Is investment protectionism on the rise?
Evidence from the OECD FDI Regulatory Restrictiveness Index

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Investment protectionism can take many forms: new rules or more rigorous enforcement of existing ones; greater conditionality attached to regulatory approval mechanisms; or a more expansive notion of strategic industries, the national interest and national security. Sometimes disapproving pronouncements by the government or fears of a popular backlash are enough to stop a potential cross-border investment in its tracks.

Given the sustained downturn in global flows of foreign direct investment (FDI), the suggestion that rising protectionism is partly to blame is gaining currency. Evidence of investment protectionism tends to be anecdotal, given the difficulties in measuring the different ways a government might discriminate against foreign investors. The OECD FDI Regulatory Restrictiveness Index (Box 1) can help to shed light on the question. It measures statutory barriers against foreign investment in over 60 countries worldwide and how they have changed over time. By looking only at discrimination on the books and not at how rules are implemented, it can only provide part of the answer, but it does provide an objective reality check on the question of whether the global policy trend is turning against foreign investment.

Over time and across countries, policies are moving towards greater openness for foreign investors

Many OECD countries undertook substantial reforms of the regime covering FDI in the 1970s and early 1980s. Screening procedures were once common but are now the exception to the rule and often circumscribed in their ability to reject investments. For emerging economies, reforms came later – in the late 1980s and 1990s – as the benefits of export-led development driven in part through FDI became more widely accepted. Since 2000, the pace of reform has slowed in most countries (Figure 1). This is partly because there are now fewer barriers to remove, but it may also reflect the fact that the low-hanging fruit of reform has already been picked and remaining reforms will involve more stakeholder opposition.

Not all countries follow this pattern of reform fatigue. Turkey and Viet Nam, for example, have both undertaken extensive reforms over the past 15 years, and both China and India liberalised further in 2016 (not currently shown in the Index which stops in 2015). Overall, however, the average scores under the Index have tended to remain flat over this period. While this suggests a loss of reform momentum recently, it does not provide any evidence that countries have become significantly more restrictive in terms of statutory barriers since the global financial crisis in 2008-
There is no upward movement in the curves shown below. The slight variation in the curve for non-OECD countries is reflects the fact that the sample size has increased over time.

**Figure 1. Changes in the overall FDI Index, 1997-2015**

![Graph](image)


The biggest reformers since 1997 have tended to be those countries that were most restrictive to start with.

The biggest reformers since 1997 have all been in Asia, many of which started with a high level of restrictions (Figure 2). Liberalisation has often been on a unilateral basis, as host governments come to recognise the potential benefits of FDI, but the pace and timing of reforms are often influenced by external factors such as WTO or OECD membership, regional free trade agreements or economic crises.

**Figure 2. The top FDI reformers, 1997-2015**

![Graph](image)

Reforms have resulted in increased inflows of foreign direct investment

Reforms of FDI restrictions are only one of the factors which can explain a country’s performance in attracting foreign investment and such reforms are usually not done in isolation but are rather part of an overall package of investment climate improvements in different policy areas. Nevertheless, there is a clear correlation between reforms and FDI inflows for the four countries presented in Figure 3. In all cases, once a critical mass of FDI-related reforms had been undertaken, FDI took off.

**Figure 3. Country experience with FDI reforms and the impact on FDI inflows, 1997-2015**

Source: OECD calculations based on the OECD FDI Regulatory Restrictiveness Index methodology and UNCTAD statistics.

**FDI restrictiveness still varies greatly across countries and regions**

Countries in the Asia-Pacific region – both OECD and non-OECD – tend to have higher scores under the Index on average (Figure 4), with a greater propensity to screen inward investment and more frequent use of foreign equity limits at a sectoral level. This finding may seem at odds with the common notion that these countries have often relied on foreign investment as part of their export-led development. This is because the regime in export processing zones in these countries, which is often more liberal, is not captured in the Index. EU countries collectively have the fewest
restrictions on FDI. Larger countries also tend to be more restrictive, partly because they may be richer in natural resources, but also because they often have larger markets which offer host governments more scope to impose discriminatory conditions on investors without discouraging inflows. Many of the most restrictive countries under the Index fall into one or both of these categories (Figure 5).

Figure 4. FDI regulatory restrictiveness per country, 2015¹

Source: OECD FDI Regulatory Restrictiveness Index database. [www.oecd.org/investment/fdiindex.htm](http://www.oecd.org/investment/fdiindex.htm)
Note: (¹) Countries without shading are not covered in the Index. Scores are preliminary for Thailand and Singapore (base year 2014), Cambodia (base year 2015), Namibia, Mozambique, Mauritius and Seychelles (base year 2013).

Equity restrictions have usually been the most common form of discrimination

Figure 5 shows the overall score for each country and by type of measure. For most countries, sector-specific limits on foreign equity ownership have been the most common form of discrimination faced by foreign investors. Countries often impose such restrictions to allow domestic investors to share in the rents from the project and in the expectation that having a domestic investor involved will help to facilitate linkages with the domestic economy and enhance technology transfers and other potential spill-overs. The extent to which joint venture requirements or foreign equity limits are an effective way to achieve these spill-overs is an open question. Many investors prefer majority ownership and hence equity limits may deter potential investors.
Figure 5. Discrimination against foreign investors by type of restriction, 2015

Source: OECD FDI Regulatory Restrictiveness Index database, [www.oecd.org/investment/fdiindex.htm](http://www.oecd.org/investment/fdiindex.htm)

Note: (*) Other restrictions refer to those on the employment of key foreign personnel and other operational restrictions. Scores are preliminary for Thailand and Singapore (based on 2014), Cambodia (2015), Namibia, Mozambique, Mauritius and Seychelles (2013).
Restrictiveness also varies greatly by sector

Although some countries still have horizontal measures which affect all foreign investors, such as approval mechanisms or a prohibition on foreign ownership of land, most restrictions are sector specific limits on foreign equity. In general, FDI in manufacturing is allowed without restrictions, except when a horizontal measure applies across the board, but many primary and service sectors remain partly off limits to foreign investors, holding back potential economy-wide productivity gains (Figure 6). Even within OECD countries, restrictions on foreign investment remain in some key network sectors such as energy and transport. The sectoral pattern of restrictions tends to be similar in both advanced and emerging economies, but the extent of restrictiveness is generally higher in the latter group of countries.

![Figure 6. FDI restrictions in OECD and non-OECD countries by sector, 2015](source)

Conclusion: No grounds for complacency

This analysis based on the OECD FDI Regulatory Restrictiveness Index provides very little evidence of backtracking of investment policy reforms but rather shows a continued reform impetus in those countries which traditionally have been the most restrictive. Governments worldwide recognise the potential benefits that FDI can bring under the right conditions. Indeed many remaining restrictions are designed more to try to maximise those benefits than they are to restrict foreign investment. Foreign investors have often responded with enthusiasm to reforms in many of the countries currently covered by the Index.

At the same time, the gradual re-imposition of screening mechanisms, often tied to national security considerations, could provide the means for backtracking in the future if the notion of national security is later stretched to encompass strategic sectors or firms. Governments are increasingly concerned about the potentially non-commercial objectives of investments by state-owned enterprises or sovereign wealth funds and about the lack of potential reciprocity in terms of the market for corporate control in the country of the investor. Multinational enterprises may also face a resurgence of restrictions on outward investment from their home country. All of this suggests that governments and stakeholders should avoid complacency in this area.

Source: OECD FDI Regulatory Restrictiveness Index database, [www.oecd.org/investment/fdindex.htm](http://www.oecd.org/investment/fdindex.htm)
Box 1. Calculating the OECD FDI Regulatory Restrictiveness Index

The OECD FDI Regulatory Restrictiveness Index covers 22 sectors, including agriculture, mining, electricity, manufacturing and main services (transport, construction, distribution, communications, real estate, financial and professional services).

For each sector, the scoring is based on the following elements:

- the level of foreign equity ownership permitted,
- the screening and approval procedures applied to inward foreign direct investment;
- restrictions on key foreign personnel; and
- other restrictions such as on land ownership, corporate organisation (e.g. branching).

Restrictions are evaluated on a 0 (open) to 1 (closed) scale. The overall restrictiveness index is a weighted average of individual sectoral scores.

The measures taken into account by the Index are limited to statutory restrictions on FDI, typically listed in countries' lists of reservations under FTAs or, for OECD countries, under the list of exceptions to national treatment. The Index does not assess actual enforcement and implementation procedures. The discriminatory nature of measures, i.e. when they apply to foreign investors only, is the central criterion for scoring a measure. State ownership and state monopolies, to the extent they do not discriminate against foreigners, are not scored. Preferential treatment in special-economic zones and for export-oriented investors is also not considered.

More information on the Index can be found at www.oecd.org/investment/index

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OECD Global Forum on International Investment

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