portion of the power generated by GAP will be consumed in the west, and the rest will be exported. It is true that in recent times a speedy industrialization related to cotton spinning and weaving has been taking place in the GAP region and its neighboring cities. If this development continues power consumption may increase. However, this will not bring about an immediate radical change in the picture.

The permanent positive effects to the GAP region will come from investments in irrigation. GAP, which will irrigate 80percent of irrigable lands, will cause significant changes in production relations in agriculture. However the southeasterners will not fully benefit from the rents generated by these state investments. Because the south-east has the most unequal land distribution in Turkey. Despite having been targeted by successive governments for land reform programs that were invariably undermined by local powerholders, there are still entire villages owned by individuals or families.

On the positive side, the new patterns of land use and investments in agriculture are likely to transform the region as a whole. When production for the market begins to predominate, and large lands turn into capitalist farms by better irrigation, the capitalist farmer-agricultural laborer differentiation process will speed up. Those who will lose out as a result of mechanization in agriculture will migrate to cities, the population composition and the urban texture will show noticeable changes. If the agro-businesses are established in cities with the help of productivity increase in agriculture, then the population that has migrated from rural

[13] Private View, Autumn 1998, TUSIAD Publication

areas will be used as manpower in factories. In short, as GAP investments raise the value added in agriculture, the region's ranking on the development scale within Turkey will move up considerably.

Although GAP investments appear to be just regional projects, their sheer volume had effects that reverberated throughout Turkey. The business volume generated by GAP investments in construction were important for large contractors based in Istanbul and Ankara. These companies that built their businesses in the Middle East and Libya in the beginning of the 1980s, had a difficult time when these countries reduced their investments due to their declining oil income. The acceleration of investments in GAP was a big boost for these contractors. Activities at GAP continued even when the economy was in a general slump, and sustained the firms that supplied the construction sector as well as the contractors.

As of now GAP investments have little effect on other eastern cities towards the GAP region. The realization of GAP's promise for the region, for western capital, and eastern cities largely depends on finding foreign markets. The surplus generated by increased production will have to be exported. This requires the use of agricultural technologies that are at par with the world as well as the diplomatic skill not to alienate the countries with potential markets. In today's world incredible increases in agricultural productivity are possible through the use of genetic research and biotechnology. This has turned many industrialized nations that were agricultural importers into agriculturally self-sufficient countries that might even have surpluses.

True, the GAP is exciting both as an utopia and as a process, but its cost is not insignificant. This project has swallowed significant government resources in the past 10-15 years. The total project cost is estimated at $ 32 billion, of which $14.8 billion have already been invested. Of this amount, $2.1 billion have come from foreign sources including the World Bank and several European governments. The Turkish government has largely financed the GAP; however, unless these investments are complemented and supplemented by productive private sector investments the full benefits cannot be realised. Even the infrastructure, which has largely been under the responsibility of the government, is now open to the private sector, on BOT (Built-Operate-Transfer) or BO basis.

GAP investments brought relative liveliness to some city centers. Military spending generated some business volume. However the gulf war, the shutting down of the oil pipelines, and the "low intensity conflict" environment had made it harder to earn a living while the risks for personal safety have risen substantially. Today, with the civil war over, it is important to think about the new dimensions of this development including greater involvement of foreign investors in agro-industry projects. There is an ever-increasing interest on the part of potential investors from other regions and abroad once the overall enabling environment improves for investors, both domestic and foreign.

7. Policy Implications and Conclusions

As highlighted in the foregoing, it is important to take into account the particular circumstances of each region. There is a great variety in terms of challenges and

opportunities. It is also necessary to bear in mind that regions are not abstract entities, nor are they best understood as territorial units. Part of the federal or unitary states, they are composed of individuals, households and communities. Measures to assist people living in a region to raise their productivity and economic participation must address their needs in all three of these dimensions. Regional-development initiatives should be tailored carefully to target the appropriate dimension. Rather than pursuit for the subsidies and incentives, a government is likely to succeed by investing in the enhancement of human capital and key infrastructure. Also creating a favourable environment for investment and private-sector development is a *community-level* activity, involving (among others) government, educational institutions, financial institutions and professional associations.

Rather than seeking to summarize the main trends and issues identified in the preceding sections, let us conclude with the following observations that may be of relevance to Brazil and other countries as they consider their policies towards FDI and regional development:

First, and most importantly, although attracting FDI can be an important element of a regional development strategy, the key to successful development will ultimately be sound domestic macroeconomic and structural policies, adequate and efficient domestic savings and investment and human capital accumulation, supported by sound and strong domestic institutions. FDI is not a substitute for getting domestic policies "right". Appropriate domestic policies will help attract FDI and maximize its benefit, while at the same time removing obstacles to local businesses.

Second, although FDI inflows into one country and region do not necessarily imply less FDI for other countries and regions, they must ultimately compete for FDI. Foreign enterprises, like domestic ones, pursue the good business environment rather than the special favours offered to induce the foreign enterprises to locate in the incentive offering regions[14]. Special and thus transitory incentives for FDI might fail to give foreign investors long-lasting interests in the host regions and would be at the risk of various types of ensuing negative side effects. Enshrine the principle of non-discrimination in national legislation and implement procedures at enforcing it at all levels of government and public administration[15].

Third, integrity, transparency and accountability of governments and corporations are fundamental conditions for providing a trustworthy and effective framework for the social, environmental and economic life of their citizens. They bring huge domestic governance challenges not only for the benefit of foreign investors, but also for domestic business and society at large as well. Among the regulatory reforms, transparency of the investment-related

[14] A sensible approach for host countries is to presume that subsidies to FDI are not warranted, and so avoid preferential treatment of FDI relative to foreign portfolio investment or domestic investment. Deviations from such a policy would be justified only where there is clear and direct evidence of substantial positive spillovers associated with multinational production and where multinationals are unlikely to choose the optimal level of production (from the host country's perspective) without a subsidy or other inducement.

[15] This implies that no special treatment would be granted to domestic enterprises under pressure from foreign entrants. However, the approach should be even-handed: efforts at attracting FDI through inducements not offered to domestic companies should equally be considered as discriminatory – except where aimed at compensating for manifest deficiencies (e.g. an "un-level playing field") in the host country business environment.

system, the removal of corruption and bribery (one indicator of poor governance and a disincentive to investment), and sound corporate governance come up as the priority items of the agenda. The central and regional authorities are advised to make policy efforts for enhancing policy and regulatory frameworks (e.g. as regards competition, financial reporting and intellectual property protection) that foster a dynamic and well-functioning business sector.

Fourth, exposure to effective competition on an even playing field is the single most important incentive for foreign and domestic companies to upgrade management and technology. Existence of significant market power risks reducing the incentives of foreign investors to improve productivity and to exploit consumers or workers in captive markets. Free entry is also the key to establishing effective linkages between foreign investors and domestic buyers or suppliers that help diffuse best practice in the economy[16].

Fifth, linkages between foreign affiliates and domestic firms can be of great importance to the dynamism and competitiveness of the domestic enterprise sectors – the bedrock of economic development. However, it is important to emphasise that these linkages cannot be created for their own sake. Rather, the objective should be to stimulate linkages that raise the efficiency of production and contribute to the diffusion of knowledge and skills from MNEs to the local enterprise sector. Uncompetitive domestic suppliers may find themselves excluded in the increasingly demanding environment of rationalised supply chain. Governments that understand the competition needs and priorities of MNEs can attract new investments more effectively and root them more deeply in their economies

Sixth, ensuring policy coherence across different government departments and different levels of government is key to any successful regional development strategy. Policies intended to meet economic, social and environmental goals in the regions are made by different ministries or agencies, often with little attention to policies being developed by other entities. Thus policies pursued to achieve one objective may sometimes conflict with those adopted to meet another. In addition, sub-national governments often bear primary responsibility for implementing policies developed at the national level. To do so, they need to be able to influence policy design at the national level, and participate in decisions on how they should be implemented, including how the costs of implementation are shared.

Seventh, rendering underdeveloped region catch-up advanced ones or breaking vicious cycles of low investment stock might require additional efforts. Central government and regional government should co-operate closely and in harmonious way in order to make their efforts bear fruitful results, which would happen only when the efforts surpass the critical mass. Advanced regions can help underdeveloped regions stand on the better position for development. Any political promotion activities or incentives, which would be necessary

[16]. The benefits from FDI tend to be maximized when foreign investors operate on an even and competitive playing field. This means they need to be treated just like domestic companies ("national treatment"). In addition, competition, free entry, customer choice and free exit, should determine who gains and who loses. China would in many ways appear the exception to the rule. Significant foreign investment went into the country despite a less than perfect policy environment. However, in the case of China the special relationship of key provinces that received a large part of foreign investment, Guangdong and Fujian with Chinese communities outside the mainland did much to make up for existing distortions in the playing field.

to jump start to attract FDI, should be terminated once the targeted development threshold has been reached and market forces can take over.

Eight, work toward increased openness to foreign trade, so as to allow the domestic enterprise sector to participate fully in emerging patterns of the global economy. This approach could be undertaken jointly with efforts at increasing business sector competition. A combined approach would allow a greater domestic and international openness to business to go hand-in-hand with safeguards against negative effects from a rise in concentration. Moreover, a successful effort at removing regional trade barriers makes the participating countries more attractive locations for FDI, owing to the concomitant expansion of the "relevant" market.

Ninth, implement internationally agreed environmental and core labour standards. Efforts at reducing child labour, eliminating discrimination at the workplace and remove impediments to collective bargaining are important in their own right. They also serve as a tool for upgrading the skills and raising the motivation of the labour force and facilitate linkages with foreign companies usually operating on higher standards. Additionally, a comparatively sound environmental and social environment becomes increasingly important for countries' ability to attract FDI operating on high standards.

Tenth, undertake efforts to put in place, and raise the quality of, relevant physical and technological infrastructure. The presence of such infrastructure is instrumental in attracting foreign investors, in allowing national enterprises to integrate the technological spin-off from foreign-owned enterprises in their production process, and in facilitating their diffusion through the host economy. Allowing foreign investment in infrastructure sectors and official development assistance (ODA) may assist in these efforts.

Eleventh, multinationals have to choose carefully and investment promotion agencies (IPAs) can help to build a region's image and attract the attention of prospective investors. IPAs are encouraged to centralise decisions on FDI regulations and promotion, co-ordinate other key government departments involved in FDI process and provide a focal contact point with private investors. Prerequisite characteristics of a successful IPA are such as political support and access to senior government leader, independence from other government departments and agencies, and inter-governmental co-operation and co-ordination[17].

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[17]. There is no single model of success in investment promotion. Nor is there one country that applies the optimal practice in all elements of investment promotion strategy. The emphasis should be on the "building blocks" rather than simply imitating practices of other countries. There is certainly much to be learned from other countries' experiences, but successful policy needs to be ultimately grounded on the specific needs, culture and opportunities of investment host countries.