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**Research Report**

## COVID-19 and FDI: How should governments respond?

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## Columbia FDI Perspectives

Perspectives on topical foreign direct investment issues

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### **COVID-19 and FDI: How should governments respond?\***

by

Ivan Anton Nimac\*\*

Policy responses to the unprecedented economic shocks caused by COVID-19 have given limited attention to the promotion of FDI, which might have a major role to play in the recovery. Based on good practices demonstrated by countries, there are certain actions that governments should consider during the pandemic's crisis and recovery phases.

To begin with, governments' economic support to keep firms operational should be extended to both domestic firms and foreign affiliates. Both types of firms contribute to employment and livelihoods, the foreign-owned often also to higher-quality jobs.

There has been a proliferation of new barriers to FDI: at least 42 new barriers to entry—mainly in the form of FDI screening and the suspension of foreign work visas—have been put in place between April and July 2020.<sup>1</sup> While some have been levelled on all incoming FDI, most measures specifically target either healthcare or “strategic” sectors (e.g., infrastructure, utilities).<sup>2</sup> New barriers to FDI entry should be clearly defined, and COVID-19 measures time bound and subject to review.

Investment promotion agencies (IPAs) should start with supporting the retention of existing investors. Successful IPAs' principal roles are marketing, information provision, assistance, and advocacy services. Retention work is intrinsic to their information provision and assistance functions. There are two strong justifications for this. First, falling global FDI flows make it vital to maintain a country's existing FDI stock. Second, 30% of FDI inflows every year are reinvestment from investors already in the country.<sup>3</sup>

Successful IPA emergency retention responses, which have supported investors seeking to manage immediate disruptions, include maintaining business continuity by working remotely (Austria, Costa Rica, Jordan), continuously communicating with investors on all government measures (Chile, Ireland, Republic of Korea), providing direct problem-solving assistance, prioritizing investors with important supply chains (Abu Dhabi, Egypt, Ethiopia), and bolstering advocacy to convey to governments the challenges faced by foreign firms (India, Saudi Arabia, Tunisia).<sup>4</sup> Since the crisis phase has proven to be of long duration, further technological adaptation by IPAs is needed to carry

on investor meetings and site visits. This calls for IPAs strengthening their capabilities to act virtually and innovating their investment-attraction tools.

In the recovery phase, governments should consider resetting their FDI policy through a four-step process to help them overcome COVID-19's impact on FDI flows and to account for such pre-existing transformation drivers as sustainability and technological development:

- Governments should first review FDI strategies to test which of their previous FDI target segments remain resilient in the post-COVID-19 economy. This requires assessing the exposure of segments in which investor outreach was being pursued pre-COVID-19, to test if their value propositions remain strong through risk assessments and competitiveness benchmarking. For example, while apparel, automobiles, retail, and leisure industries have been negatively affected, medical machinery and supplies, pharmaceuticals, information-technology-enabled services, logistics, and some media have been less impacted or grown in importance.

Reviewing also involves identifying emerging competitive segments that may arise from the global value chain/FDI footprint remapping. Not all countries will have new opportunity sectors. However, near-shoring will create prospects for countries that have not previously been significant FDI destinations, but are located close to major markets.

This exercise should also be used to consider segments that are the best fit for other national objectives (e.g., sustainable, green growth, Industry 4.0 sectors). Countries do not evaluate their FDI strategies very frequently. Doing it now requires thinking bigger than a pandemic response and considering other pressing considerations.

- Once identified, the priority segments should be confirmed. This entails prioritizing the activities of ministries and agencies responsible for business registration and operations (including licenses, work permits, visas, incentives administration), with IPAs ensuring coordinated action.
- Governments should then implement FDI policy reforms to further improve the value propositions of current and emerging priority segments. This may require (i) phasing out any crisis-related screening mechanisms; (ii) aligning the incentive regime with the new target segments; and (iii) reviewing international investment agreements and laws to address problematic issues raised by the pandemic (e.g., clarity of rights and obligations in force majeure situations). Governments should also consider establishing investor-state grievance mechanisms to capture issues before they escalate into legal disputes.
- Lastly, countries should promote new segments, with IPAs undertaking investor outreach and facilitating investments. In countries without new opportunities, the work of IPAs should focus on aftercare throughout the recovery phase. Attracting new projects requires new strategies incorporating digital marketing techniques, virtual meetings and virtual site visits. Over time, this will require IPAs to adjust their performance indicators (KPIs) and mix of investor services.

Adapting to the new sectoral landscape, bolstering investor confidence and clarifying governments' ability to develop legitimate policy responses will fortify the key role of FDI in the post COVID-19 recovery and national development agendas.

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<sup>1</sup> Team research of the Investment Climate Unit, World Bank Group, July 2021.

<sup>2</sup> [OECD, \*Acquisition- and Ownership-related Policies to Safeguard Essential Security Interests\* \(Paris: OECD, 2020\), Section 2.1.1.](#)

<sup>3</sup> [World Bank, \*Global Investment Competitiveness Report 2017/18\* \(Washington D.C.: WBG, 2018\), p. 20.](#)

<sup>4</sup> [World Bank, "The initial responses of investment promotion agencies to Covid-19 and some observed effects on FDI" \(Washington, D.C.: WBG, 2020\).](#)

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