



27-28 March 2008

# GLOBAL FORUM VII

## ON International Investment

## POLICY FRAMEWORK FOR INVESTMENT: USER'S TOOLKIT – DRAFT USER GUIDANCE ON THE PFI TRADE POLICY CHAPTER

### Session 1.2.: Trade policy

The PFI User's Toolkit project is in response to a need for specific and practical implementation guidance revealed from the experience of the countries that have undertaken projects using the PFI. Development of the Toolkit entails a process involving government users, co-operation with other organisations, OECD Committees with specialised expertise in the policy areas covered by the PFI and interested stakeholders. This document is an unedited preliminary draft of the Toolkit's guidance on the PFI trade policy chapter, prepared by an external consultant to the Secretariat. It is distributed as part of the conference documentation for the relevant session in the programme at the Global Forum on International Investment. The views expressed in this paper do not necessarily represent those of the OECD or its member governments.

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**POLICY FRAMEWORK FOR INVESTMENT: USER'S TOOLKIT  
DRAFT USER GUIDANCE ON THE PFI TRADE POLICY CHAPTER**

**3.1 What recent efforts has the government undertaken to reduce the compliance costs of customs, regulatory and administrative procedures at the border?**

**Explanation and rationale for the question**

The relationship between international trade, domestic and foreign investment has evolved significantly in recent years, responding to changes in technology, host country policies, particularly the greater openness of trade and investment regimes, as well as in the organization of production within globally-active firms. In a world economy structured around regional and/or global supply chains and production networks in manufacturing and service industries alike, cross-border investment is increasingly motivated by productivity-enhancing opportunities rather than by access to local markets or the extraction natural resources though the latter motivations clearly remain salient in certain sectors and regions. Under these new circumstances, trade policies and customs procedures that fail to conform to internationally recognised standards can result in significant delays in cross-border deliveries and increase business costs. This makes it harder for host countries to harness fully the efficiency gains resulting from global supply chains, lowering rates of return and potentially discouraging investment, both domestic and foreign. Customs procedures can often be simplified through harmonised requirements, application of internationally-agreed standards and regulatory co-operation (e.g. to enable pre-arrival clearance of shipments), with beneficial effects on the overall investment climate. More generally, because of the increasingly complementary relationship between trade and investment, trade policies and customs procedures can no longer be framed or implemented in isolation of their effects on investment performance. It is, accordingly, essential to assess periodically the impact that a host country's customs, regulatory and administrative procedures exert on the investment climate.

**Guidance and practices to scrutinise**

Question 3.1 draws attention to the manifold roles that customs administrations assume in ensuring effective compliance with national laws regarding the security and protection of consumers of foreign-produced goods and in mobilizing tariff receipts – one of the largest sources of government revenues for many developing countries, particularly least developed ones. There is considerable empirical evidence showing how a country's overall level of competitiveness and trade growth are linked to the efficiency and effectiveness of its customs procedures. Hummels (2000), for instance, estimates that each additional day of transit due to obsolete customs procedures or other inefficiencies in transportation infrastructure is equivalent to 0.8% of a shipment's import value. Wilson *et al* (2002) have estimated for the Asia-Pacific Economic Cooperation (APEC) region the trade impact of enhancing the performance of trade facilitation encompassing port logistics, customs procedures, the domestic regulatory environment, standards harmonization, business mobility, e-business activity and administrative transparency. They estimated that bringing the below-average APEC members half-way towards average APEC performance indicators would increase intra-APEC trade by about USD 280 billion. Of the total, half would come from the

improvement of port logistics alone.<sup>1</sup> In a global environment characterised by high and increasing capital mobility, cross-border trade and investment activity is quite naturally drawn to locations that offer efficient, supportive and facilitative business environments. Conversely, it tends to shun locations with weak physical infrastructures for trade and costly and unpredictable administrative procedures, both of which are typically synonymous with high cost, riskier, environments. Host countries' customs administrations and procedures must not be allowed to serve - or be perceived as serving- as a barrier to international trade and investment.

Question 3.1 also relates to the preparation, adoption and application of standards, as well as to testing and certification procedures of imported products. Compliance with a myriad of technical regulations involving various agencies in the importing country can be burdensome for manufacturers and exporters, creating unnecessary trade and investment obstacles and involving potentially significant transaction costs. Such costs may arise from the need to translate foreign regulations, the hiring of legal and technical expertise to advise on complying with foreign regulations, and the changes in production methods and/or facilities that may be required in order to fulfil such compliance. Such costs, to which one may add demands for illicit payments in some host country environments, may discourage firms from trying to sell or establish abroad. Moreover, in the absence of international disciplines, risks arise that technical regulations and standards could be adopted and applied solely to protect domestic industries and thus deter imports or foreign investment.

### **Criteria and indicators to examine in responding to the question**

An assessment of Question 3.1 calls for an examination of the following criteria and the application of the following indicators:

- Measuring the time taken for the release of imported goods responds to the concerns of traders regarding possible delays in customs clearance procedures. Doing so can help customs administrations to better respond to the need for firms to plan ahead for the movement of goods across borders in order to meet tight production schedules and just-in-time inventory and delivery systems. The time required to release goods has increasingly become the measure by which the international trading community assesses the effectiveness of a host country's customs administration. The Time Release Study prepared by the World Customs Organisation (WCO) provides guidance to customs administrations on the best way to apply this method of internal review. See [http://www.wcoomd.org/home\\_wco\\_topics\\_pfoverviewboxes\\_tools\\_and\\_instruments\\_pftoolstimerelease.htm](http://www.wcoomd.org/home_wco_topics_pfoverviewboxes_tools_and_instruments_pftoolstimerelease.htm)
- Benchmarking is a technique that assists administrations in identifying and implementing best practices in customs procedures. One example relates to comparisons of how national customs agencies control warehouses in a country. A domestic benchmarking exercise is typically a first step before a host country will consider international benchmarking. To assist countries in carrying out international benchmarking in customs procedures, the WCO has developed the Customs International Benchmarking Manual which provides guidance to administrations for improving their efficiency and effectiveness by comparing procedures or processes with the same or similar procedures and processes carried out by other administrations. It relies on collaborative initiatives between customs authorities by sharing information on processes and measures that

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<sup>1</sup> Hummels, D. (2000), "Time as a Trade Barrier", Purdue University.  
Wilson, J., C.L. Mann, Y.P. Woo N. Assanie and I. Choi (2002), "Trade Facilitation: A Development Perspective in the Asia-Pacific Region", Asia-Pacific Economic Cooperation, Singapore

encourage innovative practices and improve performance. See <http://www.wcoomd.org/pfcustomsinternationalbenchmarkingmanual.htm>

- Seeking improved efficiency and effectiveness in customs procedures is an increasingly acknowledged policy objective and the main policy goal of the International Convention on the Simplification and Harmonisation of Customs Procedures, known as the Kyoto Convention which entered into force in 1974. The revised Kyoto Convention (February 2006) provides for the application of new technology, the implementation of new business-friendly approaches towards customs controls and the willingness of private sector partners to engage with customs administrations in mutually beneficial alliances. Chief among the new governing principles is the commitment by customs administrations to provide greater transparency and predictability for all those involved in aspects of international trade. In addition, customs administrations commit to adopt the use of risk management techniques, co-operate with other relevant authorities and the business community, and adopt appropriate international standards. With 53 contracting members in mid-2007, the aims of the revised Kyoto Convention remain to be achieved in many countries, particularly developing and least developed countries. PFI user should examine the revised Kyoto Convention with a view to put in place a structure responsible for improving efficiency and effectiveness in customs procedures. See <http://www.wcoomd.org/ie/en/en.html3>
- Improving the efficiency of capacity building efforts and the avoidance of waste and duplication in trade facilitation are the main elements of a report prepared by the International Chamber of Commerce (ICC). It addresses issues such as coordination, management capacity, common standards, confidence building and the contribution of the private sector to capacity building, all of which are issues that a PFI user should examine. An Annex to the report features summary findings of a private sector study on progress under a Europe-Asia trade facilitation action plan. Another Annex of the report outlines ICC recommendations for a WTO Agreement on Trade Facilitation. See: [http://www.adb.org/Documents/Events/2003/ASEM\\_Customs\\_Procedures/text\\_kadarisman.pdf](http://www.adb.org/Documents/Events/2003/ASEM_Customs_Procedures/text_kadarisman.pdf)
- Ensuring that technical regulations and standards and conformity assessment procedures do not create unnecessary obstacles to international trade is a major policy objective of the WTO Agreement on Technical Barriers to Trade (TBT). The Agreement targets procedures that would give domestically produced goods an unfair advantage and encourages countries to recognize each other's procedures for assessing whether a product conforms to technical regulations and standards. In so doing, the Agreement encourages the adoption of - and reliance on - international standards. It also sets out a Code of Good Practice for both governments and non-governmental or industry bodies to prepare, adopt and apply voluntary standards (see Annex 3 of the TBT Agreement [http://www.wto.org/english/docs\\_e/legal\\_e/17-tbt\\_e.htm](http://www.wto.org/english/docs_e/legal_e/17-tbt_e.htm)). The Agreement furthermore provides for technical assistance in favour of developing countries. PFI users may wish to familiarise themselves with the training materials, databases on TBT and relevant documents available on the WTO website and disseminate such information and related documentation to stakeholders. See [http://www.wto.org/english/tratop\\_e/tbt\\_e/tbt\\_tech\\_e.htm](http://www.wto.org/english/tratop_e/tbt_e/tbt_tech_e.htm).

### **Reference on case studies and good practices**

- The World Bank Group has prepared a series of policy toolkits, including one dealing with reforming customs procedures and is entitled "Reforming the Regulation Procedures for Import and Export: Guide for Practitioners". It provides detailed information on best practice approaches towards clearance processes, export and duty deferral regimes (exemptions, drawback, free enterprise zones, etc).

See [http://rru.worldbank.org/Documents/Toolkits/customs/Customs\\_Full\\_Toolkit.pdf/](http://rru.worldbank.org/Documents/Toolkits/customs/Customs_Full_Toolkit.pdf/)

- The WTO's Trade Facilitation Web page contains updated information on the state of ongoing multilateral negotiations on trade facilitation and a collection of documents on the subject, including the 2001 briefing entitled "[Trade Facilitation: Cutting Red Tape at the Border](#)" which summarises discussions among WTO Members on reducing the vast amount of red tape that still affects the cross-border movement of goods across borders. See [http://www.wto.org/English/tratop\\_e/tradfa\\_e/tradfa\\_e.htm](http://www.wto.org/English/tratop_e/tradfa_e/tradfa_e.htm)
- The WTO Technical Barriers to Trade (TBT) Web page contains updated information on TBT Committee meetings and a collection of related documents. See [http://www.wto.org/english/tratop\\_e/tbt\\_e/tbt\\_e.htm](http://www.wto.org/english/tratop_e/tbt_e/tbt_e.htm)
- The Asia-Pacific Economic Cooperation (APEC) Committee on Trade and Investment has recently endorsed the [second Trade Facilitation Action Plan \(TFAP2\)](#), which contains a list of collective actions to facilitate a further five percent reduction in transaction costs by 2010 (an initial five percent reduction target was met for the 2001-06 period). The TFAP2 provides for a comprehensive review of progress in implementing this business facilitation agenda and covers measures such as:
  - Time Release Survey;
  - Implementation of the APEC Framework based on the WCO Framework of Standards to Secure and Facilitate Global Trade;
  - Simplification and harmonization based on the revised Kyoto Convention;
  - Adoption of and support for the UN/EDIFACT paperless trading initiative;
  - Harmonization of tariff structure with the HS Convention;
  - Implementation of customs-related WTO agreements;
  - Aligning APEC economies' domestic standards with international standards;
  - Achieving mutual recognition of conformity in regulated and voluntary sectors.
  - For more information on APEC activities in area of trade facilitation, see [http://www.apec.org/apec/apec\\_groups/committees/committee\\_on\\_trade/sub-committee\\_on\\_customs.html](http://www.apec.org/apec/apec_groups/committees/committee_on_trade/sub-committee_on_customs.html).

- The APEC guidebook on Compliance with the revised Kyoto Convention (International Convention on the Simplification and Harmonisation of Customs Procedures) sets out the steps needed for a country to become "Kyoto Compliant". It addresses the key substantive provisions of the revised Kyoto Convention; features a situation analysis of a country's current position in relation to the Convention; helps countries to undertake a gap analysis and to implement an action plan that will enable a country to become fully compliant with, or accede to, the Convention. See: [http://www.apecsec.org.sg/apec/apec\\_groups/committees/committee\\_on\\_trade/sub-ommittee\\_on\\_customs.downloadlinks.0004.LinkURL.Download.ver5.1.9](http://www.apecsec.org.sg/apec/apec_groups/committees/committee_on_trade/sub-ommittee_on_customs.downloadlinks.0004.LinkURL.Download.ver5.1.9)
- The Asian Development Bank has released a conference volume entitled "Simplification of Customs Procedures, Reducing Transaction Costs for Efficiency, Integrity and Trade Facilitation". It includes discussions of the fiscal and governance dimensions of customs procedures, initiatives of key international organisations towards customs simplifications, and papers on systems and procedures for improving service and efficiency in customs. See: [http://www.adb.org/Documents/Conference/Simplifications\\_of\\_Customs/](http://www.adb.org/Documents/Conference/Simplifications_of_Customs/)

**3.2 What steps has the government taken to reduce trade policy uncertainty and increase trade policy predictability for investors? Are investors and other interested parties consulted on planned changes to trade policy?**

**Explanation and rationale for the question**

Foreign investors typically approach business environments characterized by greater risk and policy uncertainty through upward adjustments in the rate of return required to undertake an investment project. There is considerable empirical evidence attesting to the dampening effects on FDI activity resulting from unpredictable host country policy. In the trade policy domain, uncertainty may result from undue administrative discretion and non-transparent regulatory regimes, and by a host of governmental actions and decisions that can obstruct the smooth functioning of international supply chains and generate instability in pricing structures. Promoting a healthy culture of transparency in trade and investment policy making assumes considerable importance in this regard. This can involve institutionalized forms of external stakeholder consultations with business and other civil society constituents, better communication of policy announcements, and locking-in of policy changes under legally-binding instruments, all of which can contribute to a more stable and predictable environment in which enterprises can plan and carry out their investment and business activities.

**Guidance and practices to scrutinise**

The issues arising from Question 3.2 highlight the importance of the quality of a host country's regulatory culture and the degree to which the process of policy-making is sensitive to the effects of domestic regulatory conduct on the investment climate. PFI user should examine the following issues and assess the degree and manner in which host country governments perform:

- To what extent has the government established effective public consultation mechanisms and procedures, including prior notification requirements prior to enacting new laws and regulations affecting the climate for doing business?

Well-publicised, well-organised, highly accessible and well-timed opportunities for public comment on proposed regulatory changes, as well as clear guidelines of accountability showing how comments from interested constituencies have been handled are important features of a well-

designed system of stakeholder consultation. Such consultations should not be limited to insiders (incumbents) but should be open to all interested parties. Good practice in this area may be encouraged by clear guidance to regulators on how such consultations are to be conducted.

- Do public consultation mechanisms allow sufficient access for all interested parties, including foreign stakeholders?

For any given regulatory proposal, too wide discretion on who is to be consulted and how may dilute the intended benefits of a broad-based consultation mechanism. In particular, new entrants, small and medium-sized enterprises (SMEs) and foreign stakeholders (particularly non-established) may be at a disadvantage if consultations are informal in character. Maintaining an appropriate balance between open consultation procedures and the flexibility of informal procedures is important, with the understanding that specific consideration of access possibilities by new foreign stakeholders may be required in certain circumstances. Although responsibility for policy decisions ultimately rests with the host country government, transparency in the way comments are solicited and received and provision of timely information on regulatory decisions as well as access to administrative tribunals in instances where decisions may be challenged by private operators can all significantly enhance the credibility of the process and the prospects of regulatory compliance by the economic actors.

- To what extent are customs and border procedures designed and implemented to provide consistency, predictability, simplicity and transparency so as to avoid unnecessary burdens on the flow of goods, services and business people?

Measures to simplify border procedures and to avoid unnecessary burdens on the flow of goods, services and business people include doing away with unnecessary or outdated requirements, such as requesting information that is already available to the authorities, or requesting information more than once from different government agencies. Addressing such problems involves the updating of domestic regulatory requirements through periodic audits or built-in sunset clauses so as to take account of changed contexts, technologies and markets and ensuring that the regulatory compliance burden remains broadly proportional to the underlying policy objectives and that, whenever available, least trade- and investment-restrictive policy options be pursued. For instance, it should not cost more to implement a specific border regulation than what is actually gained by way of customs revenue. The simplification of border procedures further implies that applicable controls take place in a way that does not add unnecessary costs to traders or generate undue delays at the border, for instance through the implementation of risk-based and targeted operations and the replacement of some border controls by post-clearance audits (see question 3.1 above).

### **Criteria and indicators to examine in responding to the question**

Moreover, an assessment of Question 3.2 calls for an examination of the following criteria and performance indicators:

- Establish regulatory arrangements that ensure that the public interest is not subordinated to that of regulated entities and other stakeholders.
- Consult with all significantly affected and potentially interested parties, whether domestic or foreign, where appropriate at the earliest possible stage while developing or reviewing regulations, ensuring that the consultation itself is timely and transparent, and that its scope is clearly understood.

- Create and update on a continuing basis public registries of regulations and business formalities, or use any other means of ensuring that domestic and foreign businesses can easily identify all regulatory requirements applicable to them. Electronically accessible, interactive Web sites should be a priority to make rulemaking information available to the public and to receive public comment on proposed legal and regulatory changes.
- Ensure that administrative procedures for applying regulations and regulatory decisions are transparent, non-discriminatory, do not unduly delay business decisions; and ensure that efficient appeals procedures are in place.
- Ensure that regulatory institutions are accountable and transparent, and include measures to promote integrity.

### **Reference on case studies and good practices**

- The Integrated Checklist on Regulatory Reform was developed through co-operative work in APEC and OECD. It is a voluntary tool for governments to evaluate their regulatory reform process, focussing on regulatory, competition and market openness policies. Market openness is addressed through questions regarding the general framework governing the development and implementation of regulation, complemented by questions drawing out possible impacts on market openness. The goal is to ensure that regulatory policies reinforce the ability of economies to benefit from globalisation and international competition. See: <http://www.oecd.org/dataoecd/3/53/36326815.pdf>
- The European Commission report below describes how policy makers in the European Union consult with stakeholders in the shaping of national and regional policies affecting small businesses. Along with providing several case studies, the report includes twelve recommendations addressed to national and regional governments on how to establish a more efficient dialogue with stakeholders and improve consultation procedures. See: [http://ec.europa.eu/enterprise/entrepreneurship/support\\_measures/stakehold/doc/final\\_report\\_en.pdf](http://ec.europa.eu/enterprise/entrepreneurship/support_measures/stakehold/doc/final_report_en.pdf)
- The report below prepared by the U.K government offers practical guidelines for maximizing the effectiveness of public consultation procedures. See: <http://www.cabinetoffice.gov.uk/REGULATION/documents/consultation/pdf/code.pdf>
- The World Bank Web page below features links to a number of reports and other sites dealing with efforts to enhance investment climates by improving legal institutions and judicial systems in host countries. See: <http://rru.worldbank.org/PapersLinks/Reducing-Business-Risks/>

### **3.3 How actively is the government increasing investment opportunities through market-expanding international trade agreements and through the implementation of its WTO commitments?**

#### **Explanation and rationale for the question**

WTO-consistent trade measures and legally-binding commitments entered into in multilateral and preferential trade and investment agreements can help to attract greater flows of investment. It can do through several channels: by creating larger markets, by raising the potential to exploit scale economies that can make investments more profitable and more broadly by locking-in recent policy changes and/or signalling future policy changes so as to promote an orderly process of adjustment to changed competitive conditions. The most recent generation of preferential trade agreements typically feature a comprehensive set of disciplines on investment protection and liberalization that complement domestic efforts at creating a sound investment climate. In particular, trade measures that are consistent with the WTO's Agreement on Trade-Related Investment Measures (TRIMs) empower enterprises to source suppliers globally, and therefore to sell their output at globally competitive prices. In the process, this may help create additional investment opportunities.

#### **Guidance and practices to scrutinise**

This broad question draws attention to the ability of governments to formulate, negotiate and implement multilateral and preferential (bilateral and regional trade and investment) agreements, and to evaluate their trade and investment impacts with a view to maximising their benefits on overall host country performance. Since the creation of the WTO, member countries are subject to the same rights and obligations that were adopted by consensus, although developing and, especially, least developed countries (LDCs), are afforded various forms of special and differential treatment in recognition of their more limited implementation capacities. Such treatment comprises longer implementation periods, lower liberalisation commitments, broader exemptions as well as the enhanced provision of trade-related technical assistance. While unilateral liberalisation continues to be practiced extensively in many countries, particularly with regard to foreign investment and service sector policies, several countries or country groupings are also seeking to speed up their economic development process through faster and broader liberalisation commitments scheduled under preferential trade and investment agreements. For some countries however, particularly LDCs, a lack of capacity and resources act as major impediments on their ability to negotiate, implement and derive concrete benefits from such greater engagement. Through preferential access granted by developed countries, such as the Generalised System of Preferences (GSP), Everything But Arms (EBA) and other similar arrangements, LDCs may often have lower incentives to further their market integration above and beyond their WTO commitments.

Question 3.3 is also about assisting stakeholders in identifying and pursuing trade and investment opportunities, and better integrating into regional and global supply chains and distribution networks. This is a particularly daunting challenge for SMEs in both developed and developing countries. Strengthening the capacity of firms to identify growing trade and investment opportunities is an important – and typically positive – externality flowing from growing international economic and trade relationships. Engagement in formal trade and investment negotiations at the bilateral, regional and multilateral levels creates a space in which enhanced trade and investment opportunities can be pursued by private sector stakeholders.

## Criteria and indicators to examine in responding to the question

The Doha Development Agenda has helped crystallize a growing awareness worldwide that the ability of governments to durably improve their capacity to formulate, negotiate and implement trade and investment agreements, and to situate such policy initiatives within the broader canvass of national development goals, requires that significant resources be channeled towards trade and investment capacity building initiatives. An assessment of Question 3.3 calls for an examination of the following criteria and performance indicators :

- For developed and (especially) developing countries, a key challenge is to strengthen trade-related analytical and negotiating capacity both in their capitals and in their permanent representations in Geneva so as to better monitor WTO developments, participate more actively in ongoing negotiations and the WTO's dispute settlement mechanism as well as to gain a better understanding of the articulation between multilateral and preferential developments in trade and investment policies.
- For LDCs, most of whom have limited or no permanent representation in Geneva, the key is to take maximum advantage of the various trade-related capacity-building activities on offer at various levels to strengthen their capacity to identify and pursue/defend offensive and defensive interests at the negotiating table (regardless of the negotiating setting) and to mainstream trade and investment policy into national development plans with a view to: (i) addressing key bottlenecks in trade infrastructure; (ii) durably enhancing analytical and negotiating skills within governments; (iii) strengthening the regulatory institutions involved in the implementation of commitments undertaken in trade and investment agreements; and (iv) enhancing the capacity to supply liberalized markets with goods and services that meet market demands and product standards. The latter challenges – those of regulatory strengthening and enhancing supply capacities – may be of direct relevance to many higher income developing countries.

As regards more specifically the issue of assisting stakeholders, particularly SMEs, in identifying and pursuing the trade and investment opportunities opened up by engagement in negotiated market opening, PFI users should examine the following criteria and performance indicators :

- Preparing a list of preferential trade and investment agreements currently in force and identifying:
  - The share of total trade covered by each agreement;
  - The share of total investment originating from parties to the preferential agreements;
  - The nature and sectoral incidence of key tariff and non-tariff barriers governed by the various agreements;
  - The stage of implementation of each agreement and an identification of implementation bottlenecks within key regulatory agencies or ministries;
  - In the case of customs unions, the share of regional trade subject to the common external tariff; and
  - Remaining obstacles regarding the right of establishment and other investment restrictions by respective agreement.
- Encouraging greater two-way communication and exploring future cooperation between relevant government agencies, industry associations and chambers of commerce of the countries involved in preferential trade and investment agreements.

- Encouraging further cooperation between investment and trade promotion agencies, especially by providing various forms of market intelligence to SMEs in priority sectors.
- Identifying capacity building priorities in relevant government ministries and agencies and directing attention to the capacity development needs of SMEs.
- Creating opportunities for business to derive greater benefits from trade and investment promotion activities, such as through participation in trade fairs.

### Reference on case studies and good practices

- The WTO Trade and Development Web page provides access to updated information on WTO-related work that takes place, *inter alia*, in the Committee on Trade and Development and the Sub-Committee on Least Developed Countries. It also provides access to various initiatives aiming at building trade capacity, *i.e.* Aid for Trade, the Enhanced Integrated Framework (EIF), and the Joint Integrated Technical Assistance Programme (JITAP). See: [http://www.wto.org/english/tratop\\_e/devel\\_e/devel\\_e.htm](http://www.wto.org/english/tratop_e/devel_e/devel_e.htm)
- The OECD document below recalls how governments have an important role to play in creating a good environment for attracting investment. It lists a series of good governance- and transparency-enhancing measures likely to improve investment climates. Strong governance and transparency encourage domestic and foreign investment in an internationally competitive environment. See: <http://www.oecd.org/dataoecd/2/36/20686331.pdf>
- The UNIDO report below summarizes the results of a survey of investor experiences in selected African countries. It provides information on the perceptions and service needs of investors, the importance of different factors in the location process (including for different sectors and types of FDI projects) as well as on the experience of investors in dealing with various investment promotion agencies. See: <http://www.unido.org/file-storage/download/?file%5fid=19589>
- The UNCTAD Web page on Investment, Technology and Enterprises Development provides access to the organization's annual flagship "World Investment Report" whose 2006 issue focused on the rise of foreign direct investment (FDI) by transnational corporations from developing and transition economies. See: <http://www.unctad.org/Templates/webflyer.asp?docid=7431&intItemID=2983&lang=1>
- The Columbia Program on International Investment in partnership with the Economist Intelligence Unit publishes an annual report *which assesses most recent* FDI flows and forecasts flows over a five year period. The latest report is entitled "*World Investment Prospects to 2011: Foreign Direct Investment and the Challenge of Political Risk*". It contains the results of a survey of over 600 corporate executives concerning their investment intentions and pays special attention to the rise of FDI protectionism and regulatory risk. See: <http://www.cpii.columbia.edu/pubs/>

### **3.4 How are trade policies that favour investment in some industries and discourage it in others reviewed with a view to reducing the costs associated with these distortions?**

#### **Explanation and rationale for the question**

Governments sometimes use trade policy instruments, such as import tariffs (including tariff peaks and tariff escalation), product standards and licensing requirements, IPR protection, contingent protection instruments (anti-dumping and safeguards) as well as subsidies (investment incentives) to promote investment in targeted industries. Considerable care must be taken in ensuring that such measures do not result in distortions that are damaging to resource allocation and the overall investment climate. Favoured (typically domestically owned or controlled targets) industries compete for resources with other enterprises, domestic and foreign, and their ability to receive special policy-induced favours can crowd out investment and production in activities that are more productive. Moreover, to the extent that the output of the targeted industry is an input to others, competitiveness in final products, including in world markets, may be durably taxed, reducing firm profitability and the attractiveness of additional investment in such export-oriented sectors. Such costs are typically long-lived, since they are often non-transparent and spread among many producers. In turn, this may lessen the incentive for governments to reform such practices.

If a host country government seeks to promote investment in a specific industry through trade policies, this should be done in a transparent manner and consistent with existing international obligations, such as those found in the WTO Agreement on Subsidies and Countervailing Measures, the TRIMs Agreement, the Agreement on Trade-Related Intellectual Property Rights (TRIPs) as well as the General Agreement on Trade in Services (GATS). A first best approach is to maintain a trade regime that allows competitive industries to develop and flourish as much as possible under conditions of non-discriminatory treatment, rather than to try to nurture competitiveness behind trade policies that tilt competitive conditions in favour of incumbents (be they domestic or foreign). This does not necessarily imply removing all forms of import protection, nor does it assign a completely passive role to domestic policy. What it entails however is a keener sense of the role – and attendant costs and benefits- of assigning to trade policy objectives that other domestic policy instruments may be more suitably equipped to pursue, such as labour market, education, innovation and SME development policies.

#### **Guidance and practices to scrutinise**

A key aspect of question 3.4 relates once more to a host country's overall regulatory and business culture and whether the public authorities are called upon to periodically assess the economy-wide impacts of existing or proposed trade policy measures favouring some industries. PFI users should examine the economy-wide impacts of newly proposed regulatory measures favouring particular industries and ensure that the terms of reference of reviews of existing trade measures pay proper attention to anticipated effects on trade and investment activity. This can be done within the context of regulatory impact assessment (RIA) analysis, a tool used today in most developed countries and in several developing countries to better measure the economic and social welfare impacts of regulation and identify the most efficient and/or least trade- or investment-restrictive alternatives. RIAs are widely recognized as important tools that can contribute to durably improving the business environment and promoting regulatory efficiency and thus the investment climate.

Question 3.4 is particularly relevant in regard to sectors characterized by a high degree of regulatory oversight, such as electricity, energy, telecommunications, transportation and financial services, which have historically been subject to various trade, investment and broader competition restrictions on grounds of various market failures. Technological advances and far-reaching reassessments of the shifting borders

between the market and the state (resulting in increasingly liberal and competitive environments) have seen trade and investment restrictions come under increasing challenges around the world. The end result has been an unprecedented wave of pro-competitive regulatory reform, privatization and market liberalization in most parts of the world. It is today widely accepted that inefficiencies in the supply of essential business services can adversely affect both the performance of firms and that of the overall economy to the extent that such services feed into all an economy produces, brings to market and trades in. Several key infrastructure services sectors that were until recently under monopolistic state ownership are today supplied competitively in markets governed by independent regulatory authorities whose decisions and rules exert direct impacts on domestic competitive conditions and consumer choices and prices. PFI users should also examine whether regulatory agencies are required to periodically assess the trade and investment impacts of their regimes and decisions with a view to minimising the risk that such decisions may nullify or impair liberalisation commitments scheduled under international trade and investment agreements.

### **Criteria and indicators to examine in responding to the question**

An assessment of Question 3.4 calls for an examination of the following criteria and performance indicators:

- Identify the underlying policy objective of existing or proposed trade policy measures (e.g. to what type of market failure or policy demand is the proposed measure responding?).
- Describe the options available to meet the underlying policy objective in the least trade- and/or investment-restrictive manner where such options are available, explain how each option would meet the regulatory requirements and the risks associated with them, and whether these can be mitigated via flanking policies or measures..
- Identify affected groups, including business sectors and members of society, on which regulatory interventions may exert disproportionate impacts.
- Compare the benefits and costs for each option considered.
- Consider the costs and benefits to consumers/individuals and to the economy at large, of proposed measures taking account of their likely economic, social and environmental effects.
- Summarize who or what sectors bear the costs and benefits of each option.
- Consider any unintended consequences and indirect costs.
- Engage in and summarize the results of public consultations relating to proposed regulatory changes and make such information available on dedicated websites.
- Encourage government agencies to periodically review existing regulatory regimes and conduct RIAs.

Several WTO Members, in particular developing countries, have expressed concern that requirements to conduct RIAs may represent a heavy and costly administrative burden in light of limited governmental capacities and resources. Such concerns have also been expressed relative to suggestions of mandating prior notification requirements in the WTO's various transparency provisions. There is no denying the legitimacy of the concerns expressed regarding the recurring costs of complying with disciplines such as those discussed above. At the same time, genuine doubts may also be expressed over the effectiveness of

lighter approaches, such as a simpler requirement to publish the rationale for new or proposed regulations rather than engaging in extensive stakeholder consultations, in helping host countries durably anchor governance-enhancing properties to their regulatory institutions and decision-making processes. This is yet another area where potentially strong dividends may be expected from targeted technical assistance and capacity strengthening.

### Reference on case studies and good practices

- The web site below contains several papers and case studies presented at a conference hosted by the U.K.-based [Centre on Regulation and Competition](http://www.competition-regulation.org.uk/conferences/mcrria03/index.shtml) on the use of regulatory impact analysis (RIA) in developing countries. The papers discuss how RIAs can be used in transition economies to appraise the costs and benefits of new regulatory proposals and evaluate the performance of existing regulations. See: <http://www.competition-regulation.org.uk/conferences/mcrria03/index.shtml>
- The study below describes the ways in which RIAs can be effectively applied in developing country contexts, providing a framework and strategy for implementing RIAs in resource constrained environments, urging a flexible, pilot-driven, step-by-step approach. The study cites examples from Serbia, Macedonia and the Slovak Republic. See: <http://www.businessenvironment.org/dyn/be/docs/80/Session3.4LadegaardDoc.pdf>
- The report referenced below examines current trends in the process and methods employed by some of the main users of RIAs. It assesses the most recent trends (2002-2006) and identifies lessons for governments who wish to be at the forefront of sound regulatory practices and processes. See: <http://www.regulatoryreform.com/pdfs/Current%20Trends%20and%20Processes%20in%20RIA%20-%20May%202006%20Jacobs%20and%20Associates.pdf>
- The following paper summarizes responses from 40 developing and transition economies to a questionnaire gauging their understanding and application of regulatory impact assessments (RIAs). The paper's findings indicate that while such assessments are being performed, opportunities for improving both the process and attendant benefits from RIAs remain in a number of areas. These include the deepening of officials' understanding of RIAs, improving the uniformity and thoroughness with which such assessments are applied to the various stages of the RIA process, examples of economic, social and environmental regulatory proposals, as well as ways of increasing the transparency of regulatory processes. See: [http://www.competition-regulation.org.uk/publications/working\\_papers/WP83.pdf](http://www.competition-regulation.org.uk/publications/working_papers/WP83.pdf)
- This report below evaluates several international models of regulatory impact analysis for their relevance to South Africa's regulatory practices. In so doing, it identifies principles for success and makes suggestions on how RIAs can be implemented. See: <http://www.safoundation.org.za/documents/DesigningAREgulatoryImpactAssessmentForSa.pdf>
- The WTO Web page on Subsidies and Countervailing Measures contains updated information on the Subsidies and Countervailing Duties Committee and a collection of related documents on the subject. See: [http://www.wto.org/english/tratop\\_e/scm\\_e/scm\\_e.htm](http://www.wto.org/english/tratop_e/scm_e/scm_e.htm)

### **3.5 To what extent do trade policies raise the cost of inputs of goods and services, thereby discouraging investment in industries that depend upon sourcing at competitive world prices ?**

#### **Explanation and rationale for the question**

Much international trade involves transactions from business to business. Modern business supply chains concern hundreds of domestic and international producers. This specialisation of production attracts investment because it results in productivity gains and lowers production costs by locating various stages of the production process in locations that are best suited to such activities. Trade policies that hinder reliable access to intermediate goods and services, and which raise their cost can significantly hold back such a process, durably affecting the ability of host countries to insert established firms into such networks or in attracting new investment in such activities. Some countries, for example, require that a minimum share of investment project inputs be sourced locally, regardless of their cost competitiveness. Such policies may be inconsistent with WTO obligations arising from the Agreement on Trade-Related Investment Measures (TRIMs). Policy makers should consider evaluating their potential dampening effects on investment.

Internationally traded services are a particularly important input for many industries and an increasingly strategic component of global value chains in manufactured and service markets alike. The four modes of supplying services – across borders, through the movement of consumers, through an established presence (i.e investment) or through the movement of service suppliers (business people) are intrinsically linked. The value of trade in services has expanded rapidly in recent years in both developed and developing countries, accounting for much of the past two decades as one of the fastest growing components of world trade. Such developments, coupled with far-reaching changes in technology and in approaches to regulation, have seen a new international division of labour arise in services trade. Despite the rising tradability of many new services, establishment-related trade remains of paramount importance in services markets, hence the onus placed on progressively liberalizing FDI regimes in services, much of which has tended to proceed along unilateral lines in recent decades. Yet rising service exports accrue from international investment and from work outsourced from home multinational enterprises. Such exports benefit the host country from which the service originates, but concurrently enhance the global competitiveness of home country firms – and their final users and consumers.

While the market environment governing e-commerce and outsourcing has to date been fairly benign in home countries (*e.g.* the OECD area)<sup>2</sup>, developing countries are quite naturally looking to lock-in and preserve such open business environments through trade and investment agreements. As well, exporters of

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<sup>2</sup> The terms outsourcing and offshoring are frequently used interchangeably to describe the process whereby intermediate goods and services are purchased from foreign suppliers, usually with slightly different definitions. In fact there is only a partial overlap between outsourcing and offshoring, and between both terms and the internationalisation of production by multinational companies. Outsourcing refers to the purchase of goods and services that were previously produced inside the purchasing company. The company providing the intermediate inputs can be located inside (domestic outsourcing) or outside (international outsourcing) the country of the sourcing company. Offshoring refers to the purchase from companies in locations outside the country of goods and services previously produced inside the purchasing company. Thus it includes not only international outsourcing, but also international insourcing, with the foreign affiliates of domestic parent companies exporting to their parents. The internationalisation of production refers to the establishment of affiliates abroad by parent companies in the home country. These affiliates may export back to the parent company (international insourcing), or provide goods and services to home and foreign markets. The goods and services produced by affiliates need not have been previously produced inside the parent company.

such services increasingly are looking for concomitant liberalisation commitments by home countries in the area of business mobility allowing entrepreneurial talent to find more niche markets and to circulate such talent between host and home countries. While policies in this area run up against potentially strong policy sensitivities relating to migration in many home countries, approaches can be found, particularly at the bilateral level, to ensure that the temporary movement of highly skilled workers yields benefits to sending and receiving countries alike.

### **Guidance and practices to scrutinise**

Today's globalised trading environment, spurred by more liberal trading and investment regimes, and combined with technological developments and productivity advances, has made it possible to fragment supply chains on a worldwide basis. This raises the salience of trade in intermediate products (parts and components) and in services and the need for trade policy to do what it can to reduce distortions on such trade so as to allow end-users and producers of final products to reap the full benefits from the creation of regional and global production networks. Such a policy concern is of critical interest to host countries who seek to insert themselves into such networks and who wish to attract greater doses of efficiency-seeking investment in both manufacturing and service industries.

Question 3.5 helps to shed needed light on the critical (and rising) role of services trade, which today constitutes a significant and growing feature of the world economy despite the still largely inadequate means of measuring the full contribution of services trade and FDI to ongoing structural change and the attendant welfare benefits (and their distribution across countries) flowing from such a new geography of trade.

Question 3.5 also draws attention to the need for trade and investment policy to be alert to the issue of effective rates of protection on intermediary inputs and their determinants. To this end, analytical resources could usefully be committed towards the creation of a database on intermediate goods and trade in services with a view to developing a set of indicators to be used in assessing the nature, impacts and implications of various policy measures on the cost and competitiveness of intermediary inputs (both goods and services).

### **Criteria and indicators to examine in responding to the question**

An assessment of Question 3.5 calls for an examination of the following criteria and performance indicators:

- Establish a database on intermediary goods by using available import data from the United Nations COMTRADE database which provides annual trade flows disaggregated by commodity and partner countries up to a 6-digit level (see: [www.comtrade.un.org](http://www.comtrade.un.org)). For this, the import data would need to be divided into two categories of goods: (1) intermediate goods, parts and components; and (2) final goods. The list of products entering the first category is available in Table A1 of the OECD (2007) document mentioned below.
- Compute a series of indicators of intermediates trade: by year; importing country or region; and sector from the database. More detailed indicators can be computed by comparing production and employment data with corresponding intermediate import data, see OECD (2007).
- Identify trends in the exported goods that enter into other countries' supply chains and trends in imported goods used in domestic supply chains.

- Identify the intermediate goods, parts and components at the 8-digit level in a country's customs tariff and their corresponding tariff rates. Compare the tariff of the final product with the tariff imposed on its inputs with a view to identifying situations of tariff inversion in which the tariff rate on an input is higher than that applied to the final good. Tariff inversion discourages domestic manufacturing and, conversely, encourages the import of finished products.
- Build a greater knowledge base on trade in services by committing resources with a view to developing a database and reliable analytical indicators of trade and FDI performance across all modes of supply. This is required to better understand the appropriate regulatory and institutional frameworks needed for effective liberalisation across various services sectors, with priority attention given to key infrastructural services that are inputs into most final goods and services.

### **Reference on case studies and good practices**

- The precise extent of international outsourcing is difficult to measure with precision and a number of different concepts are found in the literature. The OECD note below discusses some specific measures and an associated data set used to assess developments in the growth of trade in intermediate goods, parts and components over the 1989-2004 period. See: [http://www.esri.go.jp/jp/prj-2004\\_2005/forum/060123/01-2-Annex2.pdf](http://www.esri.go.jp/jp/prj-2004_2005/forum/060123/01-2-Annex2.pdf)
- The OECD (2007) document entitled "The Internationalisation of Production, International Outsourcing and Employment in the OECD" reviews some of the possible changes that may occur in the labour markets of many OECD countries as a result of international trade and the internationalisation of production by multinational companies, with a particular focus on the impact of outward foreign direct investment from OECD countries on employment in the home country of the investing firms. An Annex addresses the question of measuring outsourcing and trade in intermediate goods. See: [http://www.oilis.oecd.org/oilis/2007doc.nsf/linkto/eco-wkp\(2007\)21](http://www.oilis.oecd.org/oilis/2007doc.nsf/linkto/eco-wkp(2007)21)
- The WTO Trade and Investment Web page contains updated information on the (currently suspended) Working Group on the relationship between trade and investment, and a collection of related documents on the subject. See: [http://www.wto.org/english/tratop\\_e/invest\\_e/invest\\_e.htm](http://www.wto.org/english/tratop_e/invest_e/invest_e.htm)
- The UNCTAD Web page on Investment, Technology and Enterprises Development provides access to the annual report entitled "World Investment Report" which the 2006 report focuses on the rise of foreign direct investment (FDI) by transnational corporations from developing and transition economies. See: <http://www.unctad.org/Templates/webflyer.asp?docid=7431&intItemID=2983&lang=1>

**3.6 If a country's trade policy has a negative effect on developing country exports, what alternative means of accomplishing public policy objectives has the government considered, taking into account the dampening effect that such a restrictive trade policy also has on investment?**

**Explanation and rationale for the question**

The beneficiaries of restrictive trade policies tend to be concentrated among firms, sectors, regions or categories of workers while those that incur a cost tend to be dispersed among many businesses and consumers. An importing country's trade policy may, if it is unduly restrictive, reduce the exporting countries' sales abroad and therefore its ability to purchase imports and attract investment. Governments should consider such external costs when evaluating specific domestic trade policy measures. More generally, and as noted above already, the investment climate will tend to be enhanced if trade policy options are informed by analysis that identifies the least trade and investment restricting instruments available to policy-makers.

**Guidance and practices to scrutinise**

Question 3.6 raises once more the matter of whether and how domestic policy makers can avoid recourse to needlessly burdensome trade and investment measures whilst also safeguarding the need of regulatory authorities to address legitimate domestic policy objectives. This principle is reflected in several WTO provisions which are also found in many preferential trade and investment agreements:

- Article XX states that nothing in the GATT shall be construed to prevent the adoption of measures necessary to protect human life or health, relating to the conservation of exhaustible natural resources and necessary to attain other legitimate objectives listed in the Article. It also requires that such measures are not applied in a manner which would constitute a means of arbitrary or unjustifiable discrimination between countries where the same conditions prevail, or a disguised restriction on international trade.
- The Technical Barriers to Trade (TBT) Agreement and the Sanitary and Phytosanitary Measures (SPS) Agreement require WTO Members to ensure that regulatory measures shall not be more trade restrictive than necessary to fulfil legitimate objectives. The TBT and SPS provisions also include some procedural requirements for the application of the principle. In particular, a Member shall notify other Members of the objectives and rationale of proposed measures. Furthermore, the SPS Agreement states that each Member shall ensure that one enquiry point exists which is responsible for providing answers to all reasonable questions from interested Members as well as information concerning risk assessment procedures, factors taken into consideration, and the determination of the appropriate level of sanitary or phytosanitary protection.
- The GATS also provides a mandate to the Council for Trade in Services to develop disciplines pursuant to Article VI:4 so that measures relating to qualification requirements and procedures, technical standards and licensing requirements do not constitute unnecessary barriers to trade in services. Such disciplines would aim to ensure that those regulatory measures are, *inter alia*: (i) based on objective and transparent criteria such as competence and the ability to supply the service, (ii) not more than necessary for to ensure the quality of services and (iii) in the case of licensing procedures are not in themselves a restriction on the supply of the services. It should be noted that such disciplines have yet to be agreed among WTO Members and that no such provisions can yet be found within existing preferential trade agreements.

- The WTO dispute settlement regime also provides for the right for a Member to seek consultation with another Member on WTO matters.

In regard to more procedural matters, Question 3.6 relates to the extent to which specific provisions are put in place in the context of a regulatory impact analysis (RIA) that would require or encourage regulators to avoid unnecessary trade restrictiveness with a view to minimizing potentially adverse effects on trading partners. This question raises a concern similar to that noted under Question 3.4 about the application of RIAs to assess the impact of proposed trade policies. Moreover, the question of whether and how foreign interested parties are consulted with regard to proposed policy changes is also a relevant consideration, one that was already addressed under Question 3.2 above.

### **Criteria and indicators to examine in responding to the question**

An assessment of Question 3.6 calls for an examination of the following criteria and performance indicators:

- In respect of relevant trade policy measures, adapt the regulatory impact analysis procedures as described in Question 3.4 to include a requirement to avoid unnecessary trade restrictiveness with a view to minimising potential adverse effects on trading partners. The following steps are basically the same as elaborated under Question 3.4 except for steps c and d which are shown in italics:
  - a) Identify the policy objective;
  - b) Describe the available options to meet the objective, explain how each option would meet the requirements and the risks associated with the options, and whether these can be mitigated;
  - c) *Identify who is affected, particularly the developing countries on which there may be a disproportionate impact;*
  - d) *Assess all available options to avoid unnecessary or needlessly burdensome trade and investment restrictions*
  - e) Compare the benefits and costs for each option considered;
  - f) Consider the costs and benefits to consumers/individuals and to the economy at large, taking account of the economic, social and environmental effects;
  - g) Summarise who or what sectors bear the costs and benefits of each option;
  - h) Consider any unintended consequences and indirect costs;
  - i) Set out how the policy will be announced and monitored; and
  - j) Conduct and summarise the results of consultations with external stakeholders.
- Assess progress achieved in the Doha Round of multilateral trade negotiations against one of its main objective that “developing countries, and especially the least-developed among them, should secure a share in the growth of world trade commensurate with the needs of their economic development”.

## Reference on case studies and good practices

- This OECD Web page on integrated market access and the regulatory process provides access to documented practices in applying six efficient regulation principles including the avoidance of unnecessary trade restrictiveness principle. See: [http://www.oecd.org/LongAbstract/0,3425,fr\\_2649\\_37431\\_2494953\\_1\\_1\\_1\\_37431,00.html](http://www.oecd.org/LongAbstract/0,3425,fr_2649_37431_2494953_1_1_1_37431,00.html)
- The WTO Web pages on Technical Barriers to Trade (TBT) and the Sanitary and Phytosanitary Measures contain updated information on their respective committees and a collection of related documents. See: [http://www.wto.org/english/tratop\\_e/tbt\\_e/tbt\\_e.htm](http://www.wto.org/english/tratop_e/tbt_e/tbt_e.htm); [http://www.wto.org/english/tratop\\_e/sps\\_e/sps\\_e.htm](http://www.wto.org/english/tratop_e/sps_e/sps_e.htm)
- See also the references mentioned above under Question 3.4.

### **3.7 To what extent does trade policy support and attract investment through measures that address sectoral weaknesses in developing countries (e.g. export finance and import insurance)?**

#### **Explanation and rationale for the question**

The magnitude of trade and investment flows also depends on the existence of other markets that facilitate cross-border transactions. These include markets that hedge and transfer the risk attached to exchange rate movements, payment defaults, transit insurance as well as the financing of international commerce. These are sophisticated markets and in many countries they either do not exist or are significantly undeveloped. Experience shows that putting in place the conditions needed to support the development of such markets can take considerable time. In the interim, correcting for market failures in host countries may require help from home countries. For example, in the absence of a developed financial sector and while being careful to avoid trade distortions and ensuring a level playing field, trade financing and insurance can often best be provided by home country firms to users in developing countries.

A related dimension concerns the issue of moral hazard in financial and insurance markets. The term “moral hazard” typically refers to the prospect that insurance or other forms of public guarantees may distort the behavior of economic agents, prompting them to take excessive risks safe in the knowledge that any direct losses or negative externalities will be socialized through public intervention. In the context of question 3.7, moral hazard may be considered in the sense that the provision of insurance and guarantees from developed country trade and investment partners may remove some of the urgency to enact policies conducive to a better investment climate in host developing countries. (Selected issues relating to the development of the financial sector are discussed in chapter 9.)

#### **Guidance and practices to scrutinise**

One dimension of question 3.7 relates to the access by financial institutions in developing countries to guarantees covering payments risk on trade transactions and the technical assistance that developing countries may require to help speed up the introduction and implementation of related measures and financial instruments.

In this connection, the International Finance Corporation (IFC) of the World Bank Group has set up the Global Trade Finance Programme (GTFP) which provides partial or full guarantees covering payments risk on banks in emerging markets for trade-related transactions. These guarantees are transaction-specific and involve a variety of underlying instruments such as: letters of credit, trade-related promissory notes,

accepted drafts, bills of exchange, guarantees, bid and performance bonds and advance payment guarantees. Through the GTFP bank network, local financial institutions can establish working partnerships with a vast number of major international banks participating in the programme. This can broaden access to finance and reduce cash collateral requirements. Through the GTFP, trade finance training is also offered. The IFC may also place experienced trade finance bankers with issuing banks to help them develop trade finance and other banking skills.

The Geneva-based WTO-UNCTAD International Trade Centre (ITC) has set up a technical assistance programme aimed at strengthening schemes and mechanisms offered by financial institutions in both the private and public sectors, in the field of export finance, short-term trade credit and credit insurance and guarantees. The programme also aims to build up the capacity of entrepreneurs and credit officers in dealing with credit and financial risk management. This programme is targeted at three distinct levels where constraints and needs require a different set of activities: (i) enterprises, *i.e.* public and private manufacturers and traders; (ii) financial institutions, *i.e.* financial institutions, export-import banks, export credit insurance and guarantee agencies; and (iii) the financing environment, including organisations that have a direct impact on the availability and cost of trade finance.

A further dimension of question 3.7 concerns the issue of officially supported export credits. Many governments provide official export credits through dedicated Export Credit Agencies (ECAs) in support of national exporters competing for overseas sales. ECAs provide credits to foreign buyers either directly or via private financial institutions benefiting from their insurance or guarantee cover. Reflecting differences in financial resources, some countries may provide officially supported export credits through their ECA on terms that competing ECAs, especially in developing countries, may be unable to match. This may result in trade distortions. The OECD is involved in the maintenance and development of related disciplines (the Export Credit Arrangement) and provides a forum for discussion and coordination of national export credit agencies. The main purpose of the Export Credit Arrangement is to provide a framework for the orderly use of officially supported export credits. In practice, this means providing for a level playing field (whereby exporters compete on the basis of the price and quality of their products rather than the financial terms provided) and reducing subsidies and trade distortions related to officially supported export credits.

Question 3.7 may also be seen as relating to the issue of the Heavily Indebted Poor Countries (HIPC) Initiative which involves an agreement among all of the major international lenders to provide an opportunity for a fresh start to countries struggling with punishing external debt burdens. The HIPC Initiative was set up in 1996 and strengthened in 1999 as the Enhanced HIPC Initiative to provide deeper, broader and faster debt relief to a larger group of eligible countries and to strengthen the programme's links to ongoing poverty reduction efforts in these countries. Virtually all of the world's multilateral creditors participate in the HIPC. Under the initiative, thirty countries have received debt relief worth over US\$63 billion in 2005 net present value terms. In return for debt relief, governments in countries that decide to participate in the HIPC Initiative pledge to introduce a series of key reforms designed to encourage sustainable economic growth that will drive reductions in poverty levels. Such reforms include the pursuit of sound macroeconomic policies, reforms of the legal system and the establishment of reliable and accountable financial systems. HIPC beneficiaries must also develop detailed plans to improve the quality of their public services and access to those services by the poor. Such reforms are generally conducive towards a better investment climate

## Criteria and indicators to examine in responding to the question

An assessment of Question 3.7 calls for an examination of the following criteria and performance indicators:

- Establish a consultation mechanism involving government, financial institutions and traders to ascertain ongoing national practices in export finance and export and import insurance measures with a view to identifying potential training needs and legislative updates.
- Assess and adapt the guidelines to decision-makers and bankers on setting up of credit insurance schemes and institutions contained in the ITC's training guide entitled "Export Credit Insurance and Guarantee Schemes: A practical guide for developing and transition economies". The Guide contains an analysis of the needs and constraints related to export credit insurance, outlining the organizational structure of an export credit agency, the legal infrastructure required for its activities and the range of policies on offer. See: <http://www.intracen.org/tfs/>
- Assess the scope for taking up the training opportunities offered under the Global Trade Finance Programme by the World Bank's International Finance Corporation. See: <http://www.ifc.org/ifcext/gfm.nsf/Content/TradeFinance>
- Gradually build up national expertise in respect of export credit matters, *e.g.* official financing support, maximum repayment terms, minimum risk premiums and trade-related aid for projects, goods and services sold on credit terms of two years or more, and set up an information database on export credit matters for countries that are not parties to the OECD Export Credit Arrangement.
- Assess the main criteria of "major player" and "mutual benefit" that an applicant for observership status to the OECD Export Credit Arrangement must satisfy by taking into account the following indicative questions:
  - Does the applicant have in place a medium and long-term export credit programme providing officially supported export credits that may be covered by the disciplines of the Arrangement?
  - What is the experience and performance that the applicant has demonstrated in export credit matters, on the basis of the following quantitative and qualitative indicators: main characteristics of the export credit programme (objectives, technical features), annual flows of officially supported medium- and long-term export credits (minimum figure), and types of goods supported, in comparison with ECA participants?
  - Are the export credit programmes of the applicant in competition with those of Participants, in a specific sector or on a more general basis?
  - To what extent is the applicant willing to exchange information with Participants on its officially supported export credits programmes.?
  - For regular observers: to what extent is the applicant willing to apply the relevant disciplines and procedures of the Arrangement.
- Keep abreast of political risks, *e.g.* risk of political violence, FDI protectionism, geopolitical risk and government instability, and of the issues concerning the HIPC Initiative with a view to building up domestic expertise in political risk assessment and making full use of existing debt relief initiatives.

## Reference on case studies and good practices

- The World Bank Web page on the Heavily Indebted Poor Countries (HIPC) Initiative provides details about this initiative, including an independent evaluation of the HIPC Initiative carried out in 2006. See <http://go.worldbank.org/85B908KVE0>
- The IFC Web page on Global Financial Markets provides details about its Global Trade Finance Programme (GTFP). See: <http://www.ifc.org/ifcext/gfm.nsf/Content/TF-WhatWeOffer>
- The OECD Web page on export credits provides to access to the work of the Export Credit Group (ECG) and other related work and documentation. See: [http://www.oecd.org/about/0,3347,en\\_2649\\_34169\\_1\\_1\\_1\\_1\\_1,00.html](http://www.oecd.org/about/0,3347,en_2649_34169_1_1_1_1_1,00.html)
- The ITC Web page explains its technical assistance programmes designed to facilitate access to finance by small and medium sized enterprises exporting from developing and transition countries. See: <http://www.intracen.org/tfs/>
- The Columbia Program on International Investment in partnership with the Economist Intelligence Unit publishes an annual report *which assesses most recent* FDI flows and forecasts flows over a five year period. The latest report features the results of a survey of over 600 corporate executives concerning their investment intentions. The report also pays special attention to the rise of FDI protectionism and regulatory risks. See: <http://www.cpii.columbia.edu/pubs/>