

The time for global investment co-operation has come



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The purpose of the Investment Newsletter is to share the results of the OECD Investment Committee's work with the wider investment policy community.

A publication of the Investment Division of the Directorate for Financial and Enterprise Affairs, Organisation for Economic Co-operation and Development.

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The global environment for international investment is evolving rapidly. Many large developing and transition economies are emerging as important outward investors, technological innovations and more open markets are enabling production strategies based on global value chains, and changes in how knowledge is created, acquired and disseminated are giving impetus to strategic "asset seeking" international investments.

With the appropriate framework conditions in place these developments offer new opportunities for international investment, benefiting economic growth and development. But there are challenges too. Many of the poorest countries, especially in Africa have been left behind. There are also public concerns that the globalising environment for international investment represents a threat to countries, to their industrial base and to their economic security. This is leading some countries to rethink their international investment regulations.

Such investment policy matters, including responsible business conduct, are one of the focal areas of the current G8 Presidency and were a prominent part of the discussions at the Heiligendamm Summit. Heads of State called on the investment policy community to find ways of addressing public concerns without yielding to protectionist pressures, and asked the OECD to continue and expand its work on these issues in co-operation with non-member partners.

This edition of the Investment Newsletter highlights recent and ongoing work at the OECD addressing the new challenges of a global international investment environment. It includes articles reporting the latest FDI trends, a summary on progress made in our 'freedom of investment' project, an overview of newly developed OECD Principles for Private Sector Participation in Infrastructure and the key findings from recent analytical work exploring the linkages between FDI and intellectual assets.



Manfred Schekulin
Chair, OECD Investment Committee

The evolving FDI landscape: a statistical overview

A buoyant international corporate environment, ample liquidity, the emergence of internationally active businesses based in developing and emerging economies and of a new class of investors in the form of private equity capital and hedge funds led to rapid growth in foreign direct investment (FDI) in 2006. FDI flows to and from OECD countries reached their second highest level in history and cross-border mergers and acquisitions by companies domiciled outside the OECD area more than doubled compared with 2005.

FDI flows to the OECD area rise sharply...

In 2006 FDI outflows to and from OECD countries increased by 29 %, to reach 1.1 trillion US dollars (USD), and inflows rose by 26 % to reach levels around one trillion US dollars (see table). As a result, net FDI outflows for the OECD area rose by 70 % from the level in 2005 to USD 210 billion. The near-term outlook for FDI remains strong. Based on the year to date, investment into OECD economies is predicted to increase by a further 20 % in 2007.

The U.S regained its position as the largest recipient and source of FDI in 2006. Inflows rose by two thirds to USD 184 billion, mostly from European based companies. A number of other OECD countries recorded their highest-ever FDI inflows in 2006. These include France, Greece, Iceland, Poland, Slovak Republic, Switzerland and Turkey. Inward FDI to the United Kingdom, while remaining internationally high, fell relative to the exceptionally large inflows in 2005.

Foreign Direct Investment, billion US\$

	Outflows		Inflows	
	2005p	2006e	2005p	2006e
Australia	-34.3	21.0	-35.0	24.5
Austria	10.0	4.1	9.0	0.2
Belgium/Luxembourg
Belgium	31.8	62.6	33.9	71.5
Canada	34.1	42.1	33.8	66.6
Czech Republic	0.0	1.3	11.7	6.0
Denmark	15.0	8.2	13.1	7.0
Finland	4.5	..	4.5	3.7
France	120.9	115.1	81.0	81.1
Germany	55.5	79.5	35.8	42.9
Greece	1.5	4.2	0.6	5.4
Hungary	2.3	3.0	7.6	6.1
Iceland	7.1	4.2	3.1	3.2
Ireland	13.6	22.1	-31.1	12.8
Italy	41.8	42.1	20.0	16.6
Japan	45.8	50.2	2.8	-6.5
Korea	4.3	7.1	6.3	3.6
Luxembourg	124.0	81.6	116.3	97.0
Mexico	6.5	5.8	19.6	19.0
Netherlands	142.8	22.7	41.4	4.4
New Zealand	-0.3	-1.6	3.1	1.6
Norway	21.1	12.2	6.4	1.6
Poland	3.1	4.1	9.5	13.9
Portugal	2.1	3.5	4.0	7.4
Slovak Republic	0.1	0.4	1.9	4.2
Spain	41.8	89.7	25.0	20.0
Sweden	26.5	24.1	10.2	27.8
Switzerland	54.2	81.5	-1.3	25.1
Turkey	1.1	0.9	9.8	20.2
United Kingdom	83.7	79.5	193.7	139.6
United States	9.1	248.9	109.8	183.6
Total	869.4	1120.1	746.6	910.2

Note: data are converted to US dollars using average exchange rates.

e) Estimates

p) Preliminary

Source: OECD International Direct Investment Database

The main outward direct investors in the OECD area are the United States, France, Spain, the UK, Germany and Switzerland. Together they accounted for nearly two thirds of the OECD total in 2006. These same countries have consistently been among the major outward investors over the past decade.

... not least in the mining sector

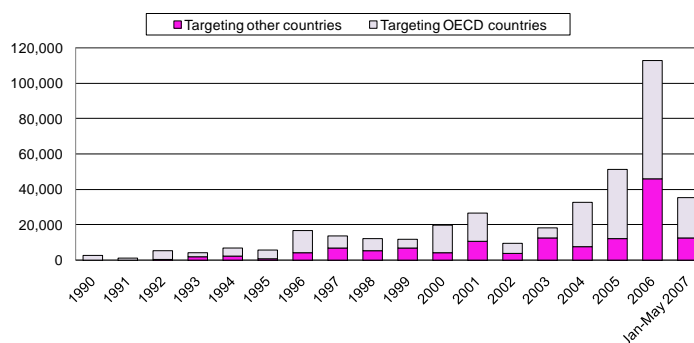
While mergers and acquisitions (M&A) are only one component of FDI they account for the majority part, and M&A data provide insights into the composition of international investment by sector. The sector with the largest value of international M&As in 2006 was mining and processing of raw materials, followed by the telecommunications and financial sectors.

The emergence of new players

The international expansion of companies from developing and emerging markets continued in 2006. Rapid economic growth, especially in Asia and oil-exporting countries, high prices for raw materials and more open investment regimes in some countries have been driving a boom in outward investment from non-OECD economies.

The value of cross-border M&As by companies domiciled outside the OECD area more than doubled in 2006 compared with 2005 (see figure). Moreover, the share of investments from these countries in the inflows of other non-OECD countries – 'south-south' investment – rose sharply. The most active 'south-south' investors are Singapore, China, Malaysia and South Africa. The most active non-OECD country investors in the OECD area are Singapore, Brazil, the United Arab Emirates and South Africa.

Cross-border M&As by companies domiciled outside the OECD area, billion US\$



Source: Thomson OneBanker

For further reading on this topic:

International Investment Perspectives, 2007 (forthcoming).

OECD work on FDI statistics:

www.oecd.org/daf/investment/statistics

Investment freedom: a focal area of the Heiligendamm G8 Summit

The Heiligendamm G8 Summit highlighted the risks a loss of investment freedom would entail for the global economy, and called for a clear signal for open investment regimes and work towards achieving equal competitive conditions for all investors in the industrial and emerging economies. The Summit Declaration asked the OECD to continue its work on Freedom of Investment, National Security and "Strategic" Industries. This article surveys recent progress and the planned next steps for this work.

The risk of "investment protectionism" is real

Existing regulatory frameworks, whether formally related to investment policy or not, have in a small number of widely publicised cases been used to deter international investment in the infrastructure and energy sectors. Moreover, several countries have recently tightened their regulatory and administrative practices and others are considering following suit. This is raising concerns that "investment protectionism" may be mounting.

"We reaffirm that freedom of investment is a crucial pillar of economic growth, prosperity and employment. We call on all developed countries, major emerging economies and others to critically assess their investment policies, the potential costs incurred from unnecessarily restrictive or arbitrary policies and the economic benefits of open investment regimes."

Declaration, G8 Summit, 7 June 2007

Against this background and to help all countries reap the benefits from an increasingly interdependent global economy, the OECD embarked on a project entitled "Freedom of Investment, National Security and 'Strategic' Industries" in 2006.

An overview of discriminatory practices

The first phase, which is now complete, focused on fact-finding, mapping existing regulatory approaches to security and other essential interests among OECD countries and other participants in the Investment Committee. Some of the findings include:

- National security concerns play a role in most countries' investment policies, but few of them clarify or attempt to define what they mean by "security".
- Half the countries surveyed publish "closed lists" of restricted activities and 22 countries maintain specific sectoral restrictions on investment on security grounds.
- Perceptions of essential interests other than national security vary widely across countries.
- Few countries practice statutory discrimination against enterprises controlled by foreign governments, whereas many apply or have the option to apply stricter scrutiny in case of foreign public control.

Shared views of principles for investment policy

Part of the second phase of the project involves seeking consensus on the principles that underpin investment policy responses to national security and other essential interests. Three principles have been proposed:

- Regulatory proportionality, whereby restrictions on investment should not be more costly or more discriminatory than needed to achieve the security objectives and they should not duplicate what is, or could be, better dealt with by other regulation.
- Predictability, whereby while it is in the interest of both investors and national administrations to maintain confidentiality of sensitive information, regulatory objectives and practices should be made as transparent as feasible so as to increase the predictability of outcomes and eliminate sources of misunderstanding.
- Accountability, whereby while improper political interferences in the normal exercise of regulatory power have to be avoided, procedures for parliamentary oversight or judiciary redress should ensure accountability.

Next steps

The second phase of the project is expected to move forward in two directions. First, to establish an enhanced mechanism for dialogue and reporting on investment impeding regulations, to better understand the potential costs to economies of unnecessarily restrictive policies to achieve security objectives and for consultation on topics of controversy, such as takeovers of domestic enterprises by foreign government supported companies.

The second direction is to translate the above principles into good practices for countries contemplating restricting investment on the grounds of national security and related essential interests. In advancing this agenda it will be essential to bring all the key players in the global economy into the discussion.

For further reading on this topic:

OECD work on "Investment protectionism":
www.oecd.org/daf/investment.

The full text of the G8 Summit Declaration can be accessed online at: www.g-8.de

OECD Principles for Private Sector Participation in Infrastructure

The needs for infrastructure investment worldwide in the coming decades are estimated to exceed US\$1,800 billion per year. Such levels of investment probably cannot be financed by the public purse alone. Encouraging private investment in infrastructure is an option that governments cannot afford to ignore. But a legacy of many failed public-private partnerships in infrastructure sectors attests to the difficult challenges facing policy makers. To help respond to these challenges the OECD Investment Committee has recently developed Principles for Private Sector Participation in Infrastructure.

The private sector is a major player in infrastructure development

Governments sometimes cannot or choose not to finance infrastructure projects alone. According to the World Bank, between 2001 and 2005, more than 850 infrastructure projects in developing economies alone were partly financed by private money at an estimated cost of USD 175 billion.

The Principles offer first step guidance to public authorities contemplating private sector involvement

The objective of the OECD Principles for Private Sector Participation in Infrastructure is to assist governments working with private sector partners to finance and bring to fruition major infrastructure projects in areas of vital economic importance, such as transport, water and power supply and telecommunications for the benefit of society and achieving sustainable development.

The Principles give governments a checklist of policy issues that they should consider in ensuring that citizens get the services they need at a fair cost and with acceptable returns to private sector partners.

“Helping countries find new ways of financing investment in areas like water supply and sanitation is one of the OECD’s priorities. These Principles will help both developed and developing countries move forward with infrastructure projects to boost economic growth and improve the lives of their citizens.”

OECD Secretary-General, Angel Gurría

The Principles cover five main areas

The Principles are designed to help governments address a range of issues that may arise in working with private sector partners. They relate to:

- Deciding on the utility and nature of potential private sector involvement;
- Providing a sound institutional and regulatory environment for infrastructure investment;
- Ensuring public and institutional support for the project and choice of financing;
- Providing disclosure and complaints procedures for an effective working partnership; and

- Ensuring responsible business conduct on the part of the private sector partner.

Before embarking on a project, the Principles state, governments should make sure that it is affordable, taking account of all potential sources of financing including loans and grants and anticipated payments by end users. An appropriate business model should share risks and responsibilities in an acceptable manner, while safeguarding the integrity of public finances.

Governments must ensure a clean and competitive business environment, free of corruption and with appropriate access to financial markets. In cases where infrastructure projects have major environmental and social implications, the Principles call for independent assessments of their sustainability in prior cost-benefit analysis.

The Principles also recommend consultations with all stakeholders during the project's implementation and the development of dispute-handling procedures to build mutual trust and to address any problems that may arise between the public and private partners during the project's life.

The Principles are relevant to a range of models of private participation, ranging from service and management contracts, to full or partial public divestiture. Any infrastructure project in which the public and private partners retain an interest, or partake in the risk in the case of failure, may benefit from the recommendations laid down in the Principles.

The Principles were developed as part of a consultative process

The Principles were developed in consultation with a broad group of public and private sector experts from OECD and non-OECD countries, as well as from non-governmental organisations. They are intended to be used in conjunction with other OECD policy guidance and tools, such as the Policy Framework for Investment and the OECD Guidelines for Multinational Enterprises.

As part of a project on Sustainable Financing to Ensure Affordable Access to Water and Sanitation, the next NEPAD-OECD Africa Investment Initiative roundtable will test draft operational guidance in the sector tailored to an African country context.

For further reading on this topic:

The full text of the Principles and additional information are available on the OECD web site at: www.oecd.org/daf/investment/instruments.

International investment and intellectual assets

Globalisation is changing the international investment landscape. To better understand the forces at work and to identify the potential investment policy challenges of tomorrow, a recent report for the Investment Committee explored the linkages between international investment and intellectual assets and the activities of multinational enterprises. This article summarises the key findings.

The internationalisation of R&D investment is on the rise

Measuring the internationalisation of R&D investment is difficult, since only indirect indicators, such as R&D outlays, patents and numbers of R&D partnerships are available. Nonetheless, these measures depict well how globalisation through FDI is changing the supply and demand side of the innovation process:

- MNEs increasingly undertake a large share of their R&D investments abroad, through outsourcing or in foreign subsidiaries;
- Large MNEs are establishing foreign subsidiaries with the purpose of undertaking R&D locally;
- Technology sectors are the most active in internationalising their R&D investment, with up to 30% of R&D activity located outside the home country of the enterprise;
- The most favoured locations for R&D investment are countries with recognised academic excellence and a high educational attainment. Small countries with these factors have the highest share of foreign-controlled R&D (see figure);
- Cross-border R&D investment is dominated by enterprises domiciled in the OECD area, but there is a diversification to include emerging economies, notably China and India.

The driving forces are multiple...

A number of factors help to explain the increasing importance of international R&D investment. Investment and trade liberalisation and strengthened intellectual property rights protection have enabled and lowered the risk to enterprises of relocating R&D activities. The codification and standardisation of R&D processes, improved communication technologies and the drive to reduce R&D costs have also allowed a greater segmentation and geographic dispersion of R&D in line with competitive cost advantages. Similarly these forces are enabling a greater reliance by firms on external sources of innovation, such as strategic alliances and joint ventures.

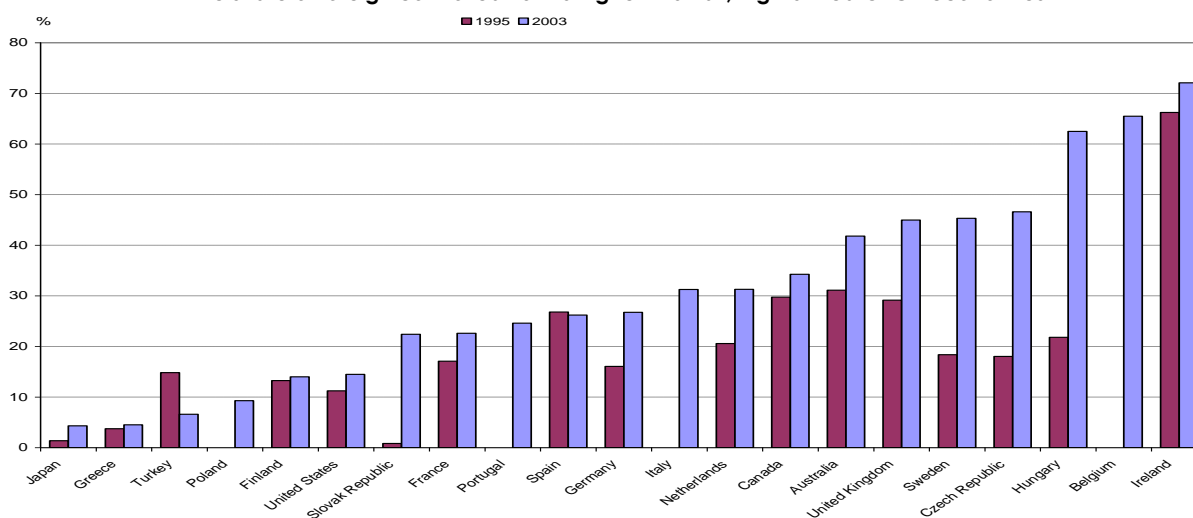
...and imply opportunities and challenges

These changes in how knowledge is created and disseminated offer new opportunities for international investment and can benefit local affiliates and enterprises via technology sourcing, boosting productivity and competitiveness. However, the positive spillovers do not occur automatically. In particular, they require sufficient absorptive capacity in the host country. There are also concerns that the acquisition of firms with substantial and geographically diversified R&D activities may lead to a concentration of R&D in a few locations, raising issues of protecting "strategic assets".

For further reading on this topic:

See *International Investment Perspectives, 2007* (forthcoming).

The share of foreign controlled R&D is higher in small, high-skilled OECD economies



Source: OECD Investment Division

Unlocking Africa's investment potential

The Africa Partnership Forum held its 8th meeting in Berlin, on 22-23 May 2007, hosted by the government of Germany. Mobilising private investment, both domestic and foreign, was one of the four key areas discussed at the meeting. The background paper prepared for the discussion drew on inputs from the OECD Investment Committee Secretariat. This article summarises some of the themes analysed in the background paper.

International investment is booming in Africa

Mobilising investment is the key to unlocking the vast potential for accelerated economic growth and development in Africa, and recent trends have been positive. FDI inflows to Africa reached US\$31 billion in 2005, surpassing bilateral ODA for the first time. Moreover, these flows are likely to be an underestimate due to the rudimentary nature of the monitoring systems in place.

FDI flows are also becoming more sectorally diversified, although they remain concentrated in the extractive industries. Food processing, textiles and services are attracting an increasing proportion of foreign investment, and from new source countries, such as China, India and Malaysia. Africa's share of global FDI, however, remains small and is geographically concentrated in a small number of African countries.

The drivers are better...

The upturn in investment is in part based upon the boom in the demand for and prices of raw materials. But it also reflects a period of relative political and economic stabilisation on the continent. Many countries have implemented democratic transition processes and economic reforms aimed at improving the investment climate.



G8 leaders with their counterparts from African countries at the Heiligendamm, G8 Summit, June 2007.

Source: Federal Government/ REGIERUNGonline / Bolesch

...but reform challenges remain

While FDI has risen sharply, the share of domestic business investment to GDP has remained steady at 19 %. Further increasing the levels of both domestic and foreign investment will be critical to achieving higher economic growth which Africa needs in order to accelerate progress towards meeting the Millennium Development Goals.

To unlock the investment potential that Africa holds the paper identifies three broad areas for action:

- Improving the regulatory environment and economic governance;
- Developing financial markets; and
- Developing infrastructure, including regional and rural infrastructure

The exact nature of the investment bottlenecks and policy responses needed, of course vary significantly across the continent. However, the APF paper attaches emphasis on the need for also taking action at the regional level, and the role which the international community can play in supporting an improved investment climate.

The key action points

The proposed action points on investment are comprehensive. They call for, inter alia, simplifying and improving labour laws, tax regulations and customs regimes, strengthening the rule of law and justice systems, and improving and enforcing anti-corruption laws and regulations. Other identified action points aim to tackle risk aversion in developing regional and rural infrastructure and to improve the commercialisation of financial market risk management products.

In implementing reforms in these areas bearing on the investment climate, the APF paper notes the important role being played by the APRM – an African owned peer review process – and the role development partners can play supporting policy capacity building programs and tools, such as the Policy Framework for Investment, developed by OECD countries with its non-member partners.

“We will individually and collectively continue to support initiatives which address the investment climate, such as... the NEPAD-OECD Africa Investment Initiative.”

Declaration, G8 Summit, 8 June 2007

Many of these action points are in the G8 Summit Declaration relating to the Africa agenda, and Heads of State declared their intention to continue to support individually and collectively initiatives which address the investment climate.

For further reading on this topic:

See background paper prepared for the 8th meeting of the African Partnership Forum on investment, available at www.africapartnershipforum.org.

Background information on the NEPAD-OECD Africa Investment Initiative is available at: www.oecd.org/daf/investment/africa.

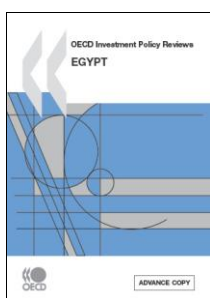
Selected investment publications

International Investment Perspectives, 2007 (forthcoming)



International Investment Perspectives is an annual publication. Each issue offers an update of recent trends and prospects in international direct investment and provides analyses of investment policy questions of topical interest. The publication aims to provide timely information to members of the international investment policy community, academia and members of the public with an interest in international investment. The 2007 issue contains two core analytic sections. The first includes four articles related to OECD work on Freedom of Investment, National Security and "Strategic" Industries. The second analytic section contains a series of articles that focus on the new opportunities arising from FDI, and the changing nature of the international economy in which investment takes place.

OECD Investment Policy Review of Egypt (forthcoming)



In July 2007, Egypt will become the 40th country to adhere to the *OECD Declaration on International Investment and Multinational Enterprises*. As part of the process, Egypt undertook a thorough review by OECD members of its international investment policies using the *Policy Framework for Investment*. This publication presents the results of this review.

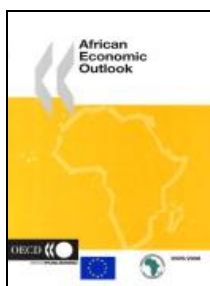
One of the main findings of the review is that international investors responded quickly to the government's policy reform efforts: foreign direct investment into Egypt increased eightfold in just three years, diversifying away from the petroleum sector and bringing investment to a broad range of manufacturing and service industries. However, the review also shows that investment climate reforms take time and many challenges still lie ahead.

OECD Principles for Private Sector Participation in Infrastructure



The *OECD Principles for Private Sector Participation in Infrastructure* aim to help governments work with private sector partners to finance and bring to fruition infrastructure projects in areas of vital economic importance such as transport, water and power supply and telecommunications. They offer authorities a checklist of policy issues to consider in ensuring that citizens get the services they need at a fair cost and with viable returns to private sector partners. The text of the Principles is available in English and French on the OECD website at: www.oecd.org/daf/investment/instruments.

African Economic Outlook, 2007



The African Economic Outlook combines the expertise of the OECD (Development Centre) with the knowledge of the African Development Bank on African economies. The objective is to review annually the recent economic situation and the likely short-term evolution of selected African countries. The 2007 focus is on Access to Drinking Water and Sanitation. The analysis examines how to expand the number of people with access to drinking water. It favours a comprehensive and integrated package, covering reforms in institutions, legal frameworks and policies that change the structure of incentives. In this context, the report reviews the experience with, and the role of alternative sources of finance, such as private participation.

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

Forthcoming events

27-28 November, 2007, Cairo, Egypt MENA-OECD Ministerial Meeting on Innovation and Investment

The second MENA-OECD Ministerial meeting will be hosted by the current Egyptian Chair of the MENA-OECD Investment Programme, represented by His Excellency Minister Mahmoud Mohieldin. The Ministerial Meeting will gather high level delegations from the countries participating in the Programme to identify elements crucial to fostering an investment climate suitable to innovation and to adopt new tools for implementation of investment policy reform. The meeting will equally attract private sector representatives from the region, who will be engaging in targeted discussions on topics which the Programme has been working on throughout 2006, including corporate governance, taxation, environment and financial sector development.

Further information on the MENA-OECD Programme can be found at: www.oecd.org/mena/investment.

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13-14 November 2007, Lusaka, Zambia NEPAD-OECD Africa Investment Initiative



The NEPAD-OECD Africa Investment Initiative aims to foster sustainable growth, employment creation and poverty reduction by advancing private sector development in African countries.

A Roundtable will take place in Lusaka, Zambia on 20-21 November 2007 (provisional). The overall aim of the Roundtable is to develop policy capacity building tools that will help NEPAD countries improve the investment related content of Africa's peer review process (APRM) and to support implementation of investment climate reform policies, with a specific focus on the investment environment conditions conducive to attracting investment for development in the water and sanitation sector.

Further information on the Initiative can be found at: www.oecd.org/daf/investment/africa.

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DID YOU KNOW...

...that African countries received for the first time more inward foreign investment than bilateral official donor assistance in 2005?

FDI inflows reached US\$31 billion in 2005, which relative to GDP is on a par with FDI flows to Asia. South Africa, the Democratic Republic of Congo and Egypt recorded among the highest FDI growth rates in developing countries.

News in brief

4th Roundtable on Freedom of Investment, National Security and "Strategic" Industries

On 30 March 2007, delegates from OECD member countries and other countries adhering to the Declaration on International Investment and Multinational Enterprises, as well as invited private sector experts, met in Paris to examine the challenge of identifying beneficiary ownership and control in the case of cross-border investment. The roundtable also focused on procedural considerations for authorities when choosing their model of investment regulation.

For a summary of the discussions visit: www.oecd.org/daf/investment

Roundtable on Corporate Responsibility OECD MNE Guidelines and the Financial Sector

On 18 June 2007, in conjunction with the Annual Meeting for National Contact Points (NCPs), the OECD held a Roundtable on "The OECD Guidelines for Multinational Enterprises and the Financial Sector" with invited experts from the financial community. The meeting allowed the NCPs to learn from practitioners about current trends in corporate responsibility practices and instruments in the financial sector and the challenges ahead, and to exchange views with financial actors on the various ways in which the OECD Guidelines can best support their efforts to promote corporate responsibility.

To find out more about the discussions, visit www.oecd.org/daf/investment/guidelines.

APEC-OECD High Level Public-Private Policy Dialogue on the Policy Framework for Investment

On 25-26 April 2007, Australia hosted a two-day APEC Public Policy Dialogue on the PFI in Melbourne. The main purpose of this event was to present the initial results of a project that is developing and testing a methodology for using the PFI as a framework for guiding policy choices in Vietnam.

In follow up, Vietnam announced at the Policy Dialogue its intention to proceed with a comprehensive assessment of its policies regarding the PFI, and to share the results of this assessment with the APEC and OECD investment policy communities in early 2008.