

## **Trends in FDI, home country measures and competitive neutrality**

Karl P. Sauvant, Persephone Economou, Ksenia Gal, Shawn Lim,  
and Witold P. Wilinski\*

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\* Karl P. Sauvant (karlsauvant@gmail.com) is Resident Senior Fellow, Columbia Center on Sustainable Investment (a joint center of Columbia Law School and The Earth Institute at Columbia University); he was the Founding Executive Director of the predecessor of that Center, the Vale Columbia Center on Sustainable International Investment, and Director of UNCTAD's Investment Division. Persephone Economou (persa.economou@gmail.com) is a staff member of the World Bank's Multilateral Investment Guarantee Agency (MIGA); before that, she was the Managing Editor of the *Journal of International Business Studies* (where she co-edited a special issue on international business negotiations) and a staff member of UNCTAD in Geneva and of the United Nations Centre on Transnational Corporations in New York. Ksenia Gal (gal.ksenia@gmail.com) is Research Associate, Vale Columbia Center on Sustainable International Investment; she holds an LL.M. degree in international legal studies from New York University Law School and a first law degree from the Russian Academy of Justice in Moscow, Russia. Shawn Lim (shawnlwk@gmail.com) is Research Associate, Vale Columbia Center on Sustainable International Investment and Juris Doctor Candidate at Columbia Law School; he holds a Bachelor of Laws (LLB) degree from the London School of Economics and Political Science. Witold P. Wilinski (witold.wilinski@gmail.com) is Assistant Professor at Warsaw School of Economics (World Economy Faculty); he was a Visiting Researcher at the Vale Columbia Center on Sustainable International Investment at Columbia University. The authors gratefully acknowledge inputs provided by Maheshwari Sundaresh and Jorge Luis Alcaraz. They, as well as Toru Kodama, Xiaoxin Li, Steven Miller, Tze-wei Ng, Evan Toma, Alexandre-Philippe Vinel, and Brian Witthuhn, were also part of a research project on home country measures, in the framework of which this chapter was prepared. We are grateful to all of them. We also gratefully acknowledge feedback from Sergey Filippov, Mark Koulen, Zhongmin Li, Alexei Kuznetsov, and Sebastian James on various parts of the chapter or the chapter as a whole. Any errors are of course those of the authors.

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The Western financial and economic crises continued to bedevil foreign direct investment (FDI) flows during 2012: after recovering during 2011, they declined again in 2012 and are projected to remain largely unchanged in 2013, about two thirds below what they had been at the end of 2007. Still, at well over US\$ 1 trillion, they remain substantial, underlining the vitality of this area of international economic transactions. This vitality can also be observed in the policy arena, at both the national and international levels: policy- and treaty-making continue unabated, even venturing into new areas.

One of these new areas concerns “competitive neutrality.” In the context of FDI, the issue is whether, and to what extent, the support that home country governments give to their firms investing abroad distorts competition among outward investors from different countries. This chapter reviews the different types of measures that home countries use to support outward FDI (OFDI). Home country measures (HCMs) supporting OFDI constitute an important, but quite underexplored area: while there is an extensive literature on measures pertaining to attracting *inward* FDI, there is much less information on measures supporting *outward* FDI. Yet, HCMs can potentially influence, among other things, the volume, quality, mode of investment, type of investor, sector of investment, and location of OFDI.

As more countries become important capital exporters and hence home countries of multinational enterprises (MNEs), it is important better to understand the types of HCMs put in place by governments and their role in meeting different objectives, ranging from accessing new markets and exploiting natural resources abroad, to acquiring new technologies and brands. Many emerging markets do not have a coherent OFDI strategy in place. This is in contrast to the position with inward FDI regimes, where most countries have adopted a clear strategy, with the necessary policy instruments in place to attract foreign investors. To change that, governments might need to understand other countries’ outward investment policies and the measures that have been adopted in order to help their firms invest abroad. Given the attention being paid to competitive neutrality in international negotiations (such as the Trans-Pacific Partnership Agreement<sup>1</sup> and the Transatlantic Trade and Investment Partnership)<sup>2</sup>, policymakers need to understand whether, and to what extent, government policies that bestow special privileges on outward investors (or special classes of outward investors, such as state-owned enterprises) distort the competitive landscape in the world FDI market.

The chapter begins with a discussion of the latest FDI trends and policy developments. Part B of the chapter provides an introduction to the main issues relating to HCMs and the institutions that grant HCMs, followed by substantive analyses of informational, financial and fiscal HCMs. The

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<sup>1</sup>An agreement aimed at enhancing trade and investment among Australia, Brunei Darussalam, Chile, Malaysia, Mexico, New Zealand, Peru, Singapore, Vietnam, and the United States (<http://www.ustr.gov/about-us/press-office/fact-sheets/2011/november/united-states-trans-pacific-partnership>). Japan is seeking to participate as well.

<sup>2</sup> Office of the United States Trade Representative, “The Transatlantic Trade and Investment Partnership is envisioned as an ambitious, high-standard trade and investment agreement that would provide significant benefit in terms of promoting U.S. international competitiveness, jobs, and growth” (<http://www.ustr.gov/about-us/press-office/fact-sheets/2013/february/US-EU-TTIP>).

chapter concludes in Part C with a discussion of issues related to HCMs and competitive neutrality.

### **A. Trends in foreign direct investment and international investment agreements**

According to UNCTAD's latest estimates,<sup>3</sup> global FDI *inflows* fell by 18% in 2012, reaching an estimated US\$ 1.4 trillion and reversing a recovery that had begun in 2010 and had continued in 2011. Underlying this trend was a 45% decline in the value of cross-border mergers and acquisitions (M&As), which fell to its lowest level since 2009, and a 33% decline in the value of announced greenfield projects. The reversal underlines the lingering negative effects of a turbulent and slow recovery in the global economy, ongoing de-leveraging in key source countries and a deteriorating environment in key destination countries. In 2013, global FDI inflows are projected to remain close to their 2012 level, as economic recovery has yet to gather speed and investor confidence is still lacking. A rebound is forecasted for 2014, to US\$ 1.6 trillion.

FDI flows into developed countries declined by almost a third in 2012, to US\$ 561 billion. The decline was sharpest in the European Union and the United States. The ongoing sovereign debt crisis and economic recession in the European Union led to sharp declines in FDI inflows in some countries: 80% in Italy, 87% in Germany and a net divestment of US\$ 1.6 billion, down from US\$ 103 billion the year before, in Belgium. Interestingly, Greece and Ireland, having suffered sharp declines in FDI flows in the previous year, saw large increases in investment in 2012. The United States continued to be the largest recipient of FDI flows in the world.

In contrast, FDI flows into emerging markets<sup>4</sup> declined by only 4% in 2012, to US\$ 703 billion; they surpassed those into developed countries by about US\$ 140 billion. While emerging markets have not been immune to the weak recovery of the global economy, they are still growing two-to-three times faster than developed economies, rendering them attractive destinations for foreign investors. FDI flows into developing Asia fell by 7% in 2012, mostly on account of declines into Hong Kong SAR China, India and Turkey. Flows into China declined only marginally and remained elevated at US\$ 121 billion. Following net divestments in 2011, FDI flows into Egypt were estimated to have rebounded to US\$ 2.8 billion in 2012. Transition economies experienced a 9% decline in FDI flows, impacted by the economic situation in the European Union, while Africa and Oceania were the only regions to have registered positive growth in FDI flows in 2012.

Global FDI *outflows* declined by 17% in 2012, reaching US\$ 1.4 trillion. OFDI from developed countries fell by 23%, reaching US\$ 909 billion, while FDI outflows from emerging markets increased slightly to US\$ 426 billion. OFDI from emerging markets reached record levels in recent years, as firms based in those markets continue to establish production facilities overseas.

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<sup>3</sup> UNCTAD, *World Investment Report 2013: Global Value Chains. Investment and Trade for Development*, Sales no.: E.13.II.D.5 (Geneva: United Nations, 2013).

<sup>4</sup> Defined as developing countries and transition economies, as classified in the UNCTAD, *World Investment Report 2013, op. cit.*, Annex 1.

On the policy front, the majority of regulatory changes continue to be toward greater openness, and the proportion of regulatory changes toward greater restrictiveness registered a decline in 2011 but increased again in 2012 (Table 1). While some countries continue to liberalize their regulatory frameworks, especially at the sectoral level, others are imposing restrictions to expand domestic control of strategic sectors. In the extractive industries, for example, 46% of all measures related to investment were in the direction of greater restrictiveness.

**Table 1. National regulatory changes, 2000-2012**

Item	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012
Number of countries that introduced changes	45	51	43	59	80	77	74	49	41	45	57	44	53
<b>Number of regulatory changes</b>	<b>81</b>	<b>97</b>	<b>94</b>	<b>126</b>	<b>166</b>	<b>145</b>	<b>132</b>	<b>80</b>	<b>69</b>	<b>89</b>	<b>112</b>	<b>67</b>	<b>86</b>
Liberalization/promotion	75	85	79	114	144	119	107	59	51	61	75	52	61
Restriction/regulation	5	2	12	12	20	25	25	19	16	24	36	15	20
Neutral/indeterminate <sup>a</sup>	1	10	3	0	2	1	0	2	2	4	1	0	5

Source: UNCTAD, Investment Policy Monitor database.

<sup>a</sup> In some cases, the expected impact of the policy measure on the investment is undetermined.

Source: UNCTAD, *World Investment Report 2013*, op. cit., p. 92.

As of end-2012, there were 3,196 international investment agreements (IIAs), of which 2,857 were bilateral investment treaties (BITs). While the number of BITs continues to grow, progress on regional initiatives is also accelerating.<sup>5</sup> These include the Trans-Pacific Partnership Agreement (currently under negotiation - it is expected to include an investment chapter with typical standards for investment liberalization and protection), the trilateral investment agreement between China, Japan and the Republic of Korea,<sup>6</sup> the European Commission's "Towards a comprehensive European international investment policy,"<sup>7</sup> and the Mexico–Central America FTA (which contains an investment chapter).<sup>8</sup>

## B. Home country measures

### 1. Introduction

<sup>5</sup> UNCTAD, *World Investment Report 2013*, op. cit., chapter 3.

<sup>6</sup> Agreement among the Government of Japan, the Government of the Republic of Korea and the Government of the People's Republic of China for the Promotion, Facilitation and Protection of Investment, available at [http://www.mofa.go.jp/announce/announce/2012/5/pdfs/0513\\_01\\_01.pdf](http://www.mofa.go.jp/announce/announce/2012/5/pdfs/0513_01_01.pdf) (last visited March 20, 2013).

<sup>7</sup> Communication from the Commission to the Council, the European Parliament, the European Economic and Social Committee and the Committee of Regions, COM (2010) 343 (July 7, 2010), available at: [http://trade.ec.europa.eu/doclib/docs/2011/may/tradoc\\_147884.pdf](http://trade.ec.europa.eu/doclib/docs/2011/may/tradoc_147884.pdf) (last visited March 20, 2013); Directorate-General for External Policies, European Parliament, "The EU Approach to International Investment Policy After the Lisbon Treaty" (2010); Julien Chaisse, "Promises and Pitfalls of the European Union Policy on Foreign Investment" 15(1) *Journal of International Economic Law* 51 (2012).

<sup>8</sup> Free Trade Agreement between Mexico, Costa Rica, El Salvador, Guatemala, Honduras and Nicaragua (the "Central America FTA"), signed in San Salvador, El Salvador on November 22, 2011, available at: [http://www.sice.oas.org/Trade/CACM\\_MEX\\_FTA/Index\\_s.asp](http://www.sice.oas.org/Trade/CACM_MEX_FTA/Index_s.asp) (last visited June 5, 2013).

### a. Outward FDI policies and the impact of OFDI on home countries

Both inward FDI and outward FDI are primarily driven by economic factors. Firms need to have certain “ownership” advantages that give them the competitive capabilities to invest successfully in foreign lands. Economic opportunities in host countries (“location-specific” advantages), in turn, entice them to invest there, assuming that FDI provides the “internalization” advantages that make such investment the preferred course of action in comparison with other modes of international economic transactions (e.g., trade). The combination of these three sets of advantages gives rise to FDI.<sup>9</sup> It is the widely held view, supported by the literature, that inward FDI on balance makes a positive contribution to a host country’s economy by bringing in a bundle of tangible and intangible resources: capital, technology, skills, management techniques, brands, and access to markets, to name a few.<sup>10</sup> However, attracting FDI does not guarantee that all the benefits it carries can be reaped by host countries. Policies need to be in place to ensure that linkages with the domestic economy are in place, that the foreign investment does not crowd out domestic firms and that appropriate competition rules are observed, among other things. This underlies the significant attention paid to policies to attract, retain and maximize the potential benefits of inward FDI.<sup>11</sup>

OFDI is beginning to receive more attention as investment flows from emerging markets have taken off.<sup>12</sup> Yet, OFDI policies have by far not received as much attention as inward FDI policies. This is partly because of the view, especially among capital importing countries, that OFDI does not carry the same benefits as inward FDI: while companies undertake OFDI for various reasons that ultimately benefit them, the economic impact of such investment on home countries themselves is perceived to be less clear than in the case of inward FDI. This is so

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<sup>9</sup> See John H. Dunning and Sarianna M. Lundan, *Multinational Enterprises and the Global Economy* (Cheltenham: Edward Elgar, 2008); Bruce Blonigen, “A review of the empirical literature on FDI determinants,” National Bureau of Economic Research, Working Paper No. 11299 (2005).

<sup>10</sup> See Dunning and Lundan, *Multinational Enterprises and the Global Economy*, 2008, op. cit. See also, UNCTAD, *World Investment Report 1999: Foreign Direct Investment and the Challenge of Development* (Geneva: UNCTAD, 1999).

<sup>11</sup> UNCTAD, *World Investment Report 2012: Towards a New Generation of Investment Policies* (Geneva: UNCTAD, 2012).

<sup>12</sup> UNCTAD, “Global players from emerging markets: strengthening enterprise competitiveness through outward investment” (New York and Geneva: United Nations, 2007); Yadong Luo, Qiuzhi Xue and Binjie Han, “How emerging market governments promote outward FDI: Experience from China,” 45 *Journal of World Business* 68 (2010); Dirk Willem te Velde, “Understanding developed country efforts to promote foreign direct investment” 16(3) *Transnational Corporations* 83 (2007), available at: [http://unctad.org/en/docs/iteiit20074a4\\_en.pdf](http://unctad.org/en/docs/iteiit20074a4_en.pdf) (last visited February 18, 2013); Marjan Svetlicic, “Outward foreign direct investment by enterprises from Slovenia”, 16(1) *Transnational Corporations* 55 (2007); Kee Hwee Wee, “Outward foreign direct investment by enterprises from Thailand,” 16(1) *Transnational Corporations* 89 (2007); Peter J. Buckley et al., “The determinants of Chinese outward foreign direct investment”, 38 *Journal of International Business Studies* 499 (2007); Rajah Rasiah, Peter Gammeltoft and Yang Jiang, “Home government policies for outward FDI from emerging economies: lessons from Asia,” 5(3/4) *International Journal of Emerging Markets* 333 (2010); Chengqi Wang, Junjie Hong, Mario Kafourous and Mike Wright, “Exploring the role of government involvement in outward FDI from emerging economies,” 43 *Journal of International Business Studies* 655 (2012).

because OFDI entails, by definition, capital and other resources leaving the (home) country, which potentially has an impact on the country's capital stock, balance of payment, employment and wages, exports/imports, and technology development, among other things. While such concerns surface from time to time in developed countries (e.g., in the context of offshoring and “delocalization”), they are particularly relevant, at least in principle, for emerging markets, as these countries, more than others, are in need of productive capacity.

There is limited literature on the subject of the impact of OFDI on home countries. The evidence is mostly mixed and focused on developed countries as home countries,<sup>13</sup> due to the fact that firms from developed economies started to invest abroad earlier than firms from emerging markets.<sup>14</sup>

From the point of view of the home country, outward FDI strengthens the competitive position of the parent firm vis-à-vis international companies of other nationalities in the recipient country. Offshore affiliates enlarge the market share of parent companies in host economies. A home country policy of discouraging outward investment would leave foreign markets dominated by international investors and exporters based in other countries, with a reduced presence on the part of firms from the first home country.<sup>15</sup>

A study of the long-term aggregate effects of United States investment abroad suggested that OFDI could be a “displacement of domestic investment”, but the “gains from increased foreign earnings largely offset the loss of domestic output.”<sup>16</sup> Another study on OFDI from the United States found that “each dollar of assets in foreign affiliates reduces the domestic capital stock by

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<sup>13</sup> For a discussion of home country effects of OFDI, see Karl P. Sauvant and Geraldine McAllister with Wolfgang Maschek, eds., *Foreign Direct Investment from Emerging Markets: The Challenges Ahead* (New York: Palgrave Macmillan, 2010); Karl P. Sauvant with Kristin Mendoza and Irmak Ince, eds., *The Rise of Transnational Corporations from Emerging Markets: Threat or Opportunity?* (Cheltenham: Edward Elgar, 2008); Andrea Goldstein, *Multinational Companies from Emerging Economies: Composition, Conceptualization and Direction in the Global Economy* (New York: Palgrave Macmillan, 2007); UNCTAD, *World Investment Report 2006: FDI from Developing and Transition Economies: Implications for Development*, Sales No: E.06.II.D.11 (Geneva: UNCTAD, 2006); Robert E. Lipsey, “Home- and Host-Country Effects of Foreign Direct Investment,” in Robert E. Baldwin and L. Alan Winters, eds., *Challenges to Globalization: Analyzing the Economics* (Chicago: University of Chicago Press, 2004), pp. 333-382; UNCTAD, *World Investment Report 1995: Transnational Corporations and Competitiveness*, Sales No: E.05.II.D.10 (Geneva: UNCTAD, 1995); Steven Globerman, “The Public and Private Interest in Outward Direct Investment,” in Steven Globerman, ed., *Canadian-Based Multinationals* (Calgary: University of Calgary Press, 1994), pp. 1-34; Fred C. Bergsten, Thomas Horst and Theodore H. Moran, *American multinationals and American interests* (Washington, D.C.: The Brookings Institution, 1978).

<sup>14</sup> Early studies on the influence of OFDI on the home country economy were related to export and employment effects; see e.g., Carl Fred Bergsten, Thomas Horst and Theodor H. Moran, *American Multinationals and American Interests* (Washington: Brookings Institution Press, 1978).

<sup>15</sup> Theodore H. Moran, *Harnessing Foreign Direct Investment for Development*, *op. cit.*, p. 100.

<sup>16</sup> Peggy Musgrave, “Direct Investment Abroad and the Multinationals: Effects on the United States Economy,” in Neil Hood and Stephen Young, eds., *The Economics of Multinational Enterprise* (London and New York: Longman 1979), p. 320.



between 20 and 40 cents.”<sup>17</sup> Firms that invest abroad have higher levels of worker productivity, and more rapid growth rates of overall productivity than firms that do not invest abroad.<sup>18</sup>

As regards employment – a key concern in home countries – studies for the United States have found that OFDI has no effect – or at most, a small positive effect, via exports – on employment at home.<sup>19</sup> Similarly, a recent study of European Union outward investment on the European Union economy has shown that “outward FDI has a positive impact on EU competitiveness” and that “there has been no impact of outward FDI on overall employment.”<sup>20</sup> A similar lack of employment effects was found in the case of Estonia, a small economy in transition.<sup>21</sup> However a recent study on FDI from Germany showed that “multinational enterprises that expand abroad retain more domestic jobs than competitors without foreign expansions. MNEs’ employment expansions abroad reduce the rate of domestic job loss by about two percentage points. Given global wage differences, a prevention of enterprises from outward FDI would lead to more domestic job losses. FDI raises domestic-worker retention more pronouncedly among highly educated workers.”<sup>22</sup> A similar positive effect on home country employment was found in Italy,<sup>23</sup> Japan,<sup>24</sup> Sweden,<sup>25</sup> and with regard to United States vertical investment.<sup>26</sup> However, commentators have noted that, “when the domestic labor market is unionized, trade liberalization between countries with similar wage levels is likely to result in domestic welfare losses as a result of outward FDI. Only when wage differences between countries are large enough, can outward FDI improve domestic welfare and optimal tariffs will be zero.”<sup>27</sup> As one study concluded: “It is possible therefore in some instances that the home economy would benefit more over time with the outward investment taking place than not taking place, even if the immediate

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<sup>17</sup> Martin S. Feldstein, “The Effects of Outbound Foreign Direct Investment on the Domestic Capital Stock,” in Martin S. Feldstein, James R. Hines Jr., R. Glenn Hubbard, eds., *The Effects of Taxation on Multinational Corporations* (Chicago: University of Chicago Press, 1995), p. 46.

<sup>18</sup> Andrew B. Bernard, J. Bradford Jensen and Peter K. Schott, “Importers, Exporters and Multinationals: A Portrait of Firms in the U. S. That Trade Goods,” Working Paper 11404, Cambridge Mass. NBER, 1–57 (2005).

<sup>19</sup> Robert Lipsey, “Home- and Host-Country Effects of Foreign Direct Investment,” 1995, *op. cit.*

<sup>20</sup> Eva R. Sunesen, Svend T. Jespersen and Martin H. Thelle, “Impacts of EU outward FDI,” Final report, Copenhagen Economics (May 20, 2010), p. 59, available at: [http://trade.ec.europa.eu/doclib/docs/2010/june/tradoc\\_146270.pdf](http://trade.ec.europa.eu/doclib/docs/2010/june/tradoc_146270.pdf) (last visited April 27, 2013).

<sup>21</sup> Jaan Masso, Urmas Varblane and Priit Vahter, “The effect of outward foreign direct investment on home-country employment in a low-cost transition economy,” 46(6) *Eastern European Economics* 25 (2008), p.51.

<sup>22</sup> Sascha O. Becker and Marc-Andreas Muendler, “The effect of FDI on job security,” 8(1) *Journal of Economic Analysis and Policy* 1 (2008).

<sup>23</sup> Davide Castellani, Ilaria Mariotti and Lucia Piscitello, “The impact of outward investments on parent company’s employment and skill composition: Evidence from the Italian case,” 19 *Structural Change and Economic Dynamics* 81 (2008).

<sup>24</sup> Nobuaki Yamashita and Kyoji Fukao, “Expansion abroad and jobs at home: Evidence from Japanese multinational enterprises,” 22 *Japan and the World Economy* 88 (2010).

<sup>25</sup> Magnus Blomstrom, Gunnar Fors, Robert E. Lipsey, “Foreign direct investment and employment: Home country experience in the United States and Sweden,” 107 *Economic Journal* 1787 (1997).

<sup>26</sup> Ann E. Harrison and Margaret S. McMillan, “Outsourcing jobs? Multinationals and US employment,” NBER Working Paper No. 12372 (2006), pp. 1–45.

<sup>27</sup> David Collie and Hylke Vandenbussche, “Can Import Tariffs Deter Outward FDI,” 16 *Open Economies Review*, 341–362 (2005).

net job impact were to be negative, but not as negative as it would be if the parent firm failed to build up distribution networks and assembly facilities abroad.”<sup>28</sup>

As regards exports/imports, a recent literature review showed that, in the majority of cases, exports and OFDI complement each other. This means that the growth of outward FDI results in the growth of the home country’s exports of intermediate goods.<sup>29</sup> For example, a recent Canadian study noted that a dollar increase in Canadian FDI abroad in the period from 1992 to 2008 corresponded to a six cents increase in terms of export volumes for the following year.<sup>30</sup> A similar positive effect on home country exports was found in Japan, Sweden and the United States.<sup>31</sup>

The implications of offshoring research and development (R&D) on the innovation capacity of parent firms from developed countries seem to be positive.<sup>32</sup> Another study on the effects of OFDI on Sweden’s economy found that the impact has been beneficial because production activities with high profits and positive externalities were retained at home, and OFDI had allowed Swedish MNEs to spend more resources on research and development than would otherwise have been possible.<sup>33</sup> However, studies on R&D offshoring in the case of developing countries suggest a negative influence on innovation capacity in the home country.<sup>34</sup>

Despite the mixed evidence, one view is that inward FDI and OFDI can be considered together as part of a country’s competitiveness-enhancing strategy.<sup>35</sup> Governments, therefore, may consider OFDI as complementary to inward FDI, with both used for accessing markets, capital, technological know-how, managerial practices, natural resources, etc.

For net capital importing countries, such as most emerging markets, an additional concern is the shortage of foreign exchange for OFDI, especially due to the need to build up reserves in order to

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<sup>28</sup> Theodore H. Moran, *Harnessing Foreign Direct Investment for Development: Policies for Developed and Developing Countries* (Washington, D.C.: Center for Global Development, 2006), p. 101.

<sup>29</sup> Shuhei Nishitaten, “Global production sharing and the FDI–trade nexus: New evidence from the Japanese automobile industry,” 27 *Journal of The Japanese and International Economies* 64 (2013), pp. 67–68.

<sup>30</sup> Danielle Goldfarb, “Direct investment abroad: A strategic tool for Canada,” The Conference Board of Canada (January 2011), p. 9.

<sup>31</sup> Robert E. Lipsey, Eric D. Ramsterrer and Magnus Blomstrom, “Outward FDI and Parent Exports and Employment: Japan, the United States, and Sweden,” Working Paper 7623 (Cambridge, MA: National Bureau of Economic Research, 2000), p. 17.

<sup>32</sup> PRO INNO Europe, “The implications of R&D offshoring on the innovation capacity of EU firms” (Helsinki: Helsinki School of Economics, 2007).

<sup>33</sup> Magnus Blomstrom and Ari Kokko, “Home country effects of foreign direct investment: Evidence from Sweden,” NBER Working Paper No. 4639 (February 1994).

<sup>34</sup> These conclusions are based on the Taiwanese economy; see Shu-Chin Huang, “Capital outflow and R&D investment in the parent firm,” 42(1) *Research Policy* 245 (2013); Ling Sun, Lilyan E. Fulginiti and Yo-Chan Chen, “Taiwanese industry competitiveness when outward FDI is defensive,” 21 *Journal of Asian Economics* 365 (2010).

<sup>35</sup> Dunning and Lundan, *Multinational Enterprises and the Global Economy*, 2008, *op. cit.*; Dierk Herzer, “The long-run relationship between outward FDI and total factor productivity: Evidence for developing countries,” Proceedings of the German Development Economics Conference, Berlin 2011, No. 41, available at: [http://econstor.eu/bitstream/10419/48299/1/41\\_herzer.pdf](http://econstor.eu/bitstream/10419/48299/1/41_herzer.pdf) (last visited June 3, 2013).

reduce vulnerability to financial crises.<sup>36</sup> A study of the OFDI by MNEs from the Republic of Korea (which only recently has become a net capital exporting country) revealed no negative effects on home country performance and positive effects on exports.<sup>37</sup>

In general, however, the literature on the effects of OFDI from emerging markets on their home countries is very limited, making conclusions difficult.<sup>38</sup>

In the inward FDI (IFDI) policy domain, there is broad consensus on what constitutes an effective policy for attracting IFDI, retaining such investment and maximizing its positive impact on the economy. In the OFDI policy domain, such consensus is more tenuous, partly because of the concerns outlined above as regards the role of such investment in the home country economy, especially the impact of OFDI on the balance of payments, but also because the objectives of OFDI policies can be more diverse and widespread than those relating to inward FDI. Partly as a result, many emerging markets have only partly liberalized their OFDI regimes (see annex table I for a description of restrictions on OFDI by country illustrating that point).

## **b. Definition and types of home country measures**

HCMs<sup>39</sup> are defined as the granting of specific advantages by the home country government (or one of its public institutions) in connection with the establishment, acquisition and expansion of an investment by a home country firm in a foreign economy (Box 1).<sup>40</sup> They are meant to

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<sup>36</sup> Restrictions on OFDI are still in the process of being relaxed gradually in many emerging markets. See generally UNCTAD, *World Investment Report 2006, op. cit.*, as well as annex table I.

<sup>37</sup> Seungjin Kim, "Effects of Outward Foreign Direct Investment on Home Country Performance: Evidence from Korea," in Takatoshi Ito and Anne O. Krueger, eds., *The Role of Foreign Direct Investment in East Asian Economic Development*, NBER-EASE Volume 9 (Chicago and London: University of Chicago Press, 2000), p. 308, available at: <http://www.nber.org/chapters/c8503.pdf> (last visited May 22, 2013).

<sup>38</sup> See e.g. Poonam Sarmah, "Home Country Measures and FDI: Implications for Host Country Development" (Jaipur: CUTS Centre for Competition, Investment & Economic Regulation, 2003).

<sup>39</sup> See also UNCTAD's definition of HCMs: "HCMs are all policy measures taken by the home countries of firms that choose to invest abroad designed to encourage FDI flows to other countries. Their formulation and application may involve both home and host country government and private sector organizations." See UNCTAD, "Report of the Expert Meeting on Home Country Measures: held at the Palais des Nations, Geneva from 8 to 10 November 2000," TD/B/COM.2/27, Commission on Investment, Technology and Related Financial Issues, Fifth session, Geneva (12-16 February 2001). The OECD, which addressed the issue as early as in 1979 in the broader context of investment measures applied by home and host governments, defined incentives (or disincentives) as "any government measure designed to influence an investment decision, and increasing (or reducing) the profit accruing to the potential investment or altering the risks attaching to it"; from OECD, *Investment Incentives and Disincentives and The International Investment Process* (OECD: Paris, 1983), p. 10.

<sup>40</sup> Sometimes, home countries themselves -- via domestic organizations, such as public financing institutions or other public entities -- engage in OFDI activities. As long as these vehicles or institutions have been set up with the explicit purpose of undertaking OFDI, they are included in the analysis of this chapter (see discussion on institutions below) -- otherwise not. Sovereign wealth funds, for example, are not established with the specific purpose of engaging in OFDI, even though they undertake such investments, and therefore are not included in the present discussion.

facilitate, support or promote outward FDI – in other words, to help firms establish foreign affiliates.

### **Box 1. HCMs and the WTO’s Agreement on Subsidies and Countervailing Measures**

This definition of “granting of a specific advantage” is similar to the definition of a “subsidy” in the World Trade Organization’s Agreement on Subsidies and Countervailing Measures (hereinafter the SCM Agreement).<sup>[a]</sup> According to this definition, a subsidy is deemed to exist when there is a “financial contribution” that confers a benefit on the recipient of the subsidy. Financial contributions take place when “(i) a government practice involves a direct transfer of funds (e.g. grants, loans, and equity infusion), potential direct transfers of funds or liabilities (e.g. loan guarantees); (ii) government revenue that is otherwise due is foregone or not collected (e.g. fiscal incentives such as tax credits) [...]; (iii) a government provides goods or services other than general infrastructure [...].”<sup>[b]</sup> Importantly, the SCM Agreement applies only to those subsidies that are “specific to an enterprise or industry or group of enterprises or industries”, meaning that access to subsidy is limited to certain enterprises under objective criteria or conditions;<sup>[c]</sup> for instance, subsidies contingent upon export performance are always deemed specific.<sup>[d]</sup> Major direct home country measures (most of which are discussed below) could be seen as falling within the same classification. Financial incentives to domestic investors in connection with their outward investment are provided in the form of loans, grants, equity, and guarantees. Fiscal incentives take the form of tax revenue that is forgone or not collected, e. g., in the case of tax credits. The third type of support (referring to support “other than general infrastructure”) could apply to information and technical assistance services and, perhaps, political risk insurance. These supports can be provided directly by the government or public bodies, through specially created funding mechanisms or private bodies entrusted or directed by the government to carry out such functions. Finally, home country measures are often provided by the same agencies that administer trade subsidies and that have come under scrutiny of WTO panels.<sup>[c]</sup>

As a matter of clarification, it is important to note that, despite many similarities, the two concepts, HCMs and subsidies under the WTO’s disciplines, differ substantially.<sup>[d]</sup> The obvious difference is that subsidies are designed to advance trade objectives, while HCMs deal with outbound investment; nevertheless, trade subsidies may affect international investment flows.<sup>[e]</sup> Overall, HCMs are not generally regulated and, as discussed in the international investment literature,<sup>[f]</sup> seem to be a broader concept than subsidies as covered by trade law.

*Source:* The authors, based on the literature references below.

<sup>[a]</sup> Agreement on Subsidies and Countervailing Measures, April 15, 1994, Marrakesh Agreement Establishing the World Trade Organization, “The Legal Texts: The Results Of The Uruguay Round Of Multilateral Trade Negotiations 275,” 1867 U.N.T.S. 14 (1999), annex 1A, art. 1, available at: [http://www.wto.org/english/docs\\_e/legal\\_e/24-scm.pdf](http://www.wto.org/english/docs_e/legal_e/24-scm.pdf) (last visited May 15, 2013).

<sup>[b]</sup> World Trade Organization, “The Legal Texts: The Results Of The Uruguay Round Of Multilateral Trade Negotiations 275,” *op. cit.*

<sup>[c]</sup> For instance, the Korean Export-Import Bank and its programs were addressed in WT/DS273/R, Korea - Measures Affecting Trade in Commercial Vessels, Panel report 7 March 2005, and Canadian EDC was discussed in WT/DS222/R, Canada — Aircraft Credits and Guarantees, Panel report 28 January 2002.

<sup>[d]</sup> It must be noted, however, that the WTO rules cover only a portion of trade-related subsidies. For example, the SCM Agreement distinguishes between prohibited, actionable and non-actionable subsidies (i.e., not specific, regional, research-related and others) and differentiates obligations of developed countries and emerging markets.

<sup>[e]</sup> OECD, *Investment Incentives and Disincentives and the International Investment Process*, op. cit. 1983, p. 12.

<sup>[f]</sup> See generally references provided in notes 11-14, 82.

It is important to distinguish HCMs from other measures that affect investment flows. HCMs must go beyond allowing outward FDI by simply liberalizing the OFDI regime (which is a necessary but not sufficient condition for a home country's firms to engage in OFDI), or even having a neutral policy once outward investment is allowed.<sup>41</sup> Rather, HCMs need to involve governmental actions that facilitate such investment (e.g., by providing information), support it (e.g., by providing political risk insurance or concluding bilateral investment and double taxation treaties) or even promote it (e.g., by providing certain financial or fiscal benefits) – or, more generally, help firms in one way or another to undertake FDI projects.<sup>42</sup>

An illustrative list of HCMs compiled for the purpose of the analysis in this chapter is presented in Box 2. Such measures are not new. Incentive schemes to facilitate private investment into developing countries were introduced in the 1950s and 1960s by the United States, the United

### **Box 2. Illustrative inventory of HCMs and OFDI institutions**

#### **Institutional framework**

1. Governmental departments/ministries, e.g.,
  - a. Ministries of foreign affairs
  - b. Ministries of commerce/trade/business
  - c. Ministries of industry/economy/competitiveness
2. Export credit agencies
  - d. Export-import banks
  - e. Trade/investment insurers
3. Development finance institutions
4. Investment/trade promotion agencies
  - f. Central offices on the national level
  - g. Foreign offices set up abroad to help investors located in host countries
5. Local trade/investment promotion agencies
6. Private organizations fulfilling governmental mandates

#### **Information and other support services**

1. Information support
  - a. Data on the economic and investment climate, legal environment, political situation in the

<sup>41</sup> For a brief discussion of the evolution of OFDI policies, see Persephone Economou and Karl P. Sauvant, “FDI trends in 2010-2011 and the challenge of investment policies for outward foreign direct investment,” in Karl P. Sauvant, ed., *Yearbook on International Investment Law and Policy 2011/2012* (New York: Oxford University Press, 2013), pp. 3-39.

<sup>42</sup> Given, as discussed earlier, that ODI may have ambiguous effects on home countries in certain areas (e.g., employment), governments are careful as to what language they use relating to the provision of HCMs – it may not be politically opportune to be seen to encourage firms to invest abroad.

- host countries, business opportunities in particular economic sectors, etc.
- b. Information and data on outward investment, e.g.,
  - i. Publications on the benefits of internationalization, legal and economic aspects of international expansion, etc.
  - ii. Statistics
- c. Information on existing HCMs and services available for outward investors
- 2. Investment missions
- 3. Match-making services
  - d. Organization of contacts with government officials and entrepreneurs in host countries
  - e. Maintaining business matchmaking databases
- 4. Educational services
  - f. Seminars, webinars and conferences on OFDI- related topics

#### Financial measures

- 1. Grants
  - a. Feasibility studies, market research and other pre-investment activities
  - b. Costs of setting up overseas offices
    - i. Rent
    - ii. Employee salaries
  - c. Training and human capital development
    - i. Training staff for employment in a foreign affiliate (e.g., immersion program, foreign language classes)
    - ii. International human resources strategy and related third-party consultancy fees
    - iii. Executive programs for managers
    - iv. Internships
    - v. Customized training programs
- 2. Loans
  - a. Concessional loans
  - b. Non-concessional loans
  - c. Structured financing options
  - d. Currency options
  - e. Syndication, public-private/public-public risk-sharing arrangements
  - f. Development financing
- 3. Financial guarantees
- 4. Equity participation
  - a. Direct equity financing
  - b. Quasi-equity financing
  - c. Development financing

#### Fiscal measures

- 1. Tax exemptions
  - a. Exemption from corporate income tax on certain incomes
    - i. Tax exemption of foreign spin-offs' income
    - ii. Tax exemption of start-up expenses of foreign operations
  - b. Tax deductions for qualifying expenditures
- 2. Corporate tax rate relief
  - a. Corporate tax rate relief for enterprises in particular sectors of economy
- 3. Tax deferral for qualifying income earned overseas
- 4. Tax credits for certain credits of expenditures
  - a. Interest expenses allocation
- 5. Allowances for qualifying activities

#### Investment insurance measures

- 1. Investment insurance

- a. Range of investment insurance products/coverages
- b. Expropriation
- c. War damage
- d. Political violence
- e. to convert local currency or transfer currency out of the host country
- f. Suspension of remittance
- g. Forced abandonment

Treaties

- 1. Bilateral investment treaties
- 2. Other international investment agreements
- 3. Double taxation treaties

*Source:* The authors, based on the discussion below.

Kingdom, Japan, Germany, and France. Most other developed countries introduced incentive measures for investment into developing countries, dating back as early as the 1970s.<sup>43</sup> An OECD publication from the early 1990s shows that every single member country of the OECD had at least a few of these measures in place at that time (Table 2).

**Table 2. Outward FDI promotion programs of OECD member countries, early 1990s**

Country	Information and technical assistance					Financing		Insurance
	Information	Matchmaking	Missions	Feasibility studies	Project development and start-up	Equity	Loans	Guarantees
Australia	X	X	X	X				
Austria	X					X	X	X
Belgium	X	X				X	X	X
Canada	X	X	X	X	X	X		
Denmark						X	X	X
Finland	X		X	X	X	X	X	X
France	X			X	X	X	X	
Germany	X	X	X	X	X	X	X	X
Italy	X	X	X	X	X	X	X	X
Japan	X	X	X	X	X	X	X	X
Netherlands	X	X	X	X		X	X	X
New Zealand	X	X		X		X		
Norway	X	X	X	X	X		X	X
Portugal	X	X	X				X	

<sup>43</sup> OECD, *Investing in Developing Countries* (Paris: OECD, 1983), p. 12.

Spain	X	X	X			X	X	X
Sweden	X	X		X		X	X	
Switzerland	X	X	X	X	X	X	X	X
United Kingdom						X	X	X
United States	X	X	X	X	X		X	X

Source: Based on OECD, *Promoting Foreign Direct Investment in Developing Countries* (Paris: OECD, 1993), pp. 14-17.

a/ May include some financial support.

The meaning of “investment” in the definition of HCMs follows the definition of FDI used in compiling balance of payments data, according to which a parent firm is one that holds an equity stake of at least 10% in a firm abroad.<sup>44</sup> As regards non-equity outward investment, only those firms with a long-term horizon when they establish a non-equity presence overseas and that have considerable involvement in the management of the project are included. To illustrate this, in the case of a build-operate-transfer/build-own-operate project, the time horizon must be sufficiently long, and the parent company must have a say in the management of the project for it to be considered as an investment that can potentially be supported by HCMs; contractual obligations, such as engineering, procurement and construction contracts or other international procurement contracts, are not considered because of the lack of management say in the project enterprise. For example, Korean companies that undertake overseas projects without establishing a foreign affiliate are eligible for overseas project credits by the Korea Eximbank for up to 80% of the funds required for the investment projects.<sup>45</sup> However, since Korean firms do not have a sufficiently long horizon or management power in the overseas project for it to qualify as an investment, HCMs that support such business transactions are not addressed here.

While a variety of HCMs exist, those addressed in this chapter fall into three main categories: information and other support services, financial measures and fiscal measures. Institutions that administer these services are also discussed in this chapter. These three categories of HCMs (to be defined further below), together with the provision of political risk insurance (not discussed in detail in this chapter), represent the most important direct measures used by governments to support OFDI today.

Although political risk insurance is not dealt with in this chapter in the interest of limiting its scope, a quick comment is in order. Political risk insurance, also referred to as investment insurance, is an instrument used by foreign investors to mitigate political risks associated with the unlawful interference by governments in the operations of foreign affiliates in host countries. Historically, governments of developed countries began to offer political risk insurance to help their firms mitigate risk in capital-importing developing countries, where risks were perceived to

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<sup>44</sup> IMF, *Balance of Payments and International Investment Position Manual* (Washington D.C.: IMF, 2011), sixth edition. The 10% share is indicative of a significant say in the management of the enterprise by the parent firm.

<sup>45</sup> The Korea Eximbank, Overseas Project Credit: terms and conditions, available at: [http://www.koreaexim.go.kr/en/banking/overseas/credit\\_02.jsp](http://www.koreaexim.go.kr/en/banking/overseas/credit_02.jsp) (last visited February 23, 2013).



be particularly high (Table 3). Indeed, such insurance has a long history in developed countries, having been offered to domestic firms for several decades. Germany,<sup>46</sup> for example, made political risk insurance available to its firms as early as 1960, by appointing the private entities PwC Deutsche Revision AG and Euler Hermes Kreditversicherungs AG to offer such insurance on its behalf.<sup>47</sup> More recently, as emerging markets have become significant outward investors, they too have begun establishing political risk insurance programs for their firms investing abroad. One such example is China's Sinosure, which was set up in 2001 and has been offering political risk insurance for investment for about a decade. Outward investors pay a premium for purchasing political risk insurance from public providers of such insurance (usually export credit agencies) in the home country. In what might be a unique feature of political risk insurance as an HCM, outward investors have the option of acquiring such insurance not only from a public provider at home (assuming that there is one), but also from the private market (e.g., a Lloyd's syndicate) or a multilateral insurance provider (e.g., the Multilateral Investment Guarantee Agency, assuming that the country is a member). This is important in the context of the discussion relating to political risk insurance as an HCM because foreign investors, in principle, are not restricted to what domestic state institutions have to offer – they are free to consider other options available in the private market.

**Table 3. Export credit agencies and other providers of political risk investment insurance in the 20 countries researched for this chapter, 2013**

Economy	Institution	Year of establishment of the ECA	Year the PRI service commenced
Belgium	ONDD	1921	1971
Canada	EDC	1944	1981
Chile	None	-	-
China	SINOSURE	2001	2001
France	COFACE <sup>a</sup>	1946	1946
Germany	PwC AG & Euler Hermes AG	1934 (PwC AG est.)/1917 (Euler Hermes AG est.)	1960 <sup>b</sup>
India	Export Credit Guarantee Corporation of India Ltd	1957	1978
Italy	SACE	1977	1979
Japan	NEXI	2001	1950 <sup>c</sup>
Kuwait	None <sup>d</sup>	-	-
Malaysia	EXIM Bank of Malaysia	1995	1977 <sup>e</sup>
Mexico	None <sup>f</sup>	-	-

<sup>46</sup> Deutsche Bundesbank, "Insurance of outward FDI in Germany," Information note prepared for the CGFS working group on FDI in the financial sector (2003), available at: <http://www.bis.org/publ/cgfs22buba2.pdf> (last visited May 22, 2013).

<sup>47</sup> Investment guarantees of the Federal Republic of Germany, information on guarantee applications: general terms and conditions (2004), available at: [http://www.agaportal.de/pdf/dia\\_ufk/formulare/e\\_dia\\_ab.pdf](http://www.agaportal.de/pdf/dia_ufk/formulare/e_dia_ab.pdf) (last visited May 25, 2013).

Republic of Korea	Korea Trade Insurance Corporation	1969	1969
Russia	Russian Agency for Export Credit and Investment Insurance (EXIAR)	2011	2013
Singapore	IE Singapore (administered), PRI provided by Singapore-registered brokers/insurers	1983	2012
Spain	CESCE	1970	1970
Switzerland	None <sup>g</sup>	-	-
Taiwan Province of China	EXIM Bank of Taiwan	1979	1979
United Kingdom	ECGD	1919	1972
United States	OPIC	1971	1948 <sup>h</sup>

Source: The authors, based on MIGA, *World Investment and Political Risk 2012* (Washington DC: MIGA, 2012), appendix 3; Berne Union, *Annual Publication 2013*, Section 5, *Directory of Berne Union and Prague Club Members*, available at <http://www.berneunion.org/news-publications/publications/>; OECD, *Promoting Private Enterprise in Developing Countries* (Paris: OECD, 1990); websites of export credit agencies and communications with export credit agencies and other political risk insurance providers.

<sup>a</sup> France's Investment Guarantee Scheme was initially offered by two institutions, BFCE and COFACE. BFCE was privatized in 1996 and now is part of Natixis (which also owns COFACE).

<sup>b</sup> Indicates the year when the companies were provided the joint mandate to manage investment guarantee scheme on behalf the German Government.

<sup>c</sup> Japan's government established and managed directly trade and investment insurance since 1950, as a part of its export promotion program.

<sup>d</sup> For more on the Arab Investment and Export Credit Guarantee Corporation, see the section on institutions.

<sup>e</sup> Before the establishment of the EXIM Bank of Malaysia, political risk insurance was offered by the Malaysia Export Credit Insurance Berhad (MECIB) since 1977.

<sup>f</sup> Mexico's Bancomext offers guarantees for export-related activities only.

<sup>g</sup> The Swiss political risk provider for exporters is SERV. For Swiss investors, guarantees were available through the Swiss Investment Risk Guarantee Agency (IRG), however the latter institution does not seem to be active now.

<sup>h</sup> In the United States, political risk insurance against currency inconvertibility risk was introduced in 1948, as part of the Marshall Plan for European economic recovery after World War II.

Also not discussed in this chapter are BITs and double taxation treaties (DTTs). Their purpose is to facilitate, if not to encourage, OFDI by, respectively, protecting such investment and facilitating the operations of MNEs, and avoiding double taxation.<sup>48</sup> In that sense, they also constitute HCMs. Both sets of instruments have expanded rapidly over the past two decades, with the number of BITs and other international investment agreements having reached 3,196 in 2012 and the number of DTTs totaling 3,091 treaties as of end-2011.<sup>49</sup> However, measures

<sup>48</sup> However, the results of empirical research of the effect of BITs and DTTs on FDI flows are ambiguous. For a collection of such studies, see Karl P. Sauvant and Lisa Sachs, eds., *The Effect of Treaties on Foreign Direct Investment: Bilateral Investment Treaties, Double Taxation Treaties, and Investment Flows* (New York: Oxford University Press, 2009).

<sup>49</sup> UNCTAD, *World Investment Report 2013*, *op. cit.*, p. 101, and UNCTAD, *World Investment Report 2012*, *op. cit.*, p. 95, respectively.

explicitly promoting OFDI that may be included in these treaties – or for that matter, other agreements – are not addressed in this chapter. As an example referring to the latter, the Cotonou agreement provides, in Chapter 7 of Title II (financial cooperation measures) that countries from Africa, the Caribbean and the Pacific (ACP states) and the European Community and its member states should put in place to promote investment and “encourage the EU private sector to invest and to provide specific assistance to its counterparts in the ACP countries under mutual business cooperation and partnerships,” and “disseminate information on investment opportunities and business operating conditions in the ACP States.”<sup>50</sup> Other articles call for financial support (Art. 76), investment guarantees (Art. 77) and investment protection (Art. 78). The Cotonou Agreement also established a joint European Union-ACP institution, the Centre for the Development of Enterprise, whose objectives include assistance for investment promotion activities, facilitation of business cooperation between European Union and ACP enterprises, and dissemination of information about business opportunities for European Union companies in ACP countries.<sup>51</sup>

Various other miscellaneous direct measures may be relevant, but these are not discussed because of lack of systematic evidence. Such measures include political efforts by home countries to influence decisions by destination countries (e.g., in the context of privatizations) and business people accompanying diplomatic missions to destination countries.

Indirect measures may also support OFDI, but these are generally not covered in this chapter. Such measures include government policies or measures that may facilitate OFDI, but are not targeted specifically to provide outright support for firms’ investments abroad. This is a very broad category of measures, ranging from pursuing a policy of low interest rates at home, which facilitates OFDI by reducing the cost of borrowing, to exempting parent firms from anti-trust enforcement, creating the possibility of above-normal profits that can be used to finance outward investment.

Trade-related measures constitute another group of indirect measures. In particular, measures supporting exports may also promote OFDI, since home country firms may benefit from the knowledge of conditions abroad and establish contacts there, which in turn can facilitate the transition from exporting to setting up foreign affiliates. Similarly, policy measures that deal with market access, while not addressing investment directly, may nonetheless encourage domestic firms to invest abroad. An example would be preferential market access measures such as the African Growth and Opportunity Act<sup>52</sup> and the Everything-but-Arms initiative,<sup>53</sup> both of

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<sup>50</sup> The Partnership Agreement between the members of the African, Caribbean and Pacific Group of States of the one part, and the European Community and its Member States of the other part, signed in Cotonou on June 23, 2000, revised in Luxembourg on 25 June 2005, revised in Ouagadougou on 22 June 2010 (hereinafter The Cotonou Agreement), art. 75, chapter 7, Title II, available at: [http://ec.europa.eu/europeaid/where/acp/overview/documents/devco-cotonou-consol-europe-aid-2012\\_en.pdf](http://ec.europa.eu/europeaid/where/acp/overview/documents/devco-cotonou-consol-europe-aid-2012_en.pdf).

<sup>51</sup> The Cotonou Agreement, Annex III, art. 2, available at: [http://ec.europa.eu/europeaid/where/acp/overview/documents/devco-cotonou-consol-europe-aid-2012\\_en.pdf](http://ec.europa.eu/europeaid/where/acp/overview/documents/devco-cotonou-consol-europe-aid-2012_en.pdf).

<sup>52</sup> African Growth and Opportunity Act, signed into law on May 18, 2000 as Title 1 of The Trade and Development Act of 2000. See AGOA website <http://www.agoa.gov/> (last visited March 27, 2013).

which also encourage greater OFDI from third countries through providing preferential access to the United States and European Union markets, respectively. Rules-of-origin regulations can have the same effect, as do some special laws such as the United States' trade provision<sup>54</sup> that gave rise to the *maquiladora* industry in Mexico. Other measures are concerned with technology transfer, focusing on improving host countries' (usually emerging markets) absorptive capabilities in order to maximize their ability to utilize commercial technologies.<sup>55</sup> Since the technological capacity of a host country is an important determinant of FDI, this type of measure makes the host country more interesting as a potential destination for investment.

A home country's private sector itself may also facilitate investment in potential destination countries, for example, by seeking to improve formal and informal business ties and establishing bilateral chambers of commerce or business councils. The capacity of the private sector to so facilitate OFDI is typically greater in developed countries than in emerging markets. While private sector measures may contribute to the ability and willingness of home country firms to engage in OFDI, they fall outside this chapter's definition of HCMs, unless these measures are administered by the private sector on behalf of the government. An example here is the Government of Canada's Global Opportunities for Associations initiative that provides funding to (private sector) business associations in Canada "whose objective is to promote sector-specific international business development for its members and industry at large,"<sup>56</sup> thus supporting Canadian companies to aid them take advantage of global business opportunities, including through OFDI.

Finally, official development assistance may also be used to support OFDI. For example, financing infrastructure projects in potential FDI destination countries may make those countries more attractive for OFDI. But such support can also be tied directly to OFDI projects, e.g., when donor governments provide finance specifically tied to OFDI projects undertaken by their firms.<sup>57</sup>

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<sup>53</sup> The EU Everything but Arms initiative provides duty-free, quota-free access for products from the least developed countries. See <http://ec.europa.eu/trade/wider-agenda/development/generalised-system-of-preferences/everything-but-arms/> (last visited March 27, 2013).

<sup>54</sup> Certain United States tariff provisions provide benefits that extend to *maquiladora* products destined for the United States. For example, under provision 9802.0030 of the Harmonized Tariff Schedule of the United States, products assembled in foreign countries from United States-made components are subject to duties only on the value added in the foreign country. United States General Accounting Office, "U.S.-Mexico trade: The Maquiladora Industry and U.S. Employment," GAO/GGD-93-129 (July 1993).

<sup>55</sup> UNCTAD, *Home Country Measures*, Sales No: E.01.II.D.19 (New York and Geneva: UNCTAD, 2001), p. 28.

<sup>56</sup> The Canadian Trade Commissioner Service, "Global Opportunities for Associations," available at: <http://www.tradecommissioner.gc.ca> (last visited on November 13, 2012).

<sup>57</sup> In recent times, some of the infrastructure-for-natural resources projects supported by China may fall into this category, e.g., the Sicomines project in the Democratic Republic of Congo; see, Johanna Jansson, Christopher Burke and Wenran Jiang, *Chinese Practices at Extractive Industries of Gabon and the DRC: Perceptions of Transparency* (Centre for Chinese Studies, University of Stellenbosch, August 2009), p. 33, available at: [http://www.ccs.org.za/wp-content/uploads/2009/11/Chinese\\_Companies\\_in\\_the\\_Extractive\\_Industries\\_of\\_Gabon\\_and\\_the\\_DRC.\\_CCS\\_report\\_August\\_2009.pdf](http://www.ccs.org.za/wp-content/uploads/2009/11/Chinese_Companies_in_the_Extractive_Industries_of_Gabon_and_the_DRC._CCS_report_August_2009.pdf) (last visited April 22, 2013). But other donor countries have done the same, at least in the past. Another example is a financing package given to the Government of Angola in 2004 by China's Export-Import Bank which is said to have led Angola to reject Royal Dutch Shell's plan to sell its share in Block 18 to an Indian

### c. Criteria for eligibility

Eligibility of investors for OFDI support lies at the core of HCMs, particularly as home countries tend to apply a set of criteria when imparting measures to foreign investors. The most important criteria pertain to the nationality of the foreign investor, the sector of investment in the home or host country, the ownership of the firm, the size of the firm, and the host country destination.

*Nationality* is an important consideration, especially since promoting outward investment is often meant to produce a positive effect for the home economy. Although it is sometimes difficult to ascertain what constitutes an “indigenous” firm, certain countries, like the United States, have specific definitions based on equity involvement and ultimate beneficial ownership.<sup>58</sup> While other countries may not provide precise specifications to determine what constitutes an indigenous firm, HCMs might not be extended to firms whose outward investment activities do not benefit the home country, as they are typically offered on a discretionary basis. In fact, countries like Spain adopt a more functional approach, offering certain HCMs not based on considerations of nationality, but based on considerations of whether the purported investment would further some sort of “Spanish interest.”

The *sector* of an investment can also be an important criterion for HCM support. Depending on their economic priorities, home countries may opt to support OFDI in such specific sectors as natural resources that are scarce at home (e.g., Republic of Korea,<sup>59</sup> China<sup>60</sup>), sectors where OFDI will increase the competitiveness of home country firms (e.g., Malaysia<sup>61</sup>) or sectors that involve future-oriented industries, such as renewable energy (e.g., Japan<sup>62</sup>). On the other hand, a

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firm; instead, its share was sold to Sinopec. See Xiaofei Li, “China's Outward Foreign Investment from a Political Perspective,” PhD Dissertation, The Catholic University of America (2008).

<sup>58</sup> See the discussion on the United States Overseas Private Investment Corporation below.

<sup>59</sup> The Korea Eximbank provides Natural Resources Development Credits for Korean and foreign companies that invest overseas for the development of natural resources; see <http://www.koreaexim.go.kr/en/banking/Natural.jsp> (last visited April 17, 2013).

<sup>60</sup> The Chinese National Development and Reform Commission and the Eximbank of China provide special loans for “overseas resource development projects which can make up for the relative insufficiency of domestic Resources;” see “Notice of the National Development and Reform Commission, the Export-Import Bank of China on Giving Credit Support to the Key Overseas Investment Projects Encouraged by the State, No. 2345 [2004] of the Foreign Investment Dept. of the NDRC promulgated on and shall come into force as of October 27, 2004,” available at:

[http://209.200.107.14/english/law2\\_disp.asp?sublawcode=SUB4885447119161114&lawcode=LAW4861112671113915&country=China](http://209.200.107.14/english/law2_disp.asp?sublawcode=SUB4885447119161114&lawcode=LAW4861112671113915&country=China) (last visited April 21, 2013).

<sup>61</sup> The Malaysia Investment Development Authority administers incentives for Malaysian companies that acquire foreign high technology companies in order to establish manufacturing facility in Malaysia or utilize acquired technology in existing operations in Malaysia; see “Guidelines for Incentive for acquiring a foreign company for high technology,” available at: <http://www.mida.gov.my/env3/uploads/Forms/Services/03082012/GD-AFC-02.pdf> (last visited April 17, 2013).

<sup>62</sup> The Japanese Bank for International Cooperation supports overseas projects of Japanese firms especially in area of power generation by developing renewable energy sources; see JBIC, “Equity participation,” available at: <http://www.jbic.go.jp/en/finance/capital/index.html> (last visited April 17, 2013).

home country may prohibit HCMs from being available to OFDI in select sectors (e.g., defense-related industries in Spain<sup>63</sup>).

HCMs may be available to select types of firms on the basis of *ownership*. A particularly important issue here is the question of support for state-owned enterprises (SOEs). SOEs are important actors in the world FDI market: in 2010, of the top 100 largest non-financial MNEs world-wide and the 100 largest headquartered in emerging markets (determined on the basis of the size of their foreign assets), 49 were SOEs.<sup>64</sup> Of these 49, 20 were headquartered in developed countries, controlling US\$ 1.4 trillion in foreign assets, while 29 were headquartered in emerging markets, controlling US\$ 0.4 trillion.<sup>65</sup> In addition to benefitting from HCMs, SOEs may benefit from measures supporting their activities at home, including various subsidies, concessionary financing, guarantees, preferential access to information, and preferential regulatory treatment (e.g., an exemption from bankruptcy rules).<sup>66</sup> Such measures alone may bestow certain advantages on SOEs when investing overseas.<sup>67</sup> While measures affecting the position of SOEs at home fall outside the scope of this study, it is important to query whether and how HCMs are used specifically to promote OFDI by SOEs. One possibility is that HCMs with wide margins of discretion are provided to SOEs under more favorable conditions than to all other enterprises: premiums could be lower, tenures longer, requirements laxer. Another possibility is that home countries may afford their SOEs special treatment through measures unavailable to other enterprises. These two types of advantages (among other things) raise concerns that SOEs can, first, distort international competition in the world FDI market by dipping into their government's budget to facilitate their overseas expansion, and, second, operate as an instrument of the national government to advance not only economic goals, but also political interests in a manner that potentially threatens the national security of other countries.<sup>68</sup>

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<sup>63</sup> Spain's CODIDES supports investment in any sector except for real estate or defense-related projects; see COFIDES, "Eligible sectors," available at <http://www.cofides.es/3sectores.html> (last visited April 17, 2013).

<sup>64</sup> See Karl P. Sauvnt and Jonathan Strauss, "State-controlled entities control nearly US\$ 2 trillion in foreign assets," *Columbia FDI Perspectives*, no. 64 (April 2, 2012). "SOEs" are defined as enterprises in which the government has a controlling interest, with "control" defined as a stake of 10% or more of voting power (*ibid.*, p. 2).

<sup>65</sup> Sauvnt and Strauss, "State-controlled entities control nearly US\$ 2 trillion in foreign assets," 2012, *op. cit.*, p. 1.

<sup>66</sup> Antonio Capobianco and Hans Christiansen, "Competitive neutrality and state-owned enterprises: Challenges and policy options," OECD Corporate Governance Working Papers, No. 1 (2011), pp. 5-7, available at: <http://dx.doi.org/10.1787/5kg9xfghg6-en>.

<sup>67</sup> See e.g., OECD, "National practices concerning competitive neutrality," Working Party on State Ownership and Privatisation Practices, DAF/CA/SOPP(2011)9/REV2 (26-27 March 2012); Capobianco and Christiansen, "Competitive neutrality and state-owned enterprises: Challenges and policy options," 2011, *op. cit.*, pp. 30-31.

<sup>68</sup> For a discussion of some of these concerns see Nilgün Gökür, "Are resurging state-owned enterprises impeding competition overseas?," *Columbia FDI Perspectives*, No. 36 (April 25, 2011), available at: <http://www.vcc.columbia.edu/content/are-resurging-state-owned-enterprises-impeding-competition-overseas> (last visited April 22, 2013); Ilan Alon and Aleh Cherp, "Is China's outward investment in oil a global security concern?," *Columbia FDI Perspectives*, No. 81 (October 22, 2012), available at: <http://www.vcc.columbia.edu/content/china-s-outward-investment-oil-global-security-concern> (last visited April 22, 2013); and Karl P. Sauvnt, Lisa Sachs and Wouter P. F. Schmit Jongbloed, eds., *Sovereign Investment: Concerns and Policy Reactions* (New York: Oxford University Press, 2012).

HCMs tailored to enterprises depending on their *size*, especially for small and medium-sized enterprises (SMEs),<sup>69</sup> are important for several reasons. Large-scale investment projects, such as construction, manufacturing, natural resources exploration, and infrastructure building, require large amounts of capital, which are typically more readily available to large firms rather than SMEs. To support large OFDI projects, some home countries have introduced separate financing lines for large companies, co-financing large projects with private institutions, or offer re-insurance and co-insurance services. Another vital aspect of investment promotion policy focuses on SMEs, for two principal reasons. First, SMEs are important for economic development: in virtually all countries, including emerging markets, SMEs constitute the bulk of the private sector.<sup>70</sup> Second, when investing abroad, SMEs face more problems than large firms with respect to adjusting to cultural differences, access to information and promotional services, and the availability of managerial resources, among other things.<sup>71</sup> Since SMEs everywhere typically have more limited access to financial resources,<sup>72</sup> HCMs have an important role to play in providing additional support for SMEs wishing to engage in OFDI and in overcoming disadvantages related to their size.<sup>73</sup> These measures may be more advantageous than those available to other firms. Countries that explicitly provide additional advantages to SMEs seeking to engage in FDI include the United States, which has specially designed programs to promote the internationalization of SMEs through trade and investment;<sup>74</sup> the Republic of Korea, which offers financial support, capacity building and on-site facilitation programs to increase the global presence of its SMEs;<sup>75</sup> and China, which in October 2000 introduced a regulation seeking to promote OFDI by Chinese SMEs.<sup>76</sup>

The *destination* of investment is another criterion used to determine eligibility. HCMs may only be available for investments in select destination countries (e.g., Taiwan Province of China's

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<sup>69</sup> Different definitions of SMEs are used across countries. For example, the European Union defines SMEs as companies with fewer than 250 employees (European Commission, Enterprise and Industry website - <http://ec.europa.eu/enterprise/policies/sme/facts-figures-analysis/sme-definition/> - accessed on March 28, 2013); the United States OPIC defines SMEs as having annual revenues of less than \$35 million (OPIC Small Business Center, <http://www.opic.gov/doing-business-us/small-business-center>, accessed February 23, 2013).

<sup>70</sup> OECD, *Promoting Private Investment for Development: The Role of ODA* (Paris: OECD, 2006), p. 18, available at: [http://www.oecd-ilibrary.org/development/promoting-private-investment-for-development\\_9789264018433-en](http://www.oecd-ilibrary.org/development/promoting-private-investment-for-development_9789264018433-en) (last visited April 22, 2013).

<sup>71</sup> UNCTAD, *Handbook on foreign direct investment by small and medium-sized enterprises: Lessons from Asia*, Sales no. E.98.II.D.4 (New York: United Nations 1998), pp. 44-51.

<sup>72</sup> Spring Singapore, *Study on SME Internationalisation: Best Practices Across Selected APEC Economies*, June 2011, p.4.

<sup>73</sup> Heinz Hollenstein, "Determinants of International Activities: Are SMEs Different?," 24(5) *Small Business Economics* 431 (2005); Peter J. Buckley, "Foreign direct investment by small and medium sized enterprises: The theoretical background," 1(2) *Small Business Economics* 89 (1989).

<sup>74</sup> See OPIC's Small Business Center, available at: <http://www.opic.gov/doing-business-us/small-business-center>, (last visited February 23, 2013).

<sup>75</sup> Seong-Bong Lee, "Korea's New Trade and Outward FDI Policies: Facilitating the Presence of Korean SMEs in Regional and Global Markets," presentation, Korea Institute for International Economic Policy, (July 2007), available at: [http://www.unescap.org/tid/artnet/mtg/tipc\\_s5lee.pdf](http://www.unescap.org/tid/artnet/mtg/tipc_s5lee.pdf) (last visited June 5, 2013).

<sup>76</sup> Yadong Luo, Qiuzhi Xue, Binjie Han, "How emerging market governments promote outward FDI: Experience from China," 45(1) *Journal of World Business* 68 (2010).

HCMs only apply to firms investing in countries with which it has diplomatic relations<sup>77</sup>), specific groups of countries (e.g., emerging markets<sup>78</sup>) or even in specific regions within a country (e.g., Northern Ireland<sup>79</sup>).

These eligibility criteria will be considered in the context of the various categories of HCMs discussed in the remainder of this chapter.

#### d. Conditionality

In a number of countries, governments may impose conditions on firms to qualify for OFDI support.<sup>80</sup> One set of conditions relates to the effect of projects on *home* countries, as their governments want to ensure that OFDI projects do not have a detrimental economic effect on the home economy, but rather, have a neutral effect, or even a positive effect on their economies. More specifically, otherwise eligible investors may not be allowed to avail themselves of HCMs if, for example, an investment has negative effects in the home country in terms of jobs or the balance of payments.<sup>81</sup> Other conditions may include having to export the output of an OFDI project back to the home country, as in the case of natural resource extraction,<sup>82</sup> as well as the repatriation of profits.<sup>83</sup> Another set of conditions relates to the *host* country and relates to projects having positive development effects in the host country, for example in terms of job

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<sup>77</sup> “Regulations for Encouraging and Financing Business Entrepreneurs to Invest in Allied Countries,” amended and promulgated by the Ministry of Foreign Affairs on May 10, 2006, available at: <http://www.mofa.gov.tw/UploadFiles/Upload/e4216d44-9cb5-4c2b-bd95-5dc807c4e142.PDF> (last visited on March 28, 2013).

<sup>78</sup> See e.g., OPIC, “Where We Operate,” available at: <http://www.opic.gov/doing-business-us/OPIC-policies/where-we-operate> (last visited on March 28, 2013).

<sup>79</sup> OPIC, “Where We Operate,” *op. cit.*

<sup>80</sup> Conditionality requirements may be quite diverse and specific. For example, the Malaysia Kitchen Program supports Malaysian restaurants overseas through financing on the condition that they serve Malaysian food, available at <http://www.matrade.gov.my/en/malaysian-exporters/services-for-exporters/export-promotion/malaysia-kitchen-programme> (last visited March 28, 2013).

<sup>81</sup> In the case of the United States, for example, OPIC must ensure that its support measures for OFDI have no negative impact on the United States economy in terms of employment and the balance of payments; see OPIC website <http://www.opic.gov/doing-business-us/OPIC-policies/economic-analysis>, last visited February 23, 2013.

<sup>82</sup> For instance, China’s guiding policy for outward investment in 2006 distinguished encouraged, allowed and prohibited outward investment projects. Encouraged projects include, among others, those that “can acquire resources or raw materials for which there is a domestic shortage and an urgent need for the national economic development”; see Outward Investment Sector Direction Policy, adopted by National Development and Reform Commission, Ministry of Commerce, Ministry of Foreign Affairs, Ministry of Finance, General Administration of Customs, State Administration of Taxation, State Administration of Foreign Exchange, July 5, 2006, available in Nathalie Bernasconi-Osterwalder, Lise Johnson and Jianping Zhang, eds., *Chinese Outward Investment: An emerging policy framework* (IISD, 2012), available at: [http://www.iisd.org/pdf/2012/chinese\\_outward\\_investment.pdf](http://www.iisd.org/pdf/2012/chinese_outward_investment.pdf) (last visited April 26, 2013).

<sup>83</sup> For instance, a home country government may introduce a fiscal incentive in form of tax holidays for repatriated foreign earned profits. About U.S. initiatives in this area, see Laura D’Andrea Tyson, Kenneth Serwin and Eric J. Drabkin, *The Benefits for the U. S. Economy of a Temporary Tax Reduction on the Repatriation of Foreign Subsidiary Earnings*, Study prepared for the for the New America Foundation (2011), available at: [http://www.brg-expert.com/media/publication/24\\_Repatriation%20Study.pdf](http://www.brg-expert.com/media/publication/24_Repatriation%20Study.pdf) (last visited April 26, 2013).



creation, infrastructure improvements and technology and knowledge transfer.<sup>84</sup> To qualify, firms may also need to provide environmental and social impact assessments, including proof that workers' rights, human rights and health and safety requirements are being respected.<sup>85</sup>

### e. Approach

This chapter draws on research on HCMs currently in place in the top ten developed countries and in the top ten emerging markets (Table 4) in terms of FDI outflows; together, they accounted for an average of 75% of the world's OFDI flows during 2007-2011.<sup>86</sup> (The list of economies excludes financial centers and intermediate jurisdictions, such as Hong Kong SAR China, as well as tax havens, such as the British Virgin Islands and the Cayman Islands, since these economies often play the role of simply rerouting FDI funds to other destinations.) For each of the included economies, research was undertaken to identify HCMs, the government agencies responsible for implementing such measures, the legal act establishing each measure, eligibility, the conditions under which they are available, and the reason(s) or objective(s) for having each measure in place. While a considerable effort was devoted to finding all HCMs for each of these economies, it is unlikely that all measures currently in place (including especially at the sub-national level) have been successfully captured in the research.<sup>87</sup> Moreover, information is more easily available for some countries than for others, which is reflected below in the uneven use of country examples. Box 2 provides an overview of the HCMs that were identified during the research.

**Table 4. Annual average OFDI flows, 2007-2011  
(US\$ billions)**

Developed economies			Emerging markets		
1	United States	334.0	1	China	53.0
2	United Kingdom	124.9	2	Russian Federation	53.0
3	France	118.7	3	Singapore	21.6
4	Germany	96.5	4	Republic of Korea	20.2

<sup>84</sup> United States' HCMs, through OPIC, in the areas of finance and insurance are given to projects that have a positive development impact on the host country, as assessed by OPIC; see OPIC Policies- <http://www.opic.gov/doing-business-us/OPIC-policies> (last visited on March 28, 2013).

<sup>85</sup> Support measures in the areas of finance and insurance are awarded by the United States through OPIC on the basis of satisfactory environmental and social impact assessments; see OPIC Policies- <http://www.opic.gov/doing-business-us/OPIC-policies> (accessed on March 28, 2013). For other examples of home countries' environmental regulations, see UNCTAD/CBS Project, *Cross border environmental management in transnational corporations*, Occasional Paper No. 8 (November 1999), available at: <http://openarchive.cbs.dk/bitstream/handle/10398/7010/occasional%20paper%205.pdf?sequence=1> (last visited April 24, 2013).

<sup>86</sup> UNCTAD, *World Investment Report 2012*, op. cit., Annex Table I.1.

<sup>87</sup> For an in-depth study of HCMs offered by Canada, India and the Republic of Korea, see Maheshwari Sundaresh, "Home Country Measures for Outward Foreign Direct Investment: Lessons for India from the Republic of Korea and Canada" (New York: Columbia University, 2012), mimeo.

5	Japan	89.4	5	India	16.5
6	Belgium	87.4	6	Malaysia	12.5
7	Spain	60.1	7	Taiwan Province of China	10.3
8	Canada	53.5	8	Chile	8.5
9	Italy	52.9	9	Kuwait	8.2
10	Switzerland	51.7	10	Mexico	7.8

Source: UNCTAD, *World Investment Report 2012, op. cit.*, Annex Table I.1.

## 2. Institutional framework and information and other support services

### a. Introduction

While OFDI and HCMs are gaining some attention,<sup>88</sup> the institutional underpinning of OFDI has received very little coverage to date.<sup>89</sup> What studies there are on this subject are typically over a decade old. Moreover, any attention that has been paid to OFDI and HCMs mainly concerns developed countries. This section aims at providing an overall picture of the institutional framework pertaining to OFDI in the developed countries and emerging markets covered in this chapter, as well as an overview of HCMs in the form of information and other support services that many of them provide.

The OFDI institutions included in this section of the present chapter are those whose objectives or functions involve the facilitation, support or promotion of outbound investment by domestic enterprises. These institutions were selected according to the following criteria. First, the institution had to be part of a national government, controlled or directed by the government or accountable for its activity to the home country's government.<sup>90</sup> According to this criterion, private market participants, such as consultancy firms, business organizations, chambers of commerce, associations, and non-governmental bilateral business councils are not included in this study. The only exception allowing for a private institution to be included in the list of OFDI institutions is when it performs a function on behalf of the government. Second, the institution

<sup>88</sup> Most coverage has been by UNCTAD; see UNCTAD, *World Investment Report 1991: The Triad in Foreign Direct Investment*, Sales No: E.91.II.A.12 (New York: United Nations, 1991), pp. 91-92; UNCTAD, *World Investment Report 1995: Transnational Corporations and Competitiveness*, op. cit., pp. 307-351; UNCTAD, *World Investment Report 2003: FDI Policies for Development: National and International Perspectives*, Sales No: E.03.II.D.8 (Geneva: United Nations, 2003), pp. 155-163; UNCTAD, *International Investment Agreements: Key Issues*, Volume III, Sales No.E.05.II.D.6 (New York: United Nations, 2005), pp. 1-28; UNCTAD, *Home Country Measures*, op. cit.; UNCTAD, "Home Country Measures: Note by the UNCTAD Secretariat," TD/B/COM.2/EM.8/2 (September 14, 2000).

<sup>89</sup> But see J. Belot and Dale R. Weigel, "Programs in industrial countries to promote foreign direct investment in developing countries", Occasional paper 3, Foreign Investment Advisory Service (Washington, D.C.: The World Bank, 1992); UNCTAD, *Handbook on outward investment agencies and institutions*, ASIT Advisory Studies, No.14 (Geneva: UNCTAD, 1999); OECD, *Promoting Private Enterprise in Developing Countries* (Paris: OECD, 1990) and OECD, *Promoting Foreign Direct Investment in Developing Countries*, op. cit.

<sup>90</sup> The present study does not specifically address institutions that administer fiscal incentives.

had to provide OFDI support mostly to firms that are registered or incorporated in the home country, or are based overseas but are owned or controlled by firms registered or incorporated in the home country. For instance, to receive financing from IE Singapore under the Internationalization Finance Scheme, eligible companies “must be Singapore-based, registered with Accounting and Corporate Regulatory Authority (ACRA) and have at least 3 strategic business functions in Singapore;”<sup>91</sup> in this case, affiliates of Singapore-based companies incorporated abroad are not eligible for support. On the other hand, in addition to traditional overseas investment loans for Korean companies, the Korea Eximbank offers overseas business credits for foreign companies in which Korean companies hold an equity share.<sup>92</sup> Finally, the institution must specifically acknowledge the provision of support for OFDI. In other words, unless there was a specific mandate to support OFDI, government-controlled banks and other financial institutions that provide loans and guarantees for business purposes were not included in the list of institutions under consideration.

All information about institutions, their activities and policies was taken from publicly available sources, such as websites, reports of international organizations and academic publications.

## **b. Institutions**

Applying the criteria just mentioned yielded more than 50<sup>93</sup> national institutions involved in OFDI in 19 of the 20 economies covered in this chapter (see Box 3 for country examples)<sup>94</sup> (No national institution that would meet the above criteria was found in Kuwait).<sup>95</sup> These institutions can be divided into five broad categories: investment promotion agencies (IPAs) and trade promotion agencies, export credit agencies (ECAs), development finance institutions (DFIs), ministries and agencies representing the executive branch of government, and special purpose institutions. It is important to note, however, that the boundaries between these categories are not

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<sup>91</sup> IE Singapore, “Internationalization Finance Scheme,” available at: [http://www.iesingapore.gov.sg/wps/wcm/connect/88fbc0004ad50175b9e2bb6ba6b73dba/IFS-PDF\\_file\\_attached\\_to\\_the\\_IE\\_website20120404.pdf?MOD=AJPERES](http://www.iesingapore.gov.sg/wps/wcm/connect/88fbc0004ad50175b9e2bb6ba6b73dba/IFS-PDF_file_attached_to_the_IE_website20120404.pdf?MOD=AJPERES) (last visited April 14, 2013).

<sup>92</sup> Korea Eximbank, “Overseas Business Credit,” available at: [http://www.koreaexim.go.kr/en/banking/overseas/credit\\_03.jsp](http://www.koreaexim.go.kr/en/banking/overseas/credit_03.jsp) (last visited April 14, 2013).

<sup>93</sup> Complex organizational structures, and the fact that some institutions are subordinated under others, complicates the calculation of the exact number of independent institutions covered. For instance, Spain’s Official Credit Institute (which provides financial assistance to Spanish enterprises investing abroad) is attached to the Ministry of Economic Affairs and Competitiveness, as well as to ICEX (a public company that provides informational services).

<sup>94</sup> Additional research might point to other agencies. In addition, in a number of countries, sub-national agencies also have responsibilities for OFDI; in the case of China, for example, all sub-national investment promotion agencies are also supporting OFDI.

<sup>95</sup> However, outward investors from Kuwait have access to political risk insurance offered by such regional providers as the Arab Investment and Export Credit Guarantee Corporation and the Kuwait Fund on Arab Economic Development (see the official website of the Fund: <http://www.kuwait-fund.org>, last visited April 9, 2013), which provides financial assistance to Arab and other emerging markets, but in its projects gives preferences to Kuwaiti companies and foreign companies associated with them.

always clear-cut.<sup>96</sup> The classification of institutions, therefore, for the purpose of this chapter, follows their self-classification or, in case of ambiguity, is based on their major field of activity. The membership of a particular institution in a relevant international association, such as the Association of European Development Finance Institutions in the case of DFIs, and the World Association of Investment Promotion Agencies in the case of IPAs, was also taken into account in the classification process.

### **Box 3. The institutional framework for OFDI in Canada, India, the Republic of Korea, and Spain**

#### Canada

Since the closure of OFDI promotion services provided in the past by the Canadian International Development Agency, Canada's HCMs have been implemented by the Canadian Trade Commissioner Service in the Department of Foreign Affairs and Trade. Export Development Canada offers political risk insurance for investment that generates economic benefits for Canada and an export-guarantee scheme under which it guarantees loans extended by financial institutions for OFDI by Canadian companies.

A number of agencies on the local level are also involved in investment promotion. For instance, the Department of Innovation, Business and Rural Development of Newfoundland and Labrador operates the Ireland Business Partnership program, which supports local businesses with information on the Irish economy and coordinates meetings with strategic Irish businesses, agencies and organizations.

#### India

The Export Import Bank of India, a government controlled bank, is charged with providing financial support for Indian investors. It also offers reports on overseas investment opportunities and provides consultancy services; the knowledge-building centers also provide training on international investment to Indian SMEs. The Export Credit Guarantee Corporation of India, also a government-controlled entity, offers political risk insurance for Indian companies investing abroad, preferably into countries with which India has signed BITs.

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<sup>96</sup> For example, OPIC is a DFI that, besides financial HCMs, also provides political risk insurance for investment. Some institutions initially started in one area (e.g., export promotion, as in the case of ProChile) and subsequently moved into additional areas, including support for OFDI, which complicates their classification into a single category.

## Republic of Korea

Major financial incentives and guarantees are offered through the Export-Import Bank of Korea (the Korea Exim Bank). The Korea Resources Corporation (Kores) was established in 1982 with the purpose of facilitating overseas mineral resource development by offering financing, technical and advisory assistance. The Korea Trade Insurance Corporation (K-Sure) offers insurance services to Korean investors, domestic financial institutions and foreign enterprises when they develop overseas resources for the benefit of the home country. The Korea Trade Investment Promotion Agency (KOTRA) and the Small and Medium Business Corporation (SMBC) offer information and consulting services, matchmaking, training, and technical assistance -- the last with an emphasis on SME Korean enterprises. The Korea Exim Bank, Kores, K-Sure, and KOTRA are all state-owned entities. SMBC is a non-profit, government-funded entity.

## Spain

The Instituto Español de Comercio Exterior (ICEX), a public company under the Ministry of Commerce and Ministry of Economy and Competitiveness, offers direct funding and subsidies to foster Spanish SME participation in foreign projects. It also provides information on foreign markets, legislation and taxation; funding for investment; match-making services; tailored advisory services; training; and investment missions. The ICEX website provides detailed information that allows the prior estimation of establishment costs and calculating the prices of ICEX services, which depend on the size of the enterprise.

Financial services for the purpose of supporting OFDI are also offered by the Ministry of Industry, Tourism and Trade, the Compañía Española de Financiación del Desarrollo (COFIDES - a development finance institution that facilitates the internationalization of Spanish enterprises) and the Instituto de Crédito Oficial (ICO - a state-owned bank attached to Ministry of Economic Affairs and Competitiveness). The Ministry of Industry, Tourism and Trade manages, through the State Secretariat for Trade, a fund established in 2010 in order financially to support export and investment activity for the benefit of Spanish economy, the Fondo para la Internacionalización de la Empresa (FIEM). ICO operates as a financial agent for the Fund. While FIEM can be used to finance up to 100% of the amount involved in a project, the ICO actively cooperates with the Compañía de Española de Seguros de Crédito a la Exportación (CESCE) and COFIDES. Potential beneficiaries of the Fund include domestic and foreign public and private enterprises and corporate groups and consortiums, both in developed and developing countries.

The Centro para el Desarrollo Tecnológico Industrial (CDTI), a public corporation under the Ministry of Science and Innovation, offers financial incentives for the internationalization of Spanish technologies, including through OFDI, as well as advisory and information services for knowledge-intensive companies. Political risk insurance for OFDI is offered by CESCE, a

joint stock company in which the government owns a majority share.

Besides these institutions, Spain has a wide net of sub-national agencies that support the internationalization of locally registered companies with financial incentives, as well as information and consultancy services. These include the Agencia Andaluza de Promoción Exterior (EXTENDA, Andalusia), Aragón Exterior (AREX, Aragon), ADE Financiación (Castile and Leon), ACCIÓ (Catalonia), the Instituto Gallego de Promoción Económica (IGAPE, Galicia), Desarrollo Internacional de Madrid (PromoMadrid, Madrid), the Instituto de Fomento de la Región de Murcia (INFO, Murcia), the Sociedad de Desarrollo de Navarra (SODENA, Navarre), the Sociedad para la Transformación Competitiva (SPRI, Basque Country), and the Instituto Valenciano de la Exportación (IVEX, Valencia).

*Source:* The authors, based on Sundaresh, *op. cit.* for Canada, India and the Republic of Korea. For Spain see: National level: [www.icex.es](http://www.icex.es), [www.comercio.gob.es](http://www.comercio.gob.es), [www.cofides.es](http://www.cofides.es), [www.ico.es](http://www.ico.es), [www.cdti.es](http://www.cdti.es), [www.cesce.es](http://www.cesce.es); sub-national level: [www.extenda.es](http://www.extenda.es), [www.aragonexterior.es](http://www.aragonexterior.es), [www.adefinanciacion.jcyl.es](http://www.adefinanciacion.jcyl.es), [www.accllo.cat](http://www.accllo.cat), [www.igape.es](http://www.igape.es), [www.promomadrid.com](http://www.promomadrid.com), [www.institutofomentomurcia.es](http://www.institutofomentomurcia.es), [www.sodena.com](http://www.sodena.com), [www.spri.es](http://www.spri.es), [www.ivex.es](http://www.ivex.es) (accessed on March 28, 2013).

While trade and investment promotion differ, these two functions are often found united in a single institution. *Investment promotion agencies and trade promotion agencies* usually offer similar services: information, matchmaking, seminars, missions, and fairs. Establishing an IPA is one of the most widely used measures to attract FDI, and IPAs typically serve as the first port of call for foreign investors.<sup>97</sup> Generally, IPAs do not engage in OFDI promotion; however, in some countries they are charged officially with both inward and outward investment promotion. The Chinese Investment Promotion Agency (CIPA), for example, is charged with “inviting in” FDI, as well as with “going out” investment promotion; it provides information and guidance to investors, organizes investment seminars, meetings and missions, conducts research on two-way investment, and fulfills other investment-related activities.<sup>98</sup> Another example of an agency whose mandate has been extended to include support for OFDI is ProChile. It was established in 1974 to promote non-traditional Chilean exports; by the early 1990s, it had shifted its focus into transforming Chilean export firms into outward investors.<sup>99</sup>

Even when it is not included in their mandate, many IPAs may engage with domestic investors who are looking to invest overseas. Typically, IPAs have direct contacts with investors and traders from other countries and are familiar with issues related to OFDI. They also interact with their foreign counterparts and exchange information on policies, regulations and incentives for

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<sup>97</sup> See e.g., Louis T. Wells and Alvin G. Wint, *Marketing a Country: Promotion as a Tool for Attracting Foreign Investment* (Washington, D.C.: Foreign Investment Advisory Service, 2000) and Jacques Morisset and Kelly Andrews-Johnson, *The Effectiveness of Promotion Agencies at Attracting Foreign Investment* (Washington, D.C.: The World Bank, 2004).

<sup>98</sup> Brief Introduction of investment promotion agency of Ministry of Commerce (CIPA), available at: [http://www.fdi.gov.cn/pub/FDI\\_EN/about/AboutusEn1.htm](http://www.fdi.gov.cn/pub/FDI_EN/about/AboutusEn1.htm) (last visited March 29, 2013).

<sup>99</sup> Chemonics International, Inc, “A Comparative Study of Export Promotion in Chile, Malaysia, South Korea and Indonesia, Study fulfilled for USAID,” p. 7, available at: [http://pdf.usaid.gov/pdf\\_docs/pnadr349.pdf](http://pdf.usaid.gov/pdf_docs/pnadr349.pdf) (last visited March 29, 2013).

investment. Relying on such information, many IPAs have developed information and advisory assistance capabilities of service to outward investors. The Japanese External Trade Organization is a good example of an agency that provides information for both inward FDI and OFDI promotion. Established in 1958 to conduct market research and organize export trade fairs, it added OFDI promotion to its functions after years of expansion.<sup>100</sup>

*Export credit agencies* are institutions that focus on the facilitation of international trade through insurance, guarantees and lending.<sup>101</sup> These institutions have expertise in facilitating cross border trade flows, and many now offer a variety of products to facilitate the cross border flow of investment. For instance, Malaysia's Export-Import Bank, an agency under the purview of the Ministry of Finance, offers the country's overseas investors loans for infrastructure and manufacturing projects, a special financing line for the establishment of Malaysian restaurants abroad and political risk insurance. ECAs can also comprise of private companies that provide political risk insurance on behalf of their governments. Examples include the Compagnie Française pour le Commerce Extérieur (COFACE) and PwC AG/Euler Hermes AG. COFACE was established in 1946 as an export credit insurance company; it was privatized in 1994, but continues to offer state-backed guarantees.<sup>102</sup> In Germany, the Federal Ministry of Economics and Technology, in consultation with the Federal Ministry of Finance, appointed for operation of Germany's investment guarantees a consortium of two companies: PwC AG and Euler Hermes AG. Details of this arrangement are stipulated in a contract between these companies and the Government of Germany; the execution of their mandates is subject to supervision by the above-mentioned ministries and the Federal Audit Office.<sup>103</sup>

A key objective of *development finance institutions* is to mobilize capital to foster economic growth in emerging markets and strengthen the development of their private sectors.<sup>104</sup> Examples include the Overseas Private Investment Corporation (OPIC, United States), Deutsche

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<sup>100</sup> JETRO, "Changes in Japanese Trade and Investment: Evolution of JETRO," available at: <http://www.jetro.go.jp/en/jetro/profile/pdf/jetro0908.pdf> (last visited March 1, 2013).

<sup>101</sup> For more information on different types of export credit agencies, see Malcolm Stephen, *The Changing Role of Export Credit Agencies* (Washington, D.C.: International Monetary Fund, 1999). On agencies that provide political risk insurance, see also Kathryn Gordon, "Investment Guarantees and Political Risk Insurance: Institutions, Incentives and Development," *Investment Policy Perspectives 2008* (Paris: OECD, 2008).

<sup>102</sup> COFACE's mandate is stipulated under Code des assurances, articles L 432-1 to L 432-4, available at: <http://www.legifrance.gouv.fr/affichCode.do?cidTexte=LEGITEXT000006073984>.

<sup>103</sup> The guidelines for granting cover for capital investments abroad in the version of October 7, 1993 (Federal German Gazette page 9589), chapter X, available at: [http://www.agaportal.de/pdf/dia\\_ufk/formulare/e\\_dia\\_richtlinien.pdf](http://www.agaportal.de/pdf/dia_ufk/formulare/e_dia_richtlinien.pdf) (last visited March 28, 2013).

<sup>104</sup> Because of the focus on HCMs that promote OFDI by domestic enterprises (and enterprises controlled by domestic firms), those DFIs that provided financial assistance to investment by any enterprise regardless of place of incorporation were excluded. One example of such a DFI is Belgium's BIO, which provides financial resources not only to local companies in emerging markets, but also to any large company with a local subsidiary regardless of nationality (General information and Investment Criteria of the BIO are available for download at <http://www.bio-invest.be/en/download-center/featured.html> (last visited March 31, 2013)). Another example is France's PROPARCO, which provides financing (loans, equity, guarantees) to any company that invests in eligible industrial and geographic sectors, regardless of nationality (PROPARCO supports the development of Africa's pharmaceutical sector, July 23, 2012, available at: [http://www.proparco.fr/lang/en/Accueil\\_PROPARCO/Publications-Proparco/News\\_PROPARCO?actuCtrlId=83485](http://www.proparco.fr/lang/en/Accueil_PROPARCO/Publications-Proparco/News_PROPARCO?actuCtrlId=83485) (last visited March 30, 2013)).

Investitions und Entwicklungsgesellschaft mbH (DEG, Germany), Società Italiana per le Imprese all'Estero (SIMEST, Italy), and the Corporation for International Investment (BMI-SBI, Belgium). DFIs operate in a manner similar to commercial banks: they provide loans, equity and guarantees to private sector enterprises to facilitate the development of emerging markets<sup>105</sup> by mobilizing private capital to help address development challenges<sup>106</sup> and improve the living standards of people,<sup>107</sup> among other things. DFIs are usually either wholly owned or controlled by their respective governments.

Ministries in a government's *executive branch* (e.g., trade, industry, foreign affairs) can play a role in OFDI as part of broader mandates. Their involvement in OFDI is two-fold. First, they create the domestic legal environment, formulate government policy and conclude international agreements that affect investment (e.g., BITs, FTAs, DTTs). Second, they undertake lobbying activities on behalf of firms investing abroad and provide general support to investors. For example, ministries of foreign affairs may offer investors information and support by allowing them to utilize the government's wide network of embassies, consulates, missions, and representatives, as well as through the provision of first-hand information about legal and economic conditions in host countries. Potential outward investors visit websites of ministries of industry or commerce because these provide information and resources useful to them, including HCMs. For instance, trade representatives of the Russian Ministry for Economic Development who are stationed in embassies abroad<sup>108</sup> provide information to Russian investors about opportunities in host markets and monitor economic conditions in them, with a view to identify barriers to entry or discrimination against Russian investors. Together with the Ministry of Economic Development, trade representatives organize business missions for Russian investors. Another example is the French Ministry of Foreign Affairs that, together with UBIFRANCE, the French Agency for International Business Development, provides (through its network of consulates) information on relocating abroad, economic and financial data, etc.<sup>109</sup>

The executive branch may also be directly involved in the provision of HCMs. For instance, the Swiss State Secretariat for Economic Affairs (SECO) established in 1997 the start-up fund for financing projects by Swiss SMEs investing in selected emerging markets.<sup>110</sup> While SECO provides financial resources for the program and makes the final decision on whether or not to finance a project, administrative operations (e.g., the selection of applications and the

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<sup>105</sup> COFIDES, "Mission statement," available at: <http://www.cofides.es/english/2mission.html> (last visited May 22, 2013).

<sup>106</sup> OPIC, "Main page," available at: <http://www.opic.gov/> (last visited May 22, 2013).

<sup>107</sup> Japan Finance Corporation, "Profile," available at: <http://www.jfc.go.jp/n/english/profile.html> (last visited March 28, 2013).

<sup>108</sup> Ministry for Economic Development of the Russian Federation, "Integrated foreign economic information portal," available at: [http://www.ved.gov.ru/rus\\_export/exporters\\_support/trade\\_representative\\_abroad/](http://www.ved.gov.ru/rus_export/exporters_support/trade_representative_abroad/) (in Russian) (last visited May 25, 2013).

<sup>109</sup> For examples, see information on Trade, Economy and Investment of the Consulate General of France in Hong Kong & Macau, available at: <http://www.consulfrance-hongkong.org/La-Mission-Economique-UBIFRANCE> (last visited May 25, 2013).

<sup>110</sup> SECO, "Presentation on Start-up fund," available at: [http://www.secostartupfund.ch/images/startupfund/presentation\\_start-up\\_fund.pdf](http://www.secostartupfund.ch/images/startupfund/presentation_start-up_fund.pdf) (last visited March 28, 2013).



management of loans) are carried out by a private limited liability company - FINANCEcontact Ltd.<sup>111</sup> However, such examples are rare. In most cases, the executive branch has supervisory control over institutions, such as IPAs and ECAs. For example, the Canadian Trade Commissioner Service, which operates knowledge and information centers and organizes webinars and trade missions, is part of the Canadian Department of Foreign Affairs, Trade and Development.<sup>112</sup> In China, the Ministry of Finance and Commerce (MOFCOM), which provides direct subsidies to eligible OFDI projects, is also in charge of CIPA, the investment promotion agency.

*Special purpose institutions* were created for reasons other than OFDI involvement, but their activities have been helpful to outward investors. This category comprises an assortment of institutions. Examples are the Japan Transport Cooperation Association, which promotes international cooperation between Japan and emerging markets in the transport sector seems to be covering OFDI projects as well; the Center for Industrial Technological Development, which promotes innovation and technological development of Spanish companies; the Innovation Network Corporation of Japan, which invests in Japanese and foreign companies to support innovative technologies; and the Korea Resources Corporation, which supports the exploration of national resources at home and abroad.

Investment/trade promotion agencies, export credit agencies, development finance institutions, the executive branch, and special purpose institutions all provide a variety of HCMs to outward investors. However, depending on the country, the same type of HCM may be administered by different institutions. Still, several general observations can be made. Export credit agencies and development finance institutions usually carry out financial measures, although, in some cases, executive agencies provide financial assistance as well. Political risk insurance in most of the covered countries is concentrated within export credit agencies.<sup>113</sup> Finally, the majority of the institutions provide some information and other support services relating to OFDI. The following section briefly reviews this last type of service.

### **c. Information and other support services**

The category of information and other support services includes the provision of information itself, advice and consulting, matchmaking services, the organization of investment missions to

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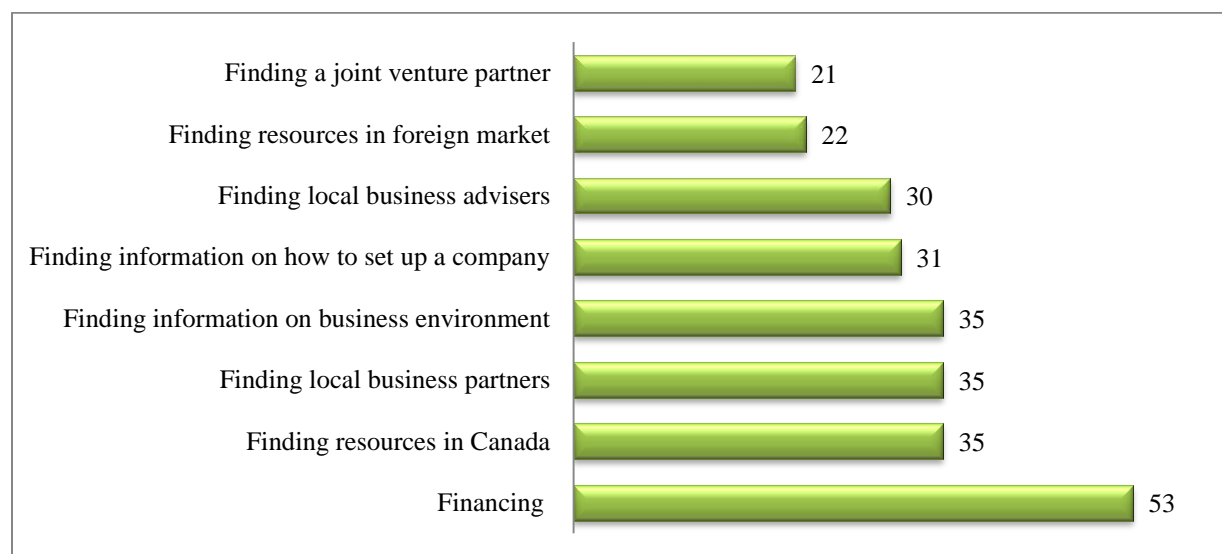
<sup>111</sup> More information on FINANCEcontact is available at: <http://www.secostartupfund.ch/fr/contact> (last visited June 5, 2013).

<sup>112</sup> The Canadian Trade Commissioner Service, “Our services,” available at: <http://www.tradecommissioner.gc.ca/eng/how-tcs-can-help.jsp> (last visited March 1, 2013).

<sup>113</sup> The notable exceptions include the United States (whose political risk provider is OPIC, a development finance institution), Germany (whose political risk providers are two private entities: PwC AG and Euler Hermes AG) and Singapore (IE Singapore, a government agency under the Ministry of Trade and Industry), which co-finances expenses of Singapore-based firms for political risk insurance obtained from Singapore-registered political risk brokers and insurers).

host countries, training (seminars, webinars, conferences), and help with feasibility studies.<sup>114</sup> The rationales for offering these products are to fill the knowledge gap that may hinder outward investment, familiarize investors with foreign market conditions, establish contacts with local entrepreneurs and governmental officials, prepare investors to enter a host country's market, and support post-investment activities. Interestingly, despite an abundance of informational resources on the Internet and services provided by various private consultancy firms, a lack of information about host countries continues to represent one of the main challenges for outward investors even for firms from a developed country like Canada (Figure 1).

**Figure 1. Main challenges facing Canadian firms prior to making foreign investment, 2010 (Percent)<sup>a</sup>**



Source: EDC, "Canadian direct investment abroad: A key growth strategy for Canadian exporters," Survey Findings, 2010, available at [https://www.edcresearchpanel.ca/MediaServer/3/documents/CDIA\\_SurveyResults\\_e.pdf](https://www.edcresearchpanel.ca/MediaServer/3/documents/CDIA_SurveyResults_e.pdf) (last visited May 20, 2013).

<sup>a</sup> Numbers represent the percent of Canadian companies that indicated a given factor as a main constraint for outward investment. The figure was prepared by the EDC's Online Research Panel; it surveyed 274 exporting businesses about their FDI activities.

As already mentioned, all types of institutions dealing with OFDI in the countries examined for this chapter provide information services. For example, the China Investment Promotion Agency,<sup>115</sup> the Malaysian Investment Development Authority<sup>116</sup> and the German Trade and

<sup>114</sup> UNCTAD addressed these measures under the heading "Information provisions and technical assistance" (see, for instance, UNCTAD, *Home Country Measures*, 2001, *op. cit.*, p. 26). The present chapter deals with measures offered by home countries to enterprises; therefore technical assistance to host countries to improve regulatory regimes and enhance investment reception capacity is not covered.

<sup>115</sup> CIPA, "Opportunities for Outbound Investment Projects," available at: [http://www.fdi.gov.cn/pub/FDI\\_EN/outboundinvestment/default.jsp](http://www.fdi.gov.cn/pub/FDI_EN/outboundinvestment/default.jsp) (last visited March 29, 2013).

<sup>116</sup> MIDA organizes trade and investment missions abroad, available at: <http://www.mida.gov.my/env3/index.php?page=detailvent&pid=101> (last visited March 29, 2013).

Invest,<sup>117</sup> all investment promotion agencies, have dedicated information websites for outward investors. Additionally, government agencies often distribute information about potential host countries on their websites. For instance, the German Federal Ministry of Economics and Technology provides consolidated information about opportunities abroad to German investors.<sup>118</sup> In Taiwan Province of China, the Department of Investment Services of the Ministry of Economic Affairs organizes seminars and conferences to share successful experiences of Taiwanese investors around the world.<sup>119</sup>

More specifically, *basic information* that is provided through databases, publications and reports includes, in particular, information about the economic climate and regulatory environment of host countries, industry data, host country legislation, and investment opportunities. For this purpose, home countries can draw on the informational resources of host countries' IPAs and multiple international databases, like those established by UNCTAD and the OECD. This information may be provided for free, tailored to the needs of particular investors for a fee,<sup>120</sup> or only made available to members.<sup>121</sup> For instance, UK Trade & Invest, the government department that brings together the work of the Department for Business, Innovation and Skills and the Foreign and Commonwealth Office, offers general information in form of publications on business opportunities abroad, as well as personalized overseas market introduction services.<sup>122</sup>

Another form of support service involves the organization of *seminars, conferences and other training events*. The content of training ranges from providing information about investment

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<sup>117</sup>GTAI, Information on international markets, available at <http://www.gtai.de/GTAI/Navigation/DE/Trade/maerkte.html> (last visited March 29, 2013).

<sup>118</sup> BMWi, "Investment in foreign countries," available at: <http://www.bmw.de/DE/Themen/Aussenwirtschaft/investieren-im-ausland.html> (last visited April 10, 2013).

<sup>119</sup> For information about recent seminars is available at the official website of the Ministry of Economic Affairs of the R.O.C., available at: [http://www.moea.gov.tw/Mns/english/news/News.aspx?kind=6&menu\\_id=176&news\\_id=29966](http://www.moea.gov.tw/Mns/english/news/News.aspx?kind=6&menu_id=176&news_id=29966) (last visited April 11, 2013).

<sup>120</sup> General information like investment and export guides or information on investment climate is typically provided for free, while more specialized information is provided on a for-charge basis. For instance, in addition to general information on investing abroad distributed for free, ICEX offers tailor-made information on foreign markets. See ICEX, "Rates for Custom services," available at: [http://www.icex.es/icex/cda/controller/pageICEX/0,6558,5518394\\_6294569\\_5589197\\_0\\_0\\_-1,00.html](http://www.icex.es/icex/cda/controller/pageICEX/0,6558,5518394_6294569_5589197_0_0_-1,00.html) (last visited March 27, 2013). JETRO offers Japanese investors investment statistics and market reports. For an annual fee, members can receive information via regular emails, magazines and annual trade and investment publications; see JETRO, "Information on members' privileges," available at: <http://www.jetro.go.jp/en/jetro/activities/members/> (last visited March 27, 2013).

<sup>121</sup> For example, the Investment Association of China, supervised by National Development and Reform Commission, offers consulting services on legal matters, accounting, audit etc. only to its members; see Investment Association of China, "Tasks," available at: [http://www.iac.org.cn/default.asp?pg=21&channel\\_id=24&item\\_id=133](http://www.iac.org.cn/default.asp?pg=21&channel_id=24&item_id=133) (last visited April 11, 2013).

<sup>122</sup> UKTI, "Overseas Market Introduction Services," available at: <http://www.ukti.gov.uk/export/howwehelp/overseasmarketintroductionservice.html> (last visited June 3, 2013).

opportunities in host countries<sup>123</sup> and experiences of domestic investors abroad,<sup>124</sup> to legal procedures for the authorization of outward investment. For instance, ProChile, despite a focus on export-related services, offers seminars for investors about doing business abroad; disseminated information includes available business opportunities, the sharing of experiences by other Chilean investors; legal and tax implications of enterprises' relocation; and information about existing Chilean HCMs.<sup>125</sup>

The organization of *missions* to potential host countries is another important service for outward investors. Among the countries examined for this chapter, only Chile, India, Kuwait, and Mexico appear not to provide this service, although it might well be that potential investors there participate in overseas trade missions.

Usually, missions are one-to-three day trips that include briefings, informational sessions, site visits, and networking with entrepreneurs and governmental officials. Missions are mostly organized on a fee basis, depending on the location and content of the program. While it is a common service in the countries covered, only a few governments offer missions for outward investors only (e.g., Spain<sup>126</sup>); in other countries, either trade missions include an investment dimension (e.g., Canada<sup>127</sup>) or trade and investment are covered by joint economic or business missions (e.g., Belgium,<sup>128</sup> Russia,<sup>129</sup> Japan<sup>130</sup>). The successful organization of such missions often requires the involvement of several institutions. For instance, trade missions for Italian entrepreneurs involve the participation of the Società Italiana per le Imprese all'Estero, the Agenzia per la promozione all'estero e l'internazionalizzazione delle imprese italiane (ICE), the General Confederation of Italian Industry (Confindustria -- which represents Italian manufacturing and services companies), along with the Ministry of Economic Affairs and the Ministry of Economic Development.<sup>131</sup> In Malaysia, trade and investment missions abroad are organized by the Ministry of International Trade and Industry and the Malaysian Investment Development

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<sup>123</sup> ICEX, "List of available seminars," available at: [http://www.icex.es/icex/cda/controller/pageICEX/0,6558,5518394\\_5519175\\_5554606\\_0\\_0\\_-1,00.html](http://www.icex.es/icex/cda/controller/pageICEX/0,6558,5518394_5519175_5554606_0_0_-1,00.html) (last visited April 11, 2013).

<sup>124</sup> JBIC, "Knowledge-sharing, list of seminars," available at: <http://www.jbic.go.jp/en/about/topics/know-how/index.html> (last visited April 11, 2013).

<sup>125</sup> For a list of other events, see ProChile, "Calendar Activities," available at: <http://www.prochile.gob.cl/calendario-actividades/> (last visited June 3, 2013).

<sup>126</sup> ICEX, "Investors missions," available at: [http://www.icex.es/icex/cda/controller/pageICEX/0,6558,5518394\\_5519260\\_5554606\\_0\\_0\\_-1,00.html](http://www.icex.es/icex/cda/controller/pageICEX/0,6558,5518394_5519260_5554606_0_0_-1,00.html) (last visited May 23, 2013).

<sup>127</sup> The Canadian Trade Commissioner Service, "Trade Missions, General information," available at: <http://www.tradecommissioner.gc.ca/eng/trade-missions/general-info.jsp> (last visited May 23, 2013).

<sup>128</sup> Economic missions are organized by the Belgian Agency for Foreign Trade, more information available at: [http://www.abh-ace.be/fr/missions\\_economiques/](http://www.abh-ace.be/fr/missions_economiques/) (last visited April 9, 2013).

<sup>129</sup> Ministry for Economic Development of the Russian Federation, "Integrated Foreign Economic Portal," Organization of business missions, available in Russian at: [http://www.ved.gov.ru/rus\\_export/business/](http://www.ved.gov.ru/rus_export/business/) (last visited May 20, 2013).

<sup>130</sup> JETRO, "Activities: Helping Japanese Business," available at: <http://www.jetro.go.jp/en/jetro/activities/overseas/> (last visited May 22, 2013).

<sup>131</sup> SIMEST, "Annual Report 2011, Promotional and Development activities," p.16, available at: [http://www.simest.it/key-listing/uploads/Abridged\\_Report\\_2011.pdf](http://www.simest.it/key-listing/uploads/Abridged_Report_2011.pdf) (last visited April 22, 2013).

Authority with the active participation of the Malaysian South-South Corporation (MASSCORP) and the Malaysia South-South Association (MASSA - a non-profit business association).<sup>132</sup>

Another subcategory consists of *matchmaking services*. They typically include the identification of potential partners, the preparation of informational notes on the legal and economic characteristics of host countries, the initial approach of partners by the organizing institution, and the establishment of contacts between investors and the local partners. Due to the individualized nature of this service, it is provided mainly on a fee basis. However, the Japan External Trade Organization offers its investors access to a free database of business contacts, TTPP, in addition to fee-for-services options.<sup>133</sup> This service is automated; proposals and inquiries are made by entrepreneurs themselves and information provided in the database is not verified by JETRO.

*Support for feasibility studies* is another service offered to encourage OFDI. Its purpose is to evaluate the economic potential of the proposed investments in host countries. Since this service requires an analysis of individual circumstances of investors, it is usually offered on a charge basis. Such support is typically provided in the form of co-financing and the reimbursement of expenses and therefore is covered in the section of this chapter on financial measures.

#### **d. Criteria for eligibility**

##### **i. Nationality**

Incorporation in the home country is one of the standard eligibility requirements used by financing institutions and political risk providers, but it is not always sufficient since ownership may also play a role. Unfortunately, many institutions do not unambiguously specify whether foreign owned entities are treated the same as domestically owned entities. Therefore, unless explicitly specified, it is not always possible to ascertain whether foreign affiliates controlled by MNEs headquartered abroad are also eligible for HCMs that are available to domestically owned firms. It is also difficult to ascertain whether, in the implementation of individual measures, domestically owned firms, including SOEs and national champions, receive special attention.

Some countries do, however, have explicit eligibility criteria (e.g., ownership/control by citizens or companies of the home country). For instance, under the financial assistance scheme of the Malaysia-Singapore Third Country Business Development Fund, joint market-research activities must be commissioned by at least one business association from Malaysia and one business association from Singapore; the Business association from Malaysia must have at least 51% of its members to be Malaysian owned companies, which in turn refers to locally incorporated companies with 51% of their shares owned by Malaysian citizens. For Singapore, the ownership

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<sup>132</sup> Information about MASSA's activity is available at: <http://www.massa.net.my/about.htm> (last visited April 11, 2013); information about MASSCORP's activity is available at <http://www.masscorp.net.my/v2/index.htm> (last visited April 11, 2013).

<sup>133</sup> JETRO, "Business Matching Database," available at: <http://www.jetro.go.jp/tppoas/> (last visited April 22, 2013).

requirement is 30% in both cases.<sup>134</sup> Another example is China's political risk provider, Sinosure, which stipulates that its eligible clients are enterprises "registered and having principal place of business in Mainland of China excluding those controlled by foreign, Hong Kong, Macau and Taiwan enterprises, institutions and citizens;"<sup>135</sup> In that case, affiliates of foreign companies in China cannot apply for investment insurance. An opposite example is France's OSEO: it provides financial guarantee for companies registered under French law that are majority-owned (directly or indirectly) by nationals or companies within the European Union.<sup>136</sup> Another important aspect relating to the nationality of an enterprise concerns support for those companies that are located abroad, but are controlled by domestically registered companies; if incorporation in the home country were the only criterion used by the home country, then such firms would be excluded from HCMs. However, some institutions explicitly state that foreign affiliates of domestically owned firms may also obtain financial or insurance products. Usually, that depends on a particular control threshold, e.g., the amount of shares owned by the domestic corporation in the capital of its foreign affiliate. For instance, OPIC provides insurance to United States citizens, corporations and other legal entities created under the laws of the United States and that are more than 50% beneficially owned by United States citizens, foreign corporations that are at least 95% owned by previously said investors, and other foreign entities that are fully United States-owned.<sup>137</sup> Japan's investment insurer, NEXI, offers overseas investment insurance not only for investments of Japanese companies abroad, but also to investments of their overseas subsidiaries into third countries.<sup>138</sup> Similarly, Italy's investment insurance provider, SACE, stipulates that foreign affiliates of Italian banks and companies can apply for investment insurance coverage through their parent firms.<sup>139</sup>

Because informational resources are generally provided on-line and free of charge, they are usually available to any firm, regardless of location or ownership. However, when institutions provide more targeted information, support feasibility studies, offer training, or organize investment missions, enterprises may have to demonstrate affiliation with the home country. For instance, Italian SIMEST offers advice and information relating to investments abroad as well as matchmaking services for Italian companies. Being a member of the Japan External Trade Organization allows companies, research institutions and individuals with an address in Japan

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<sup>134</sup> Information on eligibility requirements for Malaysia-Singapore Third Country Business Development Fund is available at:

[http://www.iesingapore.gov.sg/wps/wcm/connect/900fb800410f89779b699f3ad8984e19/Capital\\_20091214\\_MSBF\\_Guidelines.pdf?MOD=AJPERES](http://www.iesingapore.gov.sg/wps/wcm/connect/900fb800410f89779b699f3ad8984e19/Capital_20091214_MSBF_Guidelines.pdf?MOD=AJPERES) (last visited April 9, 2013).

<sup>135</sup> SINOSURE, "A brief introduction of investment insurance," available at: [http://www.sinosure.com.cn/sinosure/english/products\\_introduction01.htm](http://www.sinosure.com.cn/sinosure/english/products_introduction01.htm) (last visited March 28, 2013).

<sup>136</sup> OSEO, "Guarantee International Projects," available at: [http://www.oseo.fr/votre\\_projet/aller\\_a\\_l\\_international/aides\\_et\\_financements/garantir\\_vos\\_operations\\_internationales/garantie\\_de\\_projets\\_a\\_l\\_international](http://www.oseo.fr/votre_projet/aller_a_l_international/aides_et_financements/garantir_vos_operations_internationales/garantie_de_projets_a_l_international) (last visited April 27, 2013).

<sup>137</sup> OPIC, "Investment screener," available at: <http://www.opic.gov/what-we-offer/financial-products/financing-details/investor-screener#1>.

<sup>138</sup> NEXI, "Overseas Investment Insurance," available at: <http://www.nexi.go.jp/en/products/types/investment/> (last visited April 22, 2013).

<sup>139</sup> See SACE, "Political Risk insurance, Terms and Conditions," available at: [http://www.sace.it/GruppoSACE/content/en/consumer/products/investments\\_protection/investments/index.html?tab=2](http://www.sace.it/GruppoSACE/content/en/consumer/products/investments_protection/investments/index.html?tab=2) (last visited April 14, 2013).

access to informational resources and the free use of the foreign offices of that Organization.<sup>140</sup> Under certain conditions, however, individuals and corporations with an address in China can also become members.<sup>141</sup>

## ii. Sectors

Few of the institutions researched have stringent sector-based limitations regarding OFDI support, although a number of them specify priority sectors for support, typically in natural resources (e. g., Nippon Export and Investment Insurance (NEXI), Japan),<sup>142</sup> energy (e. g., Japan Bank for International Cooperation (JBIC))<sup>143</sup> and infrastructure (e. g., SACE, Italy).<sup>144</sup> OPIC provides insurance products for natural resources (excluding oil and gas) and, separately, enhanced insurance for investments in the oil and gas sector; for instance, for investments in oil and gas exploration, it provides extended coverage against risks of expropriation and interference with investor's operations.<sup>145</sup>

Some institutions focus their support on particular sectors only. For instance, the Innovation Network Corporation of Japan invests into domestic and foreign investment opportunities, especially in areas of the environment and energy, electronics and IT, bio-technology, and infrastructure in order to boost the competitiveness of Japanese companies.<sup>146</sup> Similarly, Spain's Center for Industrial Technological Development provides financing for Spanish SMEs that want to internationalize their own technologies in foreign markets; operations eligible for financing include costs of internationalizing intellectual property abroad and external consultancy and innovation support services, including the preparation of foreign market studies.<sup>147</sup> Foreign-based offices of the Center support Spanish companies that do technology-related business abroad.<sup>148</sup> The Korean Resources Corporation (KORES) provides long-term loans for overseas resources development, preferably to foreign affiliates of Korean companies.<sup>149</sup>

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<sup>140</sup> Information on JETRO Members services and conditions is available at: <http://www.jetro.go.jp/members/memberservice/apply/> (last visited April 9, 2013).

<sup>141</sup> JETRO, "Terms of Membership Agreement," art. 2, available at: [http://www.jetro.go.jp/members/memberservice/apply/jmrule\\_20120701.pdf](http://www.jetro.go.jp/members/memberservice/apply/jmrule_20120701.pdf) (last visited April 9, 2013).

<sup>142</sup> NEXI, "Investment and Loan Insurance for Natural Resources and Energy," available at: <http://nexi.go.jp/en/products/types/energy/> (last visited April 9, 2013).

<sup>143</sup> JBIC, "Overseas Investment Loans," available at: <http://www.jbic.go.jp/en/finance/investment/index.html#toc0>.

<sup>144</sup> SACE, "Financial guarantees," strategic infrastructure and renewable energy, available at: [http://www.sace.it/GruppoSACE/content/it/consumer/products/finanziar\\_guarantee/infrastrutture\\_rinnovabili/index.html?tab=0](http://www.sace.it/GruppoSACE/content/it/consumer/products/finanziar_guarantee/infrastrutture_rinnovabili/index.html?tab=0) (last visited April 9, 2013).

<sup>145</sup> OPIC, "Specialty products," available at: <http://www.opic.gov/what-we-offer/political-risk-insurance/types-of-coverage/specialty-products#6> (last visited April 22, 2013).

<sup>146</sup> About activities of INCJ, see <http://www.incj.co.jp/PDF/091001.pdf>, and the official website at <http://www.incj.co.jp/> (last accessed April 9, 2013).

<sup>147</sup> CDTI, "Products: Innternacionaliza," available at: <http://www.cdti.es/index.asp?MP=15&MS=645&MN=3> (last visited April 9, 2013).

<sup>148</sup> CDTI, "Annual Report 2004," p. 49, available at: [http://www.cdti.es/recursos/publicaciones/archivos/42427\\_1781782006114329.pdf](http://www.cdti.es/recursos/publicaciones/archivos/42427_1781782006114329.pdf) (last visited April 9, 2013).

<sup>149</sup> KORES, "Information about loans," available at: [http://www.kores.or.kr/gpms/sub01/work/work\\_02\\_04.jsp](http://www.kores.or.kr/gpms/sub01/work/work_02_04.jsp) (last visited April 23, 2013).

### iii. Ownership

While SOEs remain flagships of outward investment for some developing economies,<sup>150</sup> and many countries have national champions, very few institutions charged with OFDI promotion in developed countries and emerging markets make a distinction between these and other enterprises. Notable (but not typical) examples of countries that provide their SOEs with support unavailable for other companies are China and Russia. More specifically, China's State-Owned Assets Supervision and Administration Commission (SASAC) is charged with the management of Chinese SOEs, including the supervision of their OFDI activities, and the adoption of rules and regulations relating to outbound investment.<sup>151</sup> SASAC also maintains an Education and Training Center for the personnel of national and regional SOEs, offering, *inter alia*, training related to OFDI, information on legislation, market conditions and investment review processes in potential host countries.<sup>152</sup> In Russia, the Russian Ministry of Foreign Affairs has concluded agreements with INTER RAO UES and Russian Railways (both SOEs) to coordinate and support these companies' foreign projects and ensure diplomatic protection of their foreign economic interests.<sup>153</sup> Whilst such favorable SOE treatment does not appear to be the norm, it might all the same be the case that SOEs receive support from institutions other than those covered in this study or that such support is being provided on an informal basis.

### iv. Firm size

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<sup>150</sup> OECD, *State-owned enterprises in China: reviewing the evidence*, Occasional paper, OECD Working Group on Privatisation and Corporate Governance of State Owned Assets (Paris: OECD, 2009), p. 9; OECD, *State-owned enterprises in India: reviewing the evidence*, OECD Working Group on Privatisation and Corporate Governance of State Owned Assets (Paris: OECD, 2009).

<sup>151</sup> For instance, recently SASAC adopted interim measures that strengthen the supervision of OFDI by SOEs; see, The State-owned Assets Supervision and Administration Commission of the State Council, "Interim Measures for the Supervision and Administration of the Outbound Investments by Central State-owned Enterprises" (March 18, 2012). See also, Hogan Lovells, "China Issues New Rules on Outbound Investments by Centrally-administered State-owned Enterprises" (April 24, 2012), available at: <http://www.hoganlovells.com/china-issues-new-rules-on-outbound-investments-by-centrally-administered-state-owned-enterprises-04-24-2012/> (last visited April 23, 2013); text of the Interim measures is available in Chinese at: <http://www.sasac.gov.cn/n1180/n1566/n258237/n258899/14404719.html> (last visited April 23, 2013).

<sup>152</sup> Information about the SASAC Education and Training Center programs is available at: <http://www.tcsasac.com/> (last visited April 9, 2013).

<sup>153</sup> The press release about the agreement between the Russian Ministry of Foreign Affairs and INTER RAO UES is available at: [http://www.mid.ru/BDOMP/Brp\\_4.nsf/arh/5DDC499CAEE9F9F5C325714000257E89?OpenDocument](http://www.mid.ru/BDOMP/Brp_4.nsf/arh/5DDC499CAEE9F9F5C325714000257E89?OpenDocument) (in Russian, last visited April 9, 2013); the press release about the agreement between the Russian Ministry of Foreign Affairs and Russian Railways is available in Russian at: [http://www.mid.ru/BDOMP/Brp\\_4.nsf/arh/49253A38A06679A1C32570FC003BDA09?OpenDocument](http://www.mid.ru/BDOMP/Brp_4.nsf/arh/49253A38A06679A1C32570FC003BDA09?OpenDocument) (last visited April 9, 2013). The Ministry has also concluded agreements with Rusnano, Vnesheconombank and other entities. See more in Russian at: <http://www.mid.ru/bdomp/ns-dipecon.nsf/4d5db17578e45d4143256a0c003fb9a9/3f3191c7b075280bc325746a003b4ab0!OpenDocument> (last visited May 25, 2013). It must be noted that the texts of these agreements are unavailable; hence it is not possible to draw any conclusions about the extent of support rendered.



While SMEs are eligible for the same HCMs that apply to all companies, many developed countries give additional preferential support to SMEs.<sup>154</sup> For instance, the Spanish financing corporations COFIDES and the Instituto de Crédito Oficial (ICO) offer special financing lines and funds for SMEs; OPIC offers SMEs preferential treatment under certain conditions,<sup>155</sup> and the Canadian Trade Commissioner Office assesses the impact of proposed activities on Canadian SMEs when granting funding to national associations that undertake new or expand existing international business development activities.<sup>156</sup> Another example involves the Japan Bank for International Cooperation: in March 2013, it signed a loan agreement with Sumitomo Mitsui Banking Corporation (SMBC) to establish a credit line to support Japanese SMEs by funding some of their overseas business activities.<sup>157</sup>

Among the emerging markets examined, a few governments (e.g., those of India, the Republic of Korea, Singapore<sup>158</sup>) offer specialized measures to support outward investment by their SMEs distinct from general OFDI support. India's Eximbank uses established Eximius Centres of Learning for SME knowledge and capacity building.<sup>159</sup> In the Republic of Korea, the Korean Small and Medium Business Corporation, a non-profit government-funded organization, operates a global cooperation and marketing program that includes identifying overseas business opportunities and the facilitation of matchmaking and training for Korean SMEs.<sup>160</sup>

## v. Destination

A few institutions among the ones examined offer HCMs exclusively for investment into emerging markets.<sup>161</sup> Notable examples are OPIC, Germany's Investment and Development Company and Japan's Transport Cooperation Association. Japan's Bank of International

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<sup>154</sup> While not specifically addressed in this chapter, it is interesting to note that, on the regional level, the European Union is also supporting the internationalization of SMEs through trade facilitating measures, which have a positive impact on outward investment as well. In 2011, the European Union set out a new strategy for supporting the internationalization of SMEs, which (while addressing international trade) could also be viewed as providing the type of information that may also encourage OFDI, such as country and sector information through an online portal. See *Small Business, Big World: a new partnership to help SMEs seize global opportunities*, Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions, European Commission, November 9, 2011.

<sup>155</sup> OPIC, "Doing business with us: Small business sector," available at <http://www.opic.gov/doing-business-us/small-business-center> (last visited February 18, 2013).

<sup>156</sup> The Canadian Trade Commissioner Service, "Evaluation Criteria for Global Opportunities for Association," available at: <http://www.tradecommissioner.gc.ca/eng/funding/global-opportunities-associations/evaluation-criteria.jsp> (last visited February 18, 2013).

<sup>157</sup> JBIC, "Credit Line for Sumitomo Mitsui Banking Corporation," Press release, NR/2012-140, March 15, 2013, available at: <http://www.jbic.go.jp/en/about/press/2012/0315-01/index.html> (last visited April 24, 2013).

<sup>158</sup> For information about IE Singapore's Tianjin Eco-city Assistance Programme, see the Financial HCMs section below.

<sup>159</sup> Exim Bank of Korea, "SME Initiatives," available at: <http://www.eximbankindia.com/smeinit.asp> (last visited April 26, 2013).

<sup>160</sup> For more information about Korean SBC's Global cooperation and marketing services, see [http://www.sbc.or.kr/sbc/eng/business/global\\_cooperation\\_overseas.jsp](http://www.sbc.or.kr/sbc/eng/business/global_cooperation_overseas.jsp) (last visited April 24, 2013).

<sup>161</sup> The definition of "emerging markets" may, however, differ from country to country.

Cooperation, although focusing on emerging markets, allows financial support for investment into developed countries if it is undertaken in eligible sectors (e.g., transportation, traditional and renewable energy generation, distribution). Several other institutions, like France's OSEO, Spain's COFIDES and ICEX, Italy's SIMEST, and Singapore's IE, offer specialized financing lines for investment only into select<sup>162</sup> developed countries and emerging markets. Other countries do not make their support conditional on the host country destination, although many institutions focus on some countries more than on others due to historic ties or current political priorities. For instance, Russia's export credit agency EXIAR allocated most of its insurance capacity in 2012-2014 to other countries in the Commonwealth of Independent States, but also to Asia and Latin America.<sup>163</sup> Traditionally strong economic and social ties with the members of the Commonwealth of Independent States explain Russia's business interests there; Asian developing markets represent important business partners for Russia due to innovative technologies that can be obtained there and because of the economic importance of this region for the development of Russia's far east and Siberia; Latin America countries, in turn, show great potential for Russian technological and military companies.<sup>164</sup>

#### **e. Conditionality**

In general, home country institutions do not evaluate the potential effects of the investments they support on host countries. Only a few institutions, mostly from developed countries, review proposed investment projects for their compatibility with host country standards, especially, environmental, anti-corruption and human rights standards. Examples include OPIC,<sup>165</sup> Germany's Investment and Development Company,<sup>166</sup> Belgium's Corporation for International Investment,<sup>167</sup> and France's COFACE.<sup>168</sup> A number of institutions require potential investors to

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<sup>162</sup> Selection criteria differ from institution to institution, with institutions from developed countries focusing mainly on developing countries. But there are exceptions. For example, Italy's SIMEST offers separately equity financing in non-European Union and European Union countries. Spain's COFIDES focuses on investment into emerging markets, but it has a financing line specifically for investments into the United States; it also operates two funds (FIEX and FONPYME) that support Spanish investment into any country in the world. France's OSEO provides co-financing and financial guarantees for investment into any country, except into the European Union, Iceland, Liechtenstein, Norway, and Switzerland.

<sup>163</sup> It is, however, not clear what share of its insurance capacity is dedicated to investment (vs. trade). Exiar, "Products and Services," available in Russian at: <http://exiar.ru/en/prodserv/> (last visited February 18, 2013). Investment insurance is provided from 2013.

<sup>164</sup> Concept of the Foreign Policy of the Russian Federation, approved by the president of the Russian Federation V. Putin on 12 February 2013, Part IV: Regional Priorities, available at <http://mid.ru/bdcomp/ns-osndoc.nsf/1e5f0de28fe77fdcc32575d900298676/869c9d2b87ad8014c32575d9002b1c38!OpenDocument> (last visited October 7, 2013).

<sup>165</sup> "OPIC-supported projects should encourage positive host country development effects," from OPIC policies, available at: <http://www.opic.gov/doing-business-us/OPIC-policies> (last visited February 18, 2013).

<sup>166</sup> "The investment must have positive effect on the developing country" from DEG flyer for German enterprises, available at: [http://www.deginvest.de/deg/DE\\_Home/I/Download\\_Center/PDFs\\_Online-Bibliothek/DEG\\_Flyer\\_dt\\_Unternehmen.pdf](http://www.deginvest.de/deg/DE_Home/I/Download_Center/PDFs_Online-Bibliothek/DEG_Flyer_dt_Unternehmen.pdf) (last visited February 18, 2013).

<sup>167</sup> "BMI-SBI supports projects that are of general economic interest (to both Belgium and the host country)" from BMI-SBI, Our Mission, available at <http://www.bmi-sbi.be/en/> (last visited February 18, 2013).

demonstrate a positive or neutral effect on the home country. These effects may take the form of job creation,<sup>169</sup> an increase in international trade,<sup>170</sup> a positive contribution to the home country's gross domestic product,<sup>171</sup> a positive contribution to the internationalization of domestic enterprises<sup>172</sup> or, at the very least, the mitigation of any negative effects on the domestic economy.<sup>173</sup>

Some countries adhere to the principle of complementarity with private market participants. In general, institutions created to promote OFDI are not supposed to displace private companies or private sector-led initiatives that support investment and trade, such as business associations, consultancy firms and private financial institutions. To achieve this goal, OFDI institutions are encouraged to offer products and services that are complementary to what is already available in the private market. However, only a few institutions, such as the United Kingdom's ECGD,<sup>174</sup> OPIC (with respect to financing)<sup>175</sup> and Belgium's BMI-SBI<sup>176</sup> are explicit about their products being offered only when private financial institutions are not in a position to provide them.

## f. Conclusions

In virtually all of the countries covered in this chapter, the responsibility for administering HCMs lies with multiple institutions. In some countries, there is a preference for using existing institutions (usually those already charged with trade or inward investment promotion) by simply extending their mandates to cover OFDI as well. In others, new institutions are created to deal exclusively with such investment. Notable examples of the latter include the United States' Overseas Private Investment Corporation; Japan's Institute for Overseas Investment; Belgium's Corporation for International Investment; and Italy's FINEST (an Italian financial corporation that promotes cooperation with countries of Eastern Europe by supporting outward FDI by Italian enterprises located in the Northeastern region of Italy) and Agenzia per la promozione

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<sup>168</sup> Gordon, "Investment Guarantees and Political Risk Insurance: Institutions, Incentives and Development," 2008, *op. cit.*, p. 119.

<sup>169</sup> BMI-SBI, "BMI-SBI supports projects that are of general economic interest, (to both Belgium and the host country)," available at: <http://www.bmi-sbi.be/en/> (last visited February 18, 2013).

<sup>170</sup> BMI-SBI, "BMI-SBI supports projects that are of general economic interest, (to both Belgium and the host country)," *op. cit.*

<sup>171</sup> Export Development Canada, "Political risk insurance conditions," available at: <https://www.edc.ca/EN/Our-Solutions/Insurance/Pages/political-risk-insurance.aspx> (last visited February 18, 2013).

<sup>172</sup> Spain, "the Official Credit Institute, Corporate Internationalization Fund (FIEM)," available at: <http://www.ico.es/web/contenidos/5/4/9998/index.html> (last visited April 26, 2013).

<sup>173</sup> OPIC, "Investor Screener," available at: <http://www.opic.gov/doing-business-us/our-investor-screener#5> (last visited February 18, 2013).

<sup>174</sup> UK Export Finance, available at: [www.ecgd.gov.uk/](http://www.ecgd.gov.uk/).

<sup>175</sup> OPIC's website states that it complements the private sector and "can provide financing in countries where conventional financial institutions often are reluctant or unable to lend," available at: <http://www.opic.gov/what-we-offer/financial-products> (last visited April 11, 2013).

<sup>176</sup> BMI-SBI website states that its role is "complementary to that of other financial actors (banks, private equity, etc.)," available at: <http://www.bmi-sbi.be/en/strategie.html> (last visited April 11, 2013).

all'estero e l'internazionalizzazione delle imprese italiane (ICE).<sup>177</sup> In other countries, financing and insurance of OFDI is often carried out by export credit agencies together with trade promotion. The organization of missions and matchmaking events, as well as the provision of informational and training services for outward investors, are frequently undertaken jointly with inward FDI promotion under the aegis of IPAs.

This picture applies to both developed countries and emerging markets, although it is difficult to determine whether the provision of HCMs is more pronounced in the former or the latter.<sup>178</sup> In 2006, UNCTAD observed that, in most emerging markets, “proactive policies dealing with outward FDI are still uncommon, reflecting concerns that capital outflows may have adverse economic effects.”<sup>179</sup> It then continued that, while supporting home country firms’ efforts to internationalize “may help enhance the competitiveness of firms”, “[m]ost developing countries have not yet reached a stage at which a proactive approach to outward FDI is feasible or desirable.”<sup>180</sup> The emerging markets covered by the research for this chapter constitute only a small share of all emerging markets - but they are the biggest outward investors among emerging markets and therefore more likely to have elements of an OFDI policy in place, together with some instruments that implement it.<sup>181</sup> But only a few among them offer the whole range of HCMs (e. g., China, the Republic of Korea, Singapore).

Furthermore, the types of institutions offering a certain type of HCM differs across countries in both developed countries and emerging markets. To illustrate: while the ECAs of Malaysia,<sup>182</sup> Japan<sup>183</sup> and Canada<sup>184</sup> offer financial HCMs, these measures are offered by DFIs in, for example, the United States,<sup>185</sup> Germany<sup>186</sup> and Italy;<sup>187</sup> by special purpose institutions in the

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<sup>177</sup> ICE is a new agency (formed on the basis of the now defunct Institute for Foreign Trade) established in Italy in 2011 for the promotion abroad and internationalization of Italian firms; more information is available at <http://www.ice.gov.it/corporate/chiSiamo.htm> (last visited June 5, 2013).

<sup>178</sup> Moreover, it seems that a few developed countries have ceded the provision of certain HCMs to private market participants in their home countries. For instance, both Switzerland and the United Kingdom mostly rely on private markets to fulfill such a need. Switzerland, unlike other developed countries, does not offer political risk insurance, while the United Kingdom does not provide overseas investment financing.

<sup>179</sup> UNCTAD, *Investment Brief*, No. 4 (2006), available at: [http://unctad.org/en/Docs/webiteia20065\\_en.pdf](http://unctad.org/en/Docs/webiteia20065_en.pdf) (last visited February 9, 2013).

<sup>180</sup> UNCTAD, *World Investment Report 2006*, *op. cit.*, p. 202.

<sup>181</sup> According to the UNCTAD, there were at least 129 emerging markets (including overseas territories, etc.), out of a total of 173 emerging markets, that reported FDI outflows (positive or negative (i.e., disinvestments)) in any year between 2007 and 2011. Many -- if not most -- of them are not likely to have dealt with this issue in any significant manner. For the rest of the emerging markets, information on OFDI flows is not available. See UNCTAD, *World Investment Report 2012*, *op. cit.*, Annex table I.1.

<sup>182</sup> Malaysia’s Eximbank, “Overseas project/contract financing,” available at: <http://www.exim.com.my/conventional-banking/overseas-project-contract-financing> (last visited March 28, 2013).

<sup>183</sup> JBIC, “Overseas Investment Loans,” available at: <http://www.jbic.go.jp/en/finance/investment/index.html> (last visited March 28, 2013).

<sup>184</sup> EDC, “Foreign Investment Financing,” available at: <http://www.edc.ca/EN/Our-Solutions/Financing/Pages/foreign-investment.aspx> (last visited April 26, 2013).

<sup>185</sup> OPIC, “Financial products,” available at <http://www.opic.gov/what-we-offer/financial-products> (last visited March 28, 2013).

Republic of Korea;<sup>188</sup> and by governmental departments (e.g., the State Secretariat for Economic Affairs) in Switzerland.<sup>189</sup>

Finally, virtually all the home countries examined here – and the majority of the individual institutions discussed in this section – provide at least some information and other support services. They resemble information services designed to attract inward FDI and include information on the economic climate and regulatory environment of host countries, such as industry data, investment legislation and investment opportunities. These services also include access-to-information databases, the organization of face-to-face contacts with potential investors, match-making services with foreign entrepreneurs and public officials, technical support in the form of consulting services and feasibility studies, and the organization of seminars, conferences and trade and investment missions. In most cases, they are provided for free, but in some cases users need to pay for them.

Thus, the current institutional structure regarding OFDI can be characterized, in the first place, as a fragmented regime, with a variety of institutions dealing with various aspects of such investment. This fragmentation is in striking contrast to the relatively centralized inward FDI promotion regime, where many governments have established one-stop shops for incoming investment. One problem created by such a fragmented institutional set-up is that several institutions in the same home country may provide similar services, increasing the chance of duplication. That is especially true for information services.

A second characteristic is that the provision of outward investment promotion services is often joined with trade or inward investment promotion services. This is explained partly by historic circumstances. Since governments typically deal with OFDI after already having set up institutions for encouraging inward investment, they often simply opt to expand the mandate of existing agencies rather than choose to set up specialized outward investment agencies. It might also be that governments attach lesser importance to OFDI than to trade or inward investment promotion. The implication of this approach might be that financial and human resources are unevenly distributed between OFDI facilitation on the one hand and trade and inward investment promotion on the other – reflecting perhaps, in turn, the ambivalent effect of OFDI on home countries.

A third characteristic is the uneven extent to which the countries examined for this chapter have established institutions dealing with OFDI. For instance, there are only two major government institutions in the United Kingdom that provide the country's enterprises with OFDI support: the

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<sup>186</sup> DEG, "Services for German enterprises," available at: [http://www.deginvest.de/deg/EN\\_Home/Range\\_of\\_Services/Accompanying\\_German\\_enterprises/index.jsp](http://www.deginvest.de/deg/EN_Home/Range_of_Services/Accompanying_German_enterprises/index.jsp) (last visited March 28, 2013).

<sup>187</sup> SIMEST, "Equity Shareholding in non-EU companies," p. 8, available at: [http://www.simest.it/content/pdf/brochures/brochure\\_inglese\\_all.pdf](http://www.simest.it/content/pdf/brochures/brochure_inglese_all.pdf) (last visited March 28, 2013).

<sup>188</sup> See the information on capital loan for overseas mineral resources development, available at: [http://eng.kores.or.kr:8080/gpms/user.tdf?a=common.HtmlApp&c=2001&page=/english/work/work\\_02\\_04.html&mc=ENG\\_WORK\\_020\\_040](http://eng.kores.or.kr:8080/gpms/user.tdf?a=common.HtmlApp&c=2001&page=/english/work/work_02_04.html&mc=ENG_WORK_020_040) (last visited March 9, 2013).

<sup>189</sup> SECO Start-up Fund (SSF), available at: <http://secostartupfund.ch/en/> (last visited March 29, 2013).

Export Credits Guarantee Department (charged with investment insurance) and UK Trade & Invest (which offers informational services on a free or chargeable basis). Similarly, Canada and Switzerland have only a few institutions dealing with OFDI. In contrast, Belgian, Chinese, Korean, and Spanish investors obtain support from a range of institutions offering HCMs. One issue in this regard is whether countries that have a range of institutions offer more (or more specialized) HCMs than those that do not. Another issue is the extent to which fragmentation is indicative of the value home country governments place on OFDI. If the conclusions of one study<sup>190</sup> dealing with IPAs promoting inward FDI -- namely that autonomous investment promotion agencies are more effective than institutions that are part of ministries -- are equally valid for outward investment, then a more coherent approach to the administration of HCMs might be more effective than the current fragmentation. In fact, governments might eventually move toward a one-stop shop approach, as they have done in the case of inward FDI.

These differences in approach among home countries reflect not only differences in the understanding of business-government relations, but they also demonstrate where particular governments set their economic priorities. They may also have longer-term consequences for the international competitive position of home country enterprises from one country vis-à-vis those from another.

To the extent that past policy developments regarding inward FDI are a guide, the fragmentation of the institutional framework for OFDI in the countries examined for this chapter could suggest that leading home countries may be ripe to undertake a reorganization, if not a consolidation, of OFDI institutions in order better to deliver the services they offer. (It needs to be recalled, however, that, although firms in many more emerging markets have become outward investors, the great majority of these countries do not yet have a noticeable framework for these activities in place.) Such a step would help simplify the use of OFDI promotion services, avoid the risk of confusion between services offered to outward investors, exporters and contractors and, overall, most likely increase the efficiency and effectiveness of the services rendered -- including for firms, which, at the moment, need to contact a variety of institutions involved in OFDI promotion. While there may be no ultimate necessity to create a one-stop-shop institution for outward investors, some centralization of services in existing institutions, or the establishment of up-to-date directories describing the HCMs available in a given country, might be desirable. The accessibility of information offered by OFDI promotion institutions is also relevant. A final challenge is to demonstrate the effectiveness of existing institutional arrangements. Measuring the effectiveness of promotional efforts has always been a difficult methodological issue in any research on investment promotion. While some of the recent studies argue that effective home countries institutions do affect the engagement of domestic companies in the internationalization process,<sup>191</sup> further research in this regard is warranted.

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<sup>190</sup> Morisset and Andrews-Johnson, *The Effectiveness of Promotion Agencies at Attracting Foreign Investment*, *op. cit.*, p. 49. It is important to note that this study did not take into account efforts of sub-national institutions in countries like Brazil, China, India, and the United States, countries that together account for a substantial portion of international investment flows.

<sup>191</sup> See e.g., Xiaoming He and Cui Lin, "Can strong home country institutions foster the internationalization of MNEs?," 20 *Multinational Business Review* 352 (2012); te Velde, "Understanding developed country efforts to

### 3. Financial measures

#### a. Introduction

Financial HCMs provide direct financial advantages to home country firms investing abroad. It appears that firms often consider them to be one of the most important types of HCMs: one survey revealed that five out of the top ten government initiatives that SMEs found most helpful for their internationalization were financial HCMs.<sup>192</sup> By providing a cross-sectional analysis of the types of financial HCMs offered by both the developed countries and emerging markets researched for this chapter, this section seeks to shed some light on how financial HCMs are used by national governments to influence outflows of FDI.

Financial HCMs can be categorized into four distinct groups: grants, loans, financial guarantees, and equity participations.

Grants are the easiest form of financial assistance to provide. They are usually capped at a lower nominal value relative to loans and equity participations, which tend to be capital-intensive measures. The administration of grants is also more straightforward. Unlike the other three categories of financial HCMs that commit the government for a period of months or years, grants are often one-off payments that require little post-disbursement administration. While there is typically some sort of approval process for grants, that process often does not necessarily require the same sort of in-depth risk assessment that has to precede the provision of longer-term financial measures such as loans, financial guarantees or equity investments, because of the inherently limited temporal nature of a government's commitment when it comes to grants. However, while grants may be easy to provide, they do not generate any direct financial returns to the state. If a government wants to continue providing grants over a period of time, it has constantly to replenish that pool of capital.

This is in contrast to the potentially self-sustaining nature of the other three categories of financial HCMs. Most loans will eventually be repaid with interest; financial guarantees usually involve the firm paying a fee;<sup>193</sup> and the government should usually be able to sell its equity stake in any foreign affiliate for a profit. The Overseas Private Investment Corporation is an excellent illustration of a self-sustaining fund, operating “at no net cost to American

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promote foreign direct investment,” 2007, *op. cit.*, p. 100; and Juan J. Duran and Fernando Ubeda, “The efficiency of government promotion for outward FDI: The intention to invest abroad,” 9(2) *Multinational Business Review* 24 (2001).

<sup>192</sup> See, Spring Singapore, “Study on SME Internationalisation: Best Practices Across Selected APEC Economies,” 2011, *op. cit.*, p. 43.

<sup>193</sup> For example, Canada's Export Guarantee Program provides financial guarantees for a price; similarly, Italy's export credit agency, SACE, offers financial guarantees to Italian SMEs at no additional cost to the SMEs.

taxpayers.”<sup>194</sup> It offers a wide range of financial products, including loans, guarantees and equity participation, but does not provide grants.

However, while grants may be the easiest financial HCM for governments to provide, loans and equity participations are likely to provide home country firms with the most significant support for OFDI, simply because the quantum of loans extended tends to be much higher than the quantum of most grants. Of these four types of financial HCMs, it is notable that loans are the most prevalent measures offered by the countries surveyed in this chapter.

## **b. Measures**

### **i. Grants**

A grant is a form of financial support given by the government that provides firms with cash or subsidies for certain business costs. As discussed above, grants are one of the easiest financial HCMs to provide because they are easy to administer, typically involve smaller amounts of money and are one-off commitments.<sup>195</sup>

While the provision of grants to firms to support their internationalization through OFDI may create concerns regarding an inefficient use of resources, these concerns are mitigated by the requirement that businesses co-share the costs of undertaking the activity. Most countries offering grants to their firms operate on a 50-50 cost-sharing basis. Firms also have to apply for these grants through the responsible government agencies. Depending on the thoroughness of the approval process, this could be a way for governments to weed out applicants that are unlikely to make productive use of a grant.

Grants can be structured to provide either an ex ante or ex post payment to applicant firms to subsidize the cost of specific business expenses related to OFDI (with the possibility that approval is being given ex ante, while payment being made ex post). It seems like the latter option is preferable for ease of administration, as the government only subsidizes the expenses that the firm has actually incurred.

#### **(i) Feasibility studies and other pre-investment activities**

A grant for the conduct of feasibility studies is a common financial HCM aimed at supporting pre-investment activities. Canada, Germany, Malaysia, Singapore, and Spain provide grants for such pre-investment activities.

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<sup>194</sup> OPIC, “Overview,” available at: <http://www.opic.gov/who-we-are/overview> (last visited February 5, 2013).

<sup>195</sup> Many developing countries may have difficulties to provide grants, simply for reasons of resource constraints. This is however not the case for some developing countries; in addition, the amounts involved may be much smaller than in the case of developed countries (with, of course, also a smaller effect).



Measures subsidizing the cost of feasibility studies help to overcome information-related market failures, particularly where the target host country is less developed and does not have a sophisticated investment promotion agency. Investors are sometimes said to suffer from a perception bias, where they “perceive that many countries are in trouble when in fact only one country in the region is, and thus require an inordinately high rate of return from investment in the region.”<sup>196</sup> The provision of a grant for pre-investment activities such as feasibility studies lowers transaction costs that may pose an obstacle to OFDI by home country firms, especially by SMEs.

Grants for feasibility studies can either be pre-financed (meaning that the funds are repaid to the government if the studies reveal that projects are viable) or fully financed (meaning that there is no need to repay the funds).<sup>197</sup> The results of the research for this chapter suggest that most HCMs supporting feasibility studies are fully financed. Eligible expenses covered by these grants typically include third-party expenses such as fees paid to consultants, investment bankers and lawyers.

The eligibility for a grant may be dependent on a firm’s intention to proceed with an investment (i.e., the firm must be willing to proceed with the investment if the results of the feasibility study are favorable) and the financial ability to proceed with an investment if the feasibility study produces a favorable outlook. Germany’s DEG, funded by Germany’s Federal Ministry for Economic Cooperation and Development, is explicit in this respect: it co-finances “feasibility studies of German and other European companies, aimed at laying the ground for developmentally sound investments.”<sup>198</sup> Two important factors that are considered in the approval process for this HCM are a “firm investment intention, subject to a successful outcome of the feasibility study” and the firm’s capability “on a professional level as well as financially to utilise the results of the study and to carry out the planned investment.”<sup>199</sup>

A common way these grants are structured is for the government to pay for 50% of eligible expenses, up to a certain maximum amount.<sup>200</sup> The quantum of this maximum sum varies: for instance, the cap on grants offered by Malaysia and Singapore under their joint measure (the Malaysia-Singapore Third Country Business Development Fund) goes up to approximately US\$ 66,000,<sup>201</sup> while Germany’s is substantially higher, at approximately US\$ 270,000.<sup>202</sup>

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<sup>196</sup> Velde, “Understanding developed country efforts to promote foreign direct investment,” 2007, *op. cit.*, p. 86.

<sup>197</sup> UNCTAD, *Handbook on Outward Investment Agencies and Institutions*, 1999, *op. cit.*, p. 5.

<sup>198</sup> DEG, “Feasibility studies,” available at: <https://www.deginvest.de/International-financing/DEG/Unser-Angebot/F%C3%B6rderprogramme/Machbarkeitsstudien/> (last visited April 11, 2013).

<sup>199</sup> DEG, “Feasibility studies,” *op. cit.*

<sup>200</sup> See e.g., the Malaysia-Singapore Third Country Business Development Fund’s Joint Feasibility Studies, available at: [http://www.iesingapore.gov.sg/wps/wcm/connect/900fb800410f89779b699f3ad8984e19/Capital\\_20091214\\_MSBF\\_Guidelines.pdf?MOD=AJPERES](http://www.iesingapore.gov.sg/wps/wcm/connect/900fb800410f89779b699f3ad8984e19/Capital_20091214_MSBF_Guidelines.pdf?MOD=AJPERES) (last viewed January 24, 2013); see also, DEG’s feasibility study program, available at: <https://www.deginvest.de/International-financing/DEG/Unser-Angebot/F%C3%B6rderprogramme/Machbarkeitsstudien/> (last visited April 13, 2013).

<sup>201</sup> Calculated at an exchange rate of RM/USD 0.33.

<sup>202</sup> Calculated at an exchange rate of EUR/USD 1.35.

A home country can also adjust the cap based on the type of feasibility study that is undertaken. In Malaysia and Singapore, a grant for target-specific feasibility studies (i.e., where the subject of the study is a specific company or project that the applicant firm would like to invest in) is capped at approximately US\$ 66,000, while a grant for general feasibility studies with no specific target is capped at only half that amount.<sup>203</sup> This approach recognizes that targeted feasibility studies are more likely to result in actual investments being consummated, and it incentivizes home country firms to focus on specific opportunities by providing a higher level of support.

Pre-investment financial support can be provided to business associations rather than individual firms. In Canada, the Global Opportunities for Associations program “provides contribution funding to support national associations undertaking new or expanded international business development activities, in strategic markets and sectors, for the benefit of an entire industry” (which also covers OFDI projects).<sup>204</sup> The Malaysia-Singapore Third Country Business Development Fund offers financial assistance of up to US\$ 33,000 for market research commissioned by business associations in order to identify strategies for market entry, business opportunities or to analyze the business environment for a specific market and industry.<sup>205</sup> By covering a portion of the expenses incurred by business associations, home countries are able to help their firms close the information gap and lower transaction costs.

A variant on direct financial support for feasibility studies is for a home country to provide the service itself. One such example is the United Kingdom Trade & Investment’s Overseas Market Introduction Service.<sup>206</sup> Rather than providing a grant for feasibility studies conducted by third parties, the service is provided in-house, for a fee (ranging from £ 500 to several thousand British Pounds), by UK Trade & Investment.<sup>207</sup> The service includes the identification of potential business partners, feasibility studies, advice on local regulations, information on how to access and influence decision-makers, and the use of official premises such as the British Embassy for meetings and receptions. In Spain, ICEX provides in-house advice to businesses wishing to invest abroad.<sup>208</sup> Information on the legal framework and available incentives in the target destination is provided for free, while feasibility studies and more in-depth reports on the investment climate are subject to a fee.

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<sup>203</sup> IE Singapore, “Malaysia-Singapore Third Country Business Development Fund,” available at: [http://www.iesingapore.gov.sg/wps/wcm/connect/900fb800410f89779b699f3ad8984e19/Capital\\_20091214\\_MSBF\\_Guidelines.pdf?MOD=AJPERES](http://www.iesingapore.gov.sg/wps/wcm/connect/900fb800410f89779b699f3ad8984e19/Capital_20091214_MSBF_Guidelines.pdf?MOD=AJPERES) (last visited January 24, 2013), pp. 1-2.

<sup>204</sup> The Canadian Trade Commissioner Service, “Global Opportunities for Associations,” available at: <http://www.tradecommissioner.gc.ca/eng/funding/global-opportunities-associations/home.jsp> (last visited February 9, 2013).

<sup>205</sup> IE Singapore, “Malaysia-Singapore Third Country Business Development Fund,” 2009, *op. cit.*, pp. 3-5.

<sup>206</sup> UK Trade & Investment, “Overseas Market Introduction Service,” available at: <http://www.ukti.gov.uk/export/howwehelp/overseasmarketintroductionservice.html> (last visited January 24, 2013).

<sup>207</sup> UK Trade & Investment, “Kick-start your success in world markets: Helping your business to internationalise,” p. 10, available at: <http://www.ukti.gov.uk/uktihome/item/377480.html> (last visited February 9, 2013).

<sup>208</sup> ICEX, Asesoramiento sobre Inversiones en el Exterior [Advice on Overseas Investments], available at: [http://www.icex.es/icex/cda/controller/pageICEX/0,6558,5518394\\_7169551\\_5589197\\_0\\_0\\_-1,00.html](http://www.icex.es/icex/cda/controller/pageICEX/0,6558,5518394_7169551_5589197_0_0_-1,00.html) (last visited June 23, 2013).

It is notable that grants for pre-investment activities are likely to be most helpful to SMEs. The cost of these pre-investment activities could be prohibitive for many such firms because they are less likely to have significant cash reserves as compared to larger enterprises. SMEs will often opt to avoid the risk of having to expend precious funds studying the viability of investments that may not materialize. The resulting information gap may mean that valuable opportunities for growth and increased competitiveness are not being seized. Germany offers grants for feasibility studies only to SMEs within the European Union with an annual turnover of approximately US\$ 650 million, recognizing that the information gap is probably a lot more significant to SMEs than to larger enterprises.<sup>209</sup> Furthermore, one of the requirements to be eligible for such a German grant is that “[t]he study would not be carried out if public funding was not available due to the ensuing risks and costs”, thereby reflecting a policy of utilizing public funds only where necessary.<sup>210</sup>

#### (ii) Costs of setting up overseas offices

Grants can provide financial support for office rental, the salary of a small number of overseas staff, training costs, and related travel and accommodation expenses. This HCM is offered by Singapore and Taiwan Province of China.

Singapore supports the establishment of marketing offices in the Sino-Singapore Tianjin Eco-city, paying for the salaries of two overseas marketing staff, office rental costs and both “[a]irfare and accommodation costs for marketing trips made between Tianjin and other cities in China for up to two marketing personnel.”<sup>211</sup> The measure also covers third-party costs such as legal fees and engagement fees for overseas distributors. The grant appears to be available only to Singapore-based companies with clear internationalization plans, annual total business spending of at least S\$ 250,000 over the preceding three-year period, minimum paid-up capital of S\$ 50,000, and at least three managerial staff (Singapore Basic Eligibility Criteria).<sup>212</sup> While setting up an overseas office solely for marketing purposes may lead to future FDI, it is not sufficient in itself to constitute FDI.

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<sup>209</sup> DEG, “Financing of Feasibility Studies” (May 2011), available at: [https://www.deginvest.de/migration/DEG-Startseite/Development-Finance/Range-of-Services/Special-Programmes/PDF-Special-Programmes/Principles\\_-Feasibility\\_Studies\\_english.pdf](https://www.deginvest.de/migration/DEG-Startseite/Development-Finance/Range-of-Services/Special-Programmes/PDF-Special-Programmes/Principles_-Feasibility_Studies_english.pdf) (last visited April 14, 2013).

<sup>210</sup> DEG, “Feasibility studies,” available at: <https://www.deginvest.de/International-financing/DEG/Unser-Angebot/F%C3%B6rderprogramme/Machbarkeitsstudien/> (last visited April 13, 2013).

<sup>211</sup> IE Singapore, “Tianjin Eco-city Assistance Programme,” available at: [http://www.iesingapore.gov.sg/wps/wcm/connect/4b01f400458b413d93c6b7c8c607a1aa/Capital\\_20110125\\_TAP.pdf?MOD=AJPERES](http://www.iesingapore.gov.sg/wps/wcm/connect/4b01f400458b413d93c6b7c8c607a1aa/Capital_20110125_TAP.pdf?MOD=AJPERES) (last visited February 9, 2013).

<sup>212</sup> IE Singapore, “Tianjin Eco-city Assistance Programme,” *op. cit.*

Taiwan Province of China offers financial support to businesses that invest in countries with which it maintains diplomatic relations, subsidizing up to 30% of the salary of host country employees or 30% of the rent paid for factories, offices or land.<sup>213</sup>

By providing financial support for the costs involved in setting up overseas offices, this type of grant helps to reduce initial barriers to market entry faced by home country firms.

### (iii) Training and human capital development

Grants meant to cover the costs of training staff for employment in foreign affiliates help reduce obstacles to OFDI. Immersion programs for trainees in a foreign office, foreign language classes and executive programs can help employees and managers better appreciate cultural differences in a professional context, thereby reducing the “liability of foreignness” for businesses operating outside their home countries. Both China and Singapore offer to subsidize such expenses.

Singapore supports companies that send their trainees for training “attachments” overseas by co-sharing certain components of the immersion program for trainees.<sup>214</sup> These include travel expenses, language training and the basic salary of the participating staff. To qualify for this HCM, the applicant company must satisfy the Singapore Basic Eligibility Criteria. As part of the application process for this HCM, companies also have to furnish IE Singapore with resumes of the trainees and in-market mentors, training programs outlining the objectives and deliverables of the overseas attachment, and details of the trainees’ present or prospective roles in managing the overseas market from the Singapore headquarters or present or prospective job postings in the foreign market.

Another manpower-related program in Singapore is the International Human Resource Strategy Development, through which IE Singapore co-funds the costs of an international human resource strategy and third-party consultancy fees in order to implement an “effective international HR strategy”, laying “a strong foundation for successful internationalisation.”<sup>215</sup> This grant is approved on a case-by-case basis, and qualifying companies must meet the Singapore Eligibility Criteria.

Under the International Business Fellowship Executive Programme (iBF), IE Singapore supports businesses by offering short-term executive training programs for “middle and senior

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<sup>213</sup> Ministry of Foreign Affairs, Republic of China (Taiwan), *Guli yezhe fuyou bangjiao guojia touzi fuzhu banfa* [Regulation encouraging businesses to invest in countries with diplomatic relations with Taiwan], available at: [http://law.mofa.gov.tw/law\\_out/LawContent.aspx?id=FL011168](http://law.mofa.gov.tw/law_out/LawContent.aspx?id=FL011168) (last visited March 11, 2013).

<sup>214</sup> IE Singapore, “International Market Immersion Programme,” available at: <http://www.iesingapore.gov.sg/Assistance/Global-Company-Partnership/Manpower-Development/International-Human-Resource-Strategy-Development> (last visited October 4, 2013).

<sup>215</sup> IE Singapore, “International Human Resource Strategy Development,” available at: <http://www.iesingapore.gov.sg/wps/portal/GCP-ManpowerDevelopment/IHRSD> (last visited February 13, 2013).

management to gain firsthand market knowledge and build business networks” in key markets like China, India, Indonesia, the Middle East, Russia, and Vietnam.<sup>216</sup>

IE Singapore maintains a flexible approach to training and development by allowing companies to select “customised training programmes ... specially developed by third-party training providers” in order to cater to their specific needs.<sup>217</sup> Where proposals are approved by IE Singapore, the costs of training are co-shared between both the company and IE Singapore.

China has a similar HCM that covers the “expenses for adaptive training on staff dispatched overseas.”<sup>218</sup>

While these programs provide significant advantages for firms making investments abroad, “there are substantial initial costs involved that deter smaller firms from reaping the benefits.”<sup>219</sup> HCMs subsidizing third-party expenses involved in developing an international human resource strategy may not provide a significant advantage to large enterprises as these usually already have relatively sophisticated human resource policies in place. However, these HCMs can make a substantial difference to smaller businesses. On their own, SMEs will be less willing to retain third-party consultants to develop human resource strategies as the benefits may not be immediately ascertainable and the expenses incurred may be significant relative to the size of the business.

## ii. Loans

Loans are the most common financial HCM offered by the twenty countries surveyed for this chapter. While governments can either provide direct loans to businesses or operate a co-sharing scheme through which the risks of default are shared with commercial lenders, the vast majority of these countries provide direct loans to home country firms in connection with outward FDI. In most cases, firms have the option of obtaining loans denominated in either the domestic currency or a foreign currency.

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<sup>216</sup> IE Singapore, “International Business Fellowship Executive Programme,” available at: <http://www.iesingapore.gov.sg/Assistance/Global-Company-Partnership/Manpower-Development/International-Business-Fellowship-Executive-Programme> (last visited October 4, 2013).

<sup>217</sup> IE Singapore, “Customised Training Programmes for Internationalisation,” available at: <http://www.iesingapore.gov.sg/Assistance/Global-Company-Partnership/Manpower-Development/Customised-Training-Programmes-for-Internationalisation> (last visited October 4, 2013).

<sup>218</sup> Ministry of Finance and Ministry of Commerce of the People’s Republic of China, “Circular on the Declaration of Special Funds for the Foreign Trade and Technical Cooperation for the Year of 2010,” available at: <http://www.cqgo.org.cn/UIlayer/web/ShowArticle.aspx?ArticleID=745> (last visited February 12, 2013), translated in Lutz-Christian Wolff, “China’s outbound investment regime,” in Lutz-Christian Wolff, ed., *China Outbound Investments: A Guide to Law and Practice* (Hong Kong: CCH), p. 68.

<sup>219</sup> Spring Singapore, “Study on SME Internationalisation: Best Practices Across Selected APEC Economies,” 2011, *op. cit.*, p. 62.

### (i) Concessional loans

China, Italy, Japan, the Republic of Korea, and Taiwan Province of China offer concessional loans to home country firms. These are loans “extended on terms substantially more generous than market loans. The concessionality is achieved through interest rates below those available on the market or by grace periods, or a combination of these.”<sup>220</sup> For example, in 2004, China’s National Development and Reform Commission<sup>221</sup> and the Export-Import Bank of China announced that the latter “would earmark a portion of its budget for OFDI projects with at least a 2% interest rate discount and possibly other preferential lending terms,” with the Ministry of Finance financing the subsidy.<sup>222</sup>

The SME Unit of the Japan Finance Corporation provides Loans for Overseas Investment to support the internationalization of Japanese SMEs, including through OFDI.<sup>223</sup> A study by Spring Singapore, in collaboration with the Japanese Ministry of Economy, Trade and Industry and the Small and Medium Enterprise Agency, indicated that the Japan Finance Corporation loans are offered to SMEs at concessionary interest rates.<sup>224</sup>

The Japan Bank for International Cooperation offers overseas investment loans at interest rates that are linked to its cost of funding. The standard interest rate for a 10-year overseas investment loan in Japanese Yen with lump-sum repayment upon maturity is 0.875%.<sup>225</sup> Where investments contribute to the “acquisition of strategically important natural resources” or help to improve “the international competitiveness of Japanese industries”, they benefit from a special interest rate that ranges between 0.80 and 1.00%.<sup>226</sup> It offers loans that cover up to 60% of the overseas investment loans, but increases this coverage to 70% where the loan is resource-related. Furthermore, “SMEs are eligible for preferential interest rates and other favorable loan conditions.”<sup>227</sup>

Even where the interest rate on loans is not lower than what is offered in the market by private financial institutions, loans from the state often allow for more generous terms, such as generous grace periods of up to three years, which is typically not the case when commercial banks make loans.

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<sup>220</sup> OECD, “Glossary of Statistical Terms: Concessional Loans,” available at: <http://stats.oecd.org/glossary/detail.asp?ID=5901> (last visited February 10, 2013).

<sup>221</sup> The NDRC is a Chinese state agency with broad economic policymaking authority. See NDRC, “Main functions of the NDRC,” available at: <http://en.ndrc.gov.cn/mfndrc/default.htm> (last visited February 10, 2013).

<sup>222</sup> OECD, *Investment Policy Reviews: China 2008* (Paris: OECD, 2008), p. 91, available at: <http://www.oecd.org/investment/investmentfordevelopment/41792683.pdf> (last visited February 10, 2012).

<sup>223</sup> Japan Finance Corporation, Loan Programs, available at: [http://www.jfc.go.jp/n/english/sme/loan\\_finance.html](http://www.jfc.go.jp/n/english/sme/loan_finance.html) (last visited February 13, 2013).

<sup>224</sup> Spring Singapore, “Study on SME Internationalisation: Best Practices Across Selected APEC Economies, 2011,” *op. cit.*, p. 130.

<sup>225</sup> JBIC, “Annual Report 2012,” *op. cit.*, p. 97.

<sup>226</sup> JBIC, “Annual Report 2012,” *op. cit.*

<sup>227</sup> JBIC, “Annual Report 2012,” *op. cit.*

The Korea Eximbank offers loans to Korean companies planning to invest overseas under its Overseas Investment Credit program. While it is not clear whether or not the interest rate on such loans is more favorable than what is offered by private financial institutions, the maximum repayment term is 30 years and includes a three-year grace period. To qualify for a loan, a company must have more than three years of experience in that field of business. This HCM does not seem to be restricted to any particular industries.<sup>228</sup> The loans can be used for a Korean company to extend loans as long-term funds for ventures outside Korea to foreign companies in which they hold an equity stake, or to make an equity investment in foreign companies.<sup>229</sup> The credit provided by the Korea Eximbank covers up to 90% of the funds required for a foreign investment if the applicant is a Korean SME. For all other Korean companies, the HCM covers up to 80% of the funds required for a foreign investment.

In 2009, the Korea Eximbank initiated a program that aims to nurture, over a period of ten years, 100 “Hidden Champions” – “[g]lobal SMEs that export more than USD 300 million annually and whose global market shares rank among the top five in their respective sectors; or whose sales revenues exceed KRW 1 trillion, of which more than 50% consist of exports.”<sup>230</sup> Under this program, these Hidden Champions can obtain overseas investment credits at preferred interest rates, credit allowances that are up to 10% higher, unsecured loans, customized financing services, streamlined processes for loan approvals, revolving credit facilities specially tailored to their needs, and an “integrated yearly revolving credit line”.<sup>231</sup> The purpose of the Hidden Champion Initiative is to “incubate” Korean SMEs with strong growth potential and to promote “an environment of sustainable and balanced growth in which upwardly mobile SMEs can play a robust supporting role in the Korean economy.” The amount of financing dedicated to SMEs under the Hidden Champion Initiative has increased with successive years. Overseas investment financing alone rose from approximately US\$ 79 million in 2010 to US\$ 580 million in 2011.<sup>232</sup> This is part of the government’s attempt to address the “disproportionate dominance of large companies” in the country’s export sector, to the detriment of SMEs and the “middle layer of the national economy.”<sup>233</sup>

The Belgian Corporation for International Investment grants long-term loans “for terms of five-to-ten years, with a maximum grace period of three years”, with fixed or variable interest rates determined according to market conditions.<sup>234</sup> The Belgian HCM therefore does not appear to

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<sup>228</sup> According to the Korea Eximbank website, “[a]lmost all sectors are eligible” for Overseas Investment Credit. Korea Eximbank, Financial Services FAQ, available at: [http://www.koreaexim.go.kr/en/bbs/faq/view.jsp?no=9755&bbs\\_code\\_id=1316752774208&bbs\\_code\\_tp=BBS\\_8&code\\_tp=F03\\_524&code\\_tp\\_up=F03&code\\_tp\\_nm=TA;req\\_pg](http://www.koreaexim.go.kr/en/bbs/faq/view.jsp?no=9755&bbs_code_id=1316752774208&bbs_code_tp=BBS_8&code_tp=F03_524&code_tp_up=F03&code_tp_nm=TA;req_pg) (last visited February 15, 2013).

<sup>229</sup> Korea Eximbank, “Overseas Investment Credit,” available at: [http://www.koreaexim.go.kr/en/banking/overseas/credit\\_01.jsp](http://www.koreaexim.go.kr/en/banking/overseas/credit_01.jsp) (last visited February 10, 2013).

<sup>230</sup> Korea Eximbank, “Hidden Champion Initiative,” available at: <http://www.koreaexim.go.kr/en/banking/hidden.jsp> (last visited March 5, 2013).

<sup>231</sup> Korea Eximbank, “Hidden Champion Initiative,” *op. cit.*

<sup>232</sup> Korea Eximbank, “Annual Report 2011,” available at: <http://www.koreaexim.go.kr/en/exim/investor/report.jsp> (last visited March 5, 2013), p. 25.

<sup>233</sup> Korea Eximbank, “Hidden Champion Initiative,” available at: <http://www.koreaexim.go.kr/en/banking/hidden.jsp> (last visited March 5, 2013).

<sup>234</sup> BMI-SBI, “Products,” *op. cit.*

provide cheap financing to Belgian firms at low interest rates, but may still allow Belgian firms to take advantage of more generous grace periods on the repayment of their loans.

Italy's SIMEST offers Italian firms concessional loans to finance feasibility studies (including consultants' fees and salaries for in-house employees) and technical assistance (including all costs from training, travel and other expenses associated with an FDI project), with the quanta of these loans capped at € 100,000 for studies on commercial investments, € 200,000 for studies on investments in production and € 300,000 for technical assistance.<sup>235</sup> The interest rate on this type of loan is fixed at just 15% of the reference rate, provided it is not less than 0.50% per annum.<sup>236</sup> SIMEST also provides concessional loans at the same rate for some types of investments where an Italian firm is seeking to establish a presence in a new market not in the European Union; expenses eligible for this loan include the cost of establishing and maintaining permanent facilities in the new market (which encompasses, *inter alia*, warehouses, offices and showrooms).<sup>237</sup> Another financial HCM in Italy allows Italian businesses to gain access to loans at low interest rates (the government pays for 50% of the interest that is to be paid to the lending institution) if SIMEST has invested in the equity capital of a firm's foreign affiliate (see also the discussion in the section on equity participation below).<sup>238</sup>

Governments utilize concessional loan conditions as a means of pursuing specific national policies, whether they are to encourage investment in certain industries in which the government has a specific strategic interest, or even to nurture SMEs with international competitive advantages or significant growth potential.

#### (ii) Non-concessional loans

Non-concessional loans are loans offered by the relevant home country agency at market rates, with conditions identical to those that would be offered by commercial lenders.

The information on loans provided by home country governments is often vague, making it difficult to tell whether or not the terms of a particular loan are more advantageous than what is available in the market. However, even if home countries do not provide loans with concessionary terms, home country firms may still derive a financial advantage where a firm would otherwise be unable to obtain a loan in the market. For instance, it is often the case that SMEs find it difficult to obtain long-term loans from commercial lenders. Particularly when the general economic outlook seems bleak, it may be easier for these SMEs successfully to obtain loans from the government even if the terms offered by the government are not particularly advantageous. By being able to access financing for OFDI where it would otherwise not be

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<sup>235</sup> SIMEST, "Financing for pre-feasibility and feasibility studies and technical support," available at: <http://www.simest.it/page-en.php?id=15> (last visited June 23, 2013).

<sup>236</sup> SIMEST, "Financing for pre-feasibility and feasibility studies and technical support," *op. cit.*

<sup>237</sup> SIMEST, "Financing for foreign markets penetration programmes," available at: <http://www.simest.it/page-en.php?id=16> (last visited June 23, 2013).

<sup>238</sup> SIMEST, "SIMEST shareholdings in the capital stock of non EU companies," available at: <http://www.simest.it/page-en.php?id=10> (last visited June 23, 2013).



available, home country firms obtain a direct financial benefit from the state's provision of a non-concessional loan.

In other cases, it is clear that the loans are provided at market rates. The Overseas Private Investment Corporation, the United States development finance institution, is an example of a state agency offering loans without concessionary terms. It works with United States companies in the private sector to help them “gain footholds in emerging markets”,<sup>239</sup> offering medium- to long-term loans of between US\$ 350,000 and US\$ 250 million per project.<sup>240</sup> As a matter of policy, it does not support more than 75% of a total investment, and terms of the loan “typically provide for a final maturity of three to 15 years, including a suitable grace period during which only interest is payable.”<sup>241</sup> Interest rates for these loans are not concessionary because the Overseas Private Investment Corporation “supports private sector investments in financially viable projects.”<sup>242</sup> Interest rates are “generally based on an underlying cost of capital (comparable U.S. Treasury notes or other U.S. Government-guaranteed issues of similar maturity) plus a risk-premium of between 2.0 percent and 6.0 percent, depending on OPIC's assessment of the commercial and political risks involved.”<sup>243</sup> Even though the rates are not concessionary, its loans create financial advantages for United States businesses with projects in emerging markets because “conventional financial institutions often are reluctant or unable to lend on [a medium- to long-term basis to investment projects in emerging markets].”<sup>244</sup>

### (iii) Structured finance

Some countries go beyond providing straightforward term loans, employing a variety of credit facilities depending on the specific needs of each business. The Export-Import Bank of India (India Eximbank) offers equity and debt financing for the acquisition of overseas businesses, including structured financing options for leveraged buy-outs.<sup>245</sup> In the United States, the Overseas Private Investment Corporation offers structured financing options to United States businesses for large-scale, capital-intensive projects in emerging markets.<sup>246</sup> Spain's Instituto de Crédito Oficial supports overseas investments by Spanish companies by granting long-term loans

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<sup>239</sup> OPIC, “Who we are,” available at: <http://www.opic.gov/who-we-are/overview> (last visited February 18, 2013).

<sup>240</sup> OPIC, “Financing Products,” available at: <http://www.opic.gov/what-we-offer/financial-products/financing-techniques> (last visited February 18, 2013).

<sup>241</sup> OPIC, “Terms,” available at: <http://www.opic.gov/what-we-offer/financial-products/terms> (last visited February 18, 2013).

<sup>242</sup> OPIC, “Financing Details,” available at: <http://www.opic.gov/what-we-offer/financial-products/financing-details> (last visited February 18, 2013).

<sup>243</sup> OPIC, “Fees and Costs,” available at: <http://www.opic.gov/what-we-offer/financial-products/fees-costs> (last visited February 18, 2013).

<sup>244</sup> OPIC, “Financial Products,” available at: <http://www.opic.gov/what-we-offer/financial-products> (last visited February 18, 2013).

<sup>245</sup> Export-Import Bank of India, “Overseas Investment Finance,” available at: <http://www.eximbankindia.com/oif.asp> (last visited February 12, 2013).

<sup>246</sup> OPIC, “Financial Products,” available at: <http://www.opic.gov/what-we-offer/financial-products> (last visited February 12, 2013).

under its Structured Finance Programme or Corporate Finance Programme.<sup>247</sup> On top of providing long-term loans, the Belgian Corporation for International Investment also offers financial products that seek to link repayment to the success of an investment: subordinated loans may incorporate a variable component to the interest rate; convertible loans include options allowing the Corporation to convert them into shares.<sup>248</sup> Singapore's Internationalisation Finance Scheme offers asset-based financing, structured loans or bankers' guarantees, depending on the specific needs of a business, with the condition that the purpose of a loan must be to support firms' overseas expansion (e.g., by increasing their fixed asset investment abroad or financing their overseas projects to obtain loans).<sup>249</sup> Asset-based financing allows companies to borrow to finance the purchase or construction of factories overseas, or purchase fixed assets for use abroad; structured loans can be utilized to finance the working expenses of secured overseas projects; advance payment guarantees, performance guarantees or tender bond guarantees can also be issued for secured overseas projects.

Notably, on top of providing structured financing options for large, capital-intensive projects, the United States' Overseas Private Investment Corporation also provides financing to private equity funds that focus primarily on investing in emerging markets. The Corporation does not usually participate in these funds as an equity investor or limited partner. Rather, it provides financing in the form of a senior secured loan that ranges between US\$ 35 million and US\$ 150 million per fund, typically providing about a third of a fund's total capital.<sup>250</sup> These loans are securitized and sold in the capital markets to institutional investors, with the United States Government backing the certificates of participation in these loans with a "full faith and credit guaranty"; to be eligible for this financing, funds should have "U.S. participation in either the ownership of the fund manager/general partner, or in the equity capital of the fund", and proposals to the Overseas Private Investment Corporation "should demonstrate that the fund manager/general partner will be majority beneficially owned by U.S. Persons, or that the fund manager/general partner will seek to raise equity capital from U.S. Persons equivalent to 25% of OPIC's expected commitment."<sup>251</sup>

#### (iv) Risk-sharing arrangements

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<sup>247</sup> ICO, "Direct Financing Programmes," available at: <http://www.ico.es/web/contenidos/5/4/9022/index.html> (last visited February 12, 2013).

<sup>248</sup> BMI-SBI, "Products," available at: <http://www.bmi-sbi.be/en/produits.html> (last visited February 10, 2013).

<sup>249</sup> IE Singapore, "Internationalisation Finance (IF) Scheme," available at: <http://www.iesingapore.gov.sg/Assistance/Global-Company-Partnership/Access-to-Financing/Internationalisation-Finance-Scheme> (last visited October 4, 2013).

<sup>250</sup> OPIC, "FAQs," available at: <http://www.opic.gov/what-we-offer/investment-funds/calls-for-proposals/global-engagement-faqs> (last visited June 23, 2013). For a full list of funds that OPIC has invested in, see OPIC, Full List of Funds, available at: <http://www.opic.gov/what-we-offer/investment-funds/full-list-of-funds> (last visited June 24, 2013).

<sup>251</sup> OPIC, "FAQs," *op. cit.*

State institutions sometimes opt to co-finance loans with other international organizations. For example, in 2009, DEG, the German development finance institution, arranged for debt financing of € 132 million, of which € 82.3 million was financed by the European Investment Bank, and € 18 million by the Development Bank of South Africa. The financing was extended to Schwenk Zement KG, a medium-sized German enterprise that produces cement and other building materials, for the construction of a cement plant in Namibia.<sup>252</sup>

State institutions may also choose to extend loans in cooperation with private financial institutions. In Taiwan Province of China, the Taiwan Eximbank has the option to extend loans on either a “sole lender” basis or in syndication with other banks.<sup>253</sup> In Singapore, financing under the Internationalisation Finance Scheme is provided “through a system of co-sharing of default risks between IE Singapore and Participating Financial Institutions (PFIs).”<sup>254</sup>

Through syndication, a government is able to leverage private capital (or in the German example above, European Union funds) to finance home country firms’ foreign investments. Risk-sharing arrangements like the one practiced in Singapore essentially operate as financial guarantees (see the discussion below) that improve the likelihood that businesses will be able to access lines of credit for overseas investments. As is stated in the brochure for the Internationalisation Finance Scheme, “[o]verseas ventures are often associated with higher risks. This makes it a challenge for companies who are looking at increasing their fixed asset investment abroad or financing their overseas projects to obtain loans.”<sup>255</sup> By bearing some of the lender’s risk of default, the government makes it more likely that financial institutions will extend loans to smaller business enterprises.

### iii. **Financial guarantees**

A financial guarantee is essentially an instrument guaranteeing lenders’ repayment of the capital and interest they are owed. It operates in the same manner as a risk-sharing scheme where the state shares default risks with the private lender. By providing financial guarantees that protect the repayment of the loans to the financial institutions, governments can enhance home country firms’ access to credit. This measure is a relatively common one. Although the terms of the financial guarantees provided differ slightly among countries, financial guarantees are offered by a large number of the countries surveyed in this chapter, including both developed countries and emerging markets. Belgium, China, Germany, Italy, Japan, Malaysia, the Republic of Korea,

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<sup>252</sup> DEG, “Schwenk company to open works in Africa” (November 13, 2009), available at: [https://www.kfw.de/KfW-Group/Newsroom/Aktuelles/Pressemitteilungen/Pressemitteilungen-Details\\_5869.html](https://www.kfw.de/KfW-Group/Newsroom/Aktuelles/Pressemitteilungen/Pressemitteilungen-Details_5869.html) (last visited April 13, 2013).

<sup>253</sup> Export-Import Bank of the Republic of China, “Overseas Investment Credit,” available at: <http://www.eximbank.com.tw/en-us/BankServices/Loans/Pages/OIC.aspx> (last visited February 12, 2013).

<sup>254</sup> IE Singapore, “Internationalisation Finance Scheme,” available at: [http://www.iesingapore.gov.sg/wps/wcm/connect/88fbc0004ad50175b9e2bb6ba6b73dba/IFS-PDF\\_file\\_attached\\_to\\_the\\_IE\\_website20120404.pdf?MOD=AJPERES](http://www.iesingapore.gov.sg/wps/wcm/connect/88fbc0004ad50175b9e2bb6ba6b73dba/IFS-PDF_file_attached_to_the_IE_website20120404.pdf?MOD=AJPERES) (last visited February 12, 2013).

<sup>255</sup> IE Singapore, “Internationalisation Finance Scheme,” *op. cit.*

Singapore, Spain, and the United States all offer some form of financial guarantee that serves to improve overseas investors' access to credit.

For example, Italy's export credit agency, SACE, provides Italian SMEs conducting investment activities abroad with financial guarantees covering up to 70% of a loan. This guarantee is provided at no additional cost to the SME, as the "SACE fee is included as a portion of the spread paid by the company to the bank."<sup>256</sup> The portion of the risk guaranteed by SACE has a zero-risk rating under the Basel I and Basel II global regulatory standards on bank capital adequacy, making it more likely that banks will be willing to extend credit to Italian SMEs.<sup>257</sup>

The German and United States development finance institutions, DEG and the Overseas Private Investment Corporation, provide not only direct loans to private companies for operations in emerging economies but also financial guarantees for private sector borrowers.<sup>258</sup> Export Development Canada's Export Guarantee Program guarantees up to 100% of loans provided by financial institutions where Canadian companies are making direct investments abroad or are looking to set up an operating line of credit for their foreign subsidiary.<sup>259</sup> Unlike Italy's financial guarantees, the financial guarantees offered by France, Germany, the United States, and Canada require the beneficiary firms to pay a fee.

#### iv. **Equity participation**

The fourth category of financial HCMs consists of equity participation. It is a common HCM employed by the majority of the home countries surveyed. Recall that, in this chapter, HCMs are defined as measures that directly support and encourage OFDI. An equity participation HCM therefore refers to equity participation by a home country in a home country firm's foreign affiliate or a home country firm itself, on the condition that the firm engages in OFDI.<sup>260</sup>

In most cases, the responsible agency offering this HCM takes an equity stake in a foreign affiliate, rather than in the parent firm in the home country. For instance, India Eximbank offers

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<sup>256</sup> SACE, "Internationalization Guarantee," available at: [http://www.sace.it/GruppoSACE/content/en/consumer/products/financial\\_guarantee/internazionalization\\_guarantee/index.html?tab=1](http://www.sace.it/GruppoSACE/content/en/consumer/products/financial_guarantee/internazionalization_guarantee/index.html?tab=1) (last visited February 12, 2013).

<sup>257</sup> SACE, "Internationalization Guarantee," *op. cit.*

<sup>258</sup> DEG – Financial Products, available at: <https://www.deginvest.de/International-financing/DEG/Unser-Angebot/Finanzierung-und-Beratung/Finanzierungsprodukte/> (last visited April 12, 2013); OPIC – Financial Products, available at: <http://www.opic.gov/what-we-offer/financial-products> (last visited February 18, 2013).

<sup>259</sup> EDC, "Export Guarantee Program," available at: <http://www.edc.ca/EN/Our-Solutions/Financing/Documents/brochure-export-guarantee-program.pdf> (last visited February 12, 2013).

<sup>260</sup> Even when a home country acquires equity in one of the country's firms and there is no explicit condition of outward FDI in order to qualify for a HCM, such participation would strengthen the financial position of the enterprise, thereby putting it in a better position to engage in OFDI. While there are examples of such measures, this chapter's primary focus is on financial HCMs that confer a direct specific advantage on home country firms in connection with outward FDI. Measures that are not conditioned on outward investment are too indirect to be classified as financial HCMs in the context of this chapter, even if they do create specific financial advantages for home country firms.

direct equity investments in the overseas joint venture or wholly owned subsidiary of Indian companies.<sup>261</sup> This mode of equity participation seems to be the most prevalent and is also practiced by the respective state agencies in Belgium, Germany, Italy, Japan, and Spain.

Spain's Compañía Española de Financiación del Desarrollo (COFIDES), which is 61% state-owned, provides financial support for outward FDI to further Spanish interests. It aims to contribute "both to host country development and the internationalization of Spanish enterprise and the Spanish economy."<sup>262</sup> COFIDES also manages the Fondo para inversiones en el exterior (FIEX) and the Fondo para operaciones de inversión en el exterior de la pequeña y mediana empresa (FONPYME), trust funds that can be used "to financially support investment projects in any foreign country."<sup>263</sup> The FIEX fund, with a capital endowment of € 747 million in 2012, provides between € 1 million and € 25 million of equity or quasi-equity funding for "viable private projects undertaken abroad and involving some manner of Spanish interest;"<sup>264</sup> FONPYME, a separate fund for Spanish SMEs, had a capital endowment in 2012 of € 45 million; the quantum of equity or quasi-equity financing for SMEs ranges between € 250,000 and € 5 million per operation.<sup>265</sup> COFIDES also follows the principle of "shared risk," where it "never assumes greater risk in a project than the sponsors themselves."<sup>266</sup> These HCMs may be utilized by all companies, whether Spanish or foreign, as long as there is some kind of Spanish interest involved. Other factors that are taken into account when assessing project proposals are "[t]echnical, commercial and financial viability," "[s]ponsors' commitment to the project" (evaluated based on sufficient capitalization), "[e]xistence of suitable mechanisms to mitigate political and commercial risk," "[f]avourable atmosphere" in the host country, "[s]uitable management of the environmental and social aspects of the project, and [g]ood corporate governance."<sup>267</sup>

Through the Japan Bank for International Cooperation, the Japanese Government provides a measure allowing for direct equity participation in overseas projects, foreign affiliates or investment funds. The Japan Bank for International Cooperation will even invest in the equity of a fund in consortium with Japanese firms to form an international fund with other investors. Each equity investment is capped at 25%, subject to the proviso that the Bank does not become the single largest Japanese shareholder.<sup>268</sup> While "investments have to be made, in principle, in developing countries," it is permitted to support investments in developed countries as long as

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<sup>261</sup> India Eximbank, "Overseas Investment Finance," available at: <http://www.eximbankindia.com/oif.asp> (last visited February 17, 2013).

<sup>262</sup> COFIDES, "About Us," available at: <http://www.cofides.es/english/2aboutus.html> (last visited February 17, 2013). Note that COFIDES is also Spain's development finance institution.

<sup>263</sup> COFIDES, "Eligible countries," available at: <http://www.cofides.es/english/3countries.html> (last visited February 19, 2013).

<sup>264</sup> COFIDES, "FIEX," available at: <http://www.cofides.es/english/2fiex.html> (last visited February 17, 2013).

<sup>265</sup> COFIDES, "FONPYME," available at: <http://www.cofides.es/english/2fonpyme.html> (last visited February 17, 2013).

<sup>266</sup> COFIDES, "Project assessment criteria," available at: <http://www.cofides.es/english/3criteria.html> (last visited February 19, 2013).

<sup>267</sup> *Ibid.*

<sup>268</sup> JBIC, "Equity Participations," available at: <http://www.jbic.go.jp/en/finance/capital/index.html> (last visited February 17, 2013).

they contribute to “the overseas development and acquisition of resources that are strategically important for Japan.” Alternatively, investments in developed countries are also permitted if they contribute to “the maintenance and improvement of the international competitiveness of [selected] Japanese industries,” which include nuclear power generation, high-speed railways and advanced telecommunications networks.<sup>269</sup>

In Italy, SIMEST can acquire up to 49% of the equity capital of a non-EU foreign affiliate, holding such equity for up to eight years.<sup>270</sup> The conditions of the repurchase of equity held by SIMEST are agreed on at the outset of an investment.<sup>271</sup> In conjunction with such an investment by SIMEST, the Italian company also gains access to concessional financing – SIMEST provides “interest rate support” by subsidizing half of the interest that has to be paid to the lending institution.<sup>272</sup> The Italian Government has also set up the Venture Capital Fund, which is authorized to invest in foreign affiliates of Italian companies in specific geographic regions, so long as the overall shareholding of the Venture Capital Fund and SIMEST does not exceed 49% of the foreign affiliates’ registered share capital.<sup>273</sup> Equity participation by the Venture Capital Fund costs Italian companies a fee (the European Central Bank rate plus 0.5%).<sup>274</sup>

DEG, the German development finance institution, can take a direct equity participation in the foreign affiliate of a German company. DEG’s policy is to take a minority stake in such a company and, in some cases, voting rights and a seat on the board of directors.<sup>275</sup>

Belgium also provides for direct equity participation in foreign affiliates of home country firms through the Belgian Corporation for International Investment. It always takes minority stakes, requiring “the Belgian partner to retain the majority shareholding and the majority of the voting rights” in the foreign project.<sup>276</sup>

The examples of equity participation HCMs given above show that state agencies virtually always take only minority stakes in foreign affiliates.<sup>277</sup>

The government agencies also insist on clearly defined exit conditions before making investments. While most HCMs are silent on the kind of exit conditions that must apply, given that SMEs rather than large corporations are most likely to utilize these HCMs, exit opportunities for the government will most probably involve a parent company’s repurchasing the shares from the state agency. This is the practice in Spain, where these shareholdings are “subject to a

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<sup>269</sup> JBIC, “Equity Participations,” *op. cit.*

<sup>270</sup> SIMEST, SIMEST shareholdings in the capital stock of non EU companies, available at: <http://www.simest.it/page-en.php?id=10> (last visited June 23, 2013).

<sup>271</sup> SIMEST, “SIMEST shareholdings in the capital stock of non EU companies,” *op. cit.*

<sup>272</sup> SIMEST, “SIMEST shareholdings in the capital stock of non EU companies,” *op. cit.*

<sup>273</sup> SIMEST, Venture capital fund, available at: <http://www.simest.it/page-en.php?id=11> (last visited June 23, 2013).

<sup>274</sup> SIMEST, “Venture capital fund,” *op. cit.*

<sup>275</sup> DEG, “Financial Products,” available at: <https://www.deginvest.de/International-financing/DEG/Unser-Angebot/Finanzierung-und-Beratung/Finanzierungsprodukte/> (last visited April 12, 2013).

<sup>276</sup> BMI-SBI, “Products,” *op. cit.*

<sup>277</sup> DEG, BMI-SBI and JBIC all expressly require that their equity investment be a minority stake.

repurchase agreement with the Spanish investor.”<sup>278</sup> In Belgium, on top of requiring “[c]learly defined exit terms, related to the value created by the project” to be negotiated at the outset, the equity share is only held by the Belgian Corporation for International Investment for a period of five-to-ten years.<sup>279</sup>

Several state agencies express their desire to keep their involvement in day-to-day business operations and management to a minimum.<sup>280</sup> On the other hand, countries such as Belgium and Germany explicitly require some board representation and voting rights as a condition of an investment.<sup>281</sup> However, whether this assures the state agency effective control over its investment depends on whether it gets seats on the board of a parent company or in the foreign affiliates, and on the number of seats it obtains.

From a firm’s perspective, equity financing has an advantage over loans because there is typically no need for regular repayment. The usual downside of relying on equity financing from an investor is that the original business owners have to surrender some control of their business to the investor. However, where the equity is coming from the state, this seems to be less of a concern. While equity participation HCMs may be tied to board representation, it is likely that the state-controlled institution that takes an equity stake in the business will be a less proactive shareholder than a private investor. Moreover, the evidence indicates that many HCMs providing for equity participation in connection with OFDI make it clear that governments do not want to take a controlling stake in a foreign affiliate.

There are also advantages that stem from the fact that an official state agency is an equity investor in a foreign affiliate. The Japan Bank for International Cooperation explains that leveraging its “long-cultivated ties with [host country] governments and its position as an official financing institution” could help to mitigate political risk in the host country.<sup>282</sup> Investors can also draw on its knowledge of host country economies and consult it for assessments of environmental and social considerations that may be relevant to the investment project. The Belgian Corporation for International Investment similarly emphasizes that its expertise and experience, built up over 40 years of global operations, are useful for businesses in the early stages of their internationalization process.<sup>283</sup>

### **c. Criteria for eligibility**

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<sup>278</sup> COFIDES, “Investment Strategy: Products,” available at: <http://www.cofides.es/english/4products.html> (last visited February 17, 2013).

<sup>279</sup> BMI-SBI, “Products,” *op. cit.*

<sup>280</sup> See e.g., JBIC and COFIDES.

<sup>281</sup> DEG, “Financial Products,” available at: <https://www.deginvest.de/International-financing/DEG/Unser-Angebot/Finanzierung-und-Beratung/Finanzierungsprodukte/> (last visited April 12, 2013); BMI-SBI, “Products,” available at: <http://www.bmi-sbi.be/en/products.html> (last visited February 17, 2013).

<sup>282</sup> JBIC, “Equity Participations,” available at: <http://www.jbic.go.jp/en/finance/capital/index.html> (last visited February 17, 2013).

<sup>283</sup> BMI-SBI, “Products,” *op. cit.*

## i. Nationality

A large number of outward investment agencies do not clarify whether there are specific nationality requirements that have to be met in order to benefit from financial HCMs. Where specific nationality requirements are not mentioned, it would seem as if locally incorporated companies owned by foreign citizens or foreign companies would technically be able to benefit from financial HCMs. However, this might well play out differently in practice because virtually all companies are subject to an approval process by the relevant home country agencies in order to benefit for support. Given that the process is often discretionary on the part of the home country, if an assessment demonstrates that assistance would not bring benefits to the home country's economy, the application for financial support might be denied.

It is interesting to note that many of the financial HCMs offered by Spain do not have a specific nationality requirement. In many cases, it is sufficient that the investment project involves some manner of Spanish interest.<sup>284</sup> Phrased this broadly, such a guideline for eligibility can be seen as giving the home country agency greater flexibility to grant advantages to projects that will bring about benefits to the home economy; on the other hand, the greater discretion also creates problems such as a lack of transparency.

Some HCMs do, however, have elements of specific nationality requirements for locally incorporated business entities. For example, the United States' Overseas Private Investment Corporation requires entities incorporated in the United States to have at least 25% United States ownership. On the other hand, if the enterprise applying to OPIC for support is incorporated outside the United States, United States shareholders must hold majority ownership. Where individuals, rather than business associations, are applying for OPIC financing, United States citizens, lawful permanent residents and non-profit organizations organized in the United States are eligible.<sup>285</sup> On the other hand, some HCMs do not have specific ownership requirements for locally incorporated business entities. The Internationalisation Finance Scheme in Singapore seems to require only that the company be Singapore-based, registered with the Accounting and Corporate Regulatory Authority and have at least three strategic business functions in Singapore.<sup>286</sup> However, this HCM has the additional requirement that the overseas business that is being supported "complement[s] the Singapore company's core operations and result[s] in economic spin-offs to Singapore."<sup>287</sup>

One distinctive financial HCM that stands out is the Malaysia-Singapore Third Country Business Development Fund, which provides grants to Malaysian and Singaporean companies "to expand

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<sup>284</sup> See generally the instruments offered by COFIDES at COFIDES, Financial instruments, available at: <http://www.cofides.es/english/4instruments.html> (last visited June 23, 2013).

<sup>285</sup> OPIC, "Finance Eligibility Checklist," available at: <http://www.opic.gov/doing-business-us/finance-eligibility-checklist> (last visited February 19, 2013).

<sup>286</sup> IE Singapore, "Internationalisation Finance Scheme," *op. cit.* "Strategic business functions" refer to activities such as banking and finance, marketing and business planning, procurement, logistics, training, personnel management, investment planning/coordination, research and development, design, technical support, manufacturing, and other value-added activities.

<sup>287</sup> IE Singapore, "Internationalisation Finance Scheme," *op. cit.*



in the global arena together” by taking up “investment and business opportunities in ‘third countries’ outside of Malaysia and Singapore.”<sup>288</sup> The Fund was co-founded by Malaysia and Singapore and co-funded by International Enterprise Singapore (IE Singapore) and the Malaysian Industrial Development Authority (MIDA).<sup>289</sup> As a result of history and geography, the two countries share strong economic ties. This financial HCM does not only encourage outward FDI; by requiring the feasibility studies to be jointly undertaken by companies from both nations, it effectively makes economic cooperation between businesses in the two countries a condition of eligibility, thereby serving to strengthen economic ties between Malaysia and Singapore.

## ii. Sectors

Many HCMs have an industry-specific focus. The Korea Eximbank singles out “priority sectors” for financial support for outward FDI – green industries,<sup>290</sup> “new growth industries” (including robotics, defense, biomedicine, high-speed trains)<sup>291</sup> and natural resources.<sup>292</sup> The Japan Bank for International Cooperation’s equity participation in foreign affiliates of Japanese firms in developed countries is restricted to certain industries that are deemed to be strategically important for Japan, with a particular focus on natural resources and energy industries.<sup>293</sup> On top of encouraging resource-seeking FDI, Japan supports infrastructure projects associated with resource development, alternative energy industries and high-technology industries like advanced telecommunications.<sup>294</sup>

In China, the China-Africa Development Fund provides financial support to Chinese enterprises that either already have operations in Africa or plan to invest in Africa by offering equity or quasi-equity participation. The Fund can also act as a “fund of funds”, investing in other funds that invest in Africa; it also provides institutional support to Chinese companies in the form of management, consulting and financial advisory services. The Fund’s focus is on agriculture, manufacturing, infrastructure, and natural resources.

Financial HCMs that target specific industries can be designed strategically by a government to achieve broader national objectives. Japan and the Republic of Korea, for instance, place

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<sup>288</sup> MIDA and IE Singapore, “Malaysia-Singapore Third Country Business Development Fund,” available at: [http://www.mida.gov.my/env3/uploads/Publications\\_pdf/MALAYSIA-SINGAPORE\\_ThirdCountry/MSBDF\\_brochure09.pdf](http://www.mida.gov.my/env3/uploads/Publications_pdf/MALAYSIA-SINGAPORE_ThirdCountry/MSBDF_brochure09.pdf) (last visited January 26, 2013).

<sup>289</sup> MIDA and IE Singapore, “Malaysia-Singapore Third Country Business Development Fund,” *op. cit.*

<sup>290</sup> Korea Eximbank, “Green finance,” available at: <http://www.koreaexim.go.kr/en/banking/green.jsp> (last visited 26 January 2013).

<sup>291</sup> Korea Eximbank, “New Growth Industry Finance,” available at: <http://www.koreaexim.go.kr/en/banking/new.jsp> (last visited January 26, 2013).

<sup>292</sup> Korea Eximbank, “Natural Resources Development Credit,” available at: <http://www.koreaexim.go.kr/en/banking/Natural.jsp> (last visited January 26, 2013).

<sup>293</sup> JBIC, “Equity Participation,” available at: <http://www.jbic.go.jp/en/finance/capital/index.html> (last visited February 17, 2013).

<sup>294</sup> JBIC, “Energy and Natural Resource Financing,” available at: <http://www.jbic.go.jp/en/finance/resource/index.html> (last visited February 18, 2013).

emphasis on natural resources and energy industries because the country is poor of resources. Japan's continued economic growth is contingent upon access to "long-term and steady imports of energy and mineral resources, such as petroleum, natural gas and iron ore" and "stable economic relations with countries endowed with natural resources."<sup>295</sup> Moreover, the fact that natural resource development is an expensive and risky undertaking creates a greater necessity for financial support by the government. In fact, in the financial year 2011, just over 63% of the Japan Bank for International Cooperation's commitments under its Overseas Investment Loans program were dedicated to OFDI in natural resources industries.<sup>296</sup> Similarly, the Government of the Republic of Korea encourages Korean firms to pursue resource-seeking outward FDI. The Korea Eximbank provides Natural Resources Development Credits to Korean companies, foreign affiliates of Korean companies or joint ventures with Korean companies investing in oil, gas, mining, forest resource development, and agricultural development projects.<sup>297</sup>

In Spain, COFIDES, under some of its programs, offers a wide range of financial HCMs tailored to support outward investment in different industries. For example, FINSER provides financing for firms in the service sector, such as travel agencies, law firms and consultancies; FINAM provides financing for such environmentally friendly industries as renewable energy and water treatment; FINBRAND provides financing for "viable private projects sponsored by Spanish companies with a relevant "brand name," including the acquisition of foreign companies or brands, and expanding existing facilities abroad."<sup>298</sup>

Each of these instruments offers different types of financial support, as appropriate for a given industry. Financing for the service industries under FINSER comes in the form of loans of between € 250,000 and 50% of the total investments, with repayment periods of three-to-five years.<sup>299</sup> Compare this to financing for infrastructure projects under FINCONCES:<sup>300</sup> this HCM targets industries like water treatment and waste management, telecommunications, energy, and transport. Under this HCM, COFIDES does not offer loans; rather it offers only equity or quasi-equity participation, contributing up to € 30 million or half the total project investment, whichever is lower. The amount contributed by COFIDES does not exceed the promoter's contribution.

COFIDES's practice of creating a range of financial HCMs tailored to specific industries is important because it allows for specialization. Infrastructure projects in foreign countries require huge capital contributions and may require financial support for a longer period of time. Other industries (such as services) typically do not require such large sums of financial support, and

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<sup>295</sup> JBIC, "Energy and Natural Resource Financing," *op. cit.*

<sup>296</sup> JBIC, "Annual Report 2012," available at: [http://www.jbic.go.jp/en/about/business/year/2012/pdf/2012E\\_00\\_full.pdf](http://www.jbic.go.jp/en/about/business/year/2012/pdf/2012E_00_full.pdf) (last visited February 27, 2013), p. 84.

<sup>297</sup> Korea Eximbank, "Natural Resources Development Credit," available at: <http://www.koreaexim.go.kr/en/banking/Natural.jsp> (last visited April 12, 2013).

<sup>298</sup> COFIDES, "Financial Instruments," available at: <http://www.cofides.es/english/4instruments.html> (last visited January 16, 2013).

<sup>299</sup> COFIDES, "FINSER," available at: <http://www.cofides.es/english/4finser.html> (last visited February 19, 2013).

<sup>300</sup> COFIDES, "FINCONCES," available at: <http://www.cofides.es/english/4finconces.html> (last visited February 19, 2013).

any financial support can be provided for shorter time periods. If all these discrete financial HCMs were to be aggregated into one general financial HCM, the information provided would not be very helpful to applicant companies. Moreover, this practice should allow an outward investment agency's staff adequately to specialize in specific industries. This in turn should lead not only to greater efficiency in processing applications and other general administrative tasks, but also to a better appreciation of any salient developments affecting specific industries and the changing needs of relevant businesses.

Interestingly, the Export-Import Bank of Malaysia provides financing for the establishment or expansion of Malaysian restaurants overseas, on the condition that the restaurants serve "food that is traditionally and customarily consumed by Malaysians."<sup>301</sup>

Funding may even be provided to business associations rather than directly to home country firms. As already mentioned, the Canadian Trade Commissioner Service's GOA program funds national associations seeking to promote "sector-specific international business development for its members and industry at large."<sup>302</sup> Eligible activities include those that improve market access, such as market research and market intelligence reports meant to lead up to OFDI.<sup>303</sup> Business associations in a wide range of industries have been approved for GOA funding. These include business associations in the clean technology, aerospace, education, and information technology industries.<sup>304</sup>

Home countries cannot only choose to create HCMs that emphasize FDI in specific industries, but also explicitly exclude certain industries. This is commonly seen where an outward investment agency is a development finance institution. In Germany, DEG has published an Exclusion List, where "[a]s a matter of principle, financing by DEG is not possible" in cases involving, *inter alia*, gambling, weapons, munitions, hard liquors, and tobacco.<sup>305</sup> The Exclusion List also lists other public policy exclusions, such as child labor and forced labor. OPIC has a similar list of "categorically prohibited sectors."<sup>306</sup>

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<sup>301</sup> Malaysia Eximbank, "Malaysia Kitchen Financing Facility," available at: <http://www.exim.com.my/conventional-banking/malaysiakitchen-financing-facility> (last visited January 27, 2013). Thailand also offers a similar HCM for the establishment of Thai restaurants in foreign countries by Thai investors. See Export-Import Bank of Thailand, "Financial Facilities," available at: <http://www.exim.go.th/en/services/financingOP.aspx> (last visited January 27, 2013).

<sup>302</sup> The Canadian Trade Commissioner Service, "Eligibility," available at: <http://www.tradecommissioner.gc.ca/eng/funding/global-opportunities-associations/eligibility.jsp> (last visited April 12, 2013).

<sup>303</sup> The Canadian Trade Commissioner Service, "Eligibility," *op. cit.*

<sup>304</sup> The Canadian Trade Commissioner Service, "Approved GOA Recipients 2012-13," available at: <http://www.tradecommissioner.gc.ca/eng/funding/global-opportunities-associations/approved-by-sector.jsp> (last visited February 18, 2013).

<sup>305</sup> DEG, "Exclusion List," available at: <https://www.deginvest.de/migration/DEG-Startseite/Development-Finance/About-DEG/Our-Mandate/Exclusion-List.pdf> (last visited April 12, 2013).

<sup>306</sup> OPIC, "Our Investor Screener," available at: <http://www.opic.gov/doing-business-us/our-investor-screener> (last visited February 19, 2013).

### iii. Ownership

Of all the financial HCMs surveyed in the course of the research for this chapter, none explicitly favored SOEs when it comes to financial HCMs. Financial HCMs were generally directed toward home country firms, regardless of their status as private enterprises or SOEs. Even in China, where the government has historically favored large SOEs, the Government's policy appears to be shifting. In 2012, as part of the government's move to bolster the private sector, the National Development and Reform Commission and the Ministry of Finance jointly announced that the government would treat privately-owned enterprises and SOEs equally, particularly with respect to the disbursement of government funds.<sup>307</sup>

It is important to keep in mind, however, that many SOEs do not necessarily have to rely on explicit government policies in the form of financial HCMs. SOEs (as well as large firms in general) may very well benefit from easier and cheaper access to credit in the form of periodic capital injections by the state, or from state-owned banks extending concessional loans that are privately negotiated.

### iv. Firm size

Few financial HCMs are targeted specifically at big firms. However, certain types of financing, such as structured finance, are more likely to be utilized by large firms than smaller ones. OPIC's Structured Financing program, for example, is meant to support "large-scale projects that require significant amounts of capital, in such sectors as infrastructure, telecommunications, power, water, housing, airports, hotels, financial services and natural resource extraction."<sup>308</sup> Given that OPIC only contributes up to 75% of the total investment, it would be rare for an SME to be able to finance the residual 25% if the project is a large-scale infrastructure project.

On the other hand, many financial HCMs grant additional advantages to SMEs, given the importance they have in national economies and the special difficulties they face when internationalizing through FDI. For example, a study has shown that, for initial investments and subsequent projects alike, the obstacles most frequently reported were uncertainty over operating in foreign legal jurisdictions (43%), the lack of suitable business partners (36%) and problems regarding bureaucracy (34%).<sup>309</sup> Along with these "hard" factors, certain "soft" factors also emerged, which frequently cause direct investors to pull out of foreign markets after some time;

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<sup>307</sup> National Development and Reform Commission and Ministry of Finance, "Circular on the equal treatment of private investments relating to the use of government funds" (translated from Chinese) (June 1, 2012), available at: [http://www.fdi.gov.cn/pub/FDI/zcfg/law\\_ch\\_info.jsp?docid=143772](http://www.fdi.gov.cn/pub/FDI/zcfg/law_ch_info.jsp?docid=143772) (last visited February 18, 2013). See also, Shangbao.net.cn, "Private Sector Gets an Overseas Push," August 30, 2012, available at: <http://cib.shangbao.net.cn/290qi/116497.html> (last visited February 18, 2013).

<sup>308</sup> OPIC, "FAQs," available at: <http://www.opic.gov/media-connections/faqs> (last visited February 18, 2013).

<sup>309</sup> KfW, "Internationalisation in Germany's SME sector – step by step to global presence," available at: [http://www.kfw.de/kfw/en/I/II/Download\\_Center/Research/PDF\\_Dateien\\_Paper\\_and\\_Proceedings/Internationalisierung\\_im\\_deutschen\\_Mittelstand\\_KF\\_englisch.pdf](http://www.kfw.de/kfw/en/I/II/Download_Center/Research/PDF_Dateien_Paper_and_Proceedings/Internationalisierung_im_deutschen_Mittelstand_KF_englisch.pdf) (last visited February 13, 2013), p. 3.

these included language shortcomings and a lack of international experience.<sup>310</sup> In particular, one in four German SMEs indicated that “difficulties in financing are a key obstacle to their plans to go abroad or to expand their existing internationalisation activities.”<sup>311</sup> Of the direct investors that applied for external funding for foreign projects, half reported difficulties in raising external capital. A study in the United Kingdom affirmed “[f]inance is a disproportionately important obstacle for high-growth firms,” with 18% of such firms considering funding “to be the most important barrier to growth that they face ... compared to just 13% of other firms.”<sup>312</sup> Another study of “internationalization best practices” across eight selected APEC economies<sup>313</sup> surveyed the relative importance of various government initiatives to SMEs. The results showed that “readiness” (the pre-internationalization phase) and “growth initiatives” (the post-internationalization phase) were more important to SMEs than “implementation” initiatives that focused on “both environment and implementation issues that will either expedite or impede on the internationalisation process.” Financial HCMs that were consistently highly ranked by the SMEs surveyed included discounted loans and risk sharing, as well as foreign market immersion programs.<sup>314</sup>

Given these constraints on SMEs with respect to engaging in FDI, governments, not surprisingly, prioritize HCMs that address these constraints. Uncertainties due to operating in a foreign legal jurisdiction and lack of suitable business partners can be mitigated by the provision of grants that subsidize the cost of conducting feasibility studies. Other “soft” factors such as language shortcomings and a lack of international experience can be addressed through grants that support the training and development of human capital.<sup>315</sup>

It is readily apparent that one of the largest problems SMEs face when internationalizing is the lack of availability of finance. The market may not effectively provide financing to SMEs because of structural market failures, mainly relating to imperfect or asymmetric information, which can be exacerbated by macroeconomic uncertainty.<sup>316</sup> Financial institutions may perceive loans to SMEs as too risky. Government intervention is therefore necessary to correct this market failure. Unlike private financial institutions, governments are not solely focused on the rate of return on a loan or investment, but also consider the broader social benefit and positive spillover effects to the national economy. Financial HCMs that provide loans or allow for equity participation in home country SMEs help to close this debt or equity gap.

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<sup>310</sup> KfW, “Internationalisation in Germany’s SME sector – step by step to global presence,” *op. cit.*, p. 3.

<sup>311</sup> KfW, “Internationalisation in Germany’s SME sector – step by step to global presence,” *op. cit.*, p. 3.

<sup>312</sup> NESTA, “Barriers to growth: The views of high-growth and potential high-growth businesses,” November 2011, available at: <http://www.nesta.org.uk/library/documents/ResSumBarrierstoGrowth.pdf> (last visited February 13, 2013).

<sup>313</sup> Australia, Hong Kong (China), Japan, Malaysia, Peru, Singapore, Taiwan Province of China, United States.

<sup>314</sup> Spring Singapore, Study on SME Internationalisation: Best Practices Across Selected APEC Economies, 2011, *op. cit.*, pp. 6, 36-37.

<sup>315</sup> See above for examples of some of the financial HCMs supporting the training and development of human capital.

<sup>316</sup> UK Department for Business, “Innovation & Skills, SME access to external finance,” BIS Economics Paper No. 16 (January 2012), available at: [https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/32263/12-539-sme-access-external-finance.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/32263/12-539-sme-access-external-finance.pdf) (last visited February 13, 2013), p. 8.

Most of the financial HCMs surveyed in this chapter provide SMEs with financial advantages in connection with OFDI.

Some HCMs are designed to cover both SMEs and larger companies, up to a certain size. An example is Singapore's Internationalisation Finance Scheme. To be eligible for the Scheme, a company must, *inter alia*, have an annual turnover not exceeding S\$ 300 million for non-trading companies, or S\$ 500 million for trading companies.<sup>317</sup> Given that the definition of "SME" in Singapore is a company with annual sales turnover of not more than S\$ 100 million or that it employs not more than 200 workers, the Scheme covers both SMEs and large companies, up to a certain size.

Other financial HCMs do not require a firm to meet a certain size as a criterion for eligibility. For instance, the India Eximbank offers financial support for home country firms without mentioning any requirement that applicant companies be of a certain size. However, HCMs may sometimes require applicant firms to demonstrate a proven track record or relevant industry experience.<sup>318</sup>

Another example is the Korea Eximbank's Overseas Investment Credits program, which is technically available to all firms regardless of size, subject to the proviso that the Korean company has more than three years of relevant industry experience. SMEs benefit from more generous terms – credits may be granted for up to 90% of the required funds. Under the same program, non-SMEs can only obtain financing for up to 80% of the required funds for an overseas investment. In Canada, part of the application process to obtain a grant from the Global Opportunities for Associations program, which provides grants for national business associations engaging in international business development, involves an evaluation of the extent to which an applicant association's activities benefit Canadian SMEs.<sup>319</sup>

A significant number of financial HCMs exclusively target SMEs.<sup>320</sup> The Japan Finance Corporation recognizes the importance of access to stable long-term financing for SMEs. Private financial institutions less willing to lend to SMEs, even when they do extend loans, tend to offer only short-term loans of a year or less. Its SME Unit therefore specializes in offering long-term loans to SMEs. "Over 50% of the SME Unit's loans have lending periods of longer than five years, with fixed-interest rates that make it easier to map out repayment schedules."<sup>321</sup> Germany

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<sup>317</sup> IE Singapore, "Internationalisation Finance Scheme," *op. cit.*

<sup>318</sup> See e.g., financing extended by Korea Eximbank and OPIC.

<sup>319</sup> The Canadian Trade Commissioner Service, "Evaluation Criteria," available at: <http://www.tradecommissioner.gc.ca/eng/funding/global-opportunities-associations/evaluation-criteria.jsp> (last visited February 18, 2013).

<sup>320</sup> The EU is also supporting financially European SMEs. For example, the EU offers a range of financial support measures to SMEs, some of which are processed through local financial intermediaries. See, European Commission, "European Union support programmes for SMEs: An overview of the main funding opportunities available to European SMEs," (January 2012).

<sup>321</sup> Japan Finance Corporation, "Loan Programs," available at: [http://www.jfc.go.jp/n/english/sme/loan\\_finance.html](http://www.jfc.go.jp/n/english/sme/loan_finance.html) (last visited February 13, 2013).

only provides grants for feasibility studies to SMEs.<sup>322</sup> Singapore offers an SME Market Access Programme to support Singapore SMEs' first international expansion, including market entry via either a greenfield investment or acquisition.<sup>323</sup> Spain not only has FIEX, its fund for supporting overseas investments, but also a separate fund (FONPYME) that invests exclusively in Spanish SME projects undertaken abroad.<sup>324</sup>

When designing financial HCMs, home countries often take into account the size of the beneficiary firms investing abroad. SMEs make up the great majority of all business enterprises in virtually all economies and play an essential role in the success of any domestic economy. Yet, they are often hamstrung by a lack of access to long-term finance, which hinders their continued growth. Governments therefore have strong reasons to give special attention to this group of businesses.

## v. Destination

Some HCMs cater specifically to FDI in certain geographic regions in pursuit of national strategies. The Chinese government seems to have used this strategy with reasonable success. After the China-Africa Development Fund, which provides financial support for Chinese enterprises investing in Africa, was established in 2006 with initial funding of US\$ 1 billion provided by the China Development Bank (a state-controlled financial institution), Chinese FDI flows into Africa increased exponentially:<sup>325</sup> in 2005, the volume of Chinese OFDI flows to the African continent was US\$ 392 million; by 2008, it had increased 14-fold, to US\$ 5.5 billion.<sup>326</sup>

Development finance institutions typically limit financial support to investment made in emerging markets (whereby the definition of these countries varies). For example, resources of Spain's COFIDES can be used to support FDI "in any developing or emerging country,"<sup>327</sup> and the OPIC in the United States is "authorized to do business in more than 150 developing and post-conflict countries."<sup>328</sup>

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<sup>322</sup> DEG, "Feasibility Studies," available at: [http://www.deginvest.de/deg/EN\\_Home/Range\\_of\\_Services/Special\\_Programmes/Feasibility\\_studies/index.jsp](http://www.deginvest.de/deg/EN_Home/Range_of_Services/Special_Programmes/Feasibility_studies/index.jsp) (last visited February 18, 2013).

<sup>323</sup> IE Singapore, "SME Market Access Programme," April 2011, available at: [http://www.iesingapore.gov.sg/wps/wcm/connect/154a20004652bf2795f3f7335ca1adb2/SME\\_Map\\_V3\\_Apr2011.PDF?MOD=AJPERES](http://www.iesingapore.gov.sg/wps/wcm/connect/154a20004652bf2795f3f7335ca1adb2/SME_Map_V3_Apr2011.PDF?MOD=AJPERES) (last visited February 18, 2013).

<sup>324</sup> COFIDES, "FONPYME," available at: <http://www.cofides.es/english/2fonpyme.html> (last visited February 18, 2013).

<sup>325</sup> CDB, "CAD Fund," available at: <http://www.cdb.com.cn/english/Column.asp?ColumnId=176> (last visited February 18, 2013).

<sup>326</sup> See, MOFCOM, "2010 Statistical Bulletin of China's Outward Foreign Direct Investment," available at: <http://images.mofcom.gov.cn/hzs/accessory/201109/1316069658609.pdf> (last visited February 18, 2013).

<sup>327</sup> For the list of eligible developing countries, see BMZ, "DAC-Liste der Entwicklungsländer und -gebiete," available at: [http://www.bmz.de/de/ministerium/zahlen\\_fakten/DAC\\_Laenderliste\\_Berichtsjahre\\_2011\\_2013.pdf](http://www.bmz.de/de/ministerium/zahlen_fakten/DAC_Laenderliste_Berichtsjahre_2011_2013.pdf) (last visited February 19, 2013).

<sup>328</sup> OPIC, "Where We Operate," available at: <http://www.opic.gov/doing-business-us/OPIC-policies/where-we-operate> (last visited February 19, 2013).

Some HCMs even target specific geographic areas *within* a host country as destinations for outward FDI. IE Singapore offers financial support to “encourage Singapore-based companies to establish operations and participate in the Sino-Singapore Tianjin Eco-city,” a strategic cooperation project between China and Singapore.<sup>329</sup> The Chinese government adopts a similar practice, offering financial support for Chinese companies investing in the development of its approved overseas economic trade and cooperation zones; these zones were developed by Chinese companies (rather than the Chinese government), with subsidies from the government only granted after each zone satisfied certain performance requirements (which included political stability, efficiency of local officials, robust local laws and “personal safety of foreigners.”<sup>330</sup>

#### d. Conditionality

Because of the developmental nature of development finance institutions, they often attach additional criteria to the provision of financial support, most commonly with respect to the potential environmental, social and developmental impacts of an investment on the host country. OPIC requires applicants to “provide an overarching policy statement of the environmental and social objectives and principles that will be used to guide the Project and achieve sound and sustainable environmental and social performance.”<sup>331</sup> To be eligible for OPIC support, the project has to meet the workers’ rights standards of the International Labor Organization, including the right to unionize, collective bargaining, minimum age requirements, and a prohibition on forced labor.<sup>332</sup> Similarly, the Japan Bank for International Cooperation “conducts a review of environmental and social considerations when making a decision on funding,” and “conducts monitoring and follow-up after the decision has been made on funding.”<sup>333</sup> The potential environmental impact of each project funded by the Japan Bank for International Cooperation is assessed from the “earliest planning stage possible”, and “[m]ultiple alternative proposals must be examined to prevent or minimize adverse impact [*sic*].”<sup>334</sup> Where a large adverse impact on the environment is reasonably expected, the company has to produce an Environmental Impact Assessment report, which mandates consultation with affected people, local NGOs and regulators.

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<sup>329</sup> IE Singapore, “Tianjin Eco-city Assistance Programme,” available at: <http://www.iesingapore.gov.sg/wps/portal/GCP-MarketAccess/TAP> (last visited January 26, 2013).

<sup>330</sup> Deborah Bräutigam and Tang Xiaoyang, “Economic statecraft in China’s new overseas special economic zones: soft power, business or resource security?,” IFPRI Discussion Paper 01168 (2012), available at: <http://www.ifpri.org/sites/default/files/publications/ifpridp01168.pdf> (last visited January 27, 2013).

<sup>331</sup> OPIC, “Environmental and Social Policy Statement” (October 15, 2010), available at: [http://www.opic.gov/sites/default/files/consolidated\\_esps.pdf](http://www.opic.gov/sites/default/files/consolidated_esps.pdf) (last visited February 19, 2013), p. 5.

<sup>332</sup> OPIC, “Our Investor Screener,” available at: <http://www.opic.gov/doing-business-us/our-investor-screener> (last visited March 11, 2013).

<sup>333</sup> JBIC, “Guidelines for confirmation of environmental and social considerations” (April 2012), available at: [http://www.jbic.go.jp/en/about/environment/guideline/business/pdf/pdf\\_01.pdf](http://www.jbic.go.jp/en/about/environment/guideline/business/pdf/pdf_01.pdf) (last visited February 19, 2013), p. 4.

<sup>334</sup> JBIC, “Guidelines for confirmation of environmental and social considerations,” *op. cit.*, p. 14.



These standards are not necessarily limited to financial HCMs administered by development finance institutions. The same environmental and social policies to which the Japan Bank for International Cooperation adheres also apply to Japan Finance Corporation, which is not a development finance institution.<sup>335</sup>

Meanwhile, the fact that development finance institutions place significant weight on non-economic impacts on host countries does not prevent them from looking out for their own national interests. OPIC requires that the investment does not “result in the closing of a U.S. operation or the reduction of [the firm’s] U.S. workforce,” and does not “fall within a sector that has experienced significant job loss in the U.S. in the last decade.”<sup>336</sup>

### **e. Conclusions**

An analysis of the financial HCMs of the 20 countries examined in this chapter does not reveal any clear pattern distinguishing developed economies from emerging markets when it comes to the extent of the availability of financial HCMs. Developed countries like Switzerland and Canada have few financial HCMs, while Spain and Japan have a relatively broad array of such measures; similarly, within emerging markets, Singapore and the Republic of Korea employ many financial HCMs, while Chile, Kuwait and Mexico do not.

For the developed countries that do have a significant number of financial HCMs, the most significant characteristic that distinguishes them from emerging markets seems to be that their respective development finance institutions administer their financial HCMs. The significance of the greater weight placed on development means that there are more numerous concerns with such non-economic aspects of a foreign investment as environmental and social considerations. However, the fact that development finance institutions administer financial HCMs does not mean that they do not pursue national interests. In Spain, many of the financial HCMs administered by COFIDES, the Spanish development finance institution, only support investment where a Spanish interest is involved; the United States’ OPIC only provides support to United States firms or citizens, and an investment must not result in a firm reducing employment within the United States. Furthermore, while developed countries tend to have financial HCMs administered by their respective development finance institutions, each development finance institution operates differently; it is therefore difficult to identify a single representative model.

An analysis of the results of the research and the literature on the topic suggests that loans are probably the most commonly available effective category of financial HCMs. Despite the purported advantages of equity participation from the standpoint of supporting OFDI (e.g.,

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<sup>335</sup> The contents of the text are the same as the JFC Guidelines, JBIC, “Environmental Guidelines for JBIC Lending Operations,” available at: <http://www.jbic.go.jp/en/about/environment/guideline/index.html> (last visited February 19, 2013).

<sup>336</sup> OPIC, “Our Investor Screener,” available at: <http://www.opic.gov/doing-business-us/our-investor-screener> (last visited March 11, 2013).

compared to loans, the government usually does not need to make continuous payments, and the company can benefit from the reputational advantages of having a well-known government-linked investor), the data seem to indicate that the resources committed to equity participation are small relative to the resources dedicated to loans. For example, while the Japan Bank for International Cooperation appears to have a relatively sophisticated equity participation program for firms investing outside Japan, its commitment to equity participations is miniscule relative to its commitment to overseas investment loans: during the 2011 financial year, the Japan Bank for International Cooperation committed approximately US\$ 16 *million* to all equity participations (including any equity participations not conditioned upon engaging in FDI), and approximately US\$ 10 *billion* to overseas investment loans.<sup>337</sup> This disparity is similarly reflected in its commitments in the preceding years. Furthermore, since 2007, it has only approved a total of 13 equity participations, relative to 494 overseas investment loans.<sup>338</sup>

DEG also commits a larger proportion of its funds to loans rather than equity participations, but the disparity is less extreme than that of the Japan Bank for International Cooperation. During the 2011 financial year, DEG committed € 274 million to equity investments and € 945 million to loans, of which € 235 million “were arranged as loans with equity features” (i.e., quasi-equity financing).<sup>339</sup> During the financial year 2010, the commitments were € 170 million and € 1 billion for equity participations and loans, respectively.

Unfortunately, many of the other countries do not provide much information on the relative commitments given to loans and equity participations, making it difficult to show a consistent pattern of greater commitments to the former rather than the latter. To the extent that one can rely on Germany and Japan being representative of other countries, these two examples are perhaps indicative of home country governments’ perception that loans are a better tool for encouraging OFDI. A possible reason for this could be the relative ease of administration. The terms and conditions of each loan should be simpler to negotiate as compared to the terms involved in the taking of an equity stake in a foreign affiliate. For instance, the latter will likely involve negotiations over the specific terms of the exit conditions, which may require greater analysis than the provision of term loans, the conditions of which may very well be dictated by the relevant government agency. Another possible reason could be firms’ unwillingness to surrender partial control of their business enterprises by allowing the relevant government agency to take equity stakes, coupled with board representation, in their foreign affiliates. Finally, if the investment goes poorly, the government could theoretically claim repayment of debt, whereas an equity investment could be lost completely.

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<sup>337</sup> JBIC, “Annual Report 2012,” *op. cit.*, p. 84.

<sup>338</sup> JBIC, “Annual Report 2012,” *op. cit.*, p. 84.

<sup>339</sup> DEG, “Annual Report 2011,” available at: [http://www.deginvest.de/deg/EN/Home/Download\\_Center/PDFs\\_Online-Library/DEG\\_AnnualReport\\_2011.pdf](http://www.deginvest.de/deg/EN/Home/Download_Center/PDFs_Online-Library/DEG_AnnualReport_2011.pdf) (last visited March 9, 2013), p. 16.

A study of the effects of HCMs on SMEs' internationalization shows that the provision of loans, particularly discounted loans, is the most important form of financial support for SMEs.<sup>340</sup> The study also consolidated the findings from its research, identifying a list of best practices (defined as practices that are believed to be important to both governments and businesses). Included in this list are "Discounted Loans and Risk Sharing" and "Foreign Market Immersion Programmes."<sup>341</sup> The former refers to concessional loans and risk-sharing schemes in which the government co-shares the risk of default with commercial lenders and other insurance schemes; the latter refers to grants like Singapore's International Business Fellowship that helps to reduce the cost of foreignness when investing abroad.

In sum, financial HCMs are an important tool in the arsenal of tools of a number of countries to support firms investing abroad. This includes emerging markets, some of whose governments over the past ten years seemed to have increasingly sought – if data for the Republic of Korea are indicative (Figure 2) – to promote OFDI through the use of financial HCMs, as they "recognize that outward FDI can strengthen the competitiveness of their firms or bring other benefits to the home economy."<sup>342</sup> By requiring certain criteria to be met in order to benefit from these financial HCMs, governments have carefully tailored such measures to suit their national needs. For instance, special attention is paid to the internationalization of SMEs, which are often thought to form the backbone of the domestic economy. Moreover, for a number of countries, financial HCMs are designed in a way that encourages investment in strategically important industries, especially natural resources. Finally, there is some evidence that both governments and companies seem to exhibit a preference for loans over other forms of financial support with respect to outward investment.

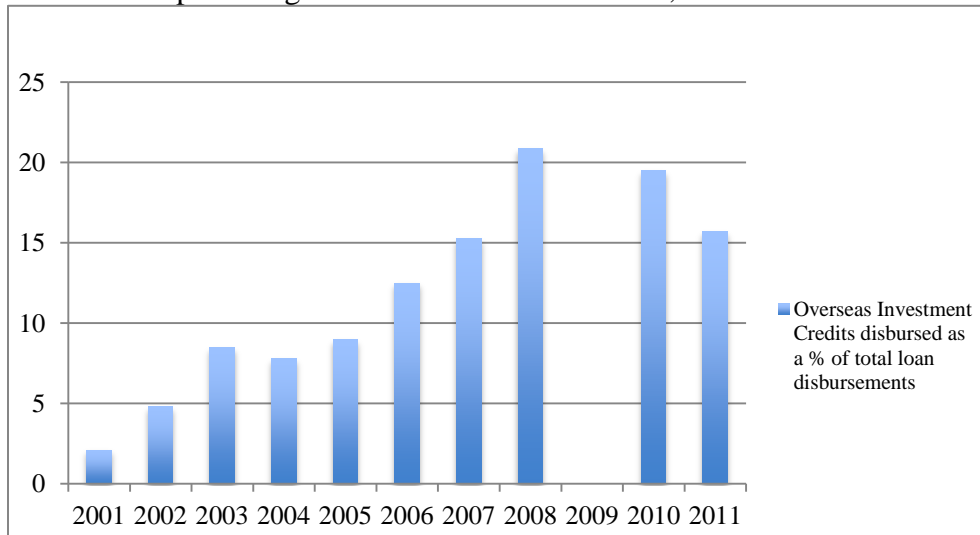
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<sup>340</sup> Spring Singapore, "Study on SME Internationalisation: Best Practices Across Selected APEC Economies," 2011, *op. cit.*, p. 37.

<sup>341</sup> Spring Singapore, "Study on SME Internationalisation: Best Practices Across Selected APEC Economies," 2011, *op. cit.*, p. 78.

<sup>342</sup> UNCTAD, *Investment Brief*, No. 4, 2006, *op. cit.*

Figure 2. Overseas investment credits disbursed by the Export-Import Bank of Korea, as a percentage of total loan disbursements, 2001-2011



Source: The Export-Import Bank of Korea, *Annual Reports*, various years (data for 2009 are not available).

#### 4. Fiscal measures

##### a. Introduction

Taxation and other fiscal measures are one means often used to attract FDI *inflows* – but they can also be used to influence FDI *outflows*. When governments introduce fiscal measures to support their firms investing abroad, they need to take into consideration the impact of any measures on their domestic tax base and future consequences for domestic firms and their economies. Bearing this concern in mind, developed countries and emerging markets offer a variety of fiscal measures to support firms investing abroad, and these are discussed in this section.

Fiscal measures entail a reduction in the overall tax burden of home country firms investing abroad, and a loss in government revenues from taxes foregone. These measures are therefore a category of tax expenditures, as they involve “provisions of tax law, regulation or practices that reduce or postpone revenue for a comparatively narrow population of taxpayers relative to a benchmark tax.”<sup>343</sup> In other words, in the context of this chapter, fiscal measures entail the use of the tax system to support a select group of taxpayers – outward investing firms – in their efforts to internationalize. For a home country, tax expenditures constitute a loss in revenue; for the foreign investor, they represent a reduction in the tax liability to the home country.

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<sup>343</sup> Barry Anderson, “Tax expenditures in OECD countries” (January 2008), available at: [www.oecd.org/dataoecd/40/6/39944419.pdf](http://www.oecd.org/dataoecd/40/6/39944419.pdf) (last visited February 15, 2013), pp. 4-5.

The OECD provides a useful definition and classification of tax expenditures. According to that classification, home country fiscal measures can be divided into the following categories: (i) exemptions, which are defined as amounts excluded from the tax base; (ii) rate relief, which is a reduced rate of tax applied to a class of taxpayer or taxable transactions; (iii) tax deferral, which is a delay in paying tax;<sup>344</sup> (iv) credits, which are amounts deducted from the tax liability; and (v) allowances, which are defined as amounts deducted from the benchmark to arrive at the tax base.<sup>345</sup>

For the countries analyzed in this chapter, it was necessary to determine their approach to taxing foreign income in advance – namely, whether they follow the territorial or the worldwide approach (Box 4). This is important because the approach applied by a country determines the method of taxation of foreign affiliate profits and thus whether or not profits can be exempted from taxes paid in the home country. Countries that follow the worldwide approach may introduce fiscal measures that apply to foreign affiliates, since their income is subject to taxation in the home country. In a sense, therefore, the territorial approach to taxation can, by itself, be considered as an HCM facilitating OFDI, even though it applies to all home country firms.

#### Box 4. Worldwide versus territorial approach to taxing foreign affiliates

Countries pursue one of two approaches to tax the profits of firms investing abroad: the worldwide or the territorial approach.

The worldwide tax policy approach taxes all income of a company regardless of where it is earned. But it gives MNEs the ability to defer taxes on foreign-sourced earnings until repatriation<sup>[a]</sup> and may, therefore, encourage firms to reinvest foreign-sourced earnings abroad to avoid taxes at home. Under this approach, if a home country's corporate income tax rate is higher than that in a host country, firms investing abroad are functioning in a non-neutral fiscal environment. In such cases, when foreign affiliates transfer earnings back to the home country, their parent firms may have to pay a higher tax rate than the parent firms of other foreign affiliates in the same host country, including MNEs headquartered in countries following the territorial approach. Consequently, when a home country's corporate income tax rate is higher than in a host country, parent firms may be at a disadvantage from a fiscal perspective in relation to competitors in the host country. To avoid paying the higher tax rate in their home country, foreign affiliates may feel encouraged, for example, to reinvest their earnings in the host country (or elsewhere, e.g., to park them in tax havens).

Under the territorial approach, a country collects taxes only on income earned within its borders. This is typically accomplished by exempting from domestic taxes the dividends received from foreign affiliates. "The territorial design thus equalizes the tax costs between international

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<sup>344</sup> When the period of deferral is very long, a tax deferral can become close to a tax exemption and can have a similar financial effect as a subsidy.

<sup>345</sup> OECD, *Tax Expenditures in OECD Countries* (Paris: OECD, 2010), p. 12, based on Anderson, "Tax expenditures in OECD countries," 2008, *op. cit.*

competitors operating in the same jurisdiction, so that all firms may compete on a level playing field, and capital may flow to where it can achieve the best after-tax return on investment.”<sup>[b]</sup> This approach seems to be more supportive of outward FDI than the worldwide approach<sup>[c]</sup> because foreign investors are not disadvantaged when transferring earnings back to their home countries with higher tax rates, and corporate income in general<sup>[d]</sup> is taxable only once.

In the worldwide approach, firms are functioning in a neutral fiscal environment only when a home country’s tax rate is lower than the host country’s tax rate. In the opposite case, when a home country’s tax rate is higher than the host country’s tax rate, domestic firms investing abroad are paying a higher tax rate in comparison to their foreign competitors. They pay taxes twice: first on profits in the host country and, in addition, when transferring dividends back to the home country. Generally, MNEs pay the difference in their home countries between the home country tax rate and the host country tax rate (usually because of the tax credit system and double taxation treaties).

Except for the United States, all developed countries examined in this chapter apply the territorial approach, while most emerging markets examined here apply the worldwide approach (Chile, China, India, Mexico, Republic of Korea, Taiwan Province of China). Japan and the United Kingdom both adopted this approach in 2009.<sup>[e]</sup> The United Kingdom shifted from the worldwide to the territorial tax system on the grounds of seeking to become more competitive: “to be more competitive, the UK’s corporate tax system should focus more on profits from UK activity in determining the tax base rather than attributing the worldwide income of a group to the UK. Moving towards a more territorial system in this way will better reflect the global reality of modern business and will allow businesses based here to be more competitive on the world stage supporting UK investment and jobs.”<sup>[f]</sup>

It is worth noting, though, that countries do not follow exclusively one approach to taxation and tend to combine them depending on particular fiscal objectives.<sup>[g]</sup> Countries with a territorial taxation system treat the issue of avoiding double taxation differently from countries having a worldwide system. The majority of the latter use foreign tax credits. If income received from abroad is subject to tax in the country of residence, any domestic tax can be offset by the amount of the incurred foreign tax. The theory is that, usually, the credit allowed is limited to the amount of the domestic tax, with no carry over if the tax is higher abroad. In all countries, exempted profits are defined by reference to individual double taxation treaties. In those countries that apply the territorial approach, the prevailing method is to exempt foreign-sourced income from domestic taxation. While specifics of the applicable tax regulation in each country affects the outcome of tax proceedings differently, both methods are endorsed by the OECD Model Tax Convention on Income and on Capital (2010)<sup>[h]</sup> and by the United Nations Model Double Taxation Convention between Developed and Developing Countries (2011).<sup>[i]</sup>

However, foreign tax credits or exemptions as tools of double taxation relief as such cannot be considered as HCMs, because they do not permit a firm not to pay home country taxes. This means that all companies (MNEs and companies operating only in the home country) originating from a given country applying the worldwide tax system are functioning under the same fiscal rules. The worldwide taxation system does not give any additional privilege to domestic firms investing abroad. In that approach, the tax level for domestic firms operating only in the home market and for domestic firms investing abroad cannot be different. In contrast, the foreign

operations of firms investing abroad are generally taxed, under the territorial system, on the basis of the foreign tax rate. This can be considered as a privilege compared to other firms operating only in domestic market, in the case when the foreign tax rate is lower than the domestic one.

Another important aspect of double taxation relief is the way in which the taxation of dividends obtained from foreign affiliates is handled. Legally, the taxation of the income of a foreign affiliate out of which dividends are paid to the parent company residing in the home country does not create a problem of international juridical double taxation, because of the separate corporate status of domestic and foreign companies. Nevertheless, many countries grant their parent companies indirect credits or participation exemptions<sup>[i]</sup> in order to stimulate international investment and encourage the repatriation of profits.

In sum, it is generally recognized that the territorial fiscal approach provides a more advantageous fiscal environment for a firm investing abroad than the worldwide fiscal approach.

*Source:* The authors, based on the literature referenced below.

[a] Thomas Gresik, “The taxing task of taxing transnationals,” *Journal of Economic Literature* 39 (2001), pp. 800-838.

[b] Philip Dittmer, “A Global Perspective on Territorial Taxation: Special Report,” Tax foundation (2012), p. 2.

[c] See Barrios Salvador, Harry Huizinga, Luc Laeven and Gaëtan Nicodème “International taxation and multinational firm location decisions,” *Journal of Public Economics* 96 (2012), pp. 946–958 and Philip Dittmer, “A Global Perspective on Territorial Taxation: Special Report,” op. cit., p. 2.

[d] Countries that operate territorial systems provide tax exemptions (either whole or partial) for dividends received from foreign sources, e.g.: “Germany applies the exemption method in international taxation, implying that dividends repatriated are not further taxed in Germany. Yet, due to stipulations concerning the deductibility of operating costs this exemption is provided only for 95 percent of the dividends repatriated [...]. Five percent of repatriated dividends are taxed by the German corporate income tax rate.” See Christian Bellak, Markus Leibrecht and Michael Wild, “Does lowering dividend tax rates increase dividends repatriated? Evidence of intra-firm cross-border dividend repatriation policies by German multinational enterprises,” *Deutsche Bundesbank Discussion Paper Series 1: Economic Studies* (2009) 19, p. 17.

[e] Philip Dittmer, “A Global Perspective on Territorial Taxation: Special Report,” op. cit., p. 2.

[f] United Kingdom HM Treasury, *Corporate Tax Reform: Delivering a more competitive system*, London, available at: [http://www.hm-treasury.gov.uk/d/corporate\\_tax\\_reform\\_complete\\_document.pdf](http://www.hm-treasury.gov.uk/d/corporate_tax_reform_complete_document.pdf) (last visited March 1, 2013), p. 13.

[g] United States Government Accountability Office, “International taxation: Study countries that exempt foreign – source income face compliance risks and burdens similar to those in the United States”, Report to the Committee of finance, U.S. Senate (September 2009), p. 2, available at <http://gao.gov/assets/300/296939.pdf> (last visited June 13, 2013).

[h] See OECD, *Model tax convention on income and on capital 2010*, art. 23A and 23B Methods for elimination of double taxation, available at [http://www.keepeek.com/Digital-Asset-Management/oecd/taxation/model-tax-convention-on-income-and-on-capital-2010/article-23-a-and-23-b-methods-for-elimination-of-double-taxation\\_9789264175181-26-en](http://www.keepeek.com/Digital-Asset-Management/oecd/taxation/model-tax-convention-on-income-and-on-capital-2010/article-23-a-and-23-b-methods-for-elimination-of-double-taxation_9789264175181-26-en) (last visited June 9, 2013).

[i] See United Nations Model double taxation convention between developed and developing countries, Part I, art. 23, available at [http://www.un.org/esa/ffd/documents/UN\\_Model\\_2011\\_Update.pdf](http://www.un.org/esa/ffd/documents/UN_Model_2011_Update.pdf) (last visited June 9, 2013).

## **b. Measures**

### **i. Exemptions from corporate income tax on certain incomes**

Fiscal incentives consisting of exemptions represent a systematic effort by a home country to exempt certain types of income related to OFDI, which would be taxable in the absence of the fiscal incentives. A fiscal measure of this kind involves a "benefit" to the recipients of the tax exemption.<sup>346</sup>

One of the key issues for outward investors is to determine the optimal legal structure of their investment in a host country. Two major choices – establishing a branch or registering a company – entail substantially different tax consideration. Many host countries clearly prefer investors to establish companies over branches because the former give them clearer taxing rights and allow the establishment of minimum levels of local participation.<sup>347</sup> On the part of a parent corporation's home country, the establishment of a foreign affiliate by its enterprises creates an issue of how to deal with foreign-sourced dividends. If left unresolved by the home country, double taxation will occur because corporate profits would be taxed first at the level of the foreign affiliate in the host country, and then at the level of the parent firm that receives distributed dividends. While this problem (which creates an obstacle for international investment<sup>348</sup>) has drawn considerable attention on the international level, it is mainly left for the governments to decide unilaterally whether and how they will deal with it. The same methods that are used to deal with double taxation – exemption or foreign tax credit (indirect credit) -- can be utilized here.

Under the territorial approach, foreign dividends are exempt wholly or partially from domestic taxation. In the group of countries analyzed in this chapter, Belgium, Canada, France, Germany, Italy, Japan, Spain, Switzerland, the United Kingdom, Kuwait, Malaysia, the Russian Federation, and Singapore have adopted the territorial approach.<sup>349</sup> Under the exemption method, parent companies are allowed to repatriate tax-exempt dividends from their foreign affiliates. In the group of countries analyzed in this chapter applying the territorial approach, dividends are exempt by 100% (Kuwait, Malaysia, Russian Federation, Singapore, Spain, United Kingdom) or

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<sup>346</sup> The definition criterion is based on WTO, Trade and Foreign Direct Investment (WTO: Geneva, 1996), available at: [http://www.wto.org/english/news\\_e/pres96\\_e/pr057\\_e.htm](http://www.wto.org/english/news_e/pres96_e/pr057_e.htm) (last visited November 26, 2012) and UNCTAD (2004). Incentives, Series on Issues in International Investment Agreements (United Nations: New York and Geneva 2004), p. 15, and Article 1 of the SCM Agreement, op. cit.

<sup>347</sup> Angharad Miller and Lynne Oats B. Bus, *Principles of International Taxation* (Haywards Heath: Tootel Publishing, 2009), p. 201. For instance, if a company in Brunei Darussalam has two directors, at least one should be a resident; joint ventures with local companies are encouraged. In Indonesia, foreign investments in infrastructure projects must be conducted via the establishment of a joint venture between foreign and Indonesian partners. See, IMF, *Annual Report on Exchange Arrangements and Exchange Restrictions 2012*. Available at: <http://www.imf.org/external/pubs/nft/2012/eaer/ar2012.pdf> (last visited: October 7, 2013).

<sup>348</sup> United Nation Model Double Taxation Convention between Developed and Developing countries, Commentary to Article 23 A & B, p. 328.

<sup>349</sup> For more information on the treatment of foreign affiliate dividends in countries using the territorial method of taxation, see PwC, "Evolution of Territorial Tax Systems in the OECD," Report prepared for the Technology CEO Council (April 2, 2013), available at: [http://www.techceocouncil.org/clientuploads/reports/Report%20on%20Territorial%20Tax%20Systems\\_20130402b.pdf](http://www.techceocouncil.org/clientuploads/reports/Report%20on%20Territorial%20Tax%20Systems_20130402b.pdf) (last visited June 17, 2013).



by 95% (Belgium, Germany, Italy, Japan, France). A high exemption level – 95 or 100% - does not discourage a dividend transfer to the home country.

Under the worldwide approach, countries grant foreign tax credits. In this case, the country of residence of the parent firm allows a credit for the amount of foreign taxes paid by a foreign affiliate on the income out of which dividends are paid (called “underlying taxes”) against its own income tax.<sup>350</sup> The foreign tax credit method is generally regarded as a more complex system that requires proper attribution of the foreign income tax paid to the dividends distributed.<sup>351</sup>

Usually, both foreign tax credits and dividend exemptions are allowed when certain conditions are met. These usually include share ownership requirements, ownership duration requirements and country-based limitations. For instance, the Republic of Korea eased in 2011 its regulation of indirect tax credits for dividends and now allows all Korean parent companies to claim foreign tax credits for underlying taxes paid by qualifying foreign affiliates. Before these amendments, the government allowed a 100% tax credit for dividends only if a tax treaty between the Republic of Korea and the country in which the Korean company’s affiliate resides allowed for an indirect foreign tax credit; otherwise, only 50% of the foreign tax was available for the indirect foreign tax credit.<sup>352</sup> For the purpose of the indirect foreign tax credit, a qualifying foreign affiliate is one in which a Korean parent company holds at least 10% of the shares at least for six consecutive months after the date of the dividend declaration.<sup>353</sup>

In Russia, to be eligible for a foreign-source dividends exemption, a parent company must hold at least 50% of the capital of the distributing foreign affiliate for at least one year. Moreover, the country of residence of the distributing foreign affiliate should not be included in the list of countries that provide preferential tax treatment and/or do not require the disclosure and provision of information when financial operations are carried out (offshore zones).<sup>354</sup> This list is approved by the Ministry of Finance of Russia. Belgium, in addition to ownership participation and duration requirements, also prohibits the application of exemptions to dividends originating from: (i) tax haven companies, (ii) offshore companies, (iii) intermediary holding companies, (iv) finance, treasury or investment companies (under certain conditions), and (v) companies having branches that benefit globally from a taxation system more advantageous than the Belgian non-resident corporate taxation system.<sup>355</sup>

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<sup>350</sup> Brian J. Arnold and Michael J. McIntyre, *International Tax Primer* (The Hague: Kluwer Law International, 2002), pp. 42-44.

<sup>351</sup> Hugh J. Ault and Brian J. Arnold, *Comparative Income Taxation: A Structural Analysis*, 3rd ed. (Alphen aan den Rijn: Kluwer Law International, 2010), p. 464.

<sup>352</sup> Deloitte, “World Tax Advisor, Korea: Various changes made to tax rules affecting cross-border transactions,” 13 January 2012, p.1, available at [http://newsletters.usdbriefs.com/2012/Tax/WTA/120113\\_6.pdf](http://newsletters.usdbriefs.com/2012/Tax/WTA/120113_6.pdf) (last visited June 17, 2013).

<sup>353</sup> PwC, “Worldwide Tax Summaries: Corporate taxes 2012/23,” p. 1025, available at: <http://www.pwc.com/gx/en/tax/corporate-tax/worldwide-tax-summaries/index.jhtml> (last visited June 17, 2013).

<sup>354</sup> Tax Code of the Russian Federation, Part II, art. 275.

<sup>355</sup> PwC, “Worldwide Tax Summaries: Corporate taxes 2012/23,” p.195, available at: <http://www.pwc.com/gx/en/tax/corporate-tax/worldwide-tax-summaries/index.jhtml> (last visited June 17, 2013).

Furthermore, countries utilize other exemptions that are not determined by the territorial or worldwide taxation approach. For instance, in Canada residents (shareholders who are individuals, trusts or corporations) who receive foreign spin-offs<sup>356</sup> shares can elect, under certain conditions, not to include these amounts in their reported income.<sup>357</sup> In France, a French-resident company may deduct certain start-up expenses of its foreign operations through a tax-deductible reserve account;<sup>358</sup> such a company may also deduct costs related to the acquisition of a foreign company.

Taiwan Province of China has sought to become a “Headquarters State” and a “High Added Value Industrial Base”. In order to encourage foreign and domestic companies to manage their international operations from Taiwan Province of China, a number of exemptions are offered to companies that establish an operational headquarters there. Companies that have reached a certain economic scale and are expected to create a significant positive effect on the home economy are exempt from corporate income tax on the following incomes: income received from the provision of management services or research and development activities for foreign-associated enterprises, royalties received from foreign-associated enterprises, and dividends and capital gains received from its foreign-associated enterprises.<sup>359</sup>

The United Kingdom grants an exemption reducing the corporate tax rate for certain activities between a parent firm and its foreign affiliates and for controlled foreign companies<sup>360</sup> whose main business is the exploitation of intellectual property. In both cases, to benefit from this exemption, the foreign companies should have a limited connection with the United Kingdom. The criteria concerning the limited connection are based on the foreign company’s income and expenditure level connected to the United Kingdom. Other exemptions that reduce corporate tax can be used by controlled foreign companies with a low profit level (less than £ 200,000 profits per annum) and foreign subsidiaries that, as a consequence of an acquisition or reorganization,

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<sup>356</sup> “Spin-off” is defined as a new business created by separating part of a company from an existing one and making it an independent entity; based on <http://dictionary.cambridge.org> (last visited November 26, 2012). Canada’s Income Act defines spin-off shares as “common shares of the capital stock of another corporation that were owned by the particular corporation immediately before their distribution to the taxpayer,” Income Tax Act (R.S.C., 1985, c. 1 (5th Supp.)), Section 86.1, (2)(b), available at: <http://laws-lois.justice.gc.ca/eng/acts/i-3.3/page-122.html#h-23> (last visited June 17, 2013).

<sup>357</sup> Canada Income Tax Act (Section 86.1), available at: <http://laws-lois.justice.gc.ca/eng/acts/I-3.3> (last visited November 20, 2012).

<sup>358</sup> Article 39 octies D I to III of the French Tax Code and Article 4 bis and Article 4 ter of Annex IV of the French Tax Code, available at: <http://www.legifrance.gouv.fr> (last visited 26 November 2012), and WTO dispute DS131, available at: [http://www.wto.org/english/tratop\\_e/dispu\\_e/cases\\_e/ds131\\_e.htm](http://www.wto.org/english/tratop_e/dispu_e/cases_e/ds131_e.htm) (last visited November 16, 2012).

<sup>359</sup> Steve Waicho Tsui “The business income tax in Taiwan: Introduction to Taiwan’s profit-seeking enterprise income tax” (2008), available at: <http://www.ipp.hit-u.ac.jp/EastAsianTaxForum/PDF/Tsui-PEIT-in-Taiwan-Part-1.pdf> (last visited February 27, 2013).

<sup>360</sup> A “controlled foreign company” is defined as a company that is: “(i) resident outside the home country; (ii) controlled by persons resident in the home country; and (iii) subject to a lower level of taxation in its territory of residence;” this definition (No. INTM202010) is adopted from the British Law and based on the following source: <http://www.hmrc.gov.uk/manuals/intmanual/INTM202010.htm> (last visited April 22, 2013).

come within the scope of the controlled foreign company regime.<sup>361</sup> All these measures are part of the United Kingdom's controlled foreign company taxation reform that began in 2011.<sup>362</sup>

In Malaysia, a locally-owned company (i.e., at least 60% Malaysian equity ownership, held for a period of five years preceding the date of application) in the manufacturing or services sector that acquires a company abroad is eligible for an incentive in the form of an annual deduction of 20% of the acquisition costs for five years. The acquired company must be a foreign firm with 100% foreign equity ownership, and the acquisition should involve a direct acquisition of at least 51% of the equity of the foreign company abroad and must be in the form of a cash transaction; acquisitions through share-swapping are not eligible for this incentive.<sup>363</sup> This incentive may be used for the following purposes: the establishment of a manufacturing facility or a services company within Malaysia (following the acquisition of the foreign-owned company) or the utilization of the acquired technology in its existing operations within Malaysia.<sup>364</sup> The purpose of these requirements is to achieve technology transfer from the acquired (foreign) company to the domestic market – in the first case, in the form of a new investment in Malaysia, while in the second case, only in terms of the utilization of the acquired technology in existing (Malaysian) operations. Additionally, if the company is resident in Malaysia and if the Minister of Finance has approved the business venture, the company may deduct pre-operational business expenditures related to outward FDI in a business venture from its income. Such expenses include the conduct of feasibility or market research studies and travel expenses of representatives of the company involved in feasibility studies or market surveys.<sup>365</sup>

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<sup>361</sup> See, United Kingdom HM Treasury, “CFC Interim Measures – Draft Guidance,” 2012, p. 2, available at: <http://www.hmrc.gov.uk/guidance/cfc-interims-draft-guid.pdf> (last visited February 20, 2013).

<sup>362</sup> There is a significant United Kingdom connection if either of the two conditions (A or B) relating to a controlled foreign company's income or expenditure is met. Condition A is met if more than 10% of the company's gross income during the accounting period is United Kingdom connected and other terms listed below do not apply. “Other terms” (with the result that Condition A will not be met) are if: (i) the controlled foreign company has sufficient staff based outside the United Kingdom with the competence and authority to undertake all or substantially all of the controlled foreign company's business; (ii) its profits do not exceed 10% of its “relevant operating expenses”, and (iii) its United Kingdom-connected gross income for the accounting period does not exceed 50% of its gross income. Condition B is met if more than 50% of the controlled foreign company's “related party business expenditure” in the accounting period is “UK connected related party business expenditure” and the controlled foreign company has been involved in a scheme where any party to the scheme had a main purpose of achieving a reduction in United Kingdom corporation tax or in controlled foreign company tax; based on: United Kingdom HM Treasury, “CFC Interim Measures – Draft Guidance,” 2012, *op. cit.* p. 4. A company is a “subsidiary” of another company, its “holding company”, if that other company holds the majority of the voting rights in it; or is a shareholder of it and has the right to appoint or remove a majority of its board of directors; or is a shareholder and controls alone, pursuant to an agreement with other shareholders, a majority of the voting rights in it, or if it is a subsidiary of a company that is itself a subsidiary of that other company. Based on the British Companies Act 2006, Section 1159, available at: <http://www.legislation.gov.uk/ukpga/2006/46/section/1159> (last visited April 25, 2013).

<sup>363</sup> For more information see MIDA, “Guidelines for incentives for acquiring a foreign company for high technology,” available at: <http://www.mida.gov.my/env3/uploads/Forms/Services/03082012/GD-AFC-02.pdf> (last visited April 25, 2013), p. 3.

<sup>364</sup> MIDA, “Guidelines for incentives for acquiring a foreign company for high technology,” *op. cit.*, p. 2.

<sup>365</sup> Malaysian Tax Code, Part X Chapter 3 Schedule 4B, available at: <http://www.hasil.gov.my/pdf/pdfam/4538.pdf> (last visited November 15, 2012).

In Singapore, a tax deduction of up to 200% for SMEs venturing abroad may be allowed on qualifying expenditures, capped at S\$ 100,000 per year, incurred for the following activities: overseas business development trips/missions, overseas investment study trips/missions, participation in overseas trade fairs, and participation in approved local trade fairs.<sup>366</sup> Under the Integrated Investment Allowance Scheme, Singapore provides an allowance for fixed capital expenditure on productive equipment placed overseas in approved projects.<sup>367</sup>

China's State Administration of Taxation offers tax deductions and exemptions to support China's "go global" strategy. These include regular deductions and exemptions for both corporate and individual incomes to avoid double taxation and tax reductions for revenues arising from oil and gas extraction overseas by Chinese enterprises.<sup>368</sup>

## ii. Corporate tax rate relief

Corporate tax rate relief is applied to certain types of enterprises or at a certain stage of an investment. In China, a reduced 15% corporate income tax rate is applied to high-technology resident enterprises' income sourced from abroad (10 percentage points lower than the normal income tax rate of 25%).<sup>369</sup> In the Republic of Korea, because of the need to import oil, there is a strong national interest in ensuring OFDI in the oil sector.<sup>370</sup> Accordingly, the Korea Eximbank encourages such investment, as well as investment in mineral resources, through various tax benefits and the extension of credit lines to Korean firms engaged in natural resource seeking activities.<sup>371</sup> Another example of tax rate relief is the Singapore Headquarters Programme, applicable to entities (including foreign affiliates) incorporated or registered in Singapore that provide corporate support and headquarters-related services/business expertise on a regional or global basis; this program offers a concessionary tax rate of 15% for three plus two years on qualifying income from abroad.<sup>372</sup>

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<sup>366</sup> Singapore Income Tax Code, Sections 14B and 14K, available at: [http://iras.gov.sg/irasHome/uploadedFiles/News\\_and\\_Events/Singapore\\_Budget\\_Tax\\_Changes/Budget\\_2012/Double%20Tax%20Deduction.pdf](http://iras.gov.sg/irasHome/uploadedFiles/News_and_Events/Singapore_Budget_Tax_Changes/Budget_2012/Double%20Tax%20Deduction.pdf) (last visited November 20, 2012).

<sup>367</sup> See Singapore Economic Development Board, "Incentives for business," available at: <http://www.edb.gov.sg/content/edb/en/why-singapore/ready-to-invest/incentives-for-businesses.html> (last visited February 20, 2013).

<sup>368</sup> State Administration of Taxation of the Peoples' Republic of China, available at: <http://www.chinatax.gov.cn/n6669073> (last visited March 20, 2013).

<sup>369</sup> See Chinese Ministry of Science and Technology, Ministry of Finance and State Administration of Taxation, "The Administrative Measures for Determination of High and New Tech Enterprises," art. 10, available at: [http://www.ciiipacn.org/hot/news\\_show.asp?id=225](http://www.ciiipacn.org/hot/news_show.asp?id=225) (last visited February 10, 2013).

<sup>370</sup> U.S. Energy Information Administration, "Information on Korea," available at: <http://www.eia.gov/countries/cab.cfm?fips=KS> (last visited March 3, 2013).

<sup>371</sup> OECD, Inventory of Estimated Budgetary Support and Tax Expenditures for Fossil Fuels (Paris: OECD, 2013), p. 241, available at: <http://www.oecd.org/site/tadffss/> (last visited March 1, 2013).

<sup>372</sup> If an applicant company satisfies all the minimum requirements by year three of the incentive period, it will enjoy the 15% concessionary tax rate for an additional two years on qualifying income, based on Singapore Economic Development Board, "Headquarters Award," p. 2, available at:

### iii. Tax deferral

Although the United States generally taxes the worldwide income of United States persons and business entities, certain active income of foreign corporations controlled by United States shareholders is not subject to United States taxation when it is earned. This income becomes taxable only when the controlling United States shareholders receive dividends or other distributions from their foreign stockholding.<sup>373</sup> The United States deferral subsidy encourages United States persons to shift operations abroad to low-tax foreign countries and to favor the accumulation of earnings in foreign affiliates. The deferral becomes close to an exemption of foreign sourced corporate tax when the period of deferral is long enough. Thus, an exemption via deferral is close to a subsidy.<sup>374</sup> In contrast, except for tax haven activities, the United States reference law baseline follows current law in treating controlled foreign companies as separate taxable entities whose income is not subject to United States tax until distributed to United States taxpayers. Under this baseline, deferral of tax on controlled foreign companies' income is not a tax expenditure because United States taxpayers generally are not taxed on accrued, but on unrealized, income.<sup>375</sup>

Deferring taxes for financial firms on certain income earned overseas<sup>376</sup> is another fiscal measure used by countries to promote outward FDI. For example, financial firms in the United States can defer taxes on income earned overseas in an active business.<sup>377</sup>

### iv. Tax credits for certain categories of expenditures

An example of a credit for certain categories of expenditures (R&D, investment in capital goods, etc.) is the United States' interest expense allocation for separate groupings of affiliated financial companies.<sup>378</sup> Under this system, an affiliate's interest expense reduces dividend payments to the parent firm, which are all allocated to foreign source income.<sup>379</sup>

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[http://www.edb.gov.sg/content/dam/edb/en/resources/pdfs/financing-and-incentives/International%20or%20Regional%20Headquarters%20\(HQ\)%20Leaflet.pdf](http://www.edb.gov.sg/content/dam/edb/en/resources/pdfs/financing-and-incentives/International%20or%20Regional%20Headquarters%20(HQ)%20Leaflet.pdf) (last visited April 23, 2013).

<sup>373</sup> United States Office of Budget and Management, "Analytical Perspectives, Budget of the U.S. Government, Fiscal Year 2012," p. 239-276, available at: <http://www.whitehouse.gov/sites/default/files/omb/budget/fy2012/assets/spec.pdf> (last visited February 27, 2013), p. 257.

<sup>374</sup> Clifton J. Fleming, Jr and Robert J. Peroni, "Reinvigorating tax expenditure analysis and its international dimension," 27 *Virginia Tax Review* 437 (2008), pp. 529-531.

<sup>375</sup> United States Office of Budget and Management, "Analytical Perspectives, Budget of the U.S. Government, Fiscal Year 2012," 2012, *op. cit.*, p. 256.

<sup>376</sup> For instance, the United States Congress temporarily extended exemptions for active financing business under Subpart F to the 1 Jan 2014, H.R. 8 (112th): American Taxpayer Relief Act of 2012, Sec. 322, available at: <http://www.govtrack.us/congress/bills/112/hr8/text> (last visited March 20, 2013).

<sup>377</sup> Subsidy scope website of Pew Charitable Trusts, "Information on Deferred taxes for financial firms on certain income earned overseas," available at: [http://subsidyscope.org/tax\\_expenditures/db/group/214/?estimate=3&year=2008](http://subsidyscope.org/tax_expenditures/db/group/214/?estimate=3&year=2008) (last visited March 20, 2013).

<sup>378</sup> Congressional Research Service, "Tax expenditures: Compendium of Background Material on Individual Provisions" Committee on the budget of the United State Senate (2010), available at:

## **v. Allowances for qualifying activities**

Examples of allowances were not commonly found in the countries examined for this chapter, with the notable exception of Singapore. To encourage companies in Singapore to grow their business through M&As abroad, the government implemented a scheme providing M&A allowances and stamp duty relief for qualifying M&As completed between April 1, 2010 and March 31, 2015. Under the scheme, and subject to conditions,<sup>380</sup> a company that acquires the ordinary shares of another company abroad is granted an M&A allowance equal to 5% of the acquisition value. The acquisition value is capped at S\$ 100 million in each financial year, translating into an M&A allowance cap of S\$ 5 million. The amount of stamp duty relief on the transfer of ordinary shares for qualifying M&As is capped at S\$ 200,000 for each financial year. A 200% tax allowance is granted on the transaction costs incurred in qualifying M&As, subject to an expenditure cap of S\$ 100,000 per year of assessment. The allowance on transaction costs is written down in one year. Transaction costs cover professional fees on due diligence (e.g., accounting and tax), legal fees and valuation fees.

## **c. Criteria of eligibility and conditionality**

### **i. Criteria of eligibility**

The fiscal home country measures of the countries analyzed for this chapter do not seem to distinguish between firms in terms of ownership, firm size and host country destination. SOEs do not seem to enjoy any formal legal fiscal advantages as regards their OFDI. As to firm size, except for Singapore, it is somewhat surprising that SMEs do not seem to receive special attention, as they do receive such attention in the case of other HCMs;<sup>381</sup> after all, the share of costs related to investing abroad compared to total costs seems to be much higher for SMEs than for large firms. The countries examined here do not seem to have any special fiscal HCMs favoring particular locations.

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<http://www.gpo.gov/fdsys/pkg/CPRT-111SPRT62799/pdf/CPRT-111SPRT62799.pdf> (last visited February 18, 2013), pp. 67-68.

<sup>379</sup> In contrast, the basic result of the worldwide interest allocation formula, if elected, is to increase the weight given to foreign assets in the allocation formula. This should in turn result in a greater proportion of the interest expense being allocated to United States-source income under the foreign tax credit formula, leading to higher foreign source income and a higher foreign tax credit for firms with excess credits; see, Congressional Research Service, "Tax expenditures: Compendium of Background Material on Individual Provisions," 2010, *op. cit.*, p. 68.

<sup>380</sup> The conditions are the following: The acquiring company must be held by an ultimate holding company incorporated in and tax resident of Singapore. Other minimum criteria are as follows: new or the expansion of substantive operations in Singapore; these may include manufacturing, headquarters, research and development, or other high value-added activities resulting from the streamlining or restructuring pursuant to the M&A deals; and valuable spin-off to the financial or professional services sectors; based on Singapore Economic Development Board, Mergers and Acquisitions Scheme, available at: <http://www.edb.gov.sg/content/dam/edb/en/resources/pdfs/financing-and-incentives/MA%20Circular.pdf> (last visited April 22, 2013).

<sup>381</sup> See the discussion elsewhere in this chapter.

As far as the nationality criterion is concerned, it appears that the majority of fiscal measures are available to all residents of a country, i.e., they do not distinguish between indigenous firms and foreign affiliates located in the country and investing abroad from there.

Some countries do, however, have clear preferences in support of some sectors. For instance, China and the Republic of Korea grant preferential support for the natural resources sector, China and Malaysia for the high technology sector, Malaysia for the manufacturing sector, and the United States for the financial sector. In the case of Malaysia, support for acquisitions of high-technology companies has the appeal of a “catching up strategy” for emerging markets. For headquarters programs (such as those offered in Singapore and Taiwan Province of China), the focus is principally on various service activities: strategic business planning and development, general management and administration, marketing, planning and brand management, human resources management and human capital development, research and development, economic or investment research and analysis, technical support services/shared services, supply chain management, and corporate finance advisory services.<sup>382</sup> The Singapore’s Regional Headquarters Award program further supports this approach by allowing companies to pay a lower tax rate (15% as opposed to 17%) for qualifying income from abroad.<sup>383</sup> These headquarters location programs may be an attractive strategy for small countries seeking to support OFDI because of the inability of home country firms to reap economies of scale in their domestic markets alone.

Countries also have preferences in the application of fiscal measures for particular types of transactions. These included start-ups (France), spin-offs (Canada), new acquisitions (Singapore, Taiwan Province of China, United Kingdom), reorganization of acquired companies (United Kingdom), intra-group activities where there are limited connections with the home country (United Kingdom), the exploitation of intellectual property where both the intellectual property and the controlled foreign companies have minimal connections with the home country (United Kingdom), reinvested income in controlled foreign companies (United States); and interest expenses in financial companies (United States). Measures related to start-ups and new acquisitions can help firms enter foreign markets by making such entry cheaper.

## ii. Conditionality

In some cases, awarding fiscal measures for outward FDI is based on certain conditions that relate to benefits for the home country. To illustrate this, Malaysia offers a deduction for expenses incurred for acquiring foreign high-technology companies on the condition that the

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<sup>382</sup> Singapore, “Headquarters Program Tax incentive information,” available at: <http://www.iyerpractice.com/html/Headquarters%20Programme.pdf> (accessed March 20, 2013) and Taiwan Province of China, Ministry of Economic Affairs, Industrial Development Bureau website. available at: [http://www.moeaidb.gov.tw/external/ctrl?lang=1&PRO=pda.Statistics\\_03](http://www.moeaidb.gov.tw/external/ctrl?lang=1&PRO=pda.Statistics_03) (last visited March 3, 2013)

<sup>383</sup> Singapore Economic Development Board, “Headquarters Award,” available at: [http://www.edb.gov.sg/content/dam/edb/en/resources/pdfs/financing-and-incentives/International%20or%20Regional%20Headquarters%20\(HQ\)%20Leaflet.pdf](http://www.edb.gov.sg/content/dam/edb/en/resources/pdfs/financing-and-incentives/International%20or%20Regional%20Headquarters%20(HQ)%20Leaflet.pdf) (last visited March 27, 2013).

acquisition of such companies results in increased performance or the enhancement of technology and processes of the company's operations in Malaysia.<sup>384</sup> In the case of Singapore's Headquarters Programme, the applicant should be the "nerve center" in terms of a firm's reporting structure at senior management levels; as discussed two paragraphs earlier, other conditions apply as well.<sup>385</sup> Other conditions to obtain a certain fiscal incentive include the hiring of ten additional professionals in Singapore and an additional S\$ 2 million in annual total business spending in Singapore,<sup>386</sup> both by the end of the third year. Moreover, if a company commits to exceed the minimum requirement of S\$ 2 million, customized incentive packages with lower concessionary tax rates on qualified income can be considered in discussions with Singapore's Economic Development Board.<sup>387</sup>

#### **d. Conclusions**

The territorial approach provides a more advantageous fiscal environment for a firm investing abroad than the worldwide approach, since the latter does not give additional support to domestic firms investing abroad. Regardless of the approach, the most widely applied fiscal measure across the countries examined in this chapter were exemptions, followed by rate relief, tax deferral, credits, and allowances. Fiscal measures for the countries analyzed in this chapter do not seem to distinguish, overall (and with few exceptions), in terms of nationality, ownership, firm size, and destination. Home countries, however, have clear preferences to support particular types of transactions or activities (e.g., start-ups, spin-offs, new acquisitions) and to support outward FDI in key sectors (e.g., natural resources, advanced technology).

Fiscal measures to support OFDI can be quickly implemented because they are relatively easy to administer and require only modifications in tax laws. Implementation costs are low (compared to, for instance, financial measures) since the existing fiscal administrative structure can be utilized. Moreover, their impact can be measured relatively easily by utilizing existing fiscal mechanisms and administration staff.

Despite the fact that countries have the sovereign authority to tax any particular category of revenue, fiscal measures seem to be less frequently applied in developed countries. For example,

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<sup>384</sup> See MIDA, "Guidelines for incentive for acquiring a foreign company for high technology," p. 1, available at: <http://www.mida.gov.my/env3/uploads/Forms/Services/03082012/GD-AFC-02.pdf>, (last visited April 23, 2013).

<sup>385</sup> See Singapore Economic Development Board, "Headquarters Award," p. 2, available at: [http://www.edb.gov.sg/content/dam/edb/en/resources/pdfs/financing-and-incentives/International%20or%20Regional%20Headquarters%20\(HQ\)%20Leaflet.pdf](http://www.edb.gov.sg/content/dam/edb/en/resources/pdfs/financing-and-incentives/International%20or%20Regional%20Headquarters%20(HQ)%20Leaflet.pdf) (last visited April 23, 2013).

<sup>386</sup> "Total business spending" refers to total operating costs minus the costs of work subcontracted outside Singapore, royalties and know-how fees paid overseas, raw materials, components, and packaging; See "Incentives under the Headquarters Programme," p. 2, available at: [http://www.edb.gov.sg/content/dam/edb/en/resources/pdfs/financing-and-incentives/International%20or%20Regional%20Headquarters%20\(HQ\)%20Leaflet.pdf](http://www.edb.gov.sg/content/dam/edb/en/resources/pdfs/financing-and-incentives/International%20or%20Regional%20Headquarters%20(HQ)%20Leaflet.pdf) (last visited March 27, 2013).

<sup>387</sup> See Singapore Economic Development Board, "Headquarters Award," available at: <http://www.edb.gov.sg/content/dam/edb/en/resources/pdfs/financing-andincentives/International%20or%20Regiona1%20Headquarters%20%28HQ%29%20Leaflet.pdf> (last visited April 23, 2013).



in the European Union, the application of fiscal incentives by individual member countries is limited by regulations concerning competition in the internal market, as they cannot introduce fiscal incentives that could distort competition in the common market.<sup>388</sup>

Fiscal measures in emerging markets may be part of broader programs supporting OFDI. Good examples are the headquarters programs of Singapore and Taiwan Province of China. Fiscal measures in the context of regional headquarters locations offered by them provide the possibility of building long-term competitive advantages because firms do not change frequently their regional headquarters locations. For countries with small domestic markets and advantageous geographic locations, establishing headquarters programs may be a good OFDI strategy. However, countries offering fiscal measures need to find the right balance between helping their home country firms to be more internationally competitive when investing abroad and protecting their own tax base.

## **C. Summary and implications for competitive neutrality**

### **1. Summary of findings**

FDI flows are still recovering from the recent Western financial and economic crises. While they rose in 2011, they declined to US\$ 1.3 trillion in 2012 and are expected to remain roughly at this level through 2013. Outflows from emerging markets remained elevated, reaching the second highest-level ever recorded in 2012.<sup>389</sup> While firms engage in FDI for various strategic reasons, their decisions do not take place in a vacuum. Rather, they are influenced, among other things, by domestic and foreign regulatory FDI frameworks, investment promotion efforts by host countries and home country measures (HCMs). The last of these are the focus of this chapter.

Developed countries have a lengthy history of offering HCMs. Part of the reason for offering such incentives was to encourage FDI flows to developing countries, to assist them in their economic development (and as a complement to the effort of host countries to attract such investment). However, HCMs often also served to advance a home country's strategic economic interests. Furthermore, by helping home country firms establish a portfolio of locational assets, thereby providing them with better access to markets and tangible and intangible resources, developed country governments enhanced the international competitiveness of their firms, strengthening in this manner their own economies.

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<sup>388</sup> More in Article 87(1), 87(2), 87(3) and 88(2) of the Treaty establishing the European Community, available at: <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:C:2006:321E:0001:0331:EN:PDF> (last visited April 22, 2013) and the Agreement on the European Economic Area, and in particular Article 62(1)(a), available at: <http://www.efta.int/~media/Documents/legal-texts/eea/the-eea-agreement/Main%20Text%20of%20the%20Agreement/EEAagreement.pdf> (last visited April 22, 2013).

<sup>389</sup> UNCTAD, *Global Investment Trends Monitor*, No. 9 (April 12, 2012), available at: [http://unctad.org/en/PublicationsLibrary/webdiaeia2012d19\\_en.pdf](http://unctad.org/en/PublicationsLibrary/webdiaeia2012d19_en.pdf) (last visited October 4, 2013).

As governments of emerging markets began to recognize the benefits of OFDI for the international competitiveness of their firms (and, by extension, their own economies, especially when part of a broader development strategy), a number of them increasingly followed the lead of their counterparts in developed countries by adopting policies to facilitate, support or promote OFDI – in other words, they pursued a policy of helping domestic enterprises internationalize through FDI. The utilization of HCMs by emerging markets is a relatively recent development, since these countries have generally had a much shorter history of investing significant amounts abroad.<sup>390</sup> More specifically, an UNCTAD report found that relatively few emerging markets by the mid-2000s had adopted explicit policies relating to outward FDI, but that there were indications that this was changing.<sup>391</sup> UNCTAD also noted that “[r]ecent official statements indicate that outward FDI promotion is emerging as a policy priority in some quarters,” citing Brazil, China, India, and Singapore as examples.<sup>392</sup> A survey of trade promotion organizations conducted in early 2006 also indicated that a number of emerging markets were planning to start promoting outward FDI.<sup>393</sup>

Overall, the development of OFDI policies appears to follow a fairly distinct path (reminiscent, in some ways, of the investment policy path regarding inward FDI). Countries begin by liberalizing the regulatory framework for outbound capital flows. They then gradually advance to facilitating such flows by, for instance, providing information about investment opportunities and concluding bilateral investment treaties and double taxation treaties. The next step is to support OFDI by, for instance, offering political risk insurance. Eventually, governments establish active promotion programs that provide financial and fiscal incentives to firms to invest abroad. In the context of this OFDI policy path, the use of HCMs falls within the stages of facilitating, supporting and actively promoting outward investment. As in the case of inward FDI promotion, national institutions supporting OFDI are based in the home country (at both the national and sub-national levels), but are also often present abroad.<sup>394</sup>

Similar to the investment policy path for inward FDI, not all countries follow exactly the same path. For instance, it is notable that, over time, some countries seem to have become somewhat less active with respect to the final stage of promoting of outward investment.

In any event, as of the beginning of 2013, virtually all the top home economies among developed countries and emerging markets had various HCMs in place (Table 5).

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<sup>390</sup> UNCTAD, *Home Country Measures*, 2001, *op. cit.*; Sarmah, “Home Country Measures and FDI: Implications for Host Country Development,” 2003, *op. cit.*

<sup>391</sup> UNCTAD, *World Investment Report 2006* (New York and Geneva: United Nations, 2012), p. 202.

<sup>392</sup> UNCTAD, *Investment Brief*, No. 4, 2006, *op. cit.*

<sup>393</sup> The trade promotion organizations of Belize, Botswana, Fiji, Mongolia, and the United Republic of Tanzania indicated that they had plans to start promoting outward FDI. See UNCTAD, *Investment Brief*, No. 4, 2006, *op. cit.*

<sup>394</sup> In 1999, UNCTAD compiled a table indicating the number of overseas offices of OFDI institutions; see UNCTAD, *Handbook on Outward Investment Agencies and Institutions*, 1999, *op. cit.*, p. 21. Since then, many institutions have expanded their foreign net. For instance, Malaysia’s MIDA increased the number of its foreign offices from 12 in 1999 to 25 in 2013.

**Table 5. Outward FDI promotion measures in the covered economies, 2012/2013**

Economy	Information and other support services		Financial measures		Fiscal measures	Investment insurance
	Information	Missions	Loans	Equity	Tax exemptions	
<b>Developed countries</b>						
Belgium	x	x	x	x	x	x
Canada	x	x	x	-	x	x
France	x	x	-	-	x	x
Germany	x	x	x	x	x	x
Italy	x	x	x	x	x	x
Japan	x	x	x	x	x	x
Spain	x	x	x	x	x	x
Switzerland	x	x	x	-	x	-
United Kingdom	x	x	-	-	x	x
United States	x	x	x	x	-	x
<b>Emerging markets</b>						
Chile	x	-	-	-	-	-
China	x	x	x	-	x	x
India	x	-	x	x	-	x
Kuwait	...	...	-	-	...	- <sup>a</sup>
Malaysia	x	x	x	-	x	x
Mexico	x		x	-	-	-
Republic of Korea	x	x	x	-	-	x
Russian Federation	x	x	-	-	x	x
Singapore	x	x	x	-	x	x
Taiwan Province of China	x	x	x	-	x	x

Source: The authors, based on the discussion above.

<sup>a</sup> Available only through the Islamic Corporation for the Insurance of Investment and Export Credit.

To shed some light on what, precisely, home country governments do to help firms invest abroad, this chapter examined measures meant to facilitate, support and promote OFDI, focusing on the top ten outward investing developed economies and the top ten emerging markets (which, together, accounted for an average of three quarters of the world's OFDI flows during 2007-2011). It is important to note, however, that these countries – especially the top outward investing emerging markets – are not a representative sample of all countries that engage in OFDI. The sample of emerging markets was intentionally designed to capture the economies that are the most important outward investors: their firms count most in the world FDI market, and they are also the economies that are most likely to have outward investment policies in place.

On the other hand, there were at least 119 additional emerging markets (i.e., countries not covered in the research undertaken for this study) that recorded OFDI in any year during the period between 2007 and 2011. In fact, the great majority of emerging markets restricts, for one reason or another (e.g., foreign exchange constraints), OFDI flows in one way or another (although many of them are liberalizing such restrictions – see annex Table I), and measures meant to support home country firms’ overseas investments are unlikely to exist. At best, firms from such emerging markets can only engage in OFDI in a limited manner. Firms from these countries are therefore handicapped in establishing an international portfolio of locational assets as a means of increasing their international competitiveness.

With this as background, the main findings of the research undertaken for this chapter are presented next.

Virtually all countries analyzed in this chapter offer some HCMs to their firms, most of which are put in place unilaterally. Nearly all countries have at least one measure under each of the following categories of measures examined in some detail: institutional, informational, financial, and fiscal measures.<sup>395</sup>

To begin with, virtually all the countries examined in this chapter have at least one institution that administers HCMs (not counting tax authorities that administer fiscal incentives). The institutional framework is, however, highly fragmented and includes one or more of the following: investment/trade promotion agencies, export credit agencies, development finance institutions, various government executive agencies, and special institutions. This can lead to duplication of work and overlapping responsibilities. Governments will need to consider whether, in the interest of efficiency and the more effective administration of HCMs, it would be desirable to establish a one-stop shop for HCMs, analogous to what most countries have done when establishing one-stop investment promotion agencies to bundle services for inward investors. (Of course, care needs to be taken to ensure that, if such a one-stop shop is established, it does not become an additional stop for outward investors to navigate.)

In the great majority of countries surveyed for this chapter, many of the individual institutions tasked with OFDI policy matters provide various types of information and other support services to outward investors, including the economic conditions in host countries, the regulatory framework for FDI and investment opportunities, often complementing the information that host countries themselves provide to incoming investors. Many of these home country institutions also offer a broad range of other support services meant to help OFDI, including missions to host countries, investment fairs and training programs.

Many countries do not offer HCMs uniformly to all firms located in their territories, but differentiate between different classes of investors. There is mixed evidence on whether HCMs are available uniformly to domestic firms and foreign affiliates incorporated in the home country.

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<sup>395</sup> It needs to be reiterated, however, that further research may well identify further measures.

In a number of instances, only domestic firms are eligible for certain types of support. Information HCMs are more likely to be uniformly available to home country firms regardless of nationality (i.e., whether they are indigenous firms or foreign affiliates located in the territory of the home country), since the marginal cost of making certain information available to additional firms, such as foreign affiliates, tends to be small.<sup>396</sup>

Firm size, sector and destination of investments are eligibility criteria commonly used by home countries to determine whether an investor qualifies for a HCM, although these criteria are unevenly applied across types of HCMs. With respect to investor size, many countries offer additional support through SME-specific HCMs or allow for more generous terms of support to SMEs looking to expand internationally through FDI. Preferential treatment of SMEs is based on the widely held view that SMEs are key drivers of economic growth, innovation and employment. Moreover, they are thought to need greater encouragement to engage in OFDI to compensate for disadvantages that stem from their small size, such as poor access to finance and information.

HCMs sometimes target investments in specific sectors for which home countries seek to promote OFDI. The choice of sectors reflects policies set by the home country and typically includes natural resources and technologically advanced activities, as well as certain services. Conversely, HCMs may not be available for certain prohibited sectors, particularly when HCMs are administered by development finance institutions and are meant to create a positive development impact in the destination country. Some examples of prohibited sectors include gambling, arms and alcohol.<sup>397</sup> Moreover, a number development finance institutions sensitive to the fact that some projects could have negative environmental, social or cultural impacts in host countries require assessment reports to be submitted by applicants as part of the HCM approval process.

Most HCMs are available to home country firms regardless of the destination of an investment. However, a number of HCMs target specific destinations, typically emerging markets,<sup>398</sup> least developed countries, conflict-affected countries, specific regions within a country, countries with particular economic or diplomatic ties with the home country, or countries with which the home country has concluded a bilateral investment treaty or another international investment

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<sup>396</sup> Political risk insurance is more likely available to both foreign affiliates and domestic firms because they both have to pay a premium for the insurance of policies and hence compensate for the cost of this type of measure.

<sup>397</sup> E.g., the United States' Overseas Private Investment Corporation's categorically prohibited sectors can be found at: <http://www.opic.gov/what-we-offer/financial-products/financing-details/investor-screener#4> (last visited April 20, 2013).

<sup>398</sup> This conclusion is supported by the International Chamber of Commerce (ICC). For example, the 2012 revision of the ICC's Guidelines for International Investment states that investors' home country governments "[s]hould examine the possibility of providing tools and technical assistance that may facilitate private investment of significance to the economic development of the host country." *ICC Guidelines for International Investment 2012* (Paris: ICC, 2012), p. 7. Note, however, that "emerging markets" are not uniformly defined across countries. For example, OPIC lists Greece, Ireland, Northern Ireland, and Portugal in its list of "developing countries" where it can do business, but these countries are excluded elsewhere; see: <http://www.opic.gov/doing-business-us/OPIC-policies/where-we-operate> (last visited on April 20, 2013).

agreement. Conversely, HCMs may not be available for investments in countries that do not have diplomatic relations with the home country, have not concluded BITs with the home country or are subject to bilateral or multilateral sanctions.

Conditionality constitutes an important dimension of HCMs. For reasons described earlier, home countries designing such measures are guided by concerns about possible detrimental effects of OFDI on their own economies. HCMs may therefore be available to home country firms only on the condition that an overseas investment will not lead to negative economic effects in the home country. This “do no harm” approach seeks to ensure that the economic situation in the home country does not deteriorate as a result of OFDI. Other countries take a different approach, explicitly specifying that OFDI should make a positive contribution to the home country. This is a stronger pro-home country approach – an OFDI project should not merely be neutral with respect to its effects on the home economy, but should generate positive economic benefits from a national and/or industry perspective. The nature of these conditions differs between developed countries and emerging markets. For instance, France’s COFACE was initially designed to promote export-generating investments that quickly raised exports of French goods and services.<sup>399</sup> In the past, capital-constrained home countries, for example, seemed to have been more concerned about a possible shortage of foreign exchange and required the repatriation of dividends on the foreign profits of outward investing firms. India was one such example: during the initial phase of the liberalization of outward investment in the early 1990s, it introduced policy changes that included the “[m]andatory repatriation of dividend from the profits from the overseas projects.”<sup>400</sup>

However, it is not unusual for home countries to make support via HCMs conditional on the effects of an investment in the host country. When the destination of OFDI is an emerging market, some home countries wish to see that the investment generates positive development effects, enhances environmental protection and takes into account social considerations. To qualify for HCMs, OFDI projects must show that they satisfy some or all of these requirements.

This chapter did not attempt to assess the effectiveness of individual HCMs. Some evidence from Chinese outward investors (Figure 3) suggests that OFDI measures are considered to be helpful to outward investors. In a 2011 survey undertaken by the China Council for the Promotion of International Trade, well over two-thirds of all respondents (privately-owned firms as well as SOEs) found the country’s overall OFDI policies to be “very helpful,” with at least 60% of all respondents rating all of the various individual HCMs listed as very helpful. Similarly, SMEs seem to have benefitted from measures supporting OFDI.<sup>401</sup> One study on the effectiveness of HCMs in supporting the internationalization of SMEs stated that “[r]espondents

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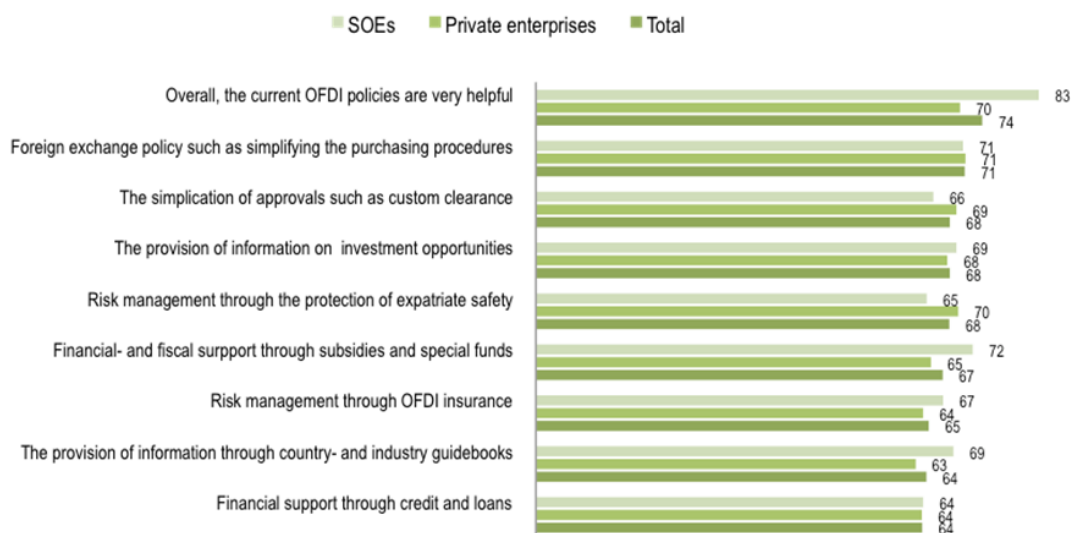
<sup>399</sup> OECD, *Investing in Developing Countries*, 1983, *op. cit.*, p. 60.

<sup>400</sup> Address delivered by Shri Harun R Khan, Deputy Governor, Reserve Bank of India at the Bombay Chamber of Commerce & Industry, Mumbai on March 2, 2012, published in Reserve Bank of India Monthly Bulletin, April 2012, p. 739.

<sup>401</sup> See e.g., Spring Singapore, “Study on SME Internationalisation: Best Practices Across Selected APEC Economies,” 2011, *op. cit.*

who applied for the schemes generally found them effective.<sup>402</sup> The study also revealed that SMEs engaging in overseas expansion had strong preferences for HCMs that provided “long-term financial and practical assistance” and that, where SMEs operated in service industries, pre-investment phase financial assistance was less important.<sup>403</sup>

**Figure 3. Benefitting from China’s OFDI policy: SOEs vs private enterprises, 2011 (Percent)<sup>a</sup>**



Source: Karl P. Sauvart and Victor Zitian Chen, “China’s outward foreign direct investment and its institutional framework”, mimeo. 2013, based on China Council for the Promotion of International Trade 2011 survey data, received from the Asia Pacific Foundation of Canada.

<sup>a</sup> Percentages indicate the share of firms that reported that they benefited from each policy.

**Table 6. The top ten HCMs, ranked according to the expressed preferences of SMEs in various countries, 2011**

Rank	Measure
1	Discounted loans and risk sharing
2	Internationalization and related workshops
3	Exporters/business working capital
4	Assistance with regulatory procedures and requirements
5	Assistance to develop competitive edge
6	Tax deductions on overseas expenses

<sup>402</sup> Spring Singapore, “Study on SME Internationalisation: Best Practices Across Selected APEC Economies,” 2011, *op. cit.*

<sup>403</sup> Spring Singapore, “Study on SME Internationalisation: Best Practices Across Selected APEC Economies,” 2011, *op. cit.*, pp. 37-38; see also table 6.

7	Incentives for reimbursing the cost of business operations
8	Foreign market immersion programs
9	Resolving logistics and transportation issues
10	Online channels for market information/updates

Source: Spring Singapore, Study on SME Internationalisation Best Practices Across Selected APEC Economies, *op. cit.*, p. 37, based on SME surveys conducted by BDO Consultants Pte Ltd.

## 2. Implications for competitive neutrality

In the past, governments viewed HCMs favorably, seeing them as another means of encouraging the flow of capital into emerging markets and contributing to their economic development.<sup>404</sup> A decade ago, UNCTAD even called for the incorporation of HCMs in international investment agreements and put forward “a few of the ways in which the consideration of HCMs might enter into discussions on IIA issues, including policy options developing countries might favour to advance their development objectives.”<sup>405</sup> Later, UNCTAD observed that “...future IIAs should contain commitments for home country measures...”<sup>406</sup> And as recently as 2008, UNCTAD noted “that home country and international measures have been developed and represent important complements to those implemented by host countries, but more efforts are required.”<sup>407</sup> In one report, UNCTAD also noted that the “strong emphasis on investment protection tends to favour the capital-exporting party to an investment agreement, because – de facto – it benefits more from the treaty rights than it is bound by the obligations. Giving more prominence to investment promotion could establish a counterweight, since one would expect that investment promotion becomes also a task of the home country of the foreign investor.”<sup>408</sup> The OECD, too, had welcomed the implementation of HCMs in the past. To illustrate, in a 1993 seminar on “Promoting direct investment in developing countries,” the Organisation’s Deputy Secretary-General remarked that “[t]his meeting will critically examine OECD’s countries’ programmes to promote FDI to developing countries, with a view to determining how they can be improved and made more relevant to those countries.”<sup>409</sup>

More recently, however, the view that HCMs are desirable appears to be changing, as MNEs from emerging markets, especially SOEs, have gained prominence as outward investors. In particular, HCMs have been placed in the context of discussions as to whether such measures convey special advantages to SOEs and in this manner distort the competitive landscape in favor

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<sup>404</sup> UNCTAD, *Home Country Measures*, 2001, *op. cit.* For an in-depth discussion of HCMs, see note 88.

<sup>405</sup> UNCTAD, *Home Country Measures*, 2001, *op. cit.*, p. 53. UNCTAD added (*ibid.*): “IIA [international investment agreement] provisions addressing HCMs could lend greater transparency, predictability and stability to the manner by which HCMs influence development concerns”.

<sup>406</sup> UNCTAD, *World Investment Report 2003*, *op. cit.*, p. 163.

<sup>407</sup> UNCTAD, *World Investment Report 2008: Transnational Corporation and the Infrastructure Challenge*, Sales No: E.08.II.D.23 (New York and Geneva: United Nations, 2008), p. 169.

<sup>408</sup> UNCTAD, *Investment Promotion Provisions in International Investment Agreements* Sales No: E.08.II.D.5 (New York and Geneva: United Nations, 2008), p. 82.

<sup>409</sup> OECD, *Promoting Foreign Direct Investment in Developing Countries*, 1993, *op. cit.*



of these enterprises. This has occurred even though OFDI by SOEs based in developed countries is much more important than such investment by SOEs based in emerging markets,<sup>410</sup> and even though, except for some countries (notably China), private enterprises account for the bulk of OFDI from emerging markets. As a result, discussions in the international arena, such as within the OECD,<sup>411</sup> the negotiations over the Trans-Pacific Partnership Agreement<sup>412</sup> and other upcoming negotiations<sup>413</sup> reportedly seek to impose disciplines on the use of government support for SOEs, as they are considered to be undesirable, distorting “competitive neutrality” in the world FDI market.

The concept “competitive neutrality” concerns the promotion of a level playing field for competition among firms,<sup>414</sup> i.e., a situation in which no business entity is advantaged or disadvantaged solely because of its ownership.<sup>415</sup> Competitive neutrality can be defined as a “legal and regulatory environment in which all enterprises, public or private, face the same set of rules, and government ownership or involvement does not confer unjustified advantages on any entity.”<sup>416</sup> In other words, competitive neutrality can be viewed as a “market framework within which no contact with the state brings a competitive advantage to any market participant.”<sup>417</sup> As stated in a 2012 OECD report on maintaining a level playing field between public and private

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<sup>410</sup> See Sauvant and Strauss, “State-controlled entities control nearly US\$ 2 trillion in foreign assets,” 2012, *op. cit.*

<sup>411</sup> In 2005, the OECD issued the “Guidelines on Corporate Governance of State-Owned Enterprises” and in 2009 OECD’s Working Group on Privatisation and Corporate Governance of State Owned Assets prepared a report that, among other issues, addresses concerns related to the international activities of SOEs; see OECD, “SOEs Operating Abroad: An application of the OECD Guidelines on Corporate Governance of State-Owned Enterprises to the cross-border operations of SOEs,” available at: <http://www.oecd.org/corporate/ca/corporategovernanceofstate-ownedenterprises/44215438.pdf> (last visited April 28, 2013). The discussions of that topic continue in the OECD.

<sup>412</sup> Office of the United States Trade Representative, “What’s Happening in the TPP on 21st-Century Issues” (March 28, 2013), available at: <http://www.ustr.gov/about-us/press-office/blog/2013/march/tpp-21st-century-issues> (last visited April 28, 2013). For a brief discussion of the SOE issue in these negotiations, see David A. Glantz, “The United States and the Trans-Pacific Partnership,” in Andrea K. Bjorklund, ed., *Yearbook of International Investment Law and Policy 2012-2013* (New York: Oxford University Press, forthcoming).

<sup>413</sup> For example, in the context of the forthcoming negotiations a Transatlantic Trade and Investment Partnership; see, Office of the United States Trade Representative, available at: <http://www.ustr.gov/about-us/press-office/factsheets/2013/february/US-EU-TTIP>.

<sup>414</sup> The 2005 OECD Guidelines on Corporate Governance of State-Owned Enterprises stipulate that “[t]he legal and regulatory framework for state-owned enterprises should ensure a level-playing field in markets where state-owned enterprises and private sector companies compete in order to avoid market distortions.” See, OECD, *Guidelines on Corporate Governance of State-Owned Enterprises* (Paris: OECD, 2005), p. 18 available at: <http://www.oecd.org/dataoecd/46/51/34803211.pdf>.

<sup>415</sup> See Capobianco and Christiansen, “Competitive neutrality and state-owned enterprises: Challenges and policy options,” 2011, *op. cit.* The precise definition of competitive neutrality varies across countries. For example, “competitive neutrality” in Australia implies that “business activities do not enjoy net competitive advantages over their private sector competitors (or potential competitors) simply by virtue of their public sector ownership.” See, Australian Government, Department of Finance and Deregulation, available online at <http://www.finance.gov.au/financial-framework/financial-management-policy-guidance/competitive-neutrality.html>.

<sup>416</sup> OECD, “State Owned Enterprises and the Principle of Competitive Neutrality,” 2010, p. 11, available at <http://www.oecd.org/daf/competition/prosecutionandlawenforcement/46734249.pdf>.

<sup>417</sup> OECD, *State Owned Enterprises and the Principle of Competitive Neutrality*, 2010, *op. cit.*, p. 11.

business: “[c]ompetitive neutrality occurs where no entity operating in an economic market is subject to undue competitive advantages or disadvantages.”<sup>418</sup>

The competitive neutrality concept is normally applied to domestic situations in areas such as tax treatment, regulatory treatment and sources of financing in the case of public enterprises, or the treatment of public enterprises in international procurement.<sup>419</sup> In many countries, at least some elements of competitive neutrality are addressed in national competition laws and policies.

More recently, however, there has been a movement to extend the concept of competitive neutrality from a largely domestic one (i.e., equal treatment of public and private actors within the same regulatory environment) to an international one (i.e., no entity in an economic market is subject to undue competitive advantages).<sup>420</sup> This effort is in part advocated by the United States Government (with strong backing from the country’s business community), which has been working with OECD member states and the OECD Secretariat to create a multilateral “Competitive Neutrality Framework”, i.e., “guidelines that would address the issues posed by ‘state capitalism’.”<sup>421</sup> One of the reasons given for this is that domestic competition law cannot be relied upon to regulate “broad state-supported anti-competitive behavior.”<sup>422</sup> In the domestic context, the provision of HCMs that apply across the board in the domestic regulatory environment to both public and private corporate entities would conform to competitive neutrality. In the international context, however, the provision of HCMs, even those available to both public and private entities, may fall foul of the principle of competitive neutrality. For instance, international investors seeking to take over firms in host countries may obtain a competitive advantage as a result of concessional financing provided by home country governments.<sup>423</sup>

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<sup>418</sup> OECD, *Competitive Neutrality: Maintaining a Level Playing Field between Public and Private Business* (Paris: OECD, 2012), p. 69, available at: <http://www.oecd-ilibrary.org/content/book/9789264178953-en> (last visited May 18, 2013).

<sup>419</sup> OECD, “National Practices Concerning Competitive Neutrality,” 2012, *op. cit.*

<sup>420</sup> For instance, the European Union recently started to address implications of State aid for the cross-border economic activities of SOEs in the context of competitive neutrality and the common market. See OECD, “Discussion on Corporate Governance and the principle of competitive neutrality for State-owned enterprises”, European Commission, submitted to Working Party No. 3 of the Competition Committee (October 20, 2009), available at: <http://ec.europa.eu/competition/international/multilateral/corporategovernance.pdf> (last visited May 25, 2013).

<sup>421</sup> Robert Hormats (United States Under-Secretary of State for Economic, Energy and Agricultural Affairs), “Ensuring a Sound Basis for Global Competition: Competitive Neutrality” (May 6, 2011), available at: [http://blogs.state.gov/index.php/site/entry/competitive\\_neutrality](http://blogs.state.gov/index.php/site/entry/competitive_neutrality) (last visited April 10, 2013). A number of OECD documents deal with competitive neutrality; see OECD, “Competitive Neutrality: A Compendium of OECD Recommendations, Guidelines and Best Practices” (Paris: OECD, 2012), pp. 40-50, available at: <http://www.oecd.org/daf/ca/50250955.pdf> (last visited May 20, 2013).

<sup>422</sup> Hormats, “Ensuring a Sound Basis for Global Competition: Competitive Neutrality,” *op. cit.*

<sup>423</sup> Given certain advantages that SOEs (and state-supported enterprises) are seen to enjoy, Hormats argues that, “[u]nder these circumstances, market entry by foreign firms, or foreign goods and services, is either impossible or extremely costly. *This is harmful to U.S. interests because it can give select foreign companies unearned competitive advantages in our own market and third country markets as well as in the market of the country applying the measures. So it is a major trade issue as well as a major investment issue -- and requires comprehensive trade and*

Notably, the discussions about competitive neutrality largely revolve around the concern with “state capitalism,” with a particular focus on SOEs, which are seen to possess various unfair advantages vis-à-vis private firms. However, in the context of OFDI and HCMs it is also possible to consider issues of competitive neutrality in ways that are not based on ownership considerations. First, governments, by introducing measures that support domestic firms’ (whether state-owned or private) overseas investment activities, place these home country firms in a more advantageous position vis-à-vis firms from other countries that do not enjoy the same help from their governments. Second, any home country firm investing abroad with the benefit of HCMs enjoys special advantages vis-à-vis any other firm in the same home country that has no intention to engage in FDI. Third, additional home country support for select categories of outward investors (such as SMEs or operators in particular industries), vis-à-vis all outward investing firms, may also be considered as offering these select investors more favorable treatment than other outward investors. Finally, in the context of competitive neutrality, it could be argued that home country firms that take advantage of home country measures for investing abroad are likely to be in a more advantageous position vis-à-vis host country firms. These various dimensions of competitive neutrality would need to be taken into account in international discussions and negotiations.

Given the focus of this chapter on home country measures meant to help firms to invest abroad, what do its findings imply for international investment policy-making in the context of the competitive neutrality discussion? And, more specifically, how do these findings bear on the discussions’ focus on SOEs benefitting from HCMs?

Since HCMs represent a deliberate attempt to influence the volume and characteristics of OFDI flows, they interfere in the workings of the world FDI market. (In this, they resemble incentives offered by host countries to attract FDI flows.) The principal purpose of these measures is to facilitate, support or promote the international expansion (through FDI) of firms, to help them maintain or increase their international competitiveness, although the desire to encourage FDI flows to emerging markets continues to play a role, at least in the case of some home countries. The governments that offer HCMs, in turn, expect that their economies benefit from having internationally competitive firms located on their territories. HCMs can therefore be part of a broader strategy of promoting the economic development of home countries.

Based on evidence from the countries analyzed for this chapter, HCMs are typically available to home country firms regardless of whether they are private firms, SOEs or national champions (whether state- or privately-owned). None of the financial and fiscal HCMs identified in the research, for example, explicitly seem to favor SOEs or national champions, at least within the formal regulatory framework of HCMs. Even in the case of China, SOEs and non-SOEs formally benefit from the same treatment, as per regulations by the State Council, which explicitly seeks

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*investment norms and disciplines* (emphasis added).”, from Hormats, “Ensuring a Sound Basis for Global Competition: Competitive Neutrality,” *op. cit.*

to encourage and support OFDI by both private companies and SOEs through various measures.<sup>424</sup>

Overall, it is therefore difficult to say that SOEs, by virtue of being SOEs, have, on account of HCMs, systematic competitive advantages over their private counterparts when engaging in FDI, and regardless of whether these SOEs are based in developed economies or emerging markets. This was also found in a recent OECD study, which remarked on the issue of the types of advantages granted to SOEs by governments with respect to cross-border activities: “[e]xisting information on such advantages is often either anecdotal or limited to individual cases.”<sup>425</sup>

However, while HCMs may formally be equally available to private firms, SOEs and national champions, there may be preferential treatment for SOEs and (privately-owned) national champions<sup>426</sup> in their de facto application – but this is difficult to ascertain in a systematic manner. It is also possible that SOEs – and, for that matter, national champions that are privately owned – can benefit from indirect, hidden or informally obtained advantages or simply benefit *more* from HCMs that are available to all, simply because they are typically large firms. Data from China (see Figure 3 above) suggest that, at least in that country, SOEs saw themselves as benefitting more from HCMs than private enterprises did (83% vs. 70%), although the majority of both types of firms considered HCMs to be beneficial to them. SOEs thought that they benefitted more than private enterprises especially with regard to financial and fiscal support through subsidies and special funds, risk management through OFDI insurance and the provision of information through country and industry guidebooks. These findings suggest that, while HCMs may not make a distinction between SOEs and private firms, their usefulness to SOEs (and large firms in general) may be slightly greater than to private firms. This is perhaps attributable to the possibility that SOEs (or large enterprises in general) find it easier to meet the eligibility criteria set by the government agencies administering HCMs.

Moreover, the very nature of being state-owned or being national champions can bestow some advantages upon firms, such as those stemming from monopoly power in the home country and easy access to finance that they may enjoy because of their inherent characteristics as government-backed or large entities. On the other hand, it needs to be noted that SOEs may also have special responsibilities that private firms do not have, ranging from providing certain services (such as housing) to their staff, to having special public goods obligations (such as

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<sup>424</sup> Huang Wenbin and Andreas Wilkes, “Analysis of China’s overseas investment policies,” Working Paper 79 (Bogor, Indonesia: CIFOR, 2011). In 2007, the Ministry of Commerce of the People’s Republic of China and the National Association of Industry and Commerce published several opinions that explicitly stated that private investors would benefit from the same support measures as SOEs with respect to finance, authorization procedures and information services, among other things. (See Webnin and Wilkes, *op. cit.*, p. 22).

<sup>425</sup> Przemyslaw Kowalski, Max Buegge, Monika Sztajerowska, and Matias Egeland, “State-owned enterprises: Trade effects and policy implications,” OECD Trade Policy Papers, No. 147 (2013), p. 10.

<sup>426</sup> Historically, privately-owned conglomerates such as Samsung Group and Hyundai Motor Co. have been nurtured as national champions and outward investors by governments of the Republic of Korea: see, Samuel Kim, *Korea’s Globalization* (Cambridge: Cambridge University Press, 2000) and Frédérique Sachwald, ed., *Going Multinational: The Korean Experience of Direct Investment* (New York, NY: Routledge, 2001).

providing postal, railroad or telephone services to isolated communities, services that would not be viable on a commercial basis). These issues were not examined in this chapter.

Should governments wish to discipline the provision of HCMs in order to be consistent with the principle of competitive neutrality, they need to take into account several considerations. Some HCMs (such as the provision of information) may be less objectionable than other measures that provide more substantive advantages to firms (such as financial HCMs). However, even within the realm of financial HCMs, it needs to be recognized that grants that subsidize the cost of feasibility studies, market research and other pre-investment activities may be a means of correcting information-related market failures, particularly where the potential host country does not have a sophisticated investment promotion agency. Furthermore, certain classes of firms face special difficulties that may warrant special treatment. For instance, to the extent that SMEs face greater difficulties in obtaining access to finance because of structural market failures, mainly relating to lack of sufficient collaterals, imperfect or asymmetric information and exacerbated by macroeconomic uncertainty,<sup>427</sup> financial HCMs that favor SMEs over other market participants may be justified in order to help these firms successfully to internationalize through FDI. Similar arguments premised on market failure could be put forward to justify financing at preferential rates offered by development finance institutions to encourage FDI flows to emerging markets, and especially the least developed countries. By complementing these countries' efforts to attract foreign capital, HCMs administered by development finance institutions contribute to their economic development.

It is also worth recognizing that firms headquartered in developed countries have typically benefitted from HCMs in the course of establishing themselves as multinational enterprises, while firms headquartered in emerging markets are usually new entrants in the world FDI market. This raises the question of whether the latter should not have the opportunity to benefit, as their competitors from developed countries did, from assistance offered by their home countries in their endeavors to internationalize through FDI. If not, to quote Friedrich List, this would be a case of "kicking away the ladder"<sup>428</sup> (or at least one ladder) for emerging market firms seeking to catch up with their developed country competitors.

Finally, it is not clear why any efforts to discipline HCMs should focus on SOEs only – it is not the nature of ownership that infringes on competitive neutrality in the world FDI market, but rather the measures that are offered to, and accepted by, firms, regardless of their ownership, size or other characteristics. In fact, a representative of the country leading the quest for disciplines for SOEs recognized this;<sup>429</sup> however, this insight does not seem to be reflected prominently in the current international discussions on this subject.

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<sup>427</sup> UK Department for Business, "Innovation & Skills, SME access to external finance," *op. cit.*

<sup>428</sup> This expression, attributed to Friedrich List, was adopted as the title of a book by Ha-Joon Chang, *Kicking Away the Ladder: Development Strategy in Historical Perspective* (London: Wimbledon Publishing, 2002).

<sup>429</sup> See Robert Hormats, "21<sup>st</sup> Century Economic Statecraft," New York Foreign Press Center, in reply to a question during a press conference: "Our concern is if the state enterprises receive certain benefits that give it – give them an artificial competitive capability, then we get concerned. But we would get concerned if a private enterprise were given a number of benefits like subsidized credit, subsidized export credit, discounted factor inputs like cheaper

One other possibility is to have HCMs regulated at the international level (if one would want to tackle that difficult issue on that level), focusing on particular types of incentives (e.g., certain financial ones) that entail up-front outlays that are costly to governments and that are not always transparent to tax payers. Another possibility is to regulate (at the national level) specific issues that may arise, such as the possibility of “HCM shopping,” i.e., a firm, instead of investing abroad from its home country, routing an investment through another country that offers HCMs from which it could benefit. Unless that latter country has substantial nationality requirements in place, it would incur the costs of the HCMs that a HCM-shopping firm would utilize without the country necessarily reaping the benefits that it has sought to obtain with them.

At the same time, it needs to be recognized that arriving at any comprehensive international agreement to discipline HCMs is very difficult to achieve.<sup>430</sup> The principal reason is that governments typically seek the flexibility to support “their” multinational enterprises in their quest to be internationally competitive, as they expect that supporting especially national “OFDI champions” will improve the performance of their own economies.

This is the case, even though it is not always clear that, what is good for General Motors or Tata (to use an arbitrary example), is also good for the United States and India, respectively. In fact, as more firms become truly multinational enterprises in terms of having a substantial part of their assets located outside their home countries and seeking to maximize their corporate performance *globally*, the more the interests of these firms may diverge from those of the countries in which they are headquartered, as governments of home countries seek to maximize the benefits associated with the activities of “their” multinational enterprises *nationally*.<sup>431</sup> If this should indeed come to pass, one implication may well be that the challenge for the future is not to

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energy, cheaper land, or exemption from antitrust laws. We would go after those whether it was a state enterprise or not, because those things distort the global competitive environment.” Available at: <http://fpc.state.gov/187301.htm>.

<sup>430</sup> See in this context the unsuccessful efforts during the Uruguay Round of multilateral trade negotiations to reach disciplines on incentives to attract FDI, as incentives for outward FDI are, to a certain extent, the mirror-image of incentives for inward FDI; see Douglas H. Brooks, Emma Xiaoqin Fan and Lea R. Sumulong, “Foreign Direct Investment: Trends, TRIMs, and WTO Negotiations,” 20 (1) *Asian Development Review* 1. But the issue has been dealt with at the regional level, namely in the context of the European Union, as the following case illustrates. Spain’s fiscal law supporting OFDI was questioned by the European Commission as regards the legality of Spanish companies’ deducting financial goodwill derived from the acquisition of shareholding of a foreign company from their taxable incomes. In its October 28, 2009 Decision on the tax amortization of financial goodwill for foreign shareholding acquisitions, the European Commission considered the issue of competitive neutrality: “In addition, the Commission considered that the measure at issue implied the use of State resources as it involved foregoing tax revenue by the Spanish Treasury. Finally, the measure could distort competition in the European business acquisition market by providing a selective economic advantage to Spanish companies engaged in the acquisition of a significant shareholding in foreign companies. Nor did the Commission find any grounds for considering the measure compatible with the common market.” See, European Commission, “Decision of 28 October 2009 on the tax amortization of financial goodwill for foreign shareholding acquisitions C 45/07 (ex NN 51/07, ex CP 9/07) implemented by Spain”, Official Journal of the European Union, available at: <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2011:007:0048:0075:EN:PDF> (last visited November 26, 2012).

<sup>431</sup> For a more in-depth discussion on this issue, see Robert Reich, “Who is us?,” *Harvard Business Review* (1990), pp. 53-64; see also Laura D’Andrea Tyson, “They are not us: why American ownership still matters,” *The American Prospect* (1991), pp. 37-48.

discipline incentives that home countries put in place to help outward FDI, but rather incentives that host countries use to attract such investment – another difficult matter.

In the meantime, governments, particularly of emerging markets that have few or no HCMs in place, need to examine whether, in the context of their overall economic strategies, they ought to develop a coherent and transparent policy on OFDI. If they do, they ought to look at the rich experience of countries that have already put such measures in place.

**D. Annex table I. Regulations relating to outward investment in selected countries, as of 2011**

Economy	Description
Algeria	Residents may transfer capital abroad to finance activities that are complementary to those undertaken in Algeria. The Council on Money and Credit sets the conditions for implementation and issues authorization (Article 126 of the Law on Money and Credit).
Angola	Angolan citizens are permitted to invest abroad, in accordance with the Exchange Law.
Antigua	Large transfers abroad for investment purposes may be made in phases over time by the financial secretary.
Argentina	Trusts established with domestic public sector contributions, resident individuals, and legal entities established in Argentina, except, effective October 28, 2011: (1) ADs; (2) unregistered commercial companies; and (3) other noncommercial companies, foundations, and associations not entered in specific registers, other than tax registers, established by law to enable such legal entities to carry out their particular activity in the country, may buy foreign exchange to make portfolio investments abroad, up to a monthly ceiling of US\$2 million in all institutions authorized to deal in foreign exchange. (Communication A 5236). Investment exceeding the ceiling requires Banco Central de la República Argentina approval. Effective October 28, 2011, additional requirements were established for customer transactions exceeding the equivalent of US\$250,000 during the calendar year, based on the customer's fiscal or financial position without changing the monthly ceiling of US\$2 million. Certain forms of direct investment abroad in the production of goods and nonfinancial services within 30 days from purchasing foreign exchange in the Single Free Exchange Market ("MULC") by firms residing in Argentina are exempt from the US\$2 million ceiling, provided access to the foreign exchange market occurred on or before February 27, 2012, and the other conditions of Communication A 5236 are satisfied.
Aruba	The Central Bank of Aruba may require divestment, repatriation, and surrender of proceeds to the CBA.
Azerbaijan	These capital transactions do not require Central Bank of Azerbaijan approval.
Bahamas	The use of official exchange for direct investment abroad is limited to B\$1 million a person or entity, with an overall limit of B\$5 million a transaction, which may be met once every three years. This limit applies to investments from which the additional benefits that are expected to accrue to the balance of payments from export receipts, profits, or other earnings within 18 months of the investment will be at least equal to the total amount of the investment and will continue thereafter. Investments abroad that do not meet the above criteria may be financed by foreign currency borrowed on suitable terms, subject to individual approval from the Central Bank of Bahamas; by foreign currency purchased in the investment currency market; or by the retained profits of foreign subsidiary companies. Permission is not given for investments that are



	likely to have adverse effects on the balance of payments.
Bangladesh	All outward transfers of capital require approval. For resident-owned capital, approval is granted only in exceptional cases.
Barbados	Commercial banks are authorized to approve investments in private and public unlisted securities in Caribbean Community (CARICOM) countries. These securities must be denominated in regional currencies.
Belarus	National Bank of the Republic of Belarus permission is required.
Benin	All investment abroad by residents is subject to Ministry of Finance (MOF) authorization. At least 75% of such investment must be financed by foreign loans. Authorization is not required for purchases of foreign securities whose issuance or offering for sale in West African Economic and Monetary Union (WAEMU) countries has been authorized by the Regional Council on Public Savings and Financial Markets (RCPSFM).
Brazil	Investment abroad by financial institutions, pension funds, mutual funds, and insurance companies is subject to prudential rules set by their regulators.
Bulgaria	According to the Bulgarian Currency Law, direct investment abroad is defined as follows: (1) acquisition of general partner's rights or equity stake amounting to 10% and more than 10% of the voting rights in the general meeting of shareholders in a nonresident company; (2) establishment of a company on an economic territory other than that of the investor; (3) granting a loan for the purpose of direct investment under item 1 or 2 or connected with an agreement for participation in the distribution of profit; (4) additional investment in an investment under item 1 or 2; or (5) acquisition of real estate on an economic territory other than that of the investor. A declaration to the Bulgarian National Bank (BNB) is required within 15 business days of a direct investment transaction abroad. Resident legal entities and sole entrepreneurs must report to the BNB changes in the initial direct investment within 15 days, according to the ordinance of the BNB. These reports must be submitted to the BNB by the 15th day of the month following the reporting quarter. Reports on the fourth quarter must be submitted to the BNB by January 25, following the reporting quarter. Any transaction in connection with direct investment abroad made by local legal persons or sole proprietors is subject to declaration, for statistical purposes, to the BNB within 15 days after the transaction is closed. Resident legal entities and sole proprietors must submit a quarterly statistical form to the BNB detailing direct investment in other countries. Transactions in connection with an initial direct investment abroad made by local legal persons or sole proprietors, a financial credit between local legal persons, or between sole proprietors and nonresidents, equal to or exceeding the equivalent of lev 50,000; and issuance by local legal persons of securities abroad and/or purchases of securities without the brokerage of a local investment broker are subject to declaration to the BNB within 15 days of the transaction. According to Council Regulation No. 961.2010, the following are prohibited: (1) the

	acquisition or extension of a participation in any Iranian person, entity, or body engaged (a) in the manufacture of goods or technology listed in the Common Military List or in annexes to UN and EU sanction lists; (b) in the manufacture of equipment that might be used for internal repression as listed in annexes to UN and EU sanction lists; (c) in the exploration or production of crude oil and natural gas, the refining of fuels, or the liquefaction of natural gas; and (2) the creation of any joint venture with any Iranian person, entity, or body engaged in (a) the manufacture of goods or technology listed in the Common Military List or in annexes to UN and EU sanction lists; (b) the manufacture of equipment that might be used for internal repression as listed in annexes to UN and EU sanction lists; (c) the exploration or production of crude oil and natural gas, the refining of fuels, or the liquefaction of natural gas; or (d) the participation, knowingly and intentionally, in activities, the object or effect of which is to circumvent the prohibitions referred to in (1) and (2).
Burkina Faso	All investment abroad by residents is subject to Ministère de l'Economie et des Finances (MEF) authorization, including investment through foreign companies under the direct or indirect control of residents of Burkina Faso and investment by foreign branches or subsidiaries of companies established in Burkina Faso. At least 75% of such investment must be financed by foreign loans. Authorization is not required for purchases of foreign securities whose issuance or offering for sale in WAEMU countries has been authorized by the RCPSFM.
Burundi	Outward direct investment is subject to Banque de la République du Burundi (BRB) approval.
Cambodia	There are no specific laws requiring approval, and capital transfers for investment abroad are not restricted. However, transactions equivalent to US\$100,000 or more require declaration to the National Bank of Cambodia (NBC).
Cameroon	Outward direct investment by Central African Economic and Monetary Community (CAEMC) countries is unrestricted when the related transactions do not exceed CFAF 100 million. Only licensed banks may verify and execute such transactions. Transactions exceeding CFAF 100 million must be reported to the MOF 30 days in advance, except for capital increases resulting from the reinvestment of undistributed earnings. The following may serve as supporting documents: (1) the list of registered shareholders of the direct investment enterprise; (2) a copy of the decision to create the enterprise or increase its capital; (3) a description of the enterprise's type of business; (4) the balance sheets, income statements, and auditors' reports for the previous three years, if the investment exceeds CFAF 100 million; and (5) projected balance sheets and income statements, in cases of new enterprises.
Canada	The Special Economic Measures (Burma) Regulations (SOR/2007-285) prohibit Canadians from making investments in property located in Myanmar and certain types of property owned by Myanmar nationals. The Special Economic Measures (Iran) Regulations (SOR/2010-165) prohibit Canadians from making certain investments in the Iranian oil and

	gas sector.
Central African Republic	Outward direct investment by CAEMC countries is unrestricted when the related transactions do not exceed CFAF 100 million. Only licensed banks may verify and execute such transactions. Transactions exceeding CFAF 100 million must be reported to the MOF 30 days in advance, except for capital increases resulting from the reinvestment of undistributed earnings. The following may serve as supporting documents: (1) the list of registered shareholders of the direct investment enterprise; (2) a copy of the decision to create the enterprise or increase its capital; (3) a description of the enterprise's type of business; (4) the balance sheets, income statements, and auditors' reports for the previous three years, if the investment exceeds CFAF 100 million; and (5) projected balance sheets and income statements, in cases of new enterprises.
Chad	Outward direct investment by CAEMC countries is unrestricted when the related transactions do not exceed CFAF 100 million. Only licensed banks may verify and execute such transactions. Transactions exceeding CFAF 100 million must be reported to the MOF 30 days in advance, except for capital increases resulting from the reinvestment of undistributed earnings. The following may serve as supporting documents: (1) the list of registered shareholders of the direct investment enterprise; (2) a copy of the decision to create the enterprise or increase its capital; (3) a description of the enterprise's type of business; (4) the balance sheets, income statements, and auditors' reports for the previous three years, if the investment exceeds CFAF 100 million; and (5) projected balance sheets and income statements, in cases of new enterprises.
China	There are no foreign exchange limits for direct investments abroad made by domestic companies; they are permitted to purchase foreign exchange to engage in direct investment abroad. Domestic institutions may use a variety of legitimate asset sources to engage in outward direct investment, including their own foreign exchange funds, foreign currency loans obtained onshore in accordance with regulations, foreign exchange funds purchased using Renminbi (RMB), or tangible or intangible assets and such profits as are kept abroad. During the preparatory stage before the formal start-up of a foreign project, with State Administration of Foreign Exchange (SAFE) approval, domestic institutions may remit a certain percentage of the total investment abroad. The protocol for review of the source of foreign exchange funds for outward direct investment is based on foreign exchange registration; no approval is required for outward remittances of funds for outward direct investments.
Colombia	Financial institutions supervised by the Financial Superintendency (SF) that want to directly make or increase their capital investment in financial institutions, the securities market, insurance and reinsurance companies, and branches and agencies domiciled abroad are subject to SF authorization. Authorization is also required if they intend to make such investments indirectly through their branches and subsidiaries abroad, provided the investment is made through one or several transactions

	within a period of one year and in compliance with any of the materiality criteria of the regulation, namely: (1) that the initial investment is more than 10% or the increase in investment is more than 5% of the subscribed and paid-up capital of the entity making the investment; and (2) that the financial supervisor in the location where the investment is to be made does not have a memorandum of understanding with the SF. Indirect capital investments or increases not covered by one of the preceding criteria must be reported to the SF before the transaction is executed.
Comoros	Controls relate to the approval of the underlying transactions, not to payments or receipts.
Congo, DR	Controls apply in accordance with the Investment Code.
Congo, Republic	Outward direct investment by CAEMC countries is unrestricted when the related transactions do not exceed CFAF 100 million. Only licensed banks may verify and execute such transactions. Transactions exceeding CFAF 100 million must be reported to the MOF 30 days in advance, except for capital increases resulting from the reinvestment of undistributed earnings. The following may serve as supporting documents: (1) the list of registered shareholders of the direct investment enterprise; (2) a copy of the decision to create the enterprise or increase its capital; (3) a description of the enterprise's type of business; (4) the balance sheets, income statements, and auditors' reports for the previous three years, if the investment exceeds CFAF 100 million; and (5) projected balance sheets and income statements, in cases of new enterprises.
Cote d'Ivoire	All investment abroad by residents, including investment through foreign companies under the direct or indirect control of residents of Côte d'Ivoire and investment by foreign branches or subsidiaries of companies established in Côte d'Ivoire, requires Ministère de l'Economie et des Finances (MEF) authorization. At least 75% of such investment must be financed by foreign loans. Authorization is not required for purchases of foreign securities whose issuance or offering for sale in WAEMU member countries has been authorized by the RCPSFM.
Curaçao and Sint Maarten	These transactions must be approved through a license if the transaction amount exceeds NA f. 100,000.
Cyprus	Direct investment by banks abroad (e.g., establishment of a subsidiary or branch abroad) is subject to approval by the Central Bank of Cyprus.
Dominican Republic	Full-service banks may invest up to 20% of their paid-up capital in branches, agencies, and representative offices abroad and may make equity investments in foreign financial institutions. Full-service banks wishing to invest abroad or to open cross-border branches must fulfill certain minimum requirements, including: (1) authorization from the Monetary Board, which requires approval by the Superintendency of Banks; (2) a solvency ratio equal to or greater than 10% and fulfillment of prudential requirements in the Monetary and Financial Law or in Monetary Board resolutions; (3) sufficient management capacity to perform offshore functions; (4) maintenance of a cooperation agreement between the Superintendency of Banks and the host-country supervisory authorities; (5) approval by the host-country authorities of the investment;

	(6) a favorable report from the host-country supervisory authorities regarding the rating and soundness of the financial intermediary in which investment is to be made; and (7) submission of necessary documentation to the Superintendency of Banks.
Equatorial Guinea	Outward direct investment by CAEMC countries is unrestricted when the related transactions do not exceed CFAF 100 million. Only licensed banks may verify and execute such transactions. Transactions exceeding CFAF 100 million must be reported to the MOF 30 days in advance, except for capital increases resulting from the reinvestment of undistributed earnings. The following may serve as supporting documents: (1) the list of registered shareholders of the direct investment enterprise; (2) a copy of the decision to create the enterprise or increase its capital; (3) a description of the enterprise's type of business; (4) the balance sheets, income statements, and auditors' reports for the previous three years, if the investment exceeds CFAF 100 million; and (5) projected balance sheets and income statements, in cases of new enterprises.
Ethiopia	Residents may not invest abroad.
Fiji	Effective January 1, 2012, individuals may invest up to the equivalent F\$10,000 offshore (previously, this had been suspended). Effective January 1, 2012, overseas investment by nonbank financial institutions and companies require Reserve Bank of Fiji approval (previously, this had been suspended).
Gabon	Outward direct investment by CAEMC countries is unrestricted when the related transactions do not exceed CFAF 100 million. Only licensed banks may verify and execute such transactions. Transactions exceeding CFAF 100 million must be reported to the MOF 30 days in advance, except for capital increases resulting from the reinvestment of undistributed earnings. The following may serve as supporting documents: (1) the list of registered shareholders of the direct investment enterprise; (2) a copy of the decision to create the enterprise or increase its capital; (3) a description of the enterprise's type of business; (4) the balance sheets, income statements, and auditors' reports for the previous three years, if the investment exceeds CFAF 100 million; and (5) projected balance sheets and income statements, in cases of new enterprises.
Ghana	Banks must report these transactions to the Bank of Ghana.
Guinea	Central Bank of the Republic of Guinea's authorization is required.
Guinea-Bissau	All investment abroad by residents is subject to MOF authorization. At least 75% of such investment must be financed by foreign loans. Authorization is not required for purchases of foreign securities whose issuance or offering for sale in WAEMU countries has been authorized by the RCPSFM.
Iceland	Investment in securities issued in foreign currency is prohibited. However, residents may reinvest within two weeks the proceeds from such investments made before November 28, 2008.

India	<p>Indian companies and registered partnership firms (Indian parties) making Overseas Direct Investment (ODI) in Joint Ventures (JVs) or Wholly-Owned Subsidiaries (WOSs) may invest up to 400% of their net worth through the automatic route. Unregistered partnership and proprietorship firms subject to certain conditions may invest abroad up to 200% of their net worth with Reserve Bank of India (RBI) approval. For the purpose of investing abroad, net worth is calculated as of the date of the company's latest audited balance sheet. Indian parties may fund ODI in JVs or WOSs with remittances through market purchases, capitalization of exports, balances in Exchange Earners' Foreign Currency (EEFC) accounts of the Indian party, External Commercial Borrowing (ECB) and ADR/GDR proceeds. Financial entities investing abroad in any activity must also obtain approval from the regulatory authorities concerned in India and abroad. However, approval from a foreign regulator is required only if the foreign subsidiary is engaged in financial services activity. Companies may also invest through share-swap transactions under the automatic route, subject to approval by the Foreign Investment Promotion Board (FIPB) for the inward leg of the transaction. ODI in Pakistan is prohibited. While ODI in Nepal is allowed only in Indian Rupees (INR), ODI in Bhutan is allowed in INR and freely convertible currencies. ODI in other countries is permitted in freely convertible currencies. ODI is prohibited for real estate and banking business. Indian entities may issue corporate guarantees on behalf of the first level operating step down subsidiary under the automatic route. Resident employees of a foreign company's office, branch, or subsidiary in India in which the foreign company holds not less than 51% equity, either directly or indirectly, may invest under an employee stock option plan without limit, subject to certain conditions. A bank guarantee issued by a resident bank on behalf of an overseas JV/WOS of the Indian party, which is backed by a counterguarantee/collateral by the Indian party, must be taken into account for the computation of the financial commitment of the Indian party. Issuance of a personal guarantee on behalf of the JV/WOS by the indirect promoters of the Indian party may be allowed with the same stipulations as for a personal guarantee by the direct promoters. For the purpose of ODI, compulsorily convertible preference shares are treated as equal to equity shares, and the Indian party may undertake financial commitments based on the exposure to JV by way of compulsorily convertible preference shares.</p>
Jamaica	<p>Licensed deposit takers are not prohibited from undertaking certain types of investments and are subject to quantitative prudential limits as regards their investment exposures. Securities dealers, which are subject to margin and capital requirements, are also precluded from undertaking investments, if this would result in the margin and/or capital requirements being breached.</p>

Japan	Outward direct investment by residents in the following industries requires prior notification: (1) fisheries and (2) manufacture of (a) leather or leather products, (b) weapons, (c) equipment related to weapons manufacturing, and (d) narcotics. Controls apply to investment in a company engaged in fishing regulated by international treaties to which Japan is a party or fishing operations under the Japanese Fisheries Law.
Kazakhstan	For statistical purposes, registration with the National Bank of Kazakhstan (NBK) is required for direct investments in excess of US\$100,000, except for direct investments by resident banks, which must notify the NBK of such transactions.
Korea	Residents are free to invest abroad on notification to designated foreign exchange banks. Overseas investment by financial institutions and insurance companies requires Financial Supervisory Commission (FSC) (previously, Ministry of Strategy and Finance - MOSF) notification and approval. Certain examination requirements, such as financing and appropriateness, are applicable only for investments in the banking and insurance businesses.
Lao	Investment by residents abroad requires approval by the relevant authority; on the basis of this authorization, the Bank of Lao PDR approves the exportation of capital. Investment abroad with funds borrowed from a domestic commercial bank is prohibited.
Lebanon	Direct investments by banks in the financial sector abroad require Banque du Liban approval and are subject to the limit set by Article 153 of the Code of Money and Credit.
Lesotho	Residents are free to invest abroad through domestic banks up to the equivalent of M 300,000 a person. Subject to Central Bank of Lesotho (CBL) approval, resident corporations and businesses may invest abroad up to the equivalent of M 100 million in Common Monetary Area (CMA) countries and M 80 million in other countries.
Libya	For prudential reasons, the Central Bank of Libya prohibits purchases of foreign exchange by commercial banks for investment abroad.
Macedonia	Residents must register investments exceeding 10% of the equity capital of a company with the CR within 60 days.
Madagascar	Investment abroad by Malagasy nationals, including by resident-owned foreign companies and their overseas branches and subsidiaries, is subject to MOF authorization.
Malawi	Approval is required.
Malaysia	Effective June 1, 2011, resident companies that meet the prudential requirements stipulated by the Bank Negara Malaysia (BNM) may make any amount of direct investment abroad.
Mali	All investment abroad by residents is subject to MOF authorization. At least 75% of such investment must be financed by foreign loans. Authorization is not required for the purchase of foreign securities whose issuance or offering for sale in the WAEMU countries has been authorized by the RCPSFM.
Mauritania	Outward direct investment is subject to Banque Centrale de Mauritanie (BCM) authorization.

Moldova	Long-term loans/credits for a period longer than five years, for the purpose of establishing or maintaining lasting economic links, are not subject to National Bank of Moldova (NBM) authorization.
Mongolia	There are no controls on outward direct investment.
Morocco	Outward direct investments are subject to Foreign Exchange Office (FEO) approval, but resident firms in operation for at least three years whose accounts have been certified by an external auditor may invest up to an annual maximum of DH 100 million for investments to be made in Africa and DH 50 million (previously, DH 30 million) for other continents. These investments must be related to the usual activities of the firm and may take various forms—in particular, the creation of new enterprises, equity participation in existing enterprises, the opening of representation or liaison offices, branches, etc. In addition, investors involved may freely reinvest the proceeds from the sale or liquidation of their investments abroad. Resident foreign nationals are free to invest abroad, provided the operations are financed from their own funds abroad or from their holdings denominated in convertible dirhams or foreign exchange.
Mozambique	Banco de Moçambique (BM) approval is required prior to the transaction.
Namibia	Applications by residents to retain funds in, or transfer them to, countries outside the CMA for bona fide long-term investment in specific development projects or for the expansion of existing projects owned or controlled by residents are considered on their merits. There is no limit on such investments. Consideration is given to foreign borrowing to finance direct investment with recourse to or guarantee from Namibia, implying that a local corporation's balance sheet may be used in negotiating such a facility. Approved foreign subsidiaries may expand activities abroad without approval, provided such expansion is financed by foreign borrowing or by profits earned by the foreign subsidiary. Namibians over 18 years old may invest abroad in any form or place in a domestic foreign exchange account up to the equivalent of N\$4 million a year on presentation of a tax clearance certificate from Namibia Inland Revenue. Income earned abroad and capital introduced into Namibia on or after July 1, 1997, by individuals resident in Namibia may be transferred abroad, provided the income and/or capital had previously been converted into Namibia dollars. The Bank of Namibia (BON) is now considering applications by private individuals to invest in fixed property (e.g., vacation homes and farms) in Southern African Development Community (SADC) member countries.
Nepal	Nepalese citizens, whether or not they reside in Nepal, may not make any type of investment in foreign countries, except as specifically permitted by government notice. Citizens living abroad who invest funds earned abroad may keep those investments after returning to Nepal if they notify the Nepal Rastra Bank (NRB). Other exemptions include the purchase and sale of insurance policies abroad and investments abroad by banking and financial institutions incorporated in Nepal. Exporters may invest abroad.



Niger	All investment abroad by residents is subject to MOF authorization. At least 75% of such investment must be financed by foreign loans. Authorization is not required for purchases of foreign securities whose issuance or offering for sale in the WAEMU countries has been authorized by the RCPSFM.
Pakistan	Direct investment abroad requires approval under foreign exchange laws. Pakistan nationals as well as residents, including firms and companies, may make equity-based investments, other than portfolio investments, in companies abroad (e.g., joint ventures); however proceeds from such investments must be repatriated. Locally established mutual funds are allowed to invest abroad for the purposes of diversification, up to 30% of aggregate funds (including foreign currency funds) in permissible categories, subject to a cap of US\$15 million or its equivalent at any given time. State Bank of Pakistan (SBP) and Securities & Exchange Commission of Pakistan (SECP) permission is required.
Philippines	Residents are free to invest abroad without restriction for investments not funded by foreign exchange purchased from Authorized Agent Banks (AABs) and/or AAB-foreign exchange corporations. Residents are allowed to purchase foreign exchange from AABs and/or AAB-foreign exchange corporations for investments abroad up to US\$60 million or its equivalent an investor a year, or a fund a year for qualified investors. Purchases to fund outward investments exceeding the limit require Bangko Sentral ng Pilipinas (BSP) approval. Residents may also purchase foreign exchange from Foreign Exchange Dealers (FXDs) and Money Changers (MCs) for outward investments, including investments in bonds or notes of the Philippines and other Philippine entities requiring settlement in foreign currency, regardless of amount, provided such purchases are supported by documents prescribed under existing regulations. Residents may also purchase foreign exchange from AABs and/or AAB-foreign exchange corporations without BSP approval for investments in bonds/notes of the Philippines or other Philippine resident entities requiring settlement in foreign currency, provided such purchases when aggregated with the aforementioned outward investments do not exceed US\$60 million an investor a year.
Poland	A National Bank of Poland permit is required for direct investment, with the exception of the purchase of shares and interests in companies based in Bilateral Investment Treaty countries. No controls apply to investments in EU, European Economic Area (EEA), or OECD countries.
Russia	Direct investments by resident individuals are permitted, provided the requirements of the foreign currency law of Russia are met. Direct investments by resident legal entities that are not credit institutions are permitted, provided the requirements of the foreign currency law of Russia are met. There are no restrictions on direct investment by resident credit institutions associated with the acquisition of stocks (stakes) of foreign entities and not leading to the establishment of subsidiaries abroad. A credit institution with a general license may have subsidiaries abroad subject to authorization and in accordance with Bank of Russia

	(BR) requirements. The BR does not issue authorization to establish subsidiaries in countries (in areas) included, in the manner specified by the laws of Russia, among those governments (areas) that do not participate in international cooperation in the area of combating money laundering and financing of terrorism. In the event of the sale of shares in a Russian credit institution acquired in a public offer (trading) abroad on the basis of BR approval (including in cases in which the percentage of the acquirer's shares in the credit institution's authorized capital will be below the lower limit approved by the BR—including below the amount for which the BR's approval is required—or if the shares in the credit institution will be sold in full by the acquirer), the acquirer is entitled, based on the same BR approval, to carry out transactions to acquire a credit institution's shares that are traded abroad, including through the placement and trading of foreign securities, in compliance with the requirements established in Paragraph (1.4), Subparagraphs (1.4.1) and (1.4.2), of the BR's February 21, 2007, Instruction No. 130-I.
Samoa	These transactions are subject to Central Bank of Samoa approval.
Senegal	All investment abroad by residents is subject to Ministère de l'Economie et des Finances (MEF) authorization. At least 75% of such investment must be financed by foreign loans. Authorization is not required for purchases of foreign securities whose issuance or offering for sale in WAEMU countries has been authorized by the RCPSFM.
Serbia	The Foreign Exchange Inspectorate must be informed of profits earned abroad.
Sierra Leone	Investment abroad is not permitted.
Solomon Islands	Investment by residents and by companies and other organizations operating in the Solomon Islands is subject to certain conditions, including the likelihood of benefit to the Solomon Islands.
South Africa	Approval is not required for FDI, if the total of such new investment does not exceed R 500 million a company a calendar year. Investment exceeding the limit is subject to approval. Requests by corporations are considered in light of the national interest, for example, in terms of the benefit to South Africa's international reserves as a result of exports of goods and services. Effective October 25, 2011, South African companies may make bona fide new outward FDI outside their current line of business. Effective October 25, 2011, the prohibition on the transfer of additional working capital funding for investment below R 500 million an applicant company a calendar year was withdrawn. Effective October 25, 2011, South African companies may acquire between 10% and 20% equity and/or voting rights, whichever is the higher, in a foreign target entity that may hold investments and/or make loans to CMA countries. Effective December 23, 201, the maximum individuals may invest abroad or deposit in a foreign exchange account in South Africa was increased by an additional R 1 million for natural persons over 18 without a tax clearance certificate to the equivalent of R 5 million a calendar year from R 4 million with a certificate, provided they obtain a tax clearance certificate from the South African Revenue Service for the R 4 million

	<p>portion of the investment. There are no restrictions on the type of investment or the way the funds are used. Applications for more than R 4 million a calendar year may be submitted to FinSurv. South African resident individuals' income earned abroad and foreign capital brought into South Africa on or after July 1, 1997, may be retransferred abroad with supporting documentary evidence to the AD that the income and/or capital was previously converted to rand. ADs may, in support of the broader strategy to make South Africa the gateway to Africa, allow private equity funds to apply for annual approval from FinSurv to invest in Africa.</p>
Sri Lanka	<p>Effective January 1, 2011, investment in shares issued by foreign companies is permitted subject to the following limits: (1) listed companies—up to US\$ 500,000 a year; (2) unlisted companies—up to US\$100,000 a year; and (3) partnerships and individuals—a lifetime limit of US\$ 100,000. Funds must be channeled through an Outward Investment Account (OIA). Investment exceeding these limits may be authorized by the MOF, depending on the payback period and other criteria. Effective January 1, 2011, local companies and partnerships may make payments to nonresidents for the purpose of setting up and maintaining places of business such as a branch, liaison, marketing agency, project, representative, or other similar office outside the country, up to US\$100,000.</p>
Suriname	<p>Foreign Exchange Commission (FEC) approval is required.</p>
Swaziland	<p>Effective March 7, 2012, the limit on foreign investment abroad by private individuals was increased from E 2 million to E 4 million. Applications by corporate entities abroad require approval, which is granted on merit.</p>
Syria	<p>These transactions are not allowed.</p>
Tajikistan	<p>Effective December 15, 2011, residents must follow a procedure of either notification (ex-post) or registration (ex-ante), depending on the size of the transaction and the duration of the activity, for transactions involving the movement of capital for residents' direct investments outside Tajikistan, including the establishment of an enterprise or joint venture, the purchase (acquisition) of a nonresident legal entity or of at least a 10% share of one or increase in such a share. The notification requirement applies to transactions up to SM 5 million (amounts in foreign currency are converted at the official National Bank of Tajikistan (NBT) rate on the date operations began) or activities with a duration of up to 12 months; notification must be sent to the NBT with the required documentation within five days of the completion of the operation. The registration requirement applies to transactions exceeding SM 5 million (amounts in foreign currency are converted at the official NBT rate on the date operations began) or activities with a duration of more than 12 months. The required documentation must be submitted to the NBT before the transaction, which the NBT registers within five days of submission; it then notifies the resident of the registration. Residents may carry out the operation only on NBT notification, which is a prerequisite for early</p>

	payment and settlement of this operation. Previously, all such transactions, regardless of the amount and duration, were subject to NBT approval.
Tanzania	These investments require Bank of Tanzania (BOT) approval.
Thailand	Thai juridical persons may (1) invest abroad in the form of direct investment or lend to affiliated companies abroad without limit and (2) lend to nonaffiliated companies up to US\$50 million or its equivalent a year.
Togo	All investment abroad by residents is subject to MOF authorization. At least 75% of such investment must be financed by foreign loans. Authorization is not required for purchases of foreign securities whose issuance or offering for sale in WAEMU countries has been authorized by the RCPSFM.
Tonga	National Reserve Bank of Tonga (NRBT) approval is required for all outward transfers for direct investment, including equity capital and portfolio investments.
Tunisia	Direct investment by residents abroad is generally subject to Banque Centrale de Tunisie (CBT) approval. However, resident exporting companies may freely transfer the equivalent of TD 50,000–500,000 a year to finance representative or liaison offices abroad; TND 100,000–1 million a year for foreign investment in the form of branches, subsidiaries, and equity participation in companies; and up to TD 3 million a year for investments funded from foreign exchange export proceeds held in professional accounts. For non-exporting companies, the limit on transfers abroad for the same types of investment is TD 50,000–250,000 to finance representative or liaison offices and TD 100,000–500,000 for branches, subsidiaries, and equity participation abroad. Residents may freely participate in the capital of nonresident companies established in Tunisia, at the time either of incorporation or of a capital increase and through the purchase of shares or equity in such companies.
Ukraine	Direct investments abroad by residents (and all other types of investments in monetary form) require National Bank of Ukraine (NBU) licenses. Holders of individual NBU licenses to perform foreign exchange transactions may buy foreign exchange for hryvnias and/or exchange foreign exchange, except where such purchases (exchanges) are prohibited by a regulatory act of the NBU.

United States	There are controls on investment transactions with or involving Cuba and Cuban nationals; the Islamic Republic of Iran; the Democratic People's Republic of Korea; Libya, effective February 25, 2011; Myanmar; Somalia; Sudan, except for specified areas, with certain restrictions; Syria, effective August 17, 2011; persons who commit, threaten to commit, or support terrorism; foreign terrorists who disrupt the Middle East peace process; certain persons who threaten international stabilization efforts in the western Balkans, including certain persons indicted by the International Criminal Tribunal for the Former Yugoslavia; certain persons undermining democratic processes or institutions in Belarus and Zimbabwe; certain persons contributing to the conflict in the Democratic Republic of the Congo, Côte d'Ivoire, and Darfur; the former Iraqi regime of Saddam Hussein, its senior officials, and their family members; certain persons who threaten stabilization efforts in Iraq; certain persons who undermine the sovereignty of Lebanon or its democratic processes and institutions; certain persons in connection with the national emergency with respect to the Syria; certain persons associated with the former Liberian regime of Charles Taylor; proliferators of WMD and their associates; significant transnational criminal organizations; and designated narcotics traffickers.
Uzbekistan	Investors may establish enterprises abroad by a decision of the legal entity's top management body. The Ministry for Foreign Economic Relations Investment and Trade (MFERIT) must be notified of the registration of an enterprise abroad. Registration with the Central Bank of Uzbekistan (CBU) is required for contributions to the authorized capital of an enterprise abroad.
Vietnam	Outward direct investment requires a Ministry of Planning and Investment (MPI) permit. Firms engaged in these investments must open an account with a bank with foreign exchange authorization and must register such accounts with the State Bank of Vietnam (SBV). All related transactions must go through these accounts.
Zimbabwe	These investments require Reserve Bank of Zimbabwe and MOF approval on a case-by-case basis.

Source: IMF AREAER database, available at <http://www.elibrary.imf.org/page/AREAER/www.imfareaer.org>.