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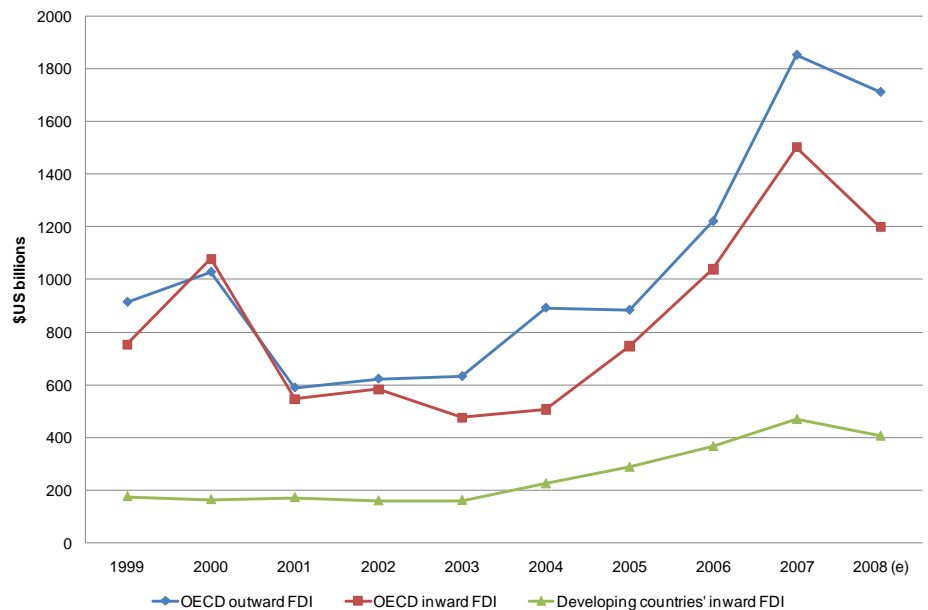
GRIM OUTLOOK FOR FDI AND SHIFTING GLOBAL INVESTMENT PATTERNS

As the financial crisis has evolved into a global economic crisis, the outlook for FDI has likewise darkened. On current trend, inflows will be down 13% and outflows by 6% by the end of the year (see Figure 1 and Table 1). These declines would be much less severe than those experienced in 2001, when FDI inflows and outflows dropped by 49% and 43%, respectively.

However, it seems likely that FDI flows will fall sharply in the second half of 2008 and continue to decline into 2009, especially considering the speed with which the global economic crisis deepened during Q3 and into Q4 of 2008.

This is reflected in international M&A activity (a major component of FDI), for which data are available into Q4 (22 October). On current trend, international M&A will decline by 29% from the record levels reached in 2007 (\$US1.7 trillion). Furthermore, the bursting of the dot.com bubble in 2000 showed how sensitive international M&A activity is to economic crises, with the value of international M&A activity declining by 47% in 2001 ▶

Figure 1. OECD FDI inflows and outflows, 1999-2008



Note: e = estimate

Source: OECD and Dealogic 2008.

GRIM OUTLOOK FOR FDI AND SHIFTING GLOBAL INVESTMENT PATTERNS continued...

and 34% in 2002 (see Figure 2). The more severe nature of the current crisis therefore suggests that there remains considerable scope for further declines in international M&A activity.

Two forces are at play that give rise to the grim outlook for FDI. First, the freezing of credit markets, combined with sharp declines in equity markets, have forced firms to rely largely on cash reserves to finance investment. In a number of industries (such as automotive), many firms are also facing severe internal liquidity constraints. Second,

with global growth forecast for 2009 at 2.2% and growth in the OECD economies expected to fall to 0.3%, the need for companies to investment in new capacity is considerably reduced.

The crisis accelerates shifting global investment patterns

Table 1. Foreign Direct Investment, billion US\$

	Inflows		Outflows	
	2007	1st half '08	2007	1st half '08
Australia	23.6	15	25.7	21
Austria	30.7	10	31.4	15
Belgium	39.1	13	51.9	15
Canada	107.4	22	49.5	35
Czech Republic	9.1	6	1.3	1
Denmark	11.3	9	16.2	22
Finland	8.5	-8	8.6	-6
France	158.0	73	224.6	141
Germany	50.9	13	167.5	119
Greece	1.9	4	5.3	2
Hungary	5.6	3	4.1	0
Iceland	3.8	-2	12.5	-1
Ireland	25.9	-3	22.1	4
Italy	40.2	-8	90.8	19
Japan	22.5	12	73.5	47
Korea	1.6	-1	15.3	7
Luxembourg	118.8	16	181.9	42
Mexico	23.2	11	8.3	1
Netherlands	99.5	32	31.2	0
New Zealand	2.9	3	2.8	33
Norway	0.6	-3	11.2	7
Poland	17.6	10	3.2	3
Portugal	5.6	3	6.2	1
Slovak Republic	2.9	1	0.2	0
Spain	53.4	49	119.6	31
Sweden	18.8	21	36.7	28
Switzerland	40.4	12	51.0	24
Turkey	22.0	8	2.1	2
United Kingdom	186.0	102	229.9	76
United States	237.5	178	333.3	171
OECD total	1369.2	599	1817.9	857

Notes: data are converted to US dollars using average exchange rates.
Sources: OECD International Direct Investment Database.

Table 2. Distribution of top 100 M&A by location of acquirer and target
US\$ million

	2004	2005	2006	2007	2008	% change 07-08
OECD into OECD	218564	289908	408395	675008	367552	-46
Non-OECD into OECD	17419	26839	56428	68894	70836	3
OECD into non-OECD	24266	39177	32685	38854	28049	-28
Non-OECD into non-OECD	7965	14006	32260	22218	10608	-52
TOTAL	268214	369930	529768	804973	477045	

Note: * Through 22 October 2008
Source: Dealogic 2008

While aggregate FDI flows are down, inward FDI into the OECD from outside the OECD has represented a rare bright spot during the crisis to date. For example, based upon current trends for the largest 100 international M&A deals (which account for approximately 50% of all international M&A activity), M&A activity in the OECD originating from non-OECD sources is set to grow by 25% in 2008 over 2007 levels. This M&A activity has already reached \$US71 billion in 2008, exceeding the total for 2007 and accounted for 15% of the value of the largest M&A investments in the OECD area in 2008 (up from 9% in 2007). As the last column of table 2 shows, M&A activity in the OECD originating from non-OECD sources is the only area in which international M&A activity has been growing. In other words, FDI has served to channel capital from places where it has been abundant to where it has become scarce during the crisis.

Barring a serious protectionist response (resulting, for example, from political pressure to stop foreign investors from "taking advantage" of the economic crisis), this positive role for international investment from developing countries will likely increase over time as both experience and available capital grow. For example, according to Deutsche Bank Research the assets under management of SWFs outside the OECD are projected to increase from their current level of around \$US3.6 trillion to \$US5 trillion by 2010 and \$US10 trillion by 2015. As long as the global economic crisis does not worsen to the point that these sources of 'rescue FDI' also begin to retreat, they could be expected to play an increasingly important role in diversifying the structure of global FDI activity and thereby increasing the positive role that FDI can play as an international channel of capital. ▶

The developing countries are vulnerable but FDI is providing stability

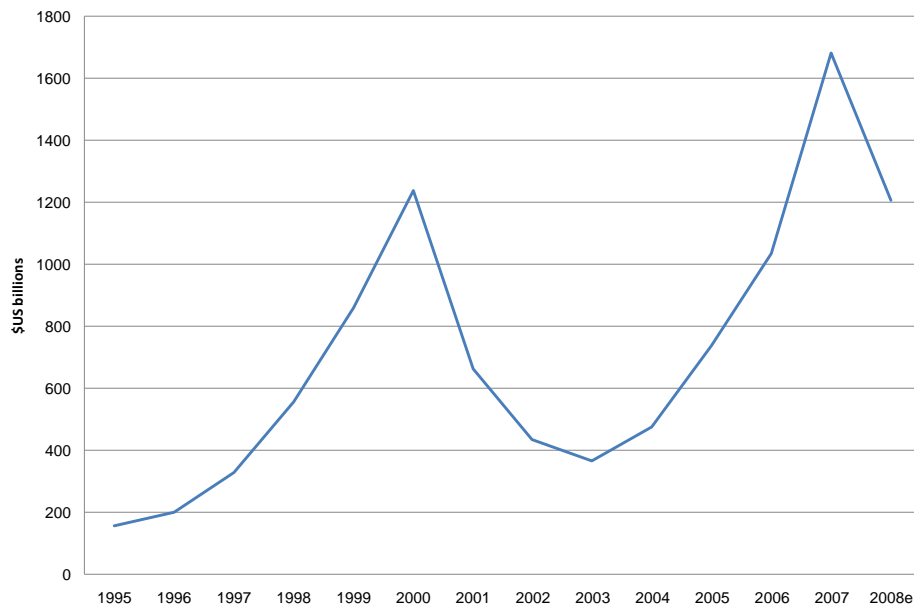
The composition of international capital flows to developing countries has changed dramatically between 1999 and 2007 (Figure 3). During this period, FDI's share of total capital inflows fell from almost 90% to under 50% and the combination of portfolio flows and private debt increase from 6% to 55% (the net position of official creditors is actually negative at US\$4 billion because loan repayments have exceeded lending). This diversification has been a positive development, and reflects a number of factors, including strong growth in developing countries, accompanied by high rates of return on investment, as well as the sound investment frameworks that developing country governments have been putting in place.

However, under the current circumstances, this increased reliance on portfolio flows and private debt could result in a sharp contraction of international capital flows for many developing countries. For example, according to the Institute of International Finance, private credit financing into 30 developing countries surveyed (including the BRICS) will decline by half between 2007 and 2009 (from US\$600 billion to \$300 billion), while net portfolio inflows, which are already negative, will decline further (from -US\$6 billion to -\$US20 billion). FDI flows into these 30 developing countries, however, are only expected to decline by 7% (from US\$302 billion to US\$282 billion).

For further reading on this topic:

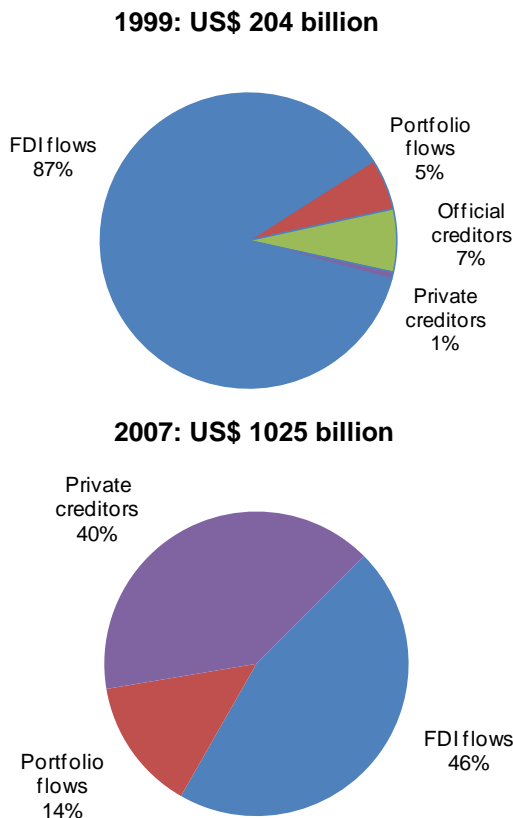
OECD work on FDI statistics
www.oecd.org/daf/investment/statistics

Figure 2. Completed cross-border M&A, 1995-2008e



Note: e = estimate
 Source: OECD and Dealogic 2008.

Figure 3. Changes in the composition of international capital flows to developing countries



Note: e = estimate
 Source: World Bank, Global Development Finance 2008

OECD GUIDANCE ON SOVEREIGN WEALTH FUNDS PRESENTED AT WORLD BANK/IMF MEETINGS

The OECD Investment Committee's project on "Freedom of Investment, National Security and 'Strategic Industries'" (FOI) has, since early 2006, provided a forum for intergovernmental dialogue on how governments can reconcile the need to preserve and expand an open international investment environment with their duty to safeguard the essential security interests of their people. With the current crisis, it is all the more important to keep capital inflows moving freely. The Investment Committee is treating the issue of recipient country policies toward Sovereign Wealth Funds (SWFs) and other government-controlled investment entities as an integral part of the FOI project.

OECD guidance complete

The final "tranche" of the OECD Guidance on SWFs was adopted by OECD members on 8 October and presented to the International Monetary and Financial Committee meeting in Washington D.C. on 11 October. The guidance has three parts:

- *OECD Ministerial Declaration on SWFs* and recipient country policies, made by Finance Ministers meeting at the OECD in June 2008: This provides high level political support for OECD guidance and increases its weight as a source of international investment law;
- *Guidance that reaffirms the relevance of long standing OECD investment principles* (first adopted in 1961) for recipient country policies toward SWFs: These are non-discrimination (treat SWFs as well as similar domestic investors); standstill (don't introduce new measures); progressive liberalisation (make progress of liberalisation); and unilateral liberalisation (don't insist on reciprocity for liberalisation measures);
- *Guidelines for recipient country investment policies relating to national security*: OECD investment instruments enshrine the right and the duty of governments to countries to take measures to safeguard essential security interests. This newer guidance, developed over the last year, provides recommendations for recipient country policies that help to make these policies both effective and to ensure that they are not used as disguised protectionism.

Next steps

Participating countries will be using the OECD's trademark "peer review" process to promote adherence to these standards. This brings peer pressure to bear on the design and implementation of investment policies. Indeed, investment related peer reviews have been going on now for nearly 50 years and have channelled decades of liberalisation in the OECD. The newer guidance on national security-related policy provides a new reference for these discussions among peers. OECD members are already actively involved in this process; for example, several in-depth discussions of proposed changes by several member countries have taken place and these have resulted in changes to draft laws.

Involving non-members

In recognition of the growing importance of the non-OECD world for international investment, OECD discussions of investment policies have been opened up -- the OECD work on SWFs has benefited from the participation of some 20 non-members including Russia, China, South Africa and Brazil. SWFs from Russia and Qatar attended the most recent discussions. In the future, the OECD will be making a special effort to invite non-member governments from countries whose investors may feel they have been harmed by an OECD country's restrictive measures -- this will give them direct access to the OECD peer review mechanisms. ■

For further reading on this topic:

The OECD guidance can be found at:

www.oecd.org/daf/investment/foi.

CHINA INTENSIFIES EFFORTS TO PROMOTE RESPONSIBLE BUSINESS CONDUCT IN CO-OPERATION WITH OECD

The Chinese government has been intensifying its efforts to promote Responsible Business Conduct (RBC) in co-operation with the OECD. Most recently this involved a Multi-stakeholder Symposium on Government Approaches to Encouraging Responsible Business Conduct jointly organised by the Chinese government and the OECD Investment Committee in Paris on 26-27 June 2008.



China is pursuing a broad-based strategy to promote responsible business conduct

A key conclusion of the Multi-stakeholder Symposium is that the Chinese government is strongly encouraging companies to adhere to high standards of responsible business conduct (RBC). It is developing framework conditions to enable RBC in China, including putting in place a series of measures to ensure disclosure by enterprises of both financial and non-financial information, enacting laws to protect the rights of workers and taking measures to protect the environment. The Chinese government is striving to ensure corporate compliance with laws relating to RBC in China and is also promoting RBC in overseas operations of Chinese enterprises. China has signed and ratified international agreements relevant to promoting RBC, including ►

United Nations and some core ILO conventions. Chinese companies are seeking to learn about RBC standards and Chinese suppliers are working with OECD-based and other foreign enterprises to improve corporate conduct.

As a result, Chinese companies have started to publish RBC reports...

One of the tangible results of the government's promotion of RBC has been the growing number of Chinese companies that publish reports on their RBC performance. The following examples illustrate how Chinese companies have started to respond to the growing demand for more information on their contributions to RBC:

- In January 2007 China Mobile produced the first RBC report issued by a domestic telecommunications company in China, in which it outlined a partnership with Nokia and Motorola to start a nationwide "Green Box" mobile phone recycling campaign at the end of 2005;
- The widely-praised 2005 State Grid RBC Report covers a broad range of issues, including environmental protection and sustainability, poverty alleviation, aid to Tibet, supplying power to the 2008 Beijing Olympic Games, donating to South-East Asian tsunami relief and establishing charitable foundations and scholarships.
- The China Ocean Steamship Corporation (COSCO), a signatory to the United Nations Global Compact, constructed its COSCO Sustainable Development Report 2005 in line with the Global Reporting Initiative (GRI) Guidelines. This report was singled out on the Global Compact web site as a Notable Communication on Progress in China.
- There are also indications that Chinese companies are adopting RBC in their foreign operations. In October 2006 a Chinese oil company, SAPET, exploring for oil in the Peruvian Amazon, announced that it would not enter the territory of isolated Indians, even though the land was inside its concession.

...and the Shenzhen Stock Exchange adopted guidelines on socially responsible conduct

In September 2006 the Shenzhen Stock Exchange published guidelines on socially responsible conduct for listed companies and has since been actively training the 488 companies listed on the Exchange in how to apply them. As a result, 21 companies listed on the Shenzhen main board published CSR reports in 2006 and more are preparing to do so in 2007. The Exchange is currently trying to develop a social responsibility index. The new guidelines were adopted in direct response to the inclusion of responsible business conduct in the latest revision of the Company Law. References consulted in preparing the guidelines include the OECD Guidelines for Multinational Enterprises.

Significant progress has been made but many challenges lie ahead

Despite the considerable efforts by the Chinese government to promote RBC, and clear signs that these efforts are leading to positive results, it remains that making RBC an integral part of the country's corporate landscape will not be achieved overnight. The OECD and China will therefore continue to work together to address the challenges that lie ahead. These include:

- **The need for broader communication:** Many enterprises in China are still unaware of the need for RBC, or of its potential benefits. There is a general perception that RBC is an unnecessary diversion from doing business, and that short-term costs far outweigh less tangible long-term benefits. The government can counter these misperceptions of RBC by strongly and repeatedly expounding the multifaceted business case for it, based on the steady accumulation of experience, including experience gained through the OECD Guidelines;

- **The promulgation-enforcement gap:**

The Chinese government has put major efforts into establishing sectoral corporate conduct codes, beginning with CSC9000T, that embody existing law. This is understandable, given widespread non-compliance. However, while such voluntary codes can play an important part in raising awareness of new laws and the specific requirements they make on enterprises, they cannot be a substitute for effective enforcement of laws by the proper authorities. Measures taken by national government are not consistently implemented at local level. Efforts to perfect the legislative framework need to be continued, but it is just as important to put in place effective enforcement and incentive measures to ensure compliance.

- **Proliferation:** A result of the government's promotion of RBC has been the proliferation of RBC guidelines across different branches of government and semi-governmental bodies, each one concentrating on its own area of responsibility. More effective "whole of government" co-ordination of the various efforts to promote RBC will be required to prevent incompatibility, ensure full coverage, and present a consistent, unified vision of RBC from which businesses can learn and benefit.

- **International coherence:** China's increasing integration into the world economy can be made easier if the various RBC codes and **guidelines** developed by the Chinese government are in line with internationally-recommended standards, such as the OECD Guidelines for Multinational Enterprises. This will be a particularly important area of focus as China and the OECD continue to work together to promote RBC. ■

For further reading on this topic:

OECD (2008, forthcoming) Investment Policy Review of China
www.oecd.org/daf/investment/china

ILO AND OECD JOIN FORCES TO PROMOTE RESPONSIBLE BUSINESS CONDUCT

Every year around June, the National Contact Points (NCPs) of the OECD Guidelines for Multinational Enterprises meet to review their experiences in implementing and promoting the Guidelines. This year, at the invitation of OECD Ministers and the G8, the annual NCP meeting was held back-to-back with a high-level conference on “Employment and Industrial Relations: Promoting Responsible Business Conduct in a Globalising Economy” jointly organised by the OECD and the International Labour Organisation (ILO).

Growing recognition and use of the Guidelines

The strong endorsement of the Guidelines by the G8 Leaders at their June 2007 Summit in Heiligendamm reflects their rising profile and impact. In his keynote address during the NCP meeting, the Special Representative of the United Nations Secretary-General on Business and Human Rights, Professor John Ruggie, put the spotlight on the wide applicability of the Guidelines and the unique features of their implementation mechanism, concluding that “the Guidelines and NCPs are critical, and in some respects unique, elements in the overall architecture”.

This prominent recognition of the Guidelines would seem to owe in particular to the increasingly pro-active nature of the NCPs. There have been several improvements of national websites and more diverse promotional techniques. New partnerships with stakeholders have emerged and led to their greater involvement. Regional co-operation among NCPs around the Guidelines has also expanded. Efforts to exploit the synergies between the Guidelines and other existing initiatives and instruments relevant to corporate responsibility are multiplying. As of June 2008, 104,000 websites referred to the Guidelines, compared to 25,000 five years ago. As a result, the Guidelines and, more generally, a pro-RBC mindset have become increasingly integrated in the daily activities of governments.



In addition, as adherence to the Declaration on International Investment and Multinational Enterprises continues to expand, more countries are using the Guidelines. Peru became the 41st adherent to the Declaration in July 2008 and further applications by non-OECD countries are pending. The Guidelines have also garnered increased visibility within the context of the OECD Investment Committee’s co-operation with China.

The NCPs remain active in efforts to resolve disputes

Although there has been a slight decline in the number of ‘specific instances’ (the term used to refer to complaints brought to the NCPs) in 2007-2008, NCP reports show continued support for the specific instances facility. There were 27 new cases in the year to June 2008, bringing the total since June 2000 to 182. Of these, 136 specific instances have been considered by NCPs. The trend of searching for amicable solutions is continuing, resulting in efforts to better coordinate and consult on cases involving multiple requests.

With the current crisis, the OECD Guidelines will play an even greater role in building trust and confidence in international investment

An area of consensus during the meetings was that there remains considerable scope for enhancing the effectiveness of the Guidelines. With a view to achieving better performance, NCPs will aim to create more opportunities for in-depth peer learning, starting with a peer review of the Dutch NCP in May 2009. Against the backdrop of the current global financial crisis, work will be undertaken over the coming year on the supporting role that the Guidelines can play in the financial sector. Finally, co-operation with the ILO and enhanced engagement with major economies on public policies to promote responsible business conduct will be actively pursued. ■

For further reading on this topic:

Guidelines website:

www.oecd.org/daf/investment/guidelines



SELECTED INVESTMENT PUBLICATIONS

FORTHCOMING: **Investment Policy Perspectives**

This publication focuses on multidisciplinary empirical and analytical research of practical relevance for the global investment policy community. While all of the papers share the common theme of best practices in promoting investment for development, together they also illustrate the broad range of investment policy issues that governments need to consider as they pursue their objectives.

FORTHCOMING: **2008 Annual Report on the OECD Guidelines for Multinational Enterprises: Employment and Industrial Relations**

This publication provides an account of the actions the 41 adhering governments have taken over the 12 months to June 2008 to enhance the contribution of the Guidelines to the improved functioning of the global economy. It also publishes key findings from the high-level OECD-ILO conference on “Employment and industrial relations: promoting responsible business conduct in a globalising economy”.

FORTHCOMING: **2008 Investment Policy Review of China Encouraging responsible business conduct**

This third review includes a full assessment of Chinese government efforts to encourage responsible business conduct against the background of recent regulatory changes and China’s increasing outward investment.

FORTHCOMING: **OECD Investment Policy Review of Peru**

This Review, undertaken as a part of Peru's adherence process and in co-operation with Peruvian authorities, shows the country's achievements in establishing an open and transparent investment regime with a limited number of restrictions, enabling Peru to rank among the most open economies. Recent governmental initiatives seek to further reduce administrative barriers to investment, streamline and simplify investment incentives and promote responsible business conduct practices.

FORTHCOMING: **OECD Benchmark Definition of Foreign Direct Investment**

Recording comprehensive, comparable and up-to-date statistics on Foreign Direct Investment is a prerequisite for economic analysis and policy making. The fourth Edition of the OECD Benchmark Definition provides operational guidance on how FDI data should be compiled to meet internationally agreed standards.

Several options are available for obtaining publications:

Additional information and links can be found via the investment portal on the OECD website:
www.oecd.org/investment

Subscribers and readers at subscribing institutions can access the online edition via the online library: www.sourceoecd.org

Non-subscribers can purchase the PDF e-book and/or paper copy via our Online Bookshop:
www.oecd.org/bookshop

Government officials can find the PDF e-book via the publication locator on OLISnet:
www.oecd.org/OLISnet

Accredited journalists can obtain password access via the Newsroom: www.oecd.org

CALENDAR OF EVENTS

10-11 DECEMBER 2008, KAMPALA, UGANDA

NEPAD-OECD Annual High-level meeting on advancing investment policy reform in Africa



The high-level meeting will explore measures for implementing concrete plans for sustainably improving the investment climates in African countries. It will seek to engage the business sector as an agent for development and discuss how comprehensive investment policy reform can best be carried through, taking advantage of Africa's own peer review process (APRM) and of multilaterally-backed policy tools such as the Policy Framework for Investment.

Expert roundtable on investment in transport infrastructure and regional integration

The roundtable will identify the factors that are holding investment back in African countries' transport sector, drawing on experience sharing and best practices.

NEPAD-OECD
AFRICA INVESTMENT
INITIATIVE



Further information on the high-level meeting and expert roundtable can be found at: www.oecd.org/daf/investment/africa

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17 DECEMBER 2008, PARIS, FRANCE

Ninth OECD Roundtable on Freedom of Investment, National Security and 'Strategic' Industries

This roundtable will take stock of discussions held to date with a view to preparing a report to the 2009 meeting of the OECD Council at ministerial level. Participants will also discuss priorities for future work in the area of freedom of investment.

Launched in early 2006 within the framework of the Investment Committee's freedom of investment project, these roundtables provide a forum for intergovernmental dialogue on how governments can reconcile the need to preserve and expand an open international investment environment with their duty to safeguard the essential security interests of their people.

Participants are the OECD members, the 11 non-members adhering to the OECD Declaration on International Investment and Multinational Enterprises and the other major emerging economies, as well as the European Commission.

Further information about the freedom of investment project can be found at: www.oecd.org/daf/investment/foi.

Contact: Kathryn Gordon, Tel: +33(0)145249842126

26-27 FEBRUARY 2009, BANGKOK, THAILAND

2nd OECD-South East Asia Regional Forum: Enhancing Competitiveness through Regional Integration

With the greater integration of China and India into the regional and global economy, countries in Southeast Asia are increasingly grappling with how to stay competitive in the changing economic landscape. Countries face the challenge of maintaining and increasing competitiveness through deeper regional integration while ensuring that the benefits of sustained growth are widely shared within the region and within countries.

This forum will provide an important opportunity to discuss and share views on economic and social aspects of regional integration and co-operation in Southeast Asia. It will also serve as a platform for launching the OECD's work with South East Asia.

Hosted by the Government of Thailand, this event will be organised by the OECD in co-operation with ASEAN and other regional organisations.

Contact: Ken Davies, Tel: +33(0)145241974

NEWS IN BRIEF

OECD GUIDANCE ON OPTIMISING PRIVATE SECTOR PARTICIPATION IN WATER AND SANITATION

OECD is developing practical guidance for governments wishing to engage the private sector in the development and management of water and sanitation infrastructure as a means to extend and accelerate access to drinking water and sanitation.

The guidance is being developed through multi-stakeholder dialogues, reviews of specific country experiences and regional consultations in Africa, Asia and South America. The most recent consultation took place in Mexico on 4-5 September. Jointly organised by OECD and the Mexican Institute of Water Technology, this expert meeting focused on lessons learnt from Latin American country experiences as well as providing a forum to discuss and better define the key elements of beneficial partnerships in this sector.

The project is due for completion in early 2009, with the guidance published in time to contribute to the 5th World Water Forum in Istanbul in March 2009.

Further information about the project can be found at: www.oecd.org/daf/investment/water

Contact: Céline Kauffmann, Tel: +33(0)145249849333