



**International Association
for the Study of Insurance Economics**
"The Geneva Association"

Route de Malagnou 53
CH-1208 Geneva
<http://www.genevaassociation.org>

Tel. +41-22-707 66 00
Fax. +41-22-736 75 36
E-mail: secretariat@genevaassociation.org

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An International Regime for Foreign Direct Investment (FDI): Implications for Services

by Karl P. Sauvant *

In September 1995, the OECD began negotiations on a Multilateral Agreement on Investment, and the possibility is being discussed to put FDI on the agenda of the WTO during the WTO's first ministerial meeting in Singapore in December of this year.¹ Why - and what does this mean for services?

I Why?

I do not need to elaborate much on the "why" because the basic reason - the importance of FDI in today's world economy - is well known.² Let me just stress four points:

- Investment in the broadest sense is the source of all economic growth, and FDI typically has the additional advantage of bringing with it not only capital but also technology, R & D, organisational and managerial practices and access to markets - in short, FDI is really a package of tangible and intangible assets. In 1995, over half of FDI flows (\$235 billion) and some half of the FDI stock (\$2.6 trillion) were in services.
- FDI is today the most important vehicle to bring goods and services to foreign markets and, beyond that, to link national economies.
- Flows of FDI are closely interrelated with trade and technology flows.
- FDI, trade and technology transfers are undertaken primarily by TNCs which are increasingly pursuing corporate strategies that make their geographically dispersed

* Karl P. Sauvant, Chief, Research and Policy Analysis Branch, UNCTAD's Division on Transnational Corporations and Investment, Rm. E-8006, Palais des Nations, CH-1211 Geneva 10, phone: +41'22'907.57.05, fax: +41'22'907.01.94. This note is based on dinner remarks at the "World Trade in Services Conference", Harvard University, John F. Kennedy School of Government, 26-27 October 1995.

¹ Brittan, Sir Leon (1995). "Investment liberalization: the next great boost to the world economy", *Transnational Corporations*, vol. 4, no. 1, pp. 1-10.

² See UNCTAD-DTCI, 1995, *World Investment Report 1995: Transnational Corporations and Competitiveness* (Geneva: United Nations), United Nations publication, Sales No. E.95.II.A.9.

affiliates subject to a unified strategy. The result is the emergence of an international production system which, in a sense, is the productive core of the globalizing world economy.

Since all countries now appreciate the importance of FDI, they all compete to attract it, and parts of this competition is carried out through policy competition. UNCTAD has monitored changes in FDI laws since 1991: out of 373 FDI law changes during the period 1991-1994, only 5 were not in the direction of greater liberalisation.³

At the national level, today, it is generally recognised that, in order to attract FDI, in order to be part of the international production system, national FDI frameworks have to incorporate standards that typically provide for national treatment, guarantee against nationalisation, allow international arbitration in cases of disputes, and permit the free transfer of funds.

It is the recognition of the importance of FDI for growth and development and the broad-based movement towards liberal national FDI-policy regimes that explains the widespread interest in FDI I mentioned earlier and that, in the opinion of a number of countries, should lead to negotiations on this issue in the WTO.

II What does this mean for GATS

Let me first emphasise that, obviously, lots still needs to be done to implement, refine and further develop the GATS framework. After all, GATS has opened the door to an entirely new world, and a big and complicated world, at that.

At the same time, on today's and tomorrow's world trade agenda, the erstwhile "new" issue of "services" is now - in a sense, unavoidably - an "old" issue. The implication is that the dynamics, the new energy, will increasingly shift to the creation of an investment regime (if not more - after all, we are dealing with international production) and, of course, other issues.

Work on this "new issue" of FDI - I know how ironic this sounds to a number of us - can (and must!) build on what GATS has accomplished, doing primarily two main things:

1. To call a spade a spade, i.e., we have to deal with investment (including investment in services) as an investment issue, not just as a form of trade, and, accordingly, to deal squarely with the whole range of issues associated with FDI, beginning with the definition, continuing with protection, and ending with RBPs.
2. We need to extend the GATS FDI provisions (or, more literally, commercial-presence provisions) to FDI in goods and expand them to include other issues that belong into an investment agreement. If this were, indeed, to happen, it would actually be the continuation of an interesting process: the old GATT Agreement for goods was the starting point for the GATS discussions; and GATS - with all due respect for the TRIMs Agreement - could well become the starting point for a General Agreement on Investment. Naturally, negotiations of such an Agreement would be exceedingly difficult (as we know from the negotiations of GATS) because such an Agreement, were it ever to be negotiated, could, quite possibly, reach much further into the national

³ Ibid., p. 272

fabric than any trade agreement ever has done.⁴ This is a reflection of the fact that FDI is a mechanism of deep integration, and that an investment agreement, therefore, would need to begin tackling the whole range of national policies associated with deep integration.

What would a General Agreement on Investment, would it ever be negotiated, mean for services? If and when such an Agreement should come into existence, it would not only build on GATS, it could also have implications for it because, after all, it would cover a good part of what today we still call trade in services. One could imagine various scenarios.

- If the OECD FDI negotiations are successful and produce, indeed, a high-standards binding agreement with a dispute-settlement mechanism, this would, it appears to me, strengthen the FDI side of GATS - at least for the OECD members, if not beyond, namely if its standards would be generalised, e.g., via GATS' MFN clause.
- If such an OECD agreement becomes a truly multilateral instrument because many important non-OECD members accede to it, this strengthening effect of GATS would be correspondingly extended to other countries as well (with, again, the caveat of a possible further extension via the applicability of MFN).
- A third possibility is that negotiations begin in the WTO - based, perhaps, on the OECD work - and lead eventually to an agreement in the WTO. It would be quite conceivable that such an agreement would not embody the same high standards that a purely OECD agreement would enshrine - but it would have the advantage of being truly multilateral. And, of course, it could be strengthened over time, in a process with which, after all, we are familiar from GATT.

Which of these three possibilities will carry the day - or, more likely, which fourth possibility will carry the day - is impossible to predict at this time. In addition, it is not inconceivable that future negotiations will have to be seen - and increasingly will take place - in a broader context, a context which also includes, e.g., competition policy. One should not forget that what is involved is, after all, not FDI per se but international production (including in services), and the architectural design for a building that houses international production may simply require a different approach than the design for a building that houses services and FDI by themselves and separately.

Two things suggest themselves:

1. The beginning of the negotiations on an investment agreement in the OECD may well have the effect of speeding up consideration of this issue at the WTO. In any event, the task of deepening the FDI side of GATS may well shift to negotiating contexts other than the GATS.
2. GATS negotiators and GATS experts have a special responsibility to make sure that the experience they have gained in negotiating the FDI parts of the GATS Agreement is made available to all those who are beginning to negotiate or discuss a multilateral arrangement for FDI. More broadly speaking, there is plenty of room for analysis of the need, nature and scope of a multilateral arrangement for FDI and, in particular, its development dimension.

⁴ See Sylvia Ostry, 1992, "The Domestic Domain: The New International Policy Arena", *Transnational Corporations*, vol. 1, no. 1, pp. 7-26.