Investment for Sustainable Development

- Private investment is a powerful development enabler: delivered in the right way it can create jobs, build skills, spur innovation, provide essential infrastructure and services, boost economies and strengthen standards in public and corporate governance.

- Investment, both foreign and domestic, needs to be scaled up significantly in the coming years to contribute to the post-2015 agenda.

- More investment is not enough, however. It must also be good quality. Even though private finance accounts for the lion’s share of capital inflows to developing countries, its contribution to development is still to fully materialise. The Sustainable Development Goals (SDGs) explicitly call for quality investment to support this transformation.

- Tapping the sustainable development potential of investment means increasing the capacity of the local economy and the public sector, reforming framework conditions to make countries attractive investment destinations, and promoting responsible business conduct along the length of global supply chains.

- The OECD plays an important role in encouraging reform to improve the enabling environment for investment and promoting international good practice and responsible business conduct in home and host countries. It does so through a wealth of policy tools, reviews and peer dialogue mechanisms, especially the Policy Framework for Investment and the OECD Guidelines for Multinational Enterprises.

How to finance development is one of the most pressing questions in the reflections on the Sustainable Development Goals for the post-2015 development agenda. Key to answering this is finding ways to involve the private sector in delivering development. Private finance already accounts for the lion’s share of capital inflows to developing countries. Foreign direct investment (FDI) makes up around 60% of inflows into developing countries, dwarfing public inflows. Public inflows, including official development assistance (ODA), net of debt repayment, account for a mere 1% of all capital inflows to African countries (World Bank Group, 2013b), while ODA represented only about 3% of African gross domestic product in 2013. This paper outlines how private investment can become a significant part of a strategy for financing the sustainable development goals, and the role of the OECD in promoting the framework conditions for quality investment to support national and regional development objectives.

Private investment in developing countries has steadily increased over the past 20 years (Figure 1). In 2012, developing economies attracted over 50% of global flows (up from less than 20% in 1990), exceeding FDI inflows to developed countries for the first time. They maintained their lead in 2013 too. Developing and transition economies now make up half of the world’s top 20 recipients of FDI inflows. FDI to developing countries has been less affected by the volatility of global investment levels in the past years, with growing South-South investment (OECD, 2014a).
Responsible investment for inclusive growth and sustainable development

Private investment can be an essential enabler of economic and human development: under the right conditions it creates jobs and boosts the activity of local firms, suppliers and distributors by creating demand and a market for their products and services. It can improve access to and the quality of infrastructure and services critical for the development of entrepreneurship and small businesses, such as banking and finance.

While most investment is undertaken by domestic firms, international investment can bring particular benefits. It can encourage innovation and spur productivity growth by bringing in or generating new information and technologies – such as through knowledge-intensive activities like research and development. It can help to spread new technologies and expertise, for example through the creation of business linkages and by providing improved access to international markets and global value chains. If adequately framed, investment can improve the human resource base by fuelling the development of skills in the host economy through educational and training programmes to meet market needs.

Companies are also increasingly driving the efforts to improve the sustainability of their operations and contribute to sustainable development. Responsible investors that respect international standards of responsible business conduct can help to identify and respond to risks of adverse impacts associated with particular products, regions, sectors or industries.

There are many practical examples of the power of investment to accelerate economic development. In Southeast Asia private investment and trade have driven development, and the region’s record in export performance speaks for itself. In some cases, however, it has been less able to translate this success into lasting and inclusive development, partly due to a lack of appropriate policy frameworks to support sustainable development through investment.

Figure 1: Foreign direct investment in developing economies, 1990-2013

![Graph showing foreign direct investment in developing economies, 1990-2013.](source: OECD statistics)

- **Developing economy share (%) of total global flows (right hand axis)**
- **Total global flows**
- **Flows into developing economies**

Source: OECD statistics
Despite the general recognition of the development potential of investment (Box 1), it remains unrealised in many parts of the world. And where there have been significant increases in FDI to developing countries in past decades, these have not always met the needs of sustainable development.

Box 1. Investment as a key part of the international development framework

The Monterrey Consensus, the outcome of the first International Conference on Financing for Development in 2002, acknowledged the role of private investment in supporting development (UN, 2003). This role has been reiterated throughout the discussion on how to finance development goals, including in the Doha Declaration, the outcome document of the 2008 Doha Conference on Financing for Development (UN, 2009), and the Report of the Intergovernmental Committee of Experts on Sustainable Development Financing (ICESDF, 2014), in preparation for the third International Conference on Financing for Development, to be held in Addis Ababa in July 2015. This emphasises the need for sound policy frameworks to encourage private investment in actions that support poverty eradication.

The Sustainable Development Goals are designed to be universal and integrate the social, environmental and economic pillars of development to transform the functioning of societies and economies for a more sustainable future. They explicitly call for quality investment to support this transformation, as detailed in the Open Working Group Proposal for Sustainable Development Goals (Open Working Group, 2014).

Greater efforts are needed to spur sustainable development through investment

In many low-income countries, investment rates are inadequate; existing investment is not always designed to bring sustainable development gains in addition to the financial returns investors are looking for. Further, all regions and sectors do not benefit equally from investment. Asia received 30% of all FDI to developing countries in 2012, while Latin America hosted just under 20% and Africa only 5% (OECD, 2014a).

Where investment does occur, the local economy does not always possess the capacity and policy tools to reap the potential benefits of private investment. Low-income countries may not have the mechanisms for integrated, whole-of-government approaches required to reap such benefits. Productivity gains are often low in the economies that would most benefit from investment, and incentives insufficient to encourage innovation. At the same time, export-oriented foreign investors may create virtual foreign enclaves of activity, bringing in foreign suppliers, employees and materials. This leaves few benefits for the host economy, as linkages with local counterparts tend to be weak and limited. Moreover, the informal economy is sizeable in most developing countries, meaning that a significant part of economic activity is left outside the protection, regulatory frameworks and taxation set by the government. It also makes it difficult for those in the informal economy to benefit from support programmes such as agro and micro-financing schemes.

Infrastructure investment for development and economic growth

Infrastructure is a crucial enabler of development and economic growth, for example through the provision of safe drinking water and sanitation, the development of agriculture and rural livelihoods and access to basic social services such as healthcare and education. Infrastructure also facilitates the flow of goods, services, people and market information, and lowers costs for business. Yet infrastructure suffers from chronic underinvestment, especially in low-income countries. According to the World Bank, two-thirds of people in sub-Saharan Africa and one-fifth of people in South Asia lack access to electricity, less than 20% of roads in sub-Saharan Africa are paved, and only 30% of people in sub-Saharan Africa and 40% in South Asia have access to improved sanitation facilities.
On the one hand, private investment in infrastructure can improve productivity and create an attractive business and investment climate (OECD, 2015a). But on the other hand, companies regularly cite problems with electricity and transportation infrastructure as some of the key hindrances to investing and doing business in developing countries (World Bank Group, 2013a). For instance, deficiencies in Nigeria’s power sector are estimated to increase the cost of goods and services by 40% due to the need to use private generators. It is estimated that annual GDP growth could be boosted from the current 7-8% to 10-11% if adequate power supplies were available. In another example, on average it costs three times as much to transport a 40-foot container from Mombasa, Kenya to Kampala in neighbouring Uganda as from Dubai to Mombasa (AfDB, 2014). These kinds of bottlenecks are binding constraints to productivity and competitiveness, including integration in global value chains where transit time and cost are of critical importance.

A total of USD 60 trillion will need to be invested in infrastructure for growing populations according to the World Economic Forum; most of this will be required in developing countries. Africa alone requires an estimated USD 93 billion of infrastructure financing every year until 2020 (World Bank, 2013a). After considering what public spending can provide, this leaves a funding gap of USD 31 billion – this is where private finance is most needed. Although this financing gap is trivial compared to the size of world capital markets, the share of private sector participation in infrastructure remains low – especially in developing countries where it accounts for less than 20% of infrastructure investment (Trebilcock & Rosenstock, 2013). Only 4% of infrastructure public-private partnership (PPP) projects took place in low-income developing countries in the past 20 years, and 37% in middle-income countries (ibid.) While in 2013 Africa saw the highest levels of private infrastructure investment since 2008 (8.8% of total infrastructure investment in the continent), and sub-Saharan Africa is the second fastest growing region in the world (with a growth rate of 5.7%), the potential of private investment is largely untapped.

Proactive steps to enhance the enabling environment for infrastructure investment in developing countries can help diminish risks posed by long-term investment horizons, mitigate the complexities of infrastructure project planning, and ensure that infrastructure investment delivers the expected sustainable development benefits. Investment policy predictability, legal and regulatory frameworks, structural separation of infrastructure markets, the role of incumbent state-owned infrastructure operators, and pricing and procurement policies in infrastructure sectors are among the policy variables that are likely to affect returns on investment in infrastructure. Coherent policy frameworks are needed to address these various gaps. Unlocking innovative forms of infrastructure financing is an important piece of the puzzle – be it through institutional investment, risk-mitigation and concessional funding by the multilateral development banks, or more sophisticated financial instruments provided by development finance institutions (such as mezzanine capital, blended loans, and asset-backed securities) to enhance private participation in infrastructure (OECD, 2014a).

What can the OECD offer?

Policy reform in developing countries will be essential to make them more attractive investment destinations for potential investors. A good investment climate is one which provides opportunities for all investors: public and private, large and small, and foreign and domestic. The heterogeneity of investors, the diversity of factors which drive investment decisions and the multiple policy objectives pursued by governments all call for a whole-of-government perspective that increases policy coherence. This policy coherence applies to each component of the investment climate, whether encouraging foreign investment, promoting linkages and technology spillovers, raising the quality of the workforce, improving infrastructure or any other area.
With its wealth of tools, policy reviews and peer dialogue mechanisms, the OECD plays a significant role in encouraging reform and promoting international good practice in all parts of the world to:

- improve the enabling environment for investment, including in specific sectors such as infrastructure, agriculture or clean energy
- promote responsible investment and responsible business conduct in home and host countries.

Creating an enabling environment: the Policy Framework for Investment

The Policy Framework for Investment (OECD, 2015c; Box 2) is the backbone of OECD work on investment for development. It is a multilaterally backed instrument that has been used extensively by developing and emerging economies in all parts of the world. By helping to create the enabling environment for responsible investment and build country-level and regional capacity, it can mobilise private resources for development and support the implementation of the Sustainable Development Goals.

The Framework addresses the issue of sustainable development through the lens of private sector-led development. Its focus on the investment climate allows for a coherent and comprehensive approach to addressing the challenges of growth and development, providing an understanding of how policies for investment and development interact.

Box 2. What is the Policy Framework for Investment?

The Policy Framework for Investment provides a checklist of key policy issues for consideration by any government interested in creating an enabling environment for all types of investment and in enhancing the development benefits of investment to society. It considers the numerous policy dimensions identified in the 2002 Monterrey Consensus as crucial for a healthy environment for all investors, from small and medium-sized firms to multinational enterprises. Through its 2015 update, the Framework addresses:

- investment policy
- investment promotion and facilitation
- trade policy
- competition policy
- tax policy
- public governance
- corporate governance
- policies for enabling responsible business conduct
- developing human resources for investment
- investment framework for green growth
- investment in infrastructure
- financing investment.

The Framework is neither prescriptive nor binding. It emphasises the fundamental principles of rule of law, transparency, non-discrimination and the protection of property rights but leaves the country concerned to choose suitable policies, based on its economic circumstances and institutional capabilities. It helps governments to design and implement policy reforms to create a truly attractive, robust and competitive environment for domestic and foreign investment.

The Framework was updated in 2015 through an inclusive global process, led by a global task force composed of both developed and developing countries, to include the most up-to-date international good policy practice.

For more information, see [www.oecd.org/investment/pfi.htm](http://www.oecd.org/investment/pfi.htm)
Self-evaluation, peer reviews, regional co-operation and multilateral discussions can all benefit from the insights offered in the Framework and help identify where to prioritise investment policy reforms for sustainable development. The Framework is a key reference point for international organisations’ capacity development programmes, for investment promotion agencies, and for providers of development co-operation as they assist developing country partners in improving their investment environment. It supports business, labour and other non-governmental organisations in their dialogue with governments, and can also serve as a basis for international co-operation on investment-related issues, exemplified by the ASEAN-OECD Investment Programme, and the NEPAD-OECD Africa Investment Initiative.4

The OECD, working with member and non-member economies, partner organisations, providers of development co-operation and other stakeholders, assists in developing methodologies, including indicators of progress, and institutional capacity building for the effective use of the Framework in light of different circumstances and needs.

The Policy Framework for Investment also provides a base for OECD work on investment in specific sectors for sustainable development, such as clean energy.

**Box 3. Investment climate reform in Myanmar**

The OECD and the World Bank Group (WBG) joined forces to provide the Myanmar government with an effective advisory service on comprehensive investment climate reform. The recommendations of the Policy Framework for Investment-based Investment Policy Review prompted requests from the government of Myanmar for support for its short-term reforms, enabling the WBG to step in to provide focused technical assistance.

In practice this has resulted in a three-way partnership in which the OECD’s analytical framing is complemented by WBG support to implement key reforms in the country. This road-tested model will be applied to other countries jointly identified by the OECD and the WBG.


The OECD has long-standing experience in helping governments improve the enabling conditions for private investment in clean energy infrastructure. The *OECD Policy Guidance for Investment in Clean Energy Infrastructure* (OECD, 2015d) is designed to assist policy makers to address investment barriers and identify ways to mobilise private investment in renewable energy and energy efficiency in the electricity sector. It identifies key issues in investment policy, investment promotion and facilitation, competition, financial markets and public governance, as well as cross-cutting issues. In addition to providing a basis for national reviews, the policy guidance can facilitate cross-country comparison and multi-stakeholder policy dialogue.
Governments must also co-operate at the multilateral level to address barriers to international trade and investment in clean energy. The OECD project on *Overcoming Barriers to International Investment in Clean Energy* (OECD, 2015b forthcoming) highlights the increasing use of policies to protect domestic manufacturers in the solar photovoltaic and wind energy sectors. For example, local-content requirements are likely to increase the cost and slow the speed of market penetration by clean energy technologies. Nonetheless, they have been planned or implemented in at least 21 OECD countries and emerging economies since the financial crisis. Conversely, preferential access to finance for outward investing and exporting state-owned enterprises can also distort clean energy markets. The OECD can host multilateral dialogue on how to fight protection and design more coherent support policies for increasing investment in clean energy.

**Promoting responsible business conduct for development**

Responsible business conduct is an essential part of today’s open trade and investment climate, given the increasingly global nature of value chains. It is also important in driving sustainable development and ensuring that enterprises create long-term value for the societies in which they operate.

Responsible business conduct is about the positive contribution the private sector can make to sustainable and inclusive development, while avoiding and addressing the negative impacts of business operations. With increasing expectations by society for responsible business conduct, demand is growing for governments to provide adequate tools to enable responsibility standards to be applied throughout the economy to ensure a level playing field, both nationally and – increasingly – internationally.

Broader uptake of responsible business practices globally would help to level the playing field for business, create a more open investment climate, and improve conditions in global value chains. The *OECD Guidelines for Multinational Enterprises* (OECD, 2011) are currently the most comprehensive set of government-backed recommendations on responsible business. The Guidelines provide voluntary principles and standards for responsible business conduct, covering areas such as employment and industrial relations, human rights, environment, information disclosure, combating bribery, consumer interests, science and technology, competition and taxation. To date, 46 countries, representing OECD, emerging and developing economies, adhere to the Guidelines.

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**Box 4. The Policy Framework for Investment in Agriculture inspires reform in Burkina Faso**

A review of the OECD Policy Framework for Agricultural Investment in Burkina Faso was completed in 2011. The development of a legal Code on Agricultural Investment was one of the major policy recommendations of the review. In response, the Government of Burkina Faso created an inter-ministerial task force to develop the code, with the support of the Institut Euro-Africain de Droit Economique (INEADEC). Local experts developed thematic notes on key issues related to agricultural investment, including the rights and responsibilities of investors, land registration, research and development, finance and taxation, agricultural trade, and family enterprises. A workshop was organised in September 2013 with the participation of OECD and the World Bank to discuss these inputs as a basis for developing the code. The Draft Code on Agricultural Investment was presented to the government in May 2014 and consultations are now underway for its adoption.

The OECD Guidelines incorporate the expectation that enterprises carry out risk-based due diligence across all major areas of business ethics for their own operations as well as their supply chains. Incorporating responsible business standards into global supply chains expands the reach of these standards to thousands of companies and can therefore be an extraordinary lever to improve business standards worldwide and to level the playing field. To help companies and governments deal effectively with due diligence along their entire supply chains, the OECD is developing government-backed, supply chain-specific standards for responsible business conduct in the extractive, finance, agriculture and textiles sectors. For example, the OECD Due Diligence Guidance for Responsible Supply Chains of Minerals from Conflict-Affected and High-Risk Areas provides a practical benchmark for companies along the entire mineral supply chain and its inclusion in international, national and industry standards and initiatives is growing.

Another unique feature of the Guidelines is that they include a grievance mechanism: all governments that adhere to the Guidelines must set up an accessible and impartial body (known as National Contact Points) to resolve complaints over poor business conduct. The contact points act as a platform to which stakeholders and the general public can bring complaints (known as “specific instances”) and engage in a dialogue about the alleged non-observance of the Guidelines by a multinational. So far, almost 300 specific instances have been submitted worldwide, mainly in the manufacturing, extractives and services sectors.

Looking forward
A part of the challenge of financing for development is strengthening frameworks to channelling private resources into the right places to support sustainable development goals. Another is increasing the capacity of the local economy and the public sector to benefit fully from private investment. Governments should consider existing frameworks and instruments such as the Policy Framework for Investment and the OECD Guidelines for Multinational Enterprises to support their efforts in maximising the positive impact of private investment for sustainable development.
NOTES

1. Development finance is discussed in depth in other papers in this Reflections Series (e.g. OECD, 2013b; OECD, 2013c).

2. Estimates of non-agricultural employment in the informal economy range from an average of 50% in the Middle East, North Africa, and Latin America, to over 70% in sub-Saharan Africa and Asia (ILO, 2012).

3. ASEAN is the Association of Southeast Asian Nations. For details of the investment programme see www.oecd.org/daf/inv/investment-policy/seasia.htm.

4. NEPAD is the New Partnership for Africa’s Development. Details of the investment programme can be found at www.oecd.org/investment/investmentfordevelopment/africa.htm.

5. The OECD Guidelines define due diligence as the process through which enterprises can identify, prevent, mitigate and account for how they address their actual and potential adverse impacts as an integral part of business decision-making and risk management systems. Where enterprises have large numbers of suppliers, they are encouraged to identify general areas where the risk of adverse impacts is most significant and, based on this risk assessment, prioritise suppliers for due diligence.

6. For more information visit http://mneguidelines.oecd.org/implementation.

7. For more information on specific instances consult the Database of Specific Instances at http://mneguidelines.oecd.org/database.
REFERENCES


The United Nations (UN) Millennium Development Goals (MDGs) were established in 2000/1 and consist of eight development objectives to be achieved by 2015. It is widely agreed that the MDGs have been effective in mobilising worldwide awareness, leveraging resources, guiding global development efforts and increasing accountability. It is also impressive how close the world will get to most of the MDGs by 2015. There is need, however, for a successor framework once the MDGs expire in 2015 to keep the momentum built to date. The OECD played a pivotal role in defining the MDGs. With two years to go, the OECD is increasing its efforts to support the achievement of the MDGs, and at the same time thinking about how it can help the UN in developing a new agenda and framework post-2015. The OECD has a number of areas of expertise which could play an important role in shaping this post-2015 agenda and framework. In the overview brochure for this series, the OECD proposes eleven areas which would be of particular relevance (Beyond the MDGs: Towards an OECD contribution to the post-2015 agenda). This brochure focuses on one of these – investment for sustainable development in the post-2015 development agenda.

Element 1: Measuring what you treasure and keeping poverty at the heart of development
Element 2: Developing a universal measure of educational success
Element 3: Achieving gender equality and women’s rights
Element 4: Integrating sustainability into development
Element 5: Strengthening national statistical systems
Element 6: Building effective institutions and accountability mechanisms
Element 7: Developing and promoting peacebuilding and statebuilding goals
Element 8: Ensuring policy coherence for development
Element 9: Sharing knowledge and engaging in policy dialogue and mutual learning
Element 10: Promoting the Global Partnership for Effective Development Co-operation

Element 11: Measuring and monitoring development finance

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