

Advance copy
25 September 2008
English only

United Nations Conference on Trade and Development

Foreign Direct Investment in Landlocked Developing Countries: Trends, Policies and the Way Forward

Issues Paper prepared by UNCTAD

High-level Investment Forum

New York, 1 October 2008

**Jointly organized by
UN-OHRLLS, UNCTAD, World Bank**

Table of contents

1. Setting	3
2. Recent trends in FDI flows to LLDCs	5
3. Challenges and opportunities for FDI in LLDCs.....	9
4. Recent policy development in LLDCs regarding FDI inflows	13
5. The way forward.....	18
Annex I: List of Investment Policy Reviews and Investment Guides for LLDCs	21
Endnotes	22

1. Setting

In the case of insufficient local factor endowment, foreign direct investment (FDI) may help accelerate development and reduce poverty through employment, transfers of technology and business processes, knowledge of export markets and non-debt creating transfers of capital. FDI can also play a key role in providing the infrastructure (transport, utilities, and telecommunications) that underpins economic activities, freeing scarce government resources for investment in education, health and other basic social services.¹ However, most LLDCs have failed to attract FDI on a sufficient scale to offset poor local factor endowment and accelerate economic development with capital imports.

Only a few of the 31 landlocked developing countries (LLDCs, for a complete list of member countries of this category see table 2) have become hosts to sizable FDI. In these mostly resource-rich LLDCs, FDI plays a critical role in restructuring and upgrading economies, particularly in the extractive industries. Often enabled by foreign equity, modernized and competitive industrial capacity has allowed these countries to reap considerable benefits from the current price surge for minerals, oil and natural gas. The economic performance of these few countries has boosted the average per capita income of LLDCs from \$361 in 2000 to \$811 in 2007.

However, international capital flows bypass the large majority of LLDCs, where per capita income stagnates at much lower levels. In fact, 10 LLDCs recorded per capita income of less than a dollar per day in 2006, placing them among the poorest developing nations. In fact, 16 LLDCs also belong to the category of least developed countries.² LLDCs lag in achieving internationally agreed development goals, such as the MDGs, and make little if any progress in reducing extreme poverty.

Economic stagnation and poverty in these countries are, *inter alia*, also a cause of low or negligible inflows of FDI. The lack of territorial access to the sea is a formidable obstacle on its own to FDI inflows. However, the detrimental effect of being landlocked is compounded by the economic, social and institutional realities in LLDCs. Disincentives to foreign

investors include small domestic markets, shortage of skilled labour, weak institutional capacity for the formulation and implementation of economic policies, and the lack of basic functioning infrastructure.

Since the United Nations General Assembly, in resolution 1028 (XI) adopted in 1957, invited Member States to give full recognition to the needs of LLDCs in the area of transit trade, LLDCs and their development partners have put considerable efforts into policies and actions aimed at improving transport infrastructure and trade facilitation. The importance of these two factors for the economic development of LLDCs was reiterated at the International Ministerial Conference of Landlocked and Transit Developing Countries and Donor Countries and International Financial and Development Institutions on Transit Transport Cooperation, held in 2003 as the latest global event dedicated to the problems of LLDCs. This Conference adopted the Almaty Programme of Action (Almaty PoA), the first United Nations Programme of Action devoted exclusively to addressing their special needs.³

The Almaty PoA emphasizes the importance of private sector investment, including FDI, in developing transport infrastructure. However, the focus of national and international efforts on this sector has yielded only mixed results. Empirical evidence and in-depth analyses of those countries that have successfully overcome the constraints of being landlocked have shown the need for economic policies and measures that reach beyond issues of transport infrastructure and trade facilitation.

Specifically, what is needed are stronger efforts for the modernization of the economic base of LLDCs and a better integration of these countries into regional trade schemes. The increasing recognition that FDI could critically contribute to the economic development of LLDCs is also reflected in the outcome of the UNCTAD XII Conference which gave a broad-based mandate to the UNCTAD secretariat to provide specific advisory services, analytical work and capacity-building programmes in the field of investment promotion for LLDCs.⁴

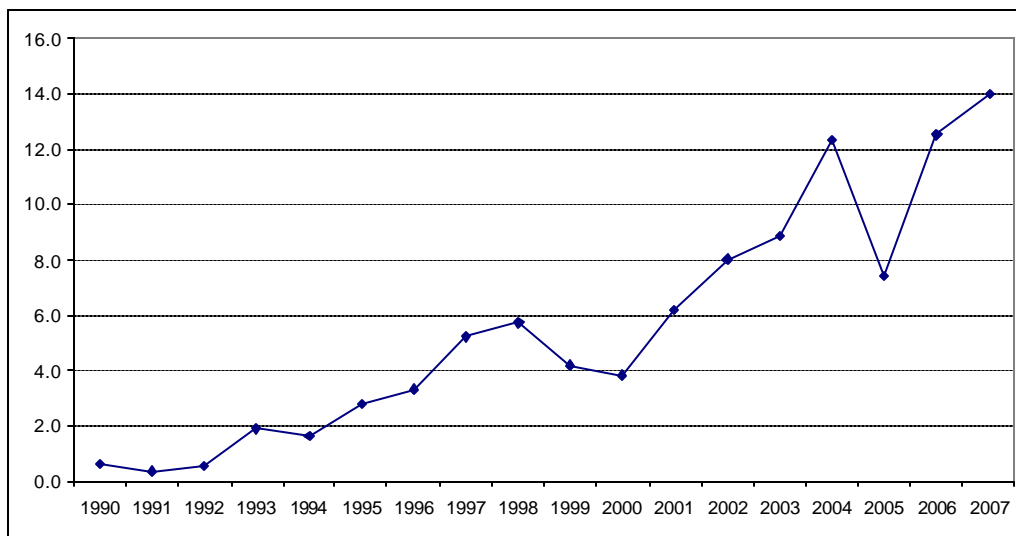
Taking its inspiration from the Almaty PoA and prepared jointly by UNCTAD's Division for Africa, Least Developed Countries (LDCs) and Special Programmes and the Division on

Investment and Enterprise, this paper shifts the scope of economic analysis and policy discussion on LLDCs and FDI from the angle of developing and maintaining transport infrastructure to a broader, economy-wide perspective. By drawing on the most recent data for investment flows to LLDCs and a synopsis of relevant policy developments, it aims at providing a better understanding of (a) latest trends in FDI flows to LLDCs; (b) challenges and opportunities for FDI in LLDCs; and (c) recent policy developments in LLDCs regarding FDI inflows. Finally, it provides some ideas for the way forward to be undertaken by LLDCs, development partners and international organizations to enhance the quantity and quality of FDI flows to LLDCs.

2. Recent trends in FDI flows to LLDCs

The slump in FDI flows to LLDCs in 2005, which interrupted the upward trend that had been ongoing since the year 2000, was a temporary halt. The combined FDI inflows to the group of LLDCs rose again in 2006 and 2007 and reached a record level of \$14 billion in the latter year. FDI flows to LLDCs doubled in 2007 as compared to 2005 and were some 12 per cent higher than in 2006.

Figure 1: FDI inflows to LLDCs, 1990-2007
(Billions of dollars)



Source: UNCTAD, FDI/TNC database (www.unctad.org/fdistatistics)

The upward trend in FDI inflows to LLDCs is remarkable, both in its own right and in comparison with other developing country groupings. From 2000 to 2007, FDI inflows to LLDCs more than tripled from \$3.9 billion to \$14 billion, and they grew significantly faster than the combined FDI flows to all developing countries or to all LDCs. On a per capita basis, FDI to LLDCs amounted to about \$36 in 2007, more than double the \$17 recorded in LDCs.

Table 1: FDI inflows to LLDCs in comparison to other country groupings

	FDI Stock as percentage of GDP	FDI inflows as share of gross fixed capital formation (per cent)	FDI inflows per capita (dollars)	FDI inflows (Millions of dollars)	Annual average of FDI inflows (Millions of dollars)	Annual average growth rate of FDI inflows (per cent)
	2007	2007	2007	2007	2000-2007	2000-2007
World	28	15	277	1 833 324	1 041 198	3.5
Developed economies	27	16	1248	1 247 635	717 783	1.2
Developing economies	30	13	94	499 747	291871	8.7
LDCs	24	15	17	13 375	8 989	16.2
LLDCs	30	17	36	14 026	9 137	17.5
Landlocked LDCs	24	19	15	4 146	2 250	23.0

Source: UNCTAD, FDI/TNC database (www.unctad.org/fdistatistics)

Nevertheless, FDI flows to the group of LLDCs are still very low in absolute terms. The combined share of all LLDCs in global inward FDI was a mere 0.8 per cent in 2007. Singapore alone received more FDI in that year than all 31 LLDCs together; per capita FDI inflows to Singapore were more than a hundred times higher than the LLDC average. Hence, the impressive growth of FDI inflows to LLDCs since the turn of the century needs to be put in perspective against the low starting point.

In addition, a growing differentiation among the LLDCs in terms of their attractiveness for FDI is gaining significance. The bulk of FDI stocks of LLDCs are concentrated in only a small number of countries. Five LLDCs account for about two-thirds of the LLDC total FDI stock, with Kazakhstan alone hosting more than 40 per cent of it.

The significant differences in FDI stocks reflect starkly differing FDI inflows. For many years, FDI has flow n primarily to a few resource-rich and economically more advanced LLDCs. In 2007, Kazakhstan alone accounted for 73 per cent of all FDI inflows to LLDCs. In contrast, inflows to LLDCs with small economies, few exploitable natural resources and low per capita income remained insignificant. Fifteen LLDCs, or half of all LLDCs, received less than 12 per cent of total LLDCs inflows in 2007. Excluding Kazakhstan, average per capita FDI inflows to the group of LLDCs are below the level of LDCs. Remarkable is also the significant outflow of FDI from Azerbaijan, which has been ongoing for several years.

Table 2: FDI Stock in and FDI flows to landlocked developing countries, 2000-2007

	FDI stock 2007	FDI stock as percent- tage of GDP, 2007	FDI stock per capita, 2007	Average annual FDI inflows, 2000-2006	FDI inflows, 2007	Share in total FDI flows to LLDCs, 2007	Per capita FDI inflows, 2007
	Millions of dollars	Per cent	Dollars	Millions of dollars	Millions of dollars	Per cent	Per cent
Afghanistan	1 115.8	11.4	41.1	115.8	288.4	2.1	10.6
Armenia	2 447.6	32.1	815.3	192.3	660.7	4.7	220.1
Azerbaijan	6 597.6	22.0	779.2	1 354.7	-4 817.0	- 34.3	- 568.9
Bhutan	105.9	8.4	161.0	3.3	78.3	0.6	119.0
Bolivia	5 323.1	44.1	558.9	342.1	204.2	1.5	21.4
Botswana	1 300.0	13.1	690.8	296.3	494.9	3.5	263.0
Burkina Faso	769.6	11.3	52.1	22.2	600.0	4.3	40.6
Burundi	47.6	4.7	5.6	1.8	0.1	0.0	0.0
Central African Republic	204.2	12.3	47.0	10.5	27.2	0.2	6.3
Chad	5 084.9	69.7	471.7	574.2	602.8	4.3	55.9
Ethiopia	3 620.1	21.8	43.6	365.6	254.1	1.8	3.1
Kazakhstan	43 381.3	46.3	2 812.9	3 021.7	10 259.4	73.1	665.2
Kyrgyzstan	818.5	22.0	153.9	64.7	207.9	1.5	39.1
Lao PDR	1 179.8	28.2	201.4	47.8	323.5	2.3	55.2
Lesotho	734.9	47.5	366.0	47.3	105.7	0.8	52.6
Macedonia, TFYR	3 083.5	41.2	1513.0	247.1	319.7	2.3	156.9
Malawi	590.3	23.8	42.4	46.8	54.6	0.4	3.9
Mali	1 325.6	19.3	107.5	141.2	360.0	2.6	29.2
Moldova, Republic of	1 812.8	43.6	477.8	139.9	459.3	3.3	121.1
Mongolia	1 326.4	35.7	504.5	124.4	327.7	2.3	124.6
Nepal	126.2	1.3	4.5	3.5	5.7	0.0	0.2
Niger	188.1	4.7	13.2	20.8	27.0	0.2	1.9
Paraguay	2 003.4	17.3	327.0	69.5	189.9	1.4	31.0
Rwanda	170.2	6.0	17.5	10.2	67.2	0.5	6.9
Swaziland	888.5	30.7	778.7	31.9	37.5	0.3	32.9
Tajikistan	1 045.9	32.7	155.3	106.8	400.6	2.9	59.5
Turkmenistan	3 928.0	49.6	791.1	329.4	804.0	5.7	161.9
Uganda	2 909.2	23.5	94.2	256.4	367.9	2.6	11.9
Uzbekistan	1 648.4	8.7	60.2	109.0	262.0	1.9	9.6
Zambia	5 375.1	47.7	450.9	311.5	983.9	7.0	82.5
Zimbabwe	1 492.0	n.a.	111.8	29.7	68.9	0.5	5.2
All LLDCs	100 644.6	30.2	258.0	8 438.5	14 026.2		35.5

Source: UNCTAD, FDI/TNC database (www.unctad.org/fdistatistics)

Although recent aggregate data for the sectoral and industrial distribution of FDI flows to LLDCs are not available, earlier studies of select LLDCs point to a concentration in

the primary and secondary sectors.⁵ The high shares of commodity-exporting LLDCs, in particular Central Asian LLDCs, Chad and Zambia, in recent total FDI flows confirm the earlier findings.

This pattern is at odds with the global FDI trend of the past quarter century toward the service sector and is paradoxical in view of the transport handicap of LLDCs. Economic activities that are disadvantaged by long distances from seaports and markets have been the preferred focus of FDI in LLDCs, whereas the provision of services, which are less sensitive to distance, have largely been neglected.

However, this paradoxical situation can be explained by several factors. Firstly, in many LLDCs there is a lack of human and institutional capacity, in terms of skilled manpower, managerial resources, know-how and technical infrastructure, that is needed for the production and international marketing of high-quality services. An improvement of this situation often depends on investments in education and professional training, which are not attractive to profit-oriented investors. Secondly, as much as many LLDCs have liberalized the goods-producing sectors of their economies, liberalization in services is often lagging. And finally, rich deposits of oil and natural gas in several LLDCs have attracted resource-seeking FDI. Such FDI benefits from high global demand and prices, as well as from cost-effective transportation through pipelines to transshipment points at seaports or directly to final consumer markets.

3. Challenges and opportunities for FDI in LLDCs

The marginalization of LLDCs in global FDI flows is related to a combination of deterrents that include locational disadvantages and economic constraints. Locational disadvantages include geographical isolation, lack of territorial access to the sea and distance from markets, while economic constraints include diseconomies of scale due to small domestic markets, poor endowments of natural resources, inadequate skilled human capital and weak institutional capacity as well as unfavourable macroeconomic

policies and regulatory frameworks that limit, if not forbid, FDI flows to various sectors.⁶

In particular, high transport-related transaction costs are severe disincentives to FDI inflows. An uncompetitive transport sector, unreliable transport infrastructure and weak telecommunication services have made transaction costs far greater in LLDCs than elsewhere in the world. This is especially true of African LDCs. Measured as a freight-to-import ratio, 18 of 30 LLDCs studied had freight costs of 10 per cent or more of the value of traded goods, with seven African LLDCs exceeding 20 per cent and five ranging between 25 per cent and 43 per cent.⁷

However, freight costs constitute only part of the higher transaction costs from the geographical isolation of LLDCs. Costs related to delays and low levels of reliability and predictability in transport also weigh heavily in production chains based on cost-effective and just-in-time delivery⁸

In fact, transport routes with poor infrastructure and weak transit transport capacity run counter to the transnational company (TNC) strategy of globally outsourcing operations when it improves their competitive edge. Such efficiency-seeking FDI flows primarily to export-oriented activities and seeks to exploit comparative advantages of production centres in different geographical locations. Since this strategy implies outsourcing, specialization and intensive intra-firm trade among TNC affiliates, infrastructure and the capacity for timely, cost-effective production and delivery of goods is a critical factor in locational decisions for efficiency-seeking investment.⁹

Moreover, in order to hedge transport and transit risks, companies would need to take preventive measures, such as increasing their inventories or switching the mode of transport (e.g. from land to air), which are costly and may negate the expected economic benefits of investment in these countries.

However, higher transaction costs are not the only factor that deters FDI flows to LLDCs. Market-seeking FDI is attracted by market size and the potential for market growth.¹⁰ If seen from the perspective of market-seeking FDI, most LLDCs are not particularly attractive host countries. In general, they are economies with small markets. GDP per capita in LLDCs equals about one-quarter of the GDP per capita for all developing countries, excluding China. Moreover, 16 LLDCs are classified as LDCs, implying low purchasing power per capita, weak domestic markets, deficiencies in social sectors and economic vulnerability to natural and economic shocks.

In fact, most FDI inflows to LLDCs can be classified as resource-seeking. Relatively low local production costs, the availability of efficient transport infrastructure for exports and high international commodity prices may outweigh the risks and costs associated with long distances to markets. Moreover, the concentration of FDI in the oil and natural gas sectors of LLDCs shows that constraints on international investment and trade are reduced when the value of exported goods is high as compared to transport costs and cost-effective and efficient transport services are provided.

Are therefore LLDCs not endowed with large deposits of minerals and energy commodities bound to be marginalized in terms of FDI inflows and deprived of a major factor of economic growth and development? Empirical evidence from several small and resource-poor landlocked countries that have successfully adjusted their economies to their geographical constraints demonstrates that these countries can attract large-scale FDI inflows. Landlocked countries such as Austria, Luxembourg and Switzerland have been recipients of steady and sizeable flows of FDI for many decades. More recently, landlocked transition economies such as the Czech Republic, Hungary and Slovakia have become hosts to FDI flows that are comparable to those of neighbouring sea-linked countries. In addition to economic restructuring, other factors, such as the proximity, cooperation with and integration in a large regional trading block, also helped these countries to become more attractive for FDI.

Several lessons can be drawn from these landlocked countries that succeeded in attracting FDI:

- A distinction needs to be made between the impact of geographical constraints on hosting FDI and economic and institutional obstacles that adversely affect the attractiveness of these countries for FDI flows.
- Geographical obstacles to FDI can be offset by a favourable investment climate, characterized by stable economic, legal and institutional frameworks; a skilled and flexible labour force; competitive fiscal and exchange rate regimes; liberal policies on capital movements; and continuous efforts to improve institutional and human capacities.
- A strategic policy choice by LLDCs should be able to attract FDI to industries and activities that are not sensitive to distance from markets. This includes services and high value-added goods. In this context, a major issue is the development of location-specific activities that enable these countries to take part in the global service and knowledge economy.
- Modern information and communication technologies (ICT) have become indispensable in the globalizing world economy. Successful landlocked countries have liberalized their telecommunications sectors and mobilized considerable amounts of public and private investments to build high-capacity telecommunications networks. Moreover, a vibrant telecommunications sector not only helps to offset geographical disadvantages in transborder contacts, but also facilitates the development of non-traditional economic activities that rely on the availability of ICT services.
- Economically successful landlocked countries are either in advanced regional economic integration organisations or maintain close economic cooperation arrangements with them. Their landlocked-related geographical and economic disadvantages have virtually disappeared in the course of strong regional

cooperation and integration processes with large markets possessing high purchasing power.

4. Recent policy developments in LLDCs regarding FDI inflows

Governments of LLDCs have increasingly realized that FDI can be a critical source of capital, know-how, technology and access to international markets, as well as for the achievement of social objectives, such as employment creation and poverty reduction. Many LLDCs have begun to actively implement policies to attract larger FDI inflows by providing investment guarantees and fiscal incentives, guaranteeing national treatment, allowing profit repatriation and simplifying administrative procedures. As part of economic liberalization policies, regulatory frameworks affecting FDI have been changed and new economic sectors have opened up for private sector activities. LLDC governments are increasingly prepared to cooperate with foreign investors, sometimes in public-private partnerships.

According to UNCTAD's annual survey on changes to national laws and regulations, 13 LLDCs introduced 28 regulatory changes affecting FDI in 2002-2003, in the period leading up to the Almaty PoA. The overwhelming majority of these regulatory changes, some 85 per cent, encouraged inward FDI. About 35 % of all policy measures were related to investment promotion and 28% were sector-specific. During the period 2006-2007, 24 LLDCs enacted 49 modifications in their laws and regulations. The share of regulatory measures encouraging FDI declined to 60 %, while the shares of policy measures related to investment promotion and of sector-specific policy changes remained largely unchanged with 34 % and 30 %, respectively.

A large number of recent sector-specific liberalization measures providing opportunities for FDI affected the utilities and services sectors. For example, Botswana, Burkina Faso, and Burundi introduced legislation in 2006 that allowed partial or full foreign ownership in the telecommunications sector. Ethiopia approved foreign concessions to its railways company, and Swaziland opened up the insurance sector to FDI.¹¹

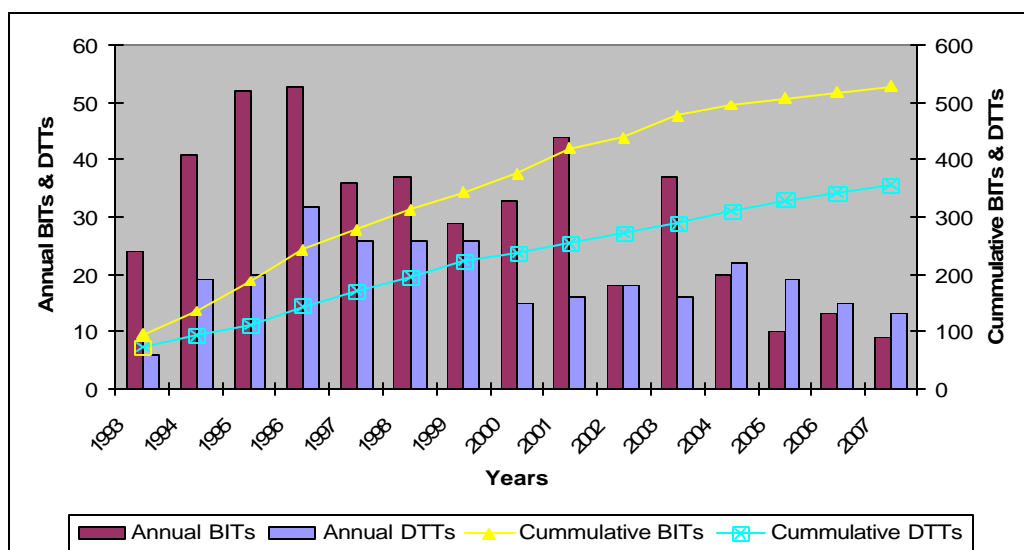
Several LLDCs facilitated the admission and/or establishment of foreign investors in their countries through the creation of investment promotion advisory councils or one-stop shops for new businesses. Other recently introduced measures to attract FDI include tax reductions (Lesotho) and the creation of specialized investment zones or parks (Botswana). Mongolia revised its tax regime with a view to improving the investment climate by reducing the corporate tax rate.

However, the share of policy changes favourable to attracting FDI declined to 70 per cent in 2006-2007. Unfavourable changes aimed to increase the local share of FDI-generated profits or protect local companies from foreign competition. For example, Zambia raised various taxes and royalties and Swaziland reserved the retail trade sector for local firms. In Bolivia, where most companies had frozen new investments after a May 2006 government decree to nationalize oil and gas resources, all foreign TNCs agreed to convert their production-sharing contracts into operation contracts and hand over control of sales to YPF, the Bolivian State-run oil company.¹²

All LLDCs except Bhutan, have concluded bilateral investment treaties (BITs). Moldova with 38 BITs has the highest number of treaties to date. LLDC members of the Commonwealth of Independent States (CIS) were the most active in concluding BITs during the last decade. On average they concluded 29 BITs each from 1992 to 2007. In the same vein, the 15 African LLDCs had concluded a 158 BITs by end 2007. Zimbabwe, with 27 BITs, leads the group. In total, LLDCs have signed 528 BITs by end 2007 (figure 1).

Similarly, LLDCs except Bhutan and Lesotho have concluded many double-taxation treaties (DTTs), mainly with developed countries. Between 2001 and 2007, 19 LLDCs signed 126 DTTs, increasing the total number of DTTs concluded by the group to 357 agreements. The Republic of Moldova leads the group with 42 DTTs while Kazakhstan is next with 37. Zambia leads African LLDCs by having concluded 19 DTTs by end 2007.

Figure 2: Number of BITs and DTTs concluded by LLDCs, Annual and Cumulative, 1993- 2007



Source: UNCTAD, FDI/TNC database

LLDCs have also concluded international investment agreements other than BITs and DTTs. Between 2000 and 2007, they concluded 16 Economic Integration Agreements (EIAs) (excluding agreements that were concluded as members of regional integration organizations (REIOs)). Most of these agreements were cooperation agreements with the European Union and trade and investment framework agreements with the United States.

Development partners have also supported LLDC by liberalizing market access for certain products originating in those countries. The most comprehensive initiatives in this respect are the Everything But Arms (EBA) Regulation introduced by the EU and the African Growth and Opportunity Act (AGOA) of the U.S.

The EBA Regulation grants duty-free and quota-free access for products from LDCs, of which 16 are landlocked, with the exception of arms and munitions. AGOA¹³ provides preferential access, especially for apparel and textiles, to the U.S. market for selected States of sub-Saharan Africa, including 13 LLDCs. In addition, the AGOA III

programme promotes investment in infrastructure projects, including for transport, ICT and agriculture, and encourages bilateral investment agreements. Although these measures have not been formulated specifically to assist LLDCs attract FDI, preferential market access may provide them with a critical advantage in location decisions by foreign investors.

Many LLDCs have also strengthened their institutions for the formulation of investment promotion policies and strategies. Currently, 27 LLDCs¹⁴ have national investment promotion agencies (IPAs) whose primary function is to promote their countries as international investment destinations. Most of these IPAs are members of the World Association of Investment Promotion Agencies (WAIPA), which not only benefits them through global networking activities, but also provides them with access to FDI-related information and training programmes.

Membership in Regional Integration Organisations (REIOs) helps address several geographical and economic constraints on FDI inflows. Currently, LLDCs are members to 12 different REIOs with investment provisions.¹⁵ Many of these have also enacted Regional Trade Agreements (RTAs) to liberalise trade among member states by abolishing customs duties and eliminating non-tariff barriers.

Table 3: Membership of LLDCs in select regional integration organisations (REIOs) and economic integration agreements (EIAs)

LLDC	Membership in REIOs with investment provisions	Bilateral and inter-regional EIAs with investment provisions
Afghanistan		Trade and Investment Framework Agreement with the United States (2004)
Bhutan	BIMSTEC, SAARC	
Bolivia	ANDEAN	Co-operation Agreement between the European Community and the Andean Community (2003); Agreement on Trade and Investment Promotion with the Republic of Argentina (2004); Economic Complementation Agreement with Peru (2004)
Botswana	COMESA, SADC	
Burkina Faso	ECOWAS, WAEMU	
Burundi	ECGL	
Central African Republic	CEMAC	
Chad	CEMAC	
Ethiopia	COMESA	
Kazakhstan		Trade and Investment Framework Agreement with the United States (2004) Agreement on trade relations with the United States (2003)
Lao PDR	ASEAN	
Lesotho	COMESA	
Macedonia, TFYR	CEFTA	Free Trade Agreement with the EFTA States (2000); Stabilization and Association Agreement with the European Community (2001); The Central European Free Trade Agreement (CEFTA) (2006)
Malawi	COMESA, SADC	
Mali	ECOWAS, WAEMU	
Republic of Moldova	CEFTA	The Central European Free Trade Agreement (CEFTA) (2006)
Mongolia		Trade and Investment Framework Agreement with the United States (2004)
Nepal	BIMSTEC, SAARC	
Niger	ECOWAS, WAEMU	
Paraguay	MERCOSUR	Economic Complementation Agreement between MERCOSUR and ANDEAN (2003)
Rwanda	ECGL	Trade and Investment Framework Agreement with the United States (2006)
Swaziland	SADC	
Tajikistan		Trade and Investment Framework Agreement with the United States (2004)
Turkmenistan		Trade and Investment Framework Agreement with the United States (2004)
Uganda	COMESA	
Uzbekistan		Trade and Investment Framework Agreement with the United States (2004)
Zambia	SADC, COMESA	
Zimbabwe	SADC, COMESA	

5. The way forward

Attracting FDI for development will continue to be a formidable challenge for most LLDCs. Based on the preceding analysis, the best choice appears to be the implementation of two complementary strategies: First, policies and measures targeting the factors that make LLDCs unattractive for FDI need to be implemented. The second strategy is to avoid excessive transaction costs and other landlocked-related impediments to international trade by attracting FDI to economic activities that are less sensitive to market distance.

The implementation of the first strategy is a complex and daunting task. The Almaty PoA calls for a series of actions that directly address landlocked-related impediments to FDI and fit well within the first strategy. The full and effective implementation of the Almaty PoA is therefore an important step towards the attenuation of investment-detering factors.

Key policies and measures of such a strategy include:

- The upgrading of transport and communication infrastructure. The Almaty PoA lists seven priority sectors for infrastructure development and maintenance: rail transport, road transport, ports, inland waterways, pipelines, air transport and communications. These infrastructure sectors are areas for FDI in themselves, and LLDCs may be able to attract investors if they can provide low political risk, larger markets through regional integration, and joint financing opportunities.
- Institutional reform and continuous efforts to improve the policy environment for FDI. The ultimate objective should be to attract more diversified and larger FDI inflows by facilitating the entry, the establishment and the retention of FDI in LLDCs.
- Better integration of LLDCs in regional cooperation and integration schemes, with a view to making landlocked countries land-linked economies. Regional cooperation and integration, as emphasized in the Almaty PoA, addresses

market size and other constraints to FDI and helps to create "win-win" situations between LLDCs and their transit neighbours, in particular in transport infrastructure projects.

- Public-private sector partnerships in the development of transport infrastructure and efficient transit transport systems. The international community, including financial and development institutions and donor countries, should join these partnerships by providing financial and technical assistance, as well as capacity-building for the public negotiation and management of such endeavours.

The second strategy requires economic restructuring to allow for the specialized production of tradables that are less affected by transport costs and distance. LLDCs should promote FDI in services such as tourism, back-office services, and in some cases even banking or other financial services. In manufacturing, they should promote high-value but low-bulk goods, such as high-precision instruments, IT components or pharmaceuticals. In agriculture, LLDCs should target high-value products, such as cut flowers or off-season fruits and vegetables that lend themselves to expeditious and cost-efficient air transport.

Policies and measures for the implementation of this strategy include:

- Facilitating entry, establishment and protection of FDI in these sectors.
- Targeted incentive schemes for such economic activities, including tax breaks and tax holidays, partnerships with R&D institutions, grants for employment creation, and financial assistance for the acquisition of industrial/commercial premises or R&D facilities. However, fiscal incentives should be used in a nuanced way, taking into account the long-term impact on government revenue.
- Strengthening the quality and quantity of the local workforce to attract FDI in sectors that rely on skilful and specialized labour, as well as technical institutions and research centres for the development of tradables in line with the objectives of this strategy.

- Concerted investment promotion efforts to target industries and companies chosen by LLDC governments, as well as investment facilitation and aftercare programmes at the national and sub-national levels to assist in the establishment and operation of new projects.

Although the primary responsibility for providing an attractive investment environment for foreign investors rests with the LLDC governments, home countries generating FDI should support FDI-seeking efforts by LLDCs. In fact, many home country governments encourage investments in LLDCs from major companies based in their countries by adopting and implementing economic, financial and legal incentives. Such measures could include investment guarantees, co-financing, tax relief and information on investment opportunities in LLDCs, as well as the conclusion of investment agreements and double-taxation treaties with LLDCs.

Moreover, the Almaty PoA calls for partnerships between the public and private sectors, both domestic and foreign, to attain its fundamental objectives. Such partnerships are also important for the creation of new investment opportunities and should be actively pursued by both LLDC governments and their bilateral and multilateral development partners.

The Almaty PoA attributes, under its Priority Four, a key role to the international community in its implementation, including the encouragement of FDI for development. Relevant United Nations organisations, such as UNCTAD, the World Bank, regional commissions and other multilateral development partners should play a more proactive role in assisting LLDCs to create conditions that attract more FDI. Pertinent actions include: advisory services, training in and the dissemination of investment promotion best practices, review of and advice on investment policies, economic analysis of investment opportunities, the organization of regional and sectoral investor meetings, assistance in forging genuine partnership between private and public sectors, and other measures that raise awareness of both the need and opportunities for FDI in LLDCs.

Annex 1

List of Investment Policy Reviews and Investment Guides for LLDCs

UNCTAD, Investment Policy Review, Zambia, 2006, UNCTAD/ITE/IPC/2006/14

UNCTAD, Investment Policy Review, Rwanda, 2006, UNCTAD/ITE/IPC/2006/11

UNCTAD, Investment Policy Review, Botswana, 2003, UNCTAD/ITE/IPC/ MISC.10

UNCTAD, Investment Policy Review, Lesotho, 2003, UNCTAD/ITE/IPC/2003/4

UNCTAD, Investment Policy Review, Nepal, 2003, UNCTAD/ITE/MISC/2003/1/Rev.1

UNCTAD, Investment Policy Review, Ethiopia, 2002, UNCTAD/ITE/IPC/MISC.4

UNCTAD, Investment Policy Review, Uganda, 2000, UNCTAD/ITE/IIP/Misc.17

UNCTAD, Investment Policy Review, Uzbekistan, 1999, UNCTAD/ITE/IIP/Misc.13

UNCTAD/ICC, An Investment Guide to Rwanda, 2006, UNCTAD/ITE/IIA/2006/3

UNCTAD/ICC, An Investment Guide to Mali, 2006, UNCTAD/ITE/IIA/2006/2

UNCTAD/ICC, An Investment Guide to Uganda, 2004, UNCTAD/ITE/IIA/2004/3

UNCTAD/ICC, An Investment Guide to Ethiopia, 2004, UNCTAD/ITE/IIA/2004/2

UNCTAD/ICC, An Investment Guide to Nepal, 2003, UNCTAD/ITE/IIA/2003/2

Endnotes

- ¹ See also UNCTAD, World Investment Report 2008, New York and Geneva 2008, Transnational corporations and the infrastructure challenge, p. 85 ff.
- ² For more information on least developed countries see: UNCTAD, The Least Developed Countries Report 2008, New York and Geneva 2008.
- ³ Almaty Programme of Action: Addressing the Special Needs of Landlocked Developing Countries within a New Global Framework for Transit Transport Cooperation for Landlocked and Transit Developing Countries. A/CONF.202/3.
- ⁴ UNCTAD, Accra Accord. Addressing the opportunities and challenges of globalization for development. UNCTAD XII Conference, Accra 2008, para. 150.
- ⁵ UNCTAD, FDI in Landlocked Developing Countries at a Glance. New York/ Geneva 2003, UNCTAD/ITE/IIA/2003/5, p. 6.
- ⁶ Chowdhury, A.K. / Erdenebileg, S., Geography against development. New York 2006, p. 7 ff.
- ⁷ Stone, J.I., Infrastructure development in landlocked and transit developing countries: Foreign Aid, Private Investment and the transport cost burden of landlocked developing countries. New York 2001, UNCTAD/LDC/112, p. 10.
- ⁸ Arvis, J.-F., Raballand, G., Marteau, J.-F., The cost of being landlocked: Logistics Costs and supply chain reality. World Bank Policy Research Paper 4258, 2007, p. 4.
- ⁹ UNCTAD, World Investment Report 1998, Geneva 1998, p. 188.
- ¹⁰ UNCTAD, World Investment Report 1998, Geneva 1998, p. 91.
- ¹¹ UNCTAD, World Investment Report 2007, pp. 38-39.
- ¹² Ibid, p. 39 ff.
- ¹³ By modifying certain provisions of the African Growth and Opportunity Act (AGOA), the AGOA Acceleration Act of 2004 (AGOA III of 12 July 2004) extends preferential access for imports from beneficiary Sub Saharan African countries until 30 September 2015.
- ¹⁴ Afghanistan, Armenia, Azerbaijan, Bolivia, Botswana, Burkina Faso, Burundi, Ethiopia, Kazakhstan, Kyrgyzstan, Lao PDR, Lesotho, Macedonia, Malawi, Mali, Moldova (Republic of), Mongolia, Nepal, Niger, Paraguay, Rwanda, Swaziland, Tajikistan, Uganda, Uzbekistan, Zambia, Zimbabwe.
- ¹⁵ The Andean Community (ANDEAN), the Association of East Asian Nations (ASEAN), the Bay of Bengal Initiative for Multi-Sectoral Technical and Economic Cooperation (BIMSTEC), the Central European Free Trade Agreement (CEFTA), the Economic and Monetary Community of Central Africa (CEMAC), the Common Market for Eastern and Southern Africa (COMESA), the Economic Community of Western African States (ECOWAS), the Economic Community of the Great Lakes Countries (ECGL), the Southern Common Market (MERCOSUR), the South Asian Association for Regional Cooperation (SAARC), the Southern African Development Community (SADC) and the West African Economic and Monetary Union (WAEMU).