



THE BENEFITS OF FOREIGN DIRECT INVESTMENT:

PROMOTING ECONOMIC
DEVELOPMENT IN
LATIN AMERICA AND
THE CARIBBEAN

What is Foreign Direct Investment?

Foreign Direct Investment (FDI) is a core aspect of the economic development policy: it has direct and indirect impacts on multiple areas of the economy, local productivity, and tax revenue. FDI is one of the main sources of external finance for developing economies.

FOREIGN INVESTORS SEEK TO:

Access available resources at a lower cost than in their country of origin.

Expand the markets for their products and services in countries they invest in and neighboring countries.

Find the best value for money and achieve efficiency.

Acquire strategic capabilities and new technologies, while building synergies.



WHAT DO COSTA RICA AND JAPAN HAVE IN COMMON?

Both are home to manufacturing plants and advanced research institutes owned by Boston Scientific, a global leader in medical device development, with operations in 125 countries. The company has invested over US\$100 million and employs over 2,000 people in each country.



WHAT DO IRELAND AND CHILE HAVE IN COMMON?

They're home to Google's regional headquarters and data centers for Europe and Latin America, respectively. Google chose them because they provided the ideal combination of reliable infrastructure, a skilled workforce, and transparent, business-friendly regulations.



Why is Foreign Direct Investment important?

Investment can have a huge impact on a country.

For each US\$1 spent on investment promotion generated US\$56 of additional FDI in the host country.

A US\$1 increase in FDI leads to another US\$1 in domestic investment.

One job created through FDI leads to the creation of one to two other jobs in the country.

Every US\$1 of FDI is associated with US\$2 in additional exports.

POSITIVE EFFECTS OF FDI ON RECEIVING ECONOMIES



SOURCE: Compiled by the authors with data from Harding and Javorcik (2011 and 2012).





A VIRTUOUS FDI CIRCLE

SOURCE:
Compiled by the authors based on data from “Rethinking Productive Development: Sound Policies and Institutions for Economic Transformation” (IDB, 2014) and “Investment Promotion and FDI Inflows: Quality Matters” (Harding and Javorcik, 2012).



How can countries attract FDI?

Investors take three key factors into consideration: the **political context**, **economics** (the availability of resources or assets, markets for goods and services, and production costs), and **investment facilitation**.

FOR AN INVESTMENT PROMOTION STRATEGY TO BE EFFECTIVE, IT MUST:

Close information gaps.

Offset imperfections in the functioning of international markets.

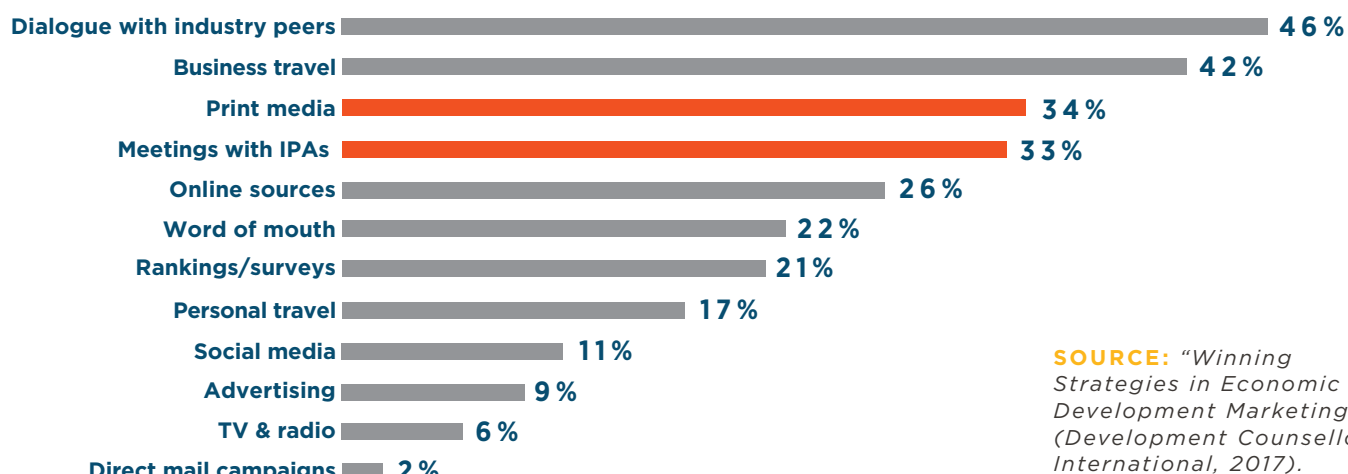
Understand the competition to improve value propositions.



Countries should establish and work with specialized organizations such as investment promotion agencies (IPAs) to improve the investment climate, close information gaps, and provide investors with appropriate support. The most important activities that IPAs carry out are **marketing, leads generation, and facilitation services.**

Investment promotion agencies

FACTORS THAT MOST INFLUENCE COMPANIES' PERCEPTIONS OF A COUNTRY'S BUSINESS CLIMATE



SOURCE: "Winning Strategies in Economic Development Marketing" (Development Counsellors International, 2017).

51%

of corporate executives rely on resources provided by the local government and chambers of commerce to establish overseas operations.

National, subnational, and local governments need to commit to attracting investment and make it a priority, the Economist Intelligence Unit argues.



New trends in FDI

The rise of new types of investment means that IPAs need to offer services that are tailored to these needs.

CURRENT TRENDS AND NEW CHALLENGES FOR IPAS:



Alignment with the Sustainable Development Goals (SDGs)



Strategic alliances



SMEs as a source of FDI



Mergers and acquisitions



Robustness and resilience of global value chains



Domestic shipping centers



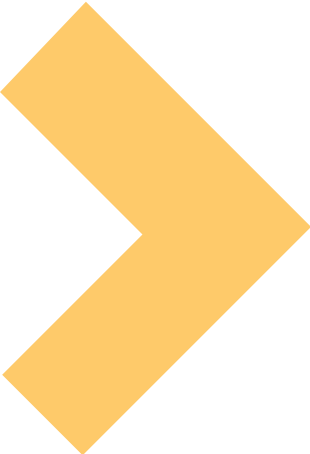
Digital competence centers



Localized manufacturing and microfactories

TRADITIONAL	Physical infrastructure	➤	Safe and secure digital infrastructure	TODAY
	Sector-specific/functional skills	➤	Digital skills	
	Database of suppliers	➤	Partner ecosystem	
	Volume of workforce/human resources	➤	Smaller/higher-quality workforce	
	Competitive labor costs	➤	Total operating costs	
	Focus on cost	➤	Cost-quality balance	
	Volume of investment and employment	➤	Impact on social and environmental sustainability	
	Individual investments	➤	Integration into regional value chains	





The most successful IPAs have a clear organizational structure, including clearly defined roles and activities, measurable budgets and objectives, and top-level support for their activities, which are grouped in the following categories:

**Image-building
(nation
branding).**

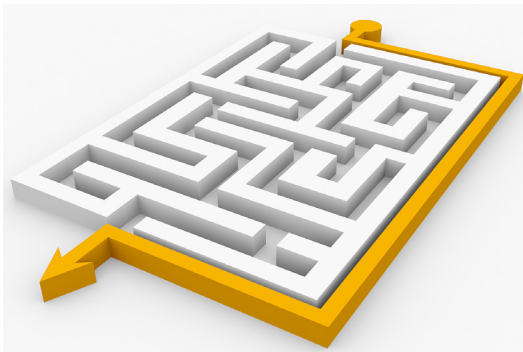
**Investment
facilitation
and retention.**

**Promoting investment and
policy improving the business
climate.**



INSTITUTIONAL FRAMEWORK

An appropriate institutional framework seeks to help countries attract FDI more efficiently and effectively. It should complement other institutional efforts and strengthen capacities. Governments should ensure that IPAs can provide support for investors throughout the investment, establishment, and reinvestment processes.



INNOVATIVE DIGITAL TOOLS

The most advanced IPAs have digital one-stop investment shops to simplify and streamline the paperwork and processes needed to operate in a given territory; platforms with access to georeferenced information systems; proptech applications with augmented and virtual reality functions; and artificial intelligence systems or data-driven solutions.



How the IDB can help

The IDB can provide support as you design and implement strategic interventions.



PRIORITIZING ACTIVITIES AND INDUSTRIAL SECTORS

Countries that focus on a selected sectors usually attract more investment. Instead of implementing broad-reaching marketing strategies, IPAs should focus on investors' needs and specialize to make their efforts more effective. The post-Covid trend toward realigning global value chains (GVCs) is an opportunity for IPAs to implement strategies that focus on strengthening and attracting investment in areas of GVCs in which their country has a clear value proposition.



NATION BRANDING

Nation branding is a strategy to position and capitalize on a country's image in the international market. The objective is to promote tourism, boost exports, and attract investment.





STRENGTHENING HUMAN CAPITAL

Having the right human capital is essential for attracting investment. Human talent needs to have the training, qualifications, and skills required by companies looking to invest in the country. According to fDi Markets, this is the third-most important location variable in LAC.

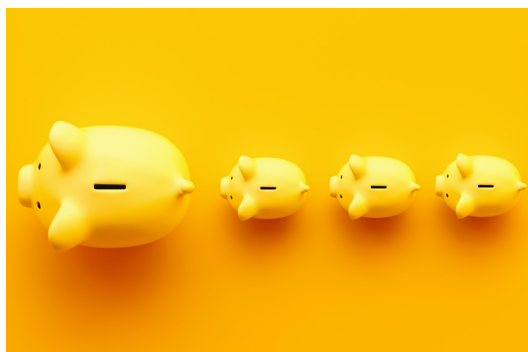


LINKAGES WITH LOCAL SMES AND SUPPLIER DATABASES

Strategies of this sort seek to “integrate” foreign investors with domestic companies. Multinationals develop ties and roots in the country, which contributes to its development and reduces the risk of relocation.



How the IDB can help



INVESTMENT RETENTION AND EXPANSION

70% of FDI projects are follow-on investments. However, countries often don't pay enough attention to helping international companies grow. Investment aftercare programs include multiple approaches to retaining investment, encouraging follow-on investments, and increasing local economic impact.



INCENTIVES FOR FOREIGN INVESTMENT

These incentives may be financial, fiscal or other (e.g., regulatory or training-related incentives). These include special economic zones or tools with a proven track record like finishing schools, which finance a percentage of the training costs of staff hired by foreign companies.



How the IDB can help



COMPETITION POLICY

Truly free competition provides a competitive environment for businesses and many benefits for consumers (lower prices, better quality, greater choice, etc.). In this sense, competition is one of the keys to integrating LAC more efficiently into global markets, improving the flow of FDI, and fostering economic growth and development.



SUSTAINABLE FDI

There is a new emphasis on facilitation services and sustainable investment. This includes establishing investment support strategies and programs that help distribute the positive impacts of investment more equitably both geographically and socially, and support host countries and investing companies contribute to achieving the SDGs.

Two examples of these approaches are support for accessing renewable energies for production and/or gender-diverse suppliers.





About the IDB

At the Trade and Investment Division of the IDB's Integration and Trade Sector, we provide support that enables LAC countries to implement innovative solutions to make the region more productive, open, and connected with the world. Our projects and applied research help reduce the major costs of trade: logistics, information, regulatory issues, and financial costs.

WORKING WITH THE TRADE AND INVESTMENT DIVISION ADDS VALUE

- ▶ Technical support during the design and implementation phases.
- ▶ A multidisciplinary team.
- ▶ Articulation with other areas of the IDB for knowledge transfer.
- ▶ A network of international contacts and experts.
- ▶ Flexible execution schemes that are in line with IDB procedures.
- ▶ Access to IDB-managed public-private networks and business meetings (ConnectAmericas, American Business Dialogue, Outsource2LAC, LACFlavors, and business summits with China, India, Dubai, Korea, and Japan, among others).
- ▶ Online training in FDI promotion and institutional strengthening.

For more information, please contact fdi@iadb.org



PROMOTING ECONOMIC DEVELOPMENT IN LATIN AMERICA AND THE CARIBBEAN



The IDB and Foreign Direct Investment

The Integration and Trade Sector* provides financial and technical support to the vast majority of countries in LAC.



48
loans



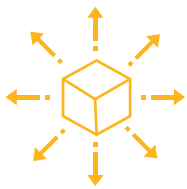
\$3,450
billion



67
technical cooperation
projects



26
countries



**Export
promotion and
investment
attraction**



**Trade
agreements
and institutions**



**Trade
facilitation and
logistics**

**Datos del 2020*



The IDB works to support investment promotion in the countries of Latin America and the Caribbean within the framework of its Vision 2025, which seeks to boost the recovery of the productive sector, promote social progress, and strengthen good governance and institutions.

