KEY MESSAGES

As the COVID-19 pandemic spreads and its economic impact deepens, supporting businesses and investors requires not only fiscal and financial stimulus, but also complementary investment climate policies and programs.

- FDI is the largest source of external finance for developing countries, and global inflows are expected to fall more than during the 2008 global financial crisis. Priority policy actions include retaining existing investment by providing targeted “investor aftercare initiatives” to key FDI firms and their lead local suppliers, preserving supply chains, and providing waivers from market access restrictions.

- Supporting private sectors firms, particularly SMEs that may be acutely affected, requires financial support and regulatory flexibility. Specific policy actions include temporary financial stimulus packages and subsidies/state aid, facilitating companies’ strategic re-orientation towards production of in-demand goods and services, and relaxing regulatory and administrative requirements and fees.

- Access to critical inputs and supplies must be underpinned by transparency and key competition principles. Priority policy actions include ensuring price transparency, limiting the use of price controls to only exceptional circumstances, and enforcing anti-cartel rules to avoid price fixing or bid rigging.

CONTEXT

The outbreak of COVID-19 is reducing global production and investor confidence. COVID-19 and government measures to contain it, coupled with international production networks and globalized consumption, disrupt business activities through four distinct channels: falling demand, reduced supply, tightening of credit conditions and liquidity crunch, and rising uncertainty (Figure 1 maps out the supply and demand shocks). As workers in many parts of the world have gone into quarantine, there is an increasing shortage of labor across many sectors. Temporary closure of production facilities has led to a sharp slowdown in production and disruptions in global value chains, such as automotive and electronics. A decline in confidence and lower consumption demand, in part reflecting income losses due to lay-offs, have led to the reduced production or even closing of many manufacturing plants around the world.

Price gouging may be expected due to the combination of a negative supply shock and a positive demand shock as people panic buy and stockpile necessities and governments procure large volumes of goods and services needed to combat the health crisis. Such shocks may also increase the risk of anti-competitive behavior, as suppliers may coordinate to disproportionally pass through price increases to final consumers or to coordinate volumes of supply.

Figure 1: COVID-19 is a demand-cum-supply shock to all the countries

This note is a living document, based on the information available as of March 31, 2020. It is prepared by the World Bank Group Global Investment Climate Team, and addresses the three investment climate areas (business regulation, competition policy and investment policy & promotion) by examining channels of impacts on countries and proposes policy responses for the immediate term.
SUPPORTING BUSINESSES AND INVESTORS
INVESTMENT CLIMATE POLICY RESPONSES TO COVID-19

Fiscal measures like public support for sick pay and health care expenditure could provide social protection to cushion against shocks; other fiscal transfers could help credit-constrained households to smooth consumption where incomes have shrunk. Financial measures, such as liquidity injections, can help firms stay in business and maintain GVC links. This note summarizes complementary investment climate policies and programs.

1. FDI is the largest source of external finance for developing countries, and global inflows are expected to fall more than during the 2008 financial crisis. Retaining investment is key.

Global foreign direct investment (FDI) was weak before the outbreak and is expected to fall more than during the 2008 financial crisis. Already, three of the most affected countries and regions—China, the EU and the US—are among the top sources of outbound FDI, effectively reducing the global “FDI pie” given the resources they need domestically. Initial estimates suggest that the future decline in global FDI in 2020 caused by COVID-19 will range from 30-40 percent (UNCTAD) to possible 50 percent (OCO Global). In February 2020, new cross-border acquisitions fell below US$10 billion from the normal monthly average of US$40-50 billion.3

Countries’ exposures to declining FDI depends on sector composition as well as openness (Figure 2). The most affected economies are (a) those with open economies in terms of trade and FDI, (b) significant exporters of services, and (c) host countries experiencing the outbreak most severely. For example, FDI flows to China were 25.6 percent lower in February 2020 than in February 2019.4

Data source: bilateral FDI database (global Investment Climate unit)
Note: Left: Critical nodes in the global FDI network (FDI stock 2017); Bilateral FDI stock = FDI stock from A to B + FDI stock from B to A; Node size denotes the weighted degree, which is the sum of all edges connected to a node weighted by the bilateral FDI flow. The thickness of edges is proportional to bilateral FDI flow. Nodes are colored based on their World Bank region. Label size is proportional to each node’s weighted degree.
Right: Top 10 countries with most COVID-19 cases as of March 31 are United States, Italy, Spain, China, Germany, France, Iran, United Kingdom, Switzerland and Turkey. Highly impacted sectors cover basic materials, consumer cyclicals (including airlines, hotels, restaurants, and leisure), energy, and industrials (including automotive and electronics), based on the MNC’s global stock index performance in all sectors (December 2019 to March 2020).

Direct impacts on FDI and value chains will be greatest in sectors such as tourism, travel, and automotive. For example, demand for the tourism and transport sectors is particularly vulnerable to pandemics as travel restrictions, lockdowns in major tourist and business destinations, and falling consumer confidence and affordability further reduce travel. This worsening business outlook will in turn drive reductions in FDI in these sectors. In addition, FDI in the automotive and electronics sectors is likely to decline due to falling demand, rising uncertainty, and potential supply chain concerns.

The world’s largest multinational corporations (MNCs) in the automotive, airlines, and tourism sectors have reduced their 2020 earnings estimates by 44 percent, 42 percent, and 21 percent, respectively, on average (UNCTAD 2020). Major hotel companies are expecting to reduce 70 percent of hourly hotel employees, and airlines cut their employees’ pay by 25-50 percent (OECD, 2020). The pandemic will also indirectly drive down FDI via reduced economic activity, and these impacts will be concentrated in cyclical industries: Demand for the energy, basic materials, retail, garments, entertainment, is particularly sensitive to overall economic performance.

FDI flows to low- and middle-income countries in the Middle East and North Africa (MENA) and Sub-Saharan Africa (SSA) are most exposed to direct and indirect COVID-related risks. FDI flows into these two regions are more likely to come from highly-impacted countries. In addition, economies in MENA and SSA tend to be more natural resource-intensive, meaning reductions in resource-seeking FDI from rapidly fallen commodity prices will disproportionately affect them. As the pandemic continues to spread across countries, other developing regions will be increasingly exposed to a possibly big drop in FDI inflows.

Efforts in current crisis situation should focus on the retention of existing foreign investors, and preservation of supply chains connecting foreign and domestic (often SME) suppliers. Investment Promotion Agencies (IPAs) are in large part shifting their principal focus from FDI attraction to retention through strengthening communication of government measures and bolstering aftercare services. For example, InvestKorea and InvestIndia have set up daily web-based updates on COVID-19 cases and policy responses related to foreign investors. Specific investment aftercare services include: identifying and directly contacting at-risk firms according to number of employees, region or sector; brokering solutions to their specific issues; and advocating for urgent government actions to solve these issues more systematically (to benefit other similar investors). IPAs are also taking steps to increase resilience by switching services to online (Jordan) or using social media to communicate closely with investors (Ethiopia). Some IPAs are also facilitating FDI companies’ expansion into new production lines in light of COVID-19, supporting local suppliers’ business continuity and strategic re-orientation to in-demand products and services (Ethiopia).

2. Supporting the survival of viable, otherwise healthy private sector firms, particularly SMEs, is vital. Governments are helping these businesses thorough financial support and regulatory flexibility to keep production and employment.

Governments globally have been swift in providing support to businesses, particularly SMEs. SMEs are often an integral part of global supply chains and exposed to the ripple effect of the crises on the demand and supply side. Furthermore, many businesses face scarce cash-flow issues. A disruption in consumer demand can easily tip them into the red or even bankruptcy. Evidence from China shows that most of the financial pressure (62.8 percent) is from paying salaries and employee insurance and social security; rent and loan payments were the second and third causes for stress. Exporters, importers, or firms integrated in global or domestic value chains are also likely to be more exposed to the shock. It is important that these firms are not left out of the support net, implicitly or explicitly, as they normally tend to be more productive. Their loss would slow recovery and depress overall productivity.

The support has mostly materialized in temporary financial support packages and subsidies/state aid, but these require fiscal space and transparent rules. Looking at the experience with fiscal and financial stimulus packages during previous economic crises, such measures can be effective, but due to the high fiscal cost are more accessible to

1 https://www.rand.org/content/dam/rand/pubs/testimonies/CTS500/CTS524/RAND_CTS524.pdf
countries with greater fiscal space. In addition to general fiscal and financial support, Governments can issue subsidies/state aid to compensate specific firms and sectors for damages directly caused by exceptional occurrences and the restrictions imposed. Such subsidies for firms and notably SMEs have either been targeted towards industries hit hardest, primarily aviation, tourism and retail in a number of countries, or focused on businesses of a certain size, like in the case of Japan and France. Overall, financial support should be designed in a way that avoids distorting the level playing field and create permanent distortions across the markets by granting some market players an undue competitive advantage.

During the COVID-19 outbreak phase, it is important that measures address immediate liquidity challenges, limit firm closures/bankruptcies, and prevent widespread layoffs in the short term. As such, these measures need to be rapid, broad-based, transparent, and time-bound, keeping targeting to an absolute minimum. In the recovery phase, more targeted policies geared towards supporting growth-oriented enterprises and promoting reallocation of resources to more efficient companies can be pursued.

To complement financial and regulatory support aimed at keeping businesses afloat and workers employed, **governments around the world are also temporarily eliminating or reducing the administrative cost on businesses**. Common measures include temporarily suspending or delaying tax and social security filings, waiving fees for government transactions such as licenses, registrations or permits, or automatically extending licenses and permits for the period of the emergency, among others. Emergency periods also allow for greater flexibility concerning licensing and regulation of key professionals such as nurses. In the United States, for example, occupational licensing laws can be suspended in emergency situations. Nineteen states already passed measures ranging from recognition of licenses of healthcare practitioners from other states to extending renewal requirements.

**Some businesses are repurposing their production lines, and regulatory authorities need to strike a balance to support them as they make these shifts.** The COVID-19 outbreak poses unprecedented challenges to businesses, governments, and societies around the world. Companies are reacting in different ways to ensure business continuity, improve the resilience of their supply chain or pivot to innovative ways to generate revenue. One measure that can be observed across industries and countries is companies repurposing their production and R&D capabilities to support the fight against COVID-19. For example, textile companies are switching production lines from producing garments to making hygienic masks and medical robes, cosmetic companies are making hand sanitizers, hotels are becoming quarantine centers, distilleries are creating disinfecting alcohol, and automotive companies are evaluating options to producing urgently needed medical devices such as ventilators.

Repurposing can serve the greater good, and at the same time, help businesses keep production lines up and running in times of low demand, generate moderate revenues, and positively impact their reputation. There are different levels of repurposing, ranging from production of simple products, standard medical devices, to more advanced medical devices. Building up capacity and capabilities to produce simple products is comparably easy and can be achieved quickly. In several cases, MNCs are leveraging their existing supplier base to avoid lengthy qualifications and onboarding processes, while keeping these suppliers’ jobs. For more complex products, receiving regulatory approval is the key challenge. Authorities need to strike a balance of regulatory requirements (e.g. for the production of medical devices) for health, safety and regulatory flexibility to meet medical demand and support repurposing businesses. Also, it is important to note that there is a risk that everyone rushes into repurposing product lines that are in high demand during the outbreak, while only a small number of firms and countries are well positioned to make it on time.

3. **Governments are monitoring, and in some cases, taking exceptional measures to ensure access to critical supplies. Transparency and competition principles remain important.**

**Governments may impose price controls to mitigate exceptional price hikes in the COVID-19 situation, but these should not deter the supply of critical inputs and goods.** Price controls on healthcare supplies such as masks and hand...
sanitizer, have been imposed in several countries such as Romania, the Philippines, Argentina, El Salvador, Paraguay, and France. Romania, the Philippines, South Africa and Argentina have also imposed price caps on certain food products. When implementing price controls, governments typically face challenges to differentiate between markets that could be supplied under prevailing market conditions and those that may merit short-term circumstantial control. Price controls might deter the supply of goods at the exact time they are in exceptionally high demand and discourage exceptional efforts to bring goods into areas where they are needed the most. Finally, they can later constitute a reference price for collusion. If price controls are still deemed necessary, prices should be set independently from producers, be time bounded and reviewed periodically. Setting price ceilings also allows for more competition than fixed prices.

**Actions against price gouging can have a similar effect as price controls but need to be taken with utmost care.** Price gouging is being monitored, and in some cases, investigated. China, Poland and the UK have initiated actions against price gouging through investigations and monitoring efforts. In China and the US, e-commerce platforms have voluntarily been monitoring prices of goods like protective gear and hand sanitizer. Platforms have also started to remove listings and even ban sales of certain products like facemasks and sanitizer. The Italian Competition Authority has launched an investigation on Amazon and Ebay related to the unjustified and substantial increase in prices recorded for the sale of hand sanitizing products, respiratory protection masks, and other sanitation products.

**Anti-cartel enforcement remains critical during emergency situations.** Provisions against refusal to supply or bundling of products by firms with market dominance may be important to ensure access to critical supplies. Although several countries announced they would allow for information sharing (UK—logistics between supermarkets), cooperation (Germany) or collaboration for urgent marketplace issues (Canada) among competitors, authorities can reinforce their efforts to detect any evidence of coordinated price fixing, output restriction, bid rigging, or market allocation for goods and services that are either affected by supply chain disruption and/or face higher demand. Competition authorities are now publicly announcing higher vigilance—a powerful deterrent to anti-competitive practices (US)—or opening investigations in healthcare markets (Greece).

**POLICY MEASURES**

In order to maintain private sector vitality and investor confidence during the COVID-19 outbreak, governments are challenged to act quickly. Under an extraordinary circumstance such as this one, governments face multiple, at times contradictory, expectations. They need to prioritize health and safety and want to keep economic activities viable for when economies reopen. They have to safeguard the domestic private sector and build its resilience without weakening its future competitiveness. Given these and other expectations, governments should adhere to the following principles to do no harm and rebuild damaged investor confidence in this crisis environment:

- Dialogue with the private sector before introducing measures and ensure that those decided upon are addressing their most stringent business needs.
- Speed is of essence, and so is transparency, both in the allocation of resources and announcement of the measures in a form that is easily accessible to public.
- In a fast evolving and complex environment, the importance of data cannot be over-emphasized—tracking and monitoring evidence and impact makes a difference.
- Remember that the immediate crisis response steps will have to be succeeded by policy measures that enable longer-term investment competitiveness taking account of the underlying global economic environment.

The policy measure table below looks at current and potential government responses to the COVID-19 crisis with a focus on investment climate policies and regulations. It currently includes policy measures during the COVID-19 outbreak with immediate implications on businesses and investors. In the future version of this note, we will add policy measures in preparation for the re-opening and recovery of businesses (i.e. over the 18 months following the outbreak) where investment climate policy measures will play a key role. Where relevant, the table includes policy principles in the form of do’s and don’ts, drawing from lessons learned during previous crises, and serving as a reminder of balancing public objectives and understanding longer-term economic consequences.
## INVESTMENT CLIMATE POLICY MEASURES RELATED TO COVID-19

### PHASE I – OUTBREAK

#### Policy Actions

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<tr>
<th>Support FDI retention and preserve supply chains</th>
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<tr>
<td>• Targeted “investor retention initiative” to identify key FDI firms (to avoid permanent closure or for re-investment) and their key local suppliers (to support their survival)</td>
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<tr>
<td>• Waiver from market restrictions (e.g. allowing FDI/joint ventures in selected segments, allowing investment in SEZ/EPZs for local supply)</td>
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<td>• Ease entry restrictions in sectors most affected by the crisis (e.g. travel, tourism, energy, health, etc.)</td>
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#### Do’s and Don’ts

| Do’s: Identify and contact highest risk FDI firms (by level of employment, region, products) and solve their issues proactively |

#### Subsidies/state aid9 to businesses

| Design and allocation of subsidies/state aid programs in line with competition principles |
| Targeted grants and investment incentives (sector-specific, activity-specific, public objective-specific) |

#### Do’s: Make support available for a broad set of companies based on objective criteria

#### Do’s: Make sure that measures are rapid, transparent and time-bound

#### Don’ts: Don’t make aid available to firms failing or with structural issues not related to the crisis

#### Regulatory flexibility to reduce costs and support repurposing businesses

| Waive, freeze, reduce or delay fees (e.g. registration, licensing, work permit, customs documents, tourism fees, penalties for late filing, land use fees, land transfer fees, utility bills) |
| Extension of deadlines (e.g. tax and social security filing, business licenses and permits, financial statement submission) |
| Simplification of professional licensing/accreditation/visa and work permit for doctors, nurses and healthcare professionals |
| Waiver from licensing requirements/speed up approvals for manufacturers of health-emergency/“essential” products (e.g. masks, sanitizers, medical robes) to respond to demand |
| Provide information on measures introduced to preserve jobs and businesses as well as integrated online platforms/services |

#### Do’s: Adjust timeframes and encourage electronic filings

#### Do’s: Strike a balance of regulatory requirements for health, safety and regulatory flexibility to meet medical demand and support repurposing businesses

#### Ensure access to critical inputs/supplies

| Price controls |
| Monitor (and if warranted, investigate) price gouging |
| Allow case-by-case exemptions from the competition law, e.g. information sharing, cooperation or collaboration for urgent marketplace issues among competitors |

#### Do’s: Maximum prices, temporary

#### Do’s: Continued vigilance or investigations in sensitive product markets

#### Don’ts: Fixed prices, open-ended

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9 Subsidies/state aid are different from general financial support measures. They do not cover general economic measures directed to the entire economy or to a region (e.g. tax measures, regulation of interest rates), or to individuals (e.g. provision of cash/checks to unemployed people). In the EU, for example, the notion of State aid covers financial assistance to a particular undertaking or undertakings resulting in a competitive advantage that unlevels the playing field and adversely affects trade. In the WTO framework, a subsidy has been defined as a financial contribution by a government or any public body, which confers a benefit to a specific recipient.