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Economic Impacts of Investment Facilitation

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After the successful adoption of the Trade Facilitation Agreement (TFA) in 2014, investment facilitation is gaining importance as the next policy priority for a plurilateral agreement under the World Trade Organization (WTO). In fact, more than 110 WTO Members aim to conclude the negotiations on the Investment Facilitation for Development (IFD) Agreement by mid-2023 after only three years of formal negotiations. Investment facilitation refers to actions taken by governments designed to attract foreign investment and maximize the effectiveness and efficiency of its administration through all stages of the investment cycle. The IFD agreement focuses on allowing investment to flow efficiently for the greatest benefit, particularly to developing and least developed member countries, with the aim of fostering sustainable development. The flow of efficiency is improved through transparency, predictability, and efficient frameworks with streamlined procedures. In addition, the agreement aims at improving intra-governmental coordination and international cooperation on investment matters.

To provide policymakers with essential information for ongoing negotiations and to fill an existing research gap on investment facilitation, we examine the economic impacts of a potential IFD agreement. Generally, quantifying such impacts is predicated on an assessment of current frictions that limit investment on an international basis and the mechanism by which policy impacts these frictions.

One consideration of the IFD is the ability to reduce regulatory and non-tariff barriers (NTBs). These barriers are sometimes difficult to quantify because they come in the form of idiosyncratic regulatory regimes. We leverage the Investment Facilitation Index (IFI) developed at the German Institute of Development and Sustainability, which evaluates the adoption of over 100 investment facilitation measures across 86 countries and illustrates that countries with lower levels of adoption (i.e., higher investment barriers) belong to the low-income and lower-middle-income country group. Thus, based on these data, we are able to simulate several scenarios of the potential IFD agreement representing different depths and country coverage, which helps to determine the degree of commitments needed to create a substantial economic impact.

Starting with a lower bound scenario, which incorporates investment facilitation commitments already present in the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (e.g., transparency of regulations affecting foreign investment, digital signature, protection of confidential information), we estimate that the IFD could improve global welfare by more than $250 billion. Pushing the boundaries of the policy scope by incorporating provisions from several proposals submitted at the beginning of the structured discussions (commitments in terms of transparency and predictability, fees and charges, and electronic governance), the ambitious IFD scenario suggests an increase of global welfare by almost $800 billion.

Furthermore, extending the country coverage to India and the United States, currently disengaged from the negotiations, might boost global gains to as much as $1.1 trillion.

Of these benefits from the IFD, G20 countries stand to gain 43-46% of total global benefits and for the EU this share ranges between 24-28%. Low and middle-income countries have the most to gain from a successful implementation of the IFD, given their low level of current practice in investment facilitation. This creates an opportunity to substantially improve their foreign direct investment environments. In monetary terms, the expected gains of these countries range between $10 and $30 billion depending on the depth of the potential IFD. This represents a substantial proportional welfare gain for these countries. In contrast, the gains are relatively modest for developed countries, such as the United States or Australia, which already have sophisticated investment facilitation frameworks and a high level of access to foreign capital.

While some benefits from the IFD will spill over into the broader global economy and impact countries taking no action, gains will rise the most with increased participation in the agreement. This is especially true for developing countries like India, which experiences the highest reduction of foreign direct investment barriers due to the current complexity in navigating the country's regulatory and business environment. The gains multiply for India if it becomes a full member of the IFD with around four time the gains associated with spillovers from reforms made by partners currently engaged in IFD negotiations. India has decided not to engage in the IFD discussions, however, based on a set of legal and philosophical objections. These include the fact that the initiation of WTO negotiations generally requires a consensus among the member countries. Plurilateral discussions, like the IFD, are inconsistent with this tradition. Furthermore, there is a concern that plurilateral initiatives are a distraction from legitimate (agreed to) negotiations. This includes unresolved issues from the Doha Development Agenda, which are important for India.

Overall our analysis shows that the potential gains from an IFD agreement exceed those available from traditional trade liberalization. This provides a strong incentive for non-participating developing countries to join the IFD, reform their investment frameworks along the IFD agenda, and use the support structure contained in the section on special and differential treatment for developing and least-developed country members.

Indeed, external technical assistance and capacity development programs are essential for on–the-ground implementation of investment facilitation provisions, since LDCs face important technical and financial barriers as well as potential opposition from actors with vested interests. Thus, the described benefits from the IFD agreement strongly depend on its actual implementation in the signatory countries.

Download the working paper to read the details of our research on investment facilitation.

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