What Matters to Investors in Developing Countries: Findings from the Global Investment Competitiveness Survey

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Developing countries compete to attract foreign direct investment (FDI) because of its potential benefits for the local economy, which include technology transfer, stronger managerial and organizational skills, increased access to foreign markets, and export diversification. FDI can enhance productivity, increase investment in research and development, and create better-paying and more stable jobs in host countries. But these benefits are not guaranteed, nor do all types of FDI have the same potential impact. Thus, host governments must adopt the right policies to maximize their gains from different types of FDI.

The *Global Investment Competitiveness Survey* (GIC Survey) offers practical evidence to help policy makers design policies and prioritize reforms that investors value. Through interviews with 754 executives of multinational corporations (MNCs) that have investments in developing countries, the survey measures the role in influencing FDI decisions of such investment climate variables as investment incentives, promotion, FDI regulations, and administrative processes (see box 1.1 for key findings, annex 1A for survey methodology, and annex 1B for profile of respondents). By identifying variables that are most valued by investors, this chapter provides practical guidance to where policy makers in host countries can focus their efforts to attract and retain FDI, and maximize its gains for development.

Policy reform initiatives must consider that FDI is heterogeneous, driven by different motivations and having different economic, environmental, and social impact. MNCs possess different characteristics that influence their perspectives and decisions. This report is based on an FDI typology that builds on a framework proposed by Dunning and Lundan (2008) (see box 1.2). The framework

BOX 1.1

Top Five Findings of the Global Investment Competitiveness Survey

Through interviews with 754 executives of multinational corporations with investments in developing countries, the GIC survey finds the following:

1. Investors involved in export-oriented efficiency-seeking FDI that look for internationally cost-competitive destinations and potential export platforms value linkages, incentives, trade agreements, and investment promotion agency (IPA) services more than other investors. Incentives such as tax holidays are important for 64 percent of investors involved in efficiency-seeking FDI, compared to only 47 percent of their counterparts involved in other types of FDI. IPA services are rated important by about half of investors involved in efficiency-seeking FDI but by only about a third of those involved in other types of FDI.
2. More than a third of investors reinvest all of their profits into the host country. Investors value policies that help them expand their business more than just policies used by governments to attract them.
3. Investment protection guarantees are critical for retaining and expanding investments in the long term across all types of FDI. Over 90 percent of all investors rate various types of legal protections as important or critically important, the highest rating among all factors included in the survey. These guarantees include the ability to transfer currency in and out of the country, and existence of legal protections against expropriation, against breach of contract, and against nontransparent or arbitrary government conduct.
4. Investors strongly value the existing capacity and skills of local suppliers, but also find that government support, such as providing information on the availability of local suppliers, matters. With foreign investors sourcing about 43 percent of their production inputs locally, supplier contracts and linkages with local businesses have the potential to create significant benefits for the local private sector.
5. For close to 30 percent of investors that have experienced shutting down an affiliate in a developing country, some reasons for exiting the investment could have been avoided, such as unstable macroeconomic conditions and increased policy and regulatory uncertainty. Three-quarters of investors have experienced disruptions in their operations due to political risk forces and events. A quarter of investors that did experience disruptions canceled or withdrew their investment. Severe cases occur fairly infrequently—about 13 percent for breach of contract and 5 percent for expropriation—but when they do, the negative impact is strong. In cases of breach of contract, over a third of investors cancel or withdraw investments, and for expropriation almost half do so.

contends that MNCs are lured to a particular location with a predominant motivation in mind: accessing domestic markets, seeking increased efficiencies of production, taking advantage of natural resources, and acquiring strategic assets. This report extends the use of this typology to explore how various policy instruments influence investors differently depending on their FDI motivation, and how the impact of investment on the host economy varies by type of FDI. As a result, different types of FDI are based not only on investors' subjective motivation for cross-border investment, but also on the inherent objective characteristics of various investment projects, and their implications for developing countries.[1]

This chapter provides a corporate perspective on the investment decision making of MNCs across the stages of the investment cycle: attraction, entry and establishment, operations and expansion, linkages with the local economy, and in some cases, divestment and exit. The survey reveals how MNCs decide on FDI and how they identify and select a country for investment. It also looks at MNCs' operational, reinvestment, and expansion experiences, as well as their encounters with political risks and their decisions to shut down foreign affiliates.

While host-country policy makers listen to investor preferences, they must also consider the public interest. Although the survey focuses

on MNC perspectives and preferences, this report does not necessarily recommend that governments simply yield to investors' wishes. Addressing investor concerns should be balanced with the public interest. For instance, low tax rates and incentives may be desirable from the perspective of MNCs, but governments should not simply lower tax rates and give more investment incentives, especially if these limit the country's gains from FDI. This chapter offers practical evidence on the relative importance of investment policies to guide policy makers in formulating and prioritizing reforms.

The following sections discuss the heterogeneity of FDI and how it affects MNCs' perceived importance of the legal and regulatory environment relative to other country characteristics, and of various investment policy–related factors. The chapter is organized according to the life cycle of investments—selecting a location, entering a country and establishing an investment, running and expanding operations, and considering divestment.

Foreign Investors Are Heterogeneous with Multiple Motivations

Investors with different motivations consider different factors in their decision to invest (box 1.2). MNCs that primarily seek access to natural resources—as in extractive industries—care more about such variables as access to land and resources they wish to exploit than other variables. Market-seeking FDI tends to prioritize the size of and purchasing power in the domestic market. Efficiency-seeking[2] FDI values policies that facilitate the import and export of goods and services, and lower production costs. Efficiency-seeking FDI also includes firms that participate in global value chains (GVCs), an important way for developing countries to integrate into the global economy. MNCs that seek strategic assets primarily pursue technologies and brands that can enhance their operations.

In addition to the subjective motivation of investors, the FDI typology considers FDI's objective impact on the host country—for example, increase in exports brought about by efficiency-seeking investments. The GIC survey focuses on the subjective motivation by asking investors to self-identify their company's motivations in a specific investment project in a developing country.

In this survey, close to 90 percent of investors said that accessing new markets or new customers was one of their motivations (figure 1.1). About half of respondents are motivated by lowering production costs or establishing a new base for exports. The motivation to coordinate a value chain occurs for two-fifths of respondents. For those investors that want to coordinate their companies' value chain, 70 percent are also motivated to cut production costs. Few respondents identify with the motivation to acquire strategic assets (15 percent) or access natural resources and raw materials (12 percent). Critically, almost two-thirds of investors selected multiple motivations and when asked about which motivation prevails, most investors (71 percent) say they are market-seeking.

Survey respondents represent a range of sectors with a combination of investor motivations (figure 1.2). They are in primary sectors (6 percent), manufacturing (47 percent), and services (45 percent), and other nonspecified sectors (2 percent). Although some sectors are naturally linked with specific motivations (for example, the primary sector being natural resource–seeking), motivations do not correlate strongly with sectors. While about 80 percent of services firms tend to be primarily market-seeking, some are also efficiency-seeking, such as services enabled by information technology (IT). Manufacturing firms are also mainly market-seeking but include a large concentration of efficiency-seeking firms and a handful of natural resource–seeking ones.

Investors involved in efficiency-seeking FDI, relative to investors involved in other types of FDI, are more sensitive to various host market characteristics, including investment climate factors. These host market

BOX 1.2

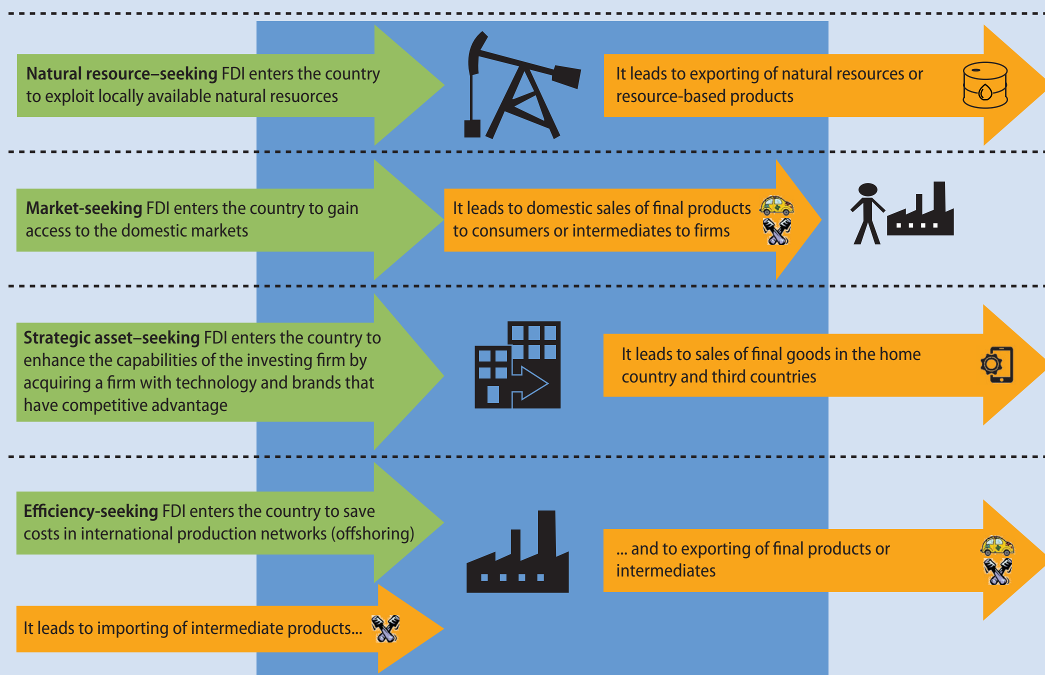
Investor Motivation Framework According to Dunning and Lundan

A well-known framework proposed by Dunning and Lundan (2008) differentiates four sources of foreign direct investment (FDI) motivation: natural resources in the host country, access to the host country market, strategic assets of firms in the host market, or cost savings through higher production efficiency (figure B1.2.1). The last type of investment is typically associated with offshoring production stages to the host country, and is thus export-oriented.

All four types of investment can have important, though varying, benefits for the host economy. For example, natural resource–seeking investment often generates sizable government revenues. Market-seeking FDI can be associated with availability of better and cheaper goods and services consumed by the population or used as inputs by other firms. Strategic asset–seeking investment allows domestic firms to expand their global networks. Efficiency-seeking investment is often seen as a means of job creation, technology transfer, and integration of a country into global value chains. The levels of benefits vary, and some carry more risks than others.

From an investment policy and promotion perspective, it is important to note that the four types of investment can respond differently to policy measures and the overall investment climate. Efficiency-seeking investors—whose investment decisions are driven largely by the motive to save costs—tend to be highly sensitive to any variables that raise their cost of operation or hinder their free exchange of goods and services with the rest of the world as part of global production networks. Natural resource–, strategic asset–, and market-seeking investments tend to be less sensitive to investment climate variables if either the resource to be exploited or the firm that possesses competitive advantages can be found in the country or if the domestic market offers attractive opportunities.

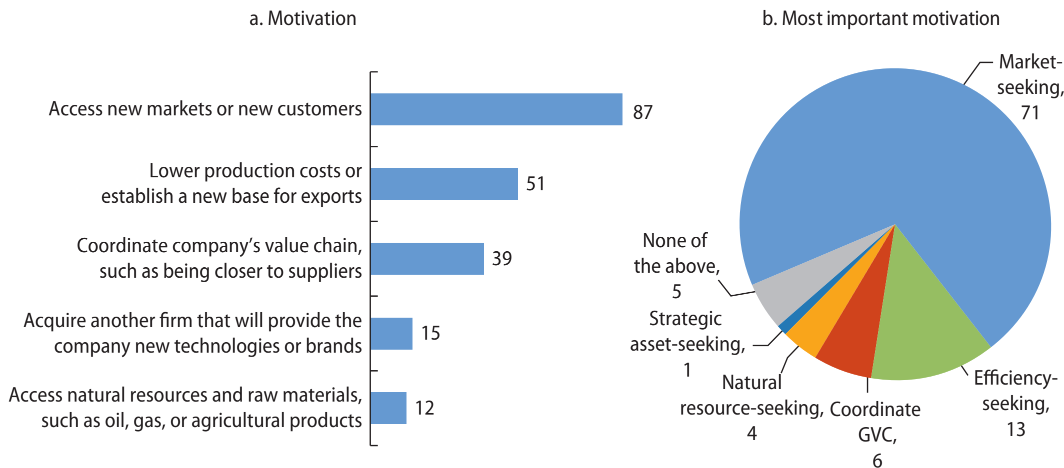
FIGURE B1.2.1 **Investor Motivation Framework According to Dunning and Lundan**



Source: Based on Dunning and Lundan 2008.

FIGURE 1.1 Most Investors Have Multiple Motivations and Are Market-Seeking

Share of respondents (percent)



Source: Computation based on the GIC Survey.

Note: The numbers on the left do not add up to 100 percent because respondents are permitted to select multiple motivations: 62 percent of respondents selected two or more motivations. Many respondents may have understood the motivation to access new markets or new customers to apply not only to the domestic market in which they were investing, but also to the regional market. In fact, this motivation was commonly selected for investments in many small developing countries with an extensive network of trade and investment agreements with other economies, suggesting that the respondents were interested in accessing new regional markets or regional consumers, rather than just the small domestic market of the host country.

characteristics include macroeconomic stability and favorable exchange rate, labor pool, physical infrastructure, tax rates, access to land, and domestic financing sources. Among investment climate variables, MNCs involved in efficiency-seeking FDI assign a higher importance to investment protection guarantees, ease of entry, local suppliers, incentives, trade agreements, and bilateral investment treaties, compared with other investors. This suggests that firms involved in efficiency-seeking FDI may be more responsive to policies and reforms aimed at improving the business environment. This chapter thus explores the differences between MNCs involved in efficiency-seeking FDI and those that are involved in other types of FDI (box 1.3).

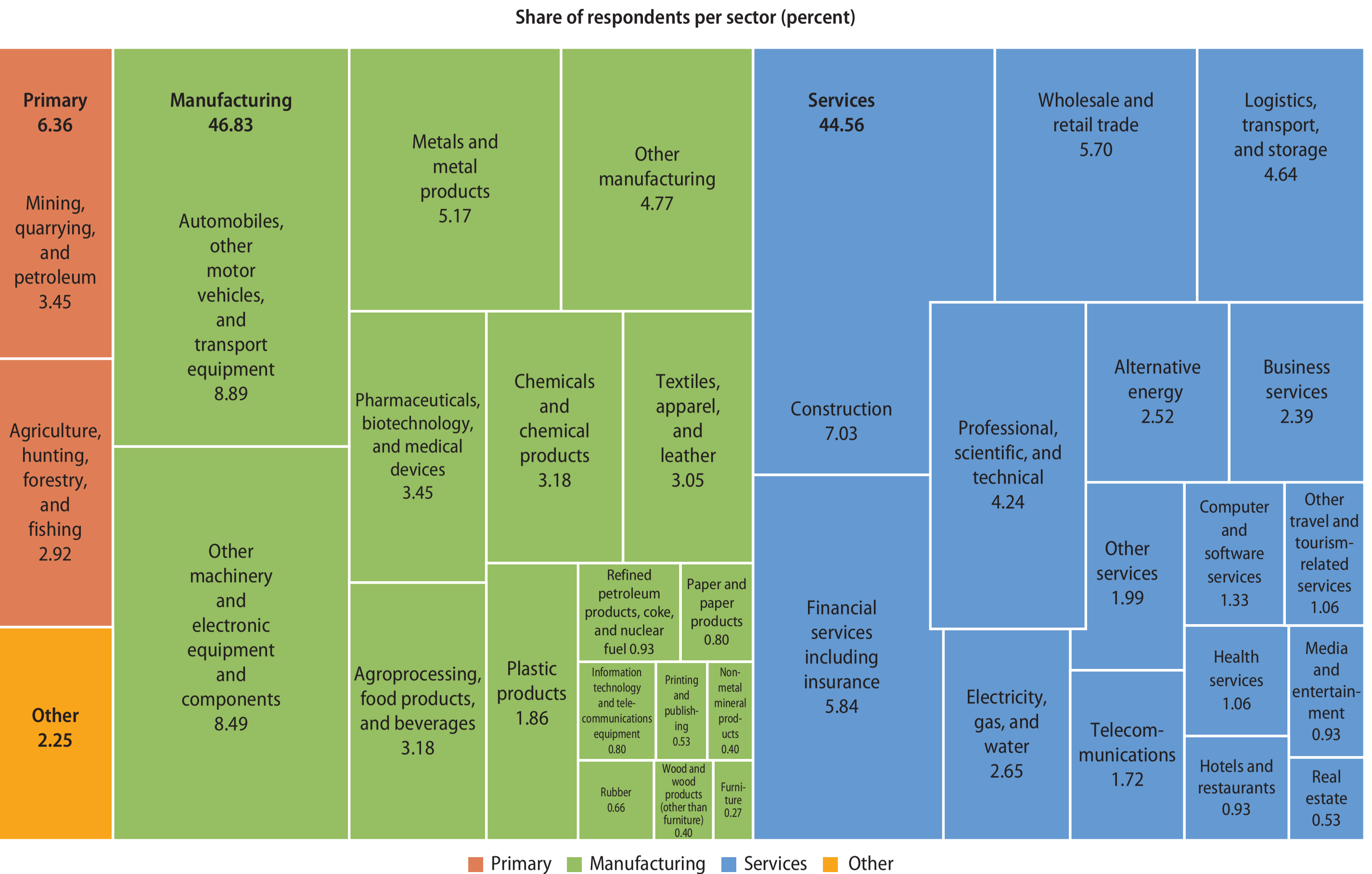
Host countries are also heterogeneous. A vast majority of survey respondents have operations in upper-middle-income countries (87 percent), about a third in lower-middle-income countries, and very few have foreign affiliates in low-income countries (8 percent). Thus, policy implications emanating from the results of this survey are based on investors' responses mostly for middle-income developing countries, although they are likely relevant to low-income countries as well.

Investment Exploration and Location Decision: First Phase in the Investment Life Cycle

What Variables Determine MNC Investment Decisions?

Investors consider a broad range of factors in deciding to invest, the most important being political stability and security, as well as a business-friendly legal and regulatory environment. These top other variables such as infrastructure, labor talent and skill, and low costs of labor and inputs. Among survey respondents, 86 percent find the legal and regulatory environment important or critically important, suggesting that it weighs heavily in investors' decision to invest (figure 1.3).

FIGURE 1.2 Respondents Represent Firms across Various Sectors

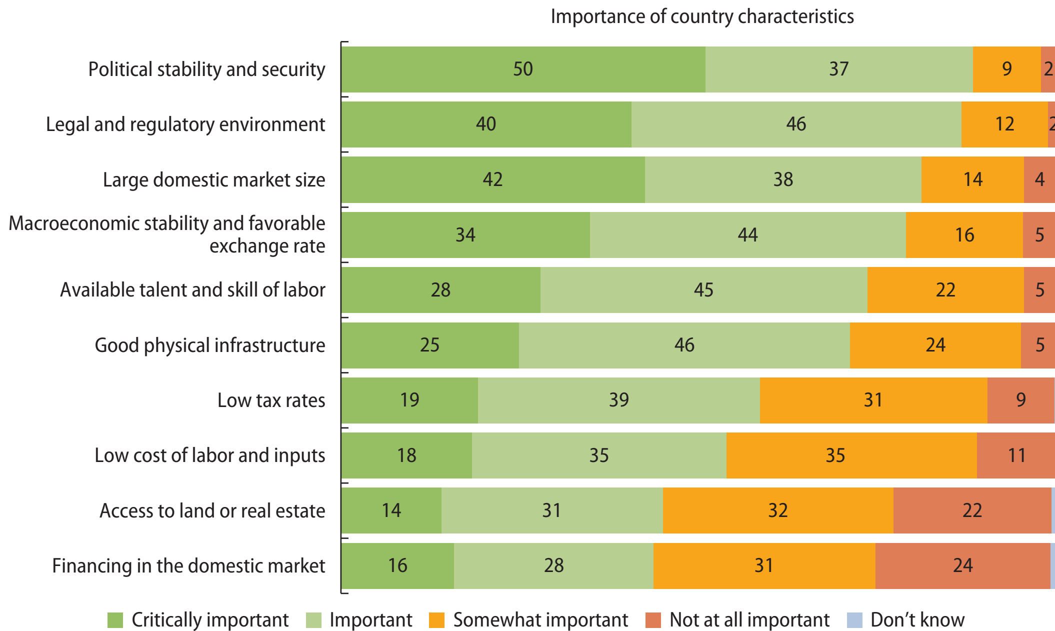


Source: Computation based on the GIC Survey.

Note: Respondents were asked to identify the main sector of their company globally, which may or may not reflect the sector of the affiliates in developing countries. About 10 percent of respondents noted that the sector in the foreign affiliate they are most familiar with is different from the main sector of the global company. See table 1B.4 for the complete list of sectors, distributional shares across respondents, and comparison with global FDI flows.

FIGURE 1.3 Business-Friendly Legal and Regulatory Environment Is Important for Investors

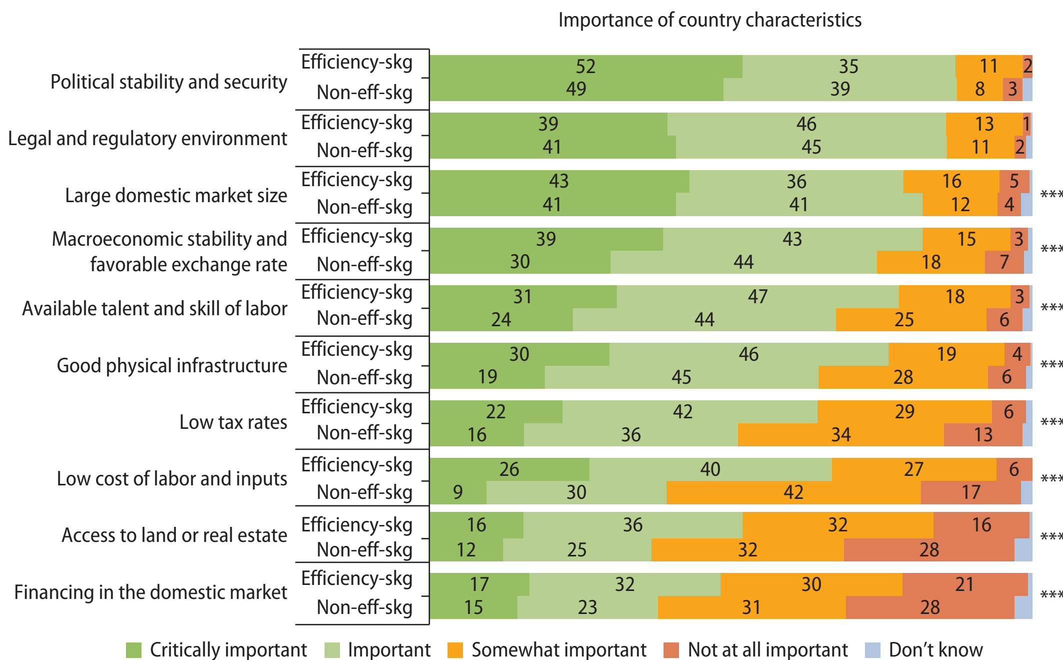
Share of respondents (percent)



Source: Computation based on the GIC Survey.
Note: Respondents were asked, "How important are the following characteristics to your company's decision to invest in developing countries?" Factors were asked in random order. They are listed in the graph in descending order of importance, based on the combination of "critically important" and "important" in dark green and light green bars. Critically important means it is a deal-breaker; by itself this factor could change a company's decision to invest or not in a country.

FIGURE 1.4 MNCs Involved in Efficiency-Seeking FDI Are More Selective

Share of respondents (percent)



Source: Computation based on the GIC Survey.
Note: Country characteristics that have statistically significant differences between investors involved in efficiency-seeking FDI and investors involved in other types of FDI are marked on the right side of the graph. The differences between the two groups are significant at ***p<0.01, **p<0.05 and *p<0.1.

BOX 1.3

MNCs Involved in Efficiency-Seeking Investments Tend to Be More Selective

Investors' preferences and behavior differ depending on their motivation for investing in developing countries. In this survey, about half of respondents said that at least one of their motivations is to lower production costs or establish a new base for exports. Relative to investors with other motivations, these efficiency-seeking firms differ in the following ways:

1. MNCs involved in efficiency-seeking investments view most characteristics of host countries as more important than investors involved in other types of FDI. These characteristics include stable macroeconomic conditions and favorable exchange rate, available talent and skill of labor, good physical infrastructure, low tax rates, low cost of labor and inputs, access to land or real estate, and available financing in the domestic market. Among these, the difference is largest for low cost of labor and inputs, which 66 percent of firms involved in efficiency-seeking investment find important or critically important compared with only 39 percent of investors with other motivations.
2. Investors involved in efficiency-seeking FDI also rate most investment policy factors as more important than investors involved in other types of FDI. These include investment protection guarantees, ease of obtaining approvals, investment incentives, preferential trade agreements, and bilateral investment treaties. The difference is notable for preferential trade agreements, which 65 percent of firms involved in efficiency-seeking investment find important or critically important compared with only 45 percent of investors with other motivations.
3. Incentives also matter more for firms with efficiency-seeking investments. In this group, 63 percent find incentives important or critically important, in contrast with only 43 percent of investors with other motivations. Firms with efficiency-seeking investments rated eight different incentive instruments more highly than other investors with a difference of about 13 percentage points on average. They also received incentives more often in a typical investment.
4. In terms of ease of entry, MNCs involved in efficiency-seeking FDI view efficiency of obtaining approvals, owning all equity, easily bringing in expatriate staff, and importing production inputs as more important compared with investors involved in other types of FDI. For firms with an efficiency-seeking motivation, the ability to import production inputs is rated slightly more important (73 percent) than the ability to bring in expatriate staff (71 percent) while the reverse is true for firms with other motivations (61 and 65 percent, respectively).
5. Capacity and skills of local suppliers are important or critically important for 77 percent of MNCs involved in efficiency-seeking FDI, compared with 70 percent of investors with other motivations. Government initiatives including information about availability of local suppliers, upgrading potential suppliers, and incentives to invest in supplier upgrading are rated more important by about 8 to 12 percentage points more by firms involved in efficiency-seeking FDI relative to firms involved in other types of FDI. To promote linkages, 55 percent of MNCs involved in efficiency-seeking FDI have internal "talent scouts" to find local suppliers, compared with only 45 percent of investors involved in other types of FDI.
6. MNCs involved in efficiency-seeking FDI value the services of investment promotion agencies (IPAs) more highly, with 52 percent of respondents identifying IPA services as important or critically important, compared with 37 percent of investors involved in other types of FDI. Specifically, meetings with agency officers to discuss investment opportunities, information and assistance in setting up an affiliate, and assistance in problem resolution are valued more by firms with efficiency-seeking investments, by about 9 to 12 percentage points, than by other investors.

Firms involved in efficiency-seeking FDI are more sensitive to a broad range of factors. MNCs seeking cost-competitive locations for their mostly export-oriented production value macroeconomic stability, labor skills, reliable infrastructure, low tax rates, low costs of labor and input, access to land, and domestic financing more than other investors. Because these investors are more sensitive to costs, they more carefully consider factors that directly affect

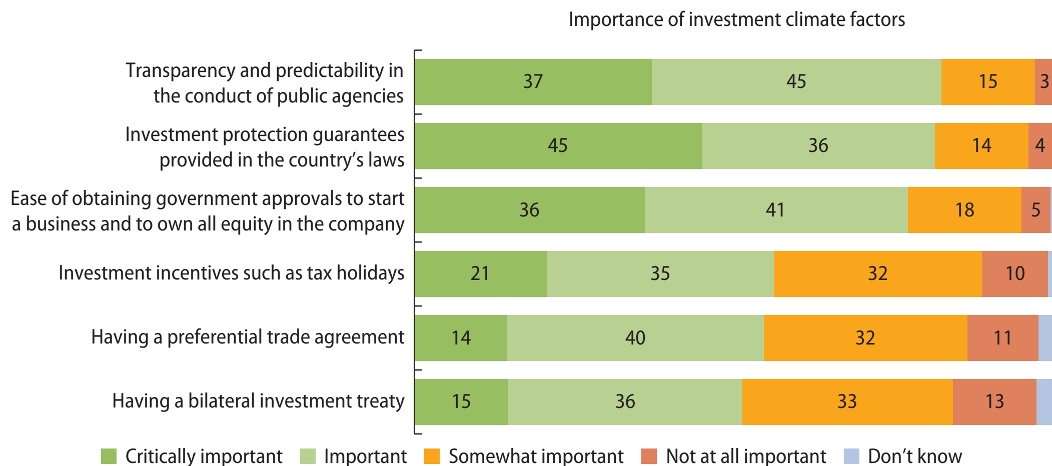
their cost structure and productivity. The size of the domestic market is valued slightly more by investors without an efficiency-seeking motivation, which are predominantly motivated by accessing new markets. The two most important factors—political stability and security, and the legal and regulatory environment—are consistently valued highly across all types of investors (figure 1.4). (See figures 1C.1, 1C.2, and 1C.3 for differences in importance rating by manufacturing versus services firms, developed versus developing source countries, and parent company versus affiliate.)

Investors seek both strong legal protections and predictability and efficiency in implementing laws and regulations (figure 1.5). Many developing countries have inefficient bureaucracies, opaque regulations, complex procedures, and high transaction costs that undermine their competitiveness. Not surprisingly, four out of five surveyed investors rate transparency and predictability in the conduct of public agencies, investment protection guarantees provided in the country's laws, and the ease of starting a business as important in their decision on where to invest. Moreover, about a third of investors rate these as critically important, or potential deal-breakers. Transparency and predictability may be interpreted as a reflection of the overall interaction between MNCs and host governments—comprising both regulations themselves and their implementation.

Investors value policies that help them expand their business more than policies to attract them. Forty-five percent of respondents rate investment protection guarantees as critically important or deal-breakers, highest among all investment climate factors. Over 90 percent of investors rate various types of legal protections as critical, including the ability to transfer currency in and out of the country as well as legal protections against expropriation, against breach of contract, and against nontransparent or arbitrary government conduct. All investors—regardless of sector, source country, or FDI motivation—find these guarantees of greatest value. These policies are bigger deal-breakers than investment incentives, preferential trade agreements, and bilateral investment treaties. These results suggest that host countries need to pay as much attention to investor aftercare as they do to attracting investors to their country. Given that respondents are investors that already

FIGURE 1.5 Investors Seek Predictable, Transparent, and Efficient Conduct of Public Agencies

Share of respondents (percent)



Source: Computation based on the GIC Survey.

have ongoing operations in developing countries and not prospective investors, this partly explains the emphasis on aftercare.

MNCs involved in efficiency-seeking FDI place more importance on investment climate factors compared to firms involved in other types of FDI. Except for transparency and predictability in the conduct of public agencies, which firms find most important regardless of motivation, firms involved in efficiency-seeking FDI value most investment policies more highly (figure 1.6). This suggests that MNCs involved in efficiency-seeking FDI may be more sensitive to these factors when deciding to invest. Such results are not surprising, given that most efficiency-seeking investment is export oriented and highly selective in where it locates, hence the importance of trade agreements and investment incentives. As such, policy makers in host countries should target their initiatives to attract these investors. (See figures 1C.4, 1C.5, and 1C.6 for differences in importance rating by manufacturing versus services firms, developed versus developing source economies, and parent company versus affiliate.)

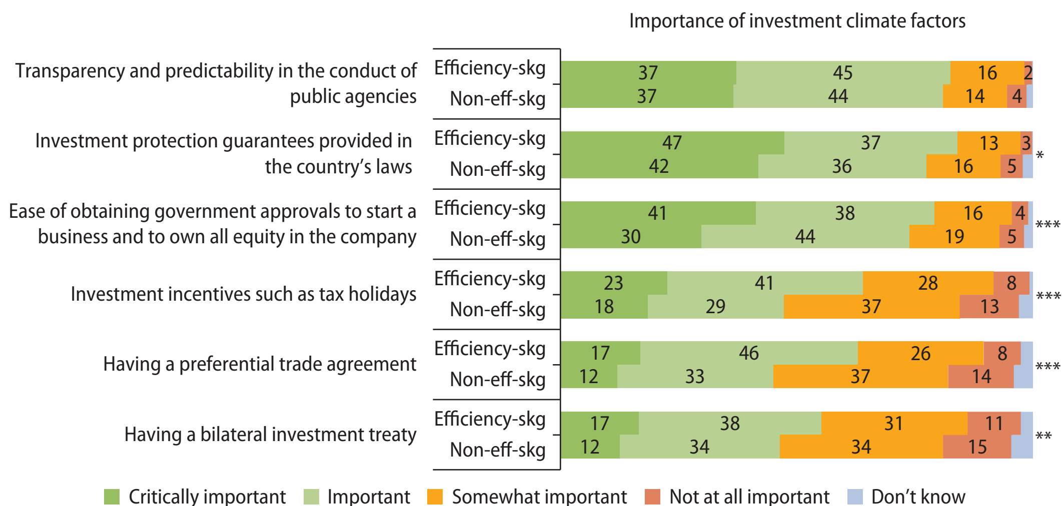
How Critical Are Incentives in Attracting FDI?

Investment incentives to attract FDI are widespread and used by governments in both high-income and developing countries. Developing country policy makers often view incentives as necessary for their countries to compete for FDI. As discussed later in this report, incentives impose sizable costs on host countries through fiscal losses from non-collection of taxes, rent-seeking by firms, and associated tax evasion. Countries must thus walk a fine line between remaining competitive by offering incentives and ensuring that benefits outweigh their costs.

Investment incentives rank only fourth in importance to investors out of six investment climate characteristics listed in the GIC survey. They rank lower than transparent government conduct, investment protection guarantees, and ease of establishing a business (figure 1.5). Overall only one in five investors finds the absence of investment incentives as deal-breakers in deciding to invest. Another third of respondents find incentives to be important

FIGURE 1.6 MNCs Involved in Efficiency-Seeking FDI Value Incentives, Trade Agreements, and Ease of Entry More than Other Investors

Share of respondents (percent)



Source: Computation based on the GIC Survey.

Note: Most investment climate factors in this graph have statistically significant differences between investors involved in efficiency-seeking FDI and investors involved in other types of FDI. The differences between the two groups are significant at ***$p<0.01$, **$p<0.05$ and *$p<0.1$.

but not deal-breakers. This does not necessarily suggest that incentives can be completely eliminated but that, by themselves, they are unlikely to convince investors to shift the location of their investment. The policy fundamentals of the investment climate must be addressed before policy makers resort to incentives as a means of attracting investors.

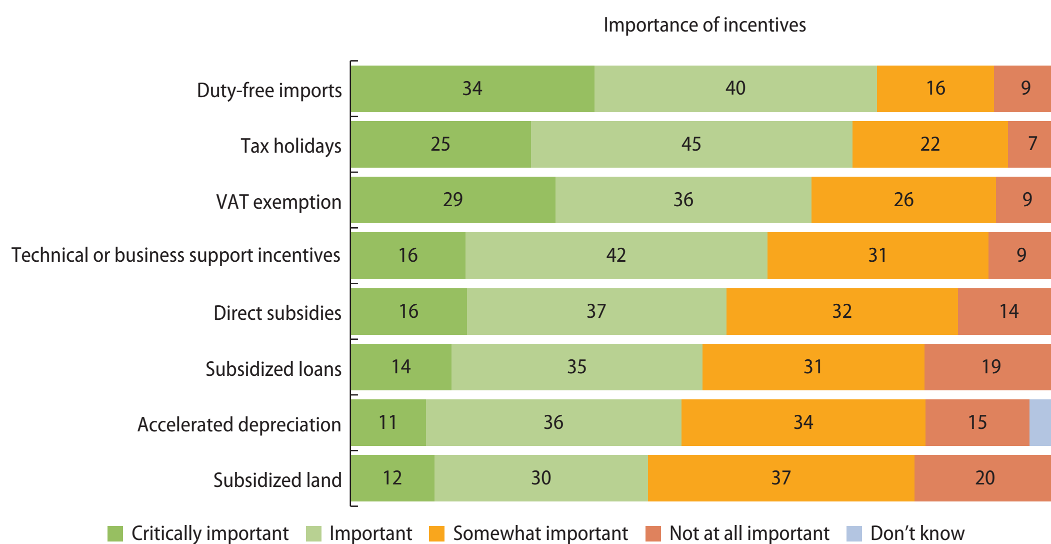
MNCs involved in efficiency-seeking FDI, however, value incentives more than investors with other motivations. Among investors motivated by cutting production costs and finding new export platforms, 64 percent find incentives important or critically important, in contrast with only 47 percent of investors with other motivations (figure 1.6). Investors involved in efficiency-seeking FDI are also granted certain incentives—duty-free imports, subsidized loans, and value added tax (VAT) exemption—more often than other investors. This suggests that they may be more responsive to incentives than investors with other motivations such as accessing new markets and natural resources.

Duty-free imports, tax holidays, and VAT exemptions are the top three most important incentives for investors (figure 1.7). About two-thirds of investors who said that incentives are at least somewhat important find these three instruments to be important or critically important. MNCs involved in efficiency-seeking FDI rated all types of incentives more highly compared with investors involved in other types of FDI, with a difference of about 13 percentage points on average. They also received incentives more often in a typical investment. When asked about the specific incentives that their companies have received, respondents identified the same three types of instruments—duty-free imports, tax holidays, and VAT exemption—as most frequently received. This suggests that the respondents' high rating of these types may owe to their familiarity with the specific instruments.

Obtaining fiscal and financial incentives typically takes three months but varies from about a week to over a year, depending on the

FIGURE 1.7 Duty-Free Imports, Tax Holidays, and VAT Exemptions Are the Most Attractive Investment Incentives

Share of respondents (percent)



Source: Computation based on the GIC Survey.
Note: The question on incentives was answered by 663 respondents. These respondents answered somewhat important, important, or critically important on incentives in the question in figure 1.5. VAT = value added tax.

country and type of incentive. About one quarter of surveyed investors said obtaining incentives took less than one month, while about 6 percent noted it took more than a year.

Investment Entry and Establishment: Second Phase in the Investment Life Cycle

How Do Policies and Administrative Procedures for Business Establishment Affect FDI Decisions?

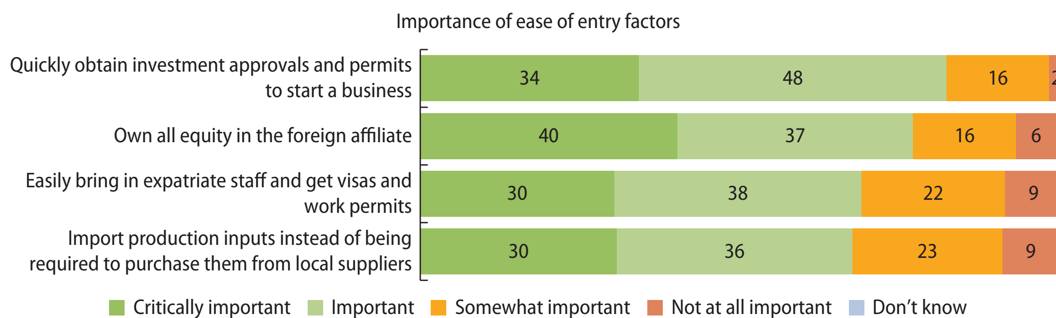
Investors strongly value business-friendly policies and efficient procedures related to business establishment. About four out of five respondents say that the ease of obtaining approvals for their investment is important or critically important, while only 2 percent say it is not at all important (figure 1.8). In fact, the speed of obtaining approvals and permits ranks even higher than investors' ability to own all equity in a project, to easily bring in expatriate staff, and to import production inputs. For MNCs involved in efficiency-seeking FDI, all these characteristics are rated as more important relative to investors involved in other types of FDI. For firms involved in efficiency-seeking FDI, the ability to import production inputs is rated slightly more important (73 percent) than the ability to bring in expatriate staff (71 percent) while the reverse is true for firms involved in other types of FDI (61 and 65 percent respectively).

Although efficiency in obtaining permits is most important overall, restrictions on foreign equity ownership appear to be the biggest deal-breaker. Forty percent of respondents claim that owning all equity in their affiliate and not being required to share ownership with local firms or the government is critically important, highest among all policy factors considered. This result is significant in the context of foreign ownership restrictions still being relatively prevalent across developing countries, especially in services.

Obtaining investment approvals and permits to start a business typically takes three months, but varies by country and type of investment (figure 1.9). The variation is quite wide: on one end of the spectrum, about 10 percent of respondents say they waited less than a month while on the other end, another 10 percent of investors waited a year or longer. Respondents who value efficiency of government approvals encountered somewhat shorter waits. For this group, only 12 percent had processing times exceeding

FIGURE 1.8 Investors Strongly Value Business-Friendly Policies and Procedural Efficiency of Entry and Establishment of Affiliates

Share of respondents (percent)



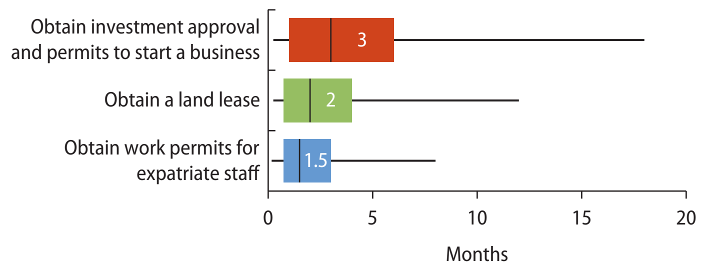
Source: Computation based on the GIC Survey.

Note: The questions on ease of entry were answered by 709 respondents. These respondents answered somewhat important, important, or critically important on ease of entry in the question in figure 1.5.

six months compared with 25 percent otherwise. This confirms that investors who value efficiency tend to favor destinations where approvals are quicker to obtain.

The median length of time for obtaining a land lease is two months, and for obtaining work permits is about 1.5 months. The dispersion of responses for both of these formalities also appears tighter than for obtaining initial investment approvals. Fewer respondents also experience wait times longer than six months—9 percent of respondents when obtaining a land lease and only 6 percent when obtaining work permits.

FIGURE 1.9 Wait Times for Investment Approvals Vary but Typically Take Three Months



Source: Computation based on the GIC Survey.
Note: The boxplot shows the median point (with data label) as the middle bar. The ends of the boxes represent the 25th and 75th percentiles. The ends of the black lines show the 5th and 95th percentiles.

Investment Operations and Growth: Third Phase in the Investment Life Cycle

What Role Do Local Suppliers Play in MNCs' Operations?

FDI brings potential benefits to the host country through a variety of channels including linkages with the local private sector. Linkages between foreign firms and local suppliers enable knowledge and technology transfer, including know-how and practices that allow domestic suppliers to upgrade the quality and efficiency of their production. Linkages also expand the multiplier effect in the local economy. When foreign investors source inputs locally instead of importing them, they boost production of local firms and create jobs in the local economy. As such, policy makers try to promote linkages through various policies and programs. One such policy is local content requirements, where a certain percentage or absolute amount of local input is required of foreign firms. Research finds, however, that local content requirements and similar measures have a largely negative effect and discourage FDI.[3]

While investors resist being mandated to source their inputs locally, many of them prefer to do so if they are able to find in the local market the quality and quantity of the production inputs they need. On average, 43 percent of material inputs, supplies, and services are sourced locally, versus 34 percent of inputs sourced from another unit of the company and 23 percent of inputs imported (figure 1.10). The percentage of inputs sourced locally varies widely: about 13 percent of surveyed companies do not source any inputs locally, another 13 percent source all their inputs locally, and the rest of the firms (about 74 percent) source some portion of their inputs locally. Linkages are more prevalent for MNCs in service sectors compared with manufacturing firms.

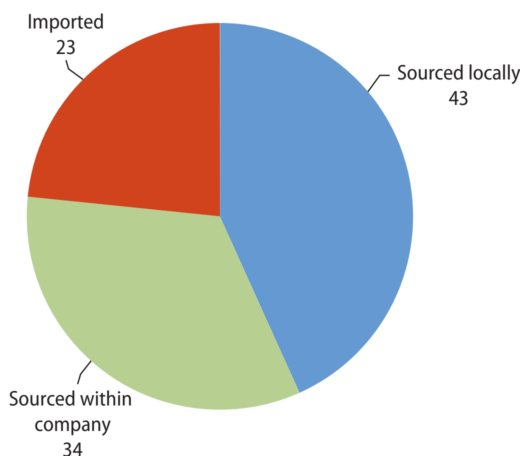
Overall, 61 percent of MNCs consider linkages as important or critically important in their location decisions. Among those investors who identified linkages as at least somewhat important, 74 percent find that capacity and skills of local suppliers are important or critically important (figure 1.11). Local skills and capacity are valued even more by MNCs involved in efficiency-seeking FDI (77 percent). This suggests that government initiatives to promote linkages will only be effective if local companies can offer the capacity and skills expected by MNCs. At the same time, governments of host countries have the scope to facilitate linkages. Investors value information on the availability of local suppliers, rated as important or critically important by 68 percent of respondents. About 61 percent

of respondents also rate supplier upgrading as important, whether in the form of direct financial incentives for companies to invest in supplier development or governments' own initiatives to upgrade suppliers. Only 42 percent of respondents value matchmaking events with suppliers. These government initiatives are rated as important by about 8 to 12 percentage points more by firms involved in efficiency-seeking FDI relative to other investors.

When capacity and quality constraints in the local market prevent investors from finding appropriate suppliers, investors value being able to import inputs instead of being required to source them locally. This is especially true for MNCs involved in efficiency-seeking FDI and manufacturing firms. Many manufacturing MNCs invest in developing countries to reduce their cost of production. At the same time, to maintain a high quality of final products, which are often intended for export, foreign manufacturers appreciate the flexibility of importing their own inputs for production rather than sourcing them locally. Of the surveyed manufacturing firms, 68 percent rate the ability to import inputs as important or critically important, as opposed to only 56 percent of services companies. Among firms involved in efficiency-seeking FDI, 73 percent find this attribute important or critically important while only 61 percent of firms involved in other types of FDI consider it important.

FIGURE 1.10 Nearly Half of Material Inputs, Supplies, and Services Are Sourced Locally

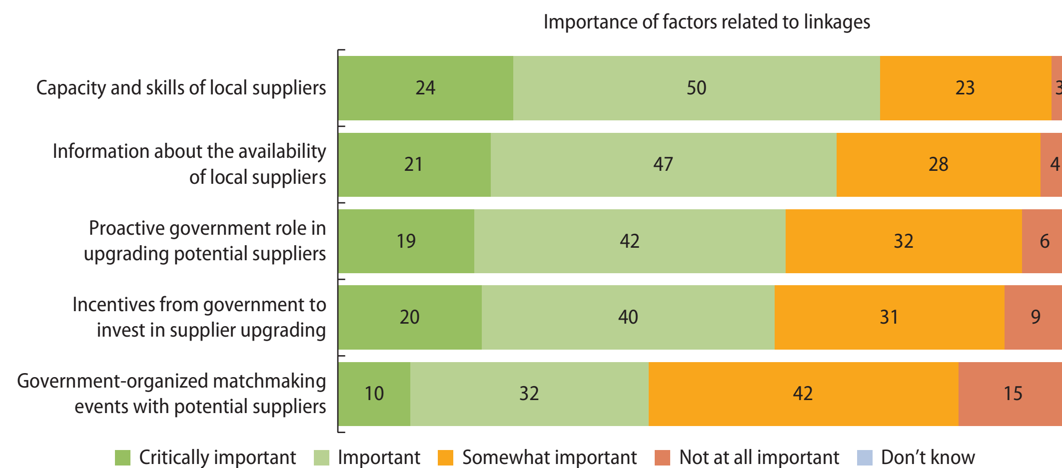
Share of respondents (percent)



Source: Computation based on the GIC Survey.
Note: The number of respondents for each source vary and are fewer than 754 because some respondents answered "don't know."

FIGURE 1.11 Capacity and Skills of Suppliers Are Critical Linkages-Related Features

Share of respondents (percent)

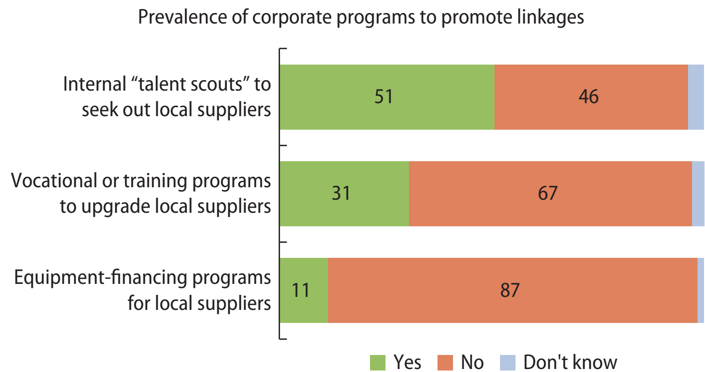


Source: Computation based on the GIC Survey.
Note: The questions on linkages were answered by 679 respondents who answered somewhat important, important, or critically important on the question, "How important are the capabilities of local firms to act as suppliers in your decision to invest in developing countries?"

Foreign investors themselves also have an interest in promoting linkages, but company-initiated programs are uncommon. Sourcing inputs, supplies, and services locally instead of importing them can reduce costs for foreign-owned firms. Some MNCs have their own programs to promote linkages, but these are not widespread. The survey finds that, among the foreign firms that do source locally, half use internal "talent scouts" to find local suppliers. Firms involved in efficiency-seeking FDI tend to have talent scouts more often (55 percent) than investors involved in other types of FDI (45 percent). Over 30 percent have vocational or training programs to upgrade local suppliers, and 11 percent have equipment-financing programs for local suppliers (figure 1.12). Among firms that have vocational or training programs, about a third sponsor certification programs and partner with local technical colleges and universities.

FIGURE 1.12 Corporate Programs to Promote Linkages Are Not Very Widespread

Share of respondents (percent)



Source: Computation based on the GIC Survey.
Note: These questions on corporate programs to promote linkages were answered by 454 respondents. These respondents answered somewhat important, important, or critically important on the question "How important are the capabilities of local firms to act as suppliers in your decision to invest in developing countries?" and source some or all of their inputs locally.

How Much Do MNCs Reinvest in Host Countries?

Host countries not only need to attract and retain FDI but also need to facilitate its growth to motivate investors to reinvest their earnings in the host country. Many variables may influence investors in deciding on the share of their profits to repatriate as dividends versus reinvest in growing their operations in the host country. These variables include taxation systems, transfer costs, investment opportunities in the ongoing business and elsewhere, relative costs of shifting financial resources out of the host country, and need to expand the ongoing business. Reinvested earnings are becoming an increasingly important source of FDI, growing from less than 30 percent of FDI flows in 2007 to about 50 percent in 2015 (UNCTAD 2016). This trend is confirmed by the survey results, where over a third of respondents say that they reinvest all their profits in the host country, and another 14 percent reinvests more than half (figure 1.13). This trend highlights the importance for host economies of retaining and expanding existing investments in addition to attracting new ones.

How Do Investors Respond to Political Risks?

Among survey respondents, 76 percent experienced political risks in their investment projects. Political risk is the probability of disruption of business operations by political forces or events, and especially by government actions. About half of respondents experienced lack of transparency and predictability in dealing with developing country public agencies. Almost half encountered adverse regulatory changes and delays in obtaining necessary government permits and approvals to start or operate a business. Over 40 percent encountered restrictions in transferring and converting currency. In these cases, about one in four investors canceled a planned investment or withdrew an existing investment owing to political risks (figure 1.14).

More severe cases of political risk occur less frequently but with far worse impact. Only 13 percent of respondents experienced breach of contract by the government but

FIGURE 1.13 More than a Third of Investors Reinvest All Their Affiliate-Generated Profits Back into the Affiliate

Source: Computation based on the GIC Survey.
Note: The question on reinvested earnings was answered by 597 respondents. The remaining 158 either refused, did not know the answer, or made the investment within the year. Respondents were asked about reinvested earnings in a specific developing country of their choice.

the impact was much greater—35 percent of those investors canceled a planned investment or withdrew an existing one. Expropriation was even more extreme: while only 5 percent of respondents experienced it, almost half of them canceled or withdrew an investment.

Investments in services tend to be more affected by political risk than manufacturing. Firms in the services sector experienced more disruptions related to political risk, particularly restrictions in transferring and converting currency, breach of contract by the government, and expropriation. Services—such as energy, telecommunications, or finance—are more tightly regulated than manufacturing, and thus more exposed to potential political interference. In particular, according to survey results, companies in the utilities sector—including electricity, gas, alternative energy, and telecommunications—experience more frequent adverse regulatory changes and expropriation and more delays in obtaining permits. Construction and business services sectors report more frequent experiences of breach of contract by the government and lack of transparency and predictability in dealing with public agencies.

Governments should more adequately manage investor grievances. According to the survey, governments often do not effectively address grievances related to political risks. Only about one in five affected investors felt that their grievances were promptly resolved by the government, that the process of complaint was clear and efficient, or that the government introduced a systematic solution to address or prevent such grievances in the future.

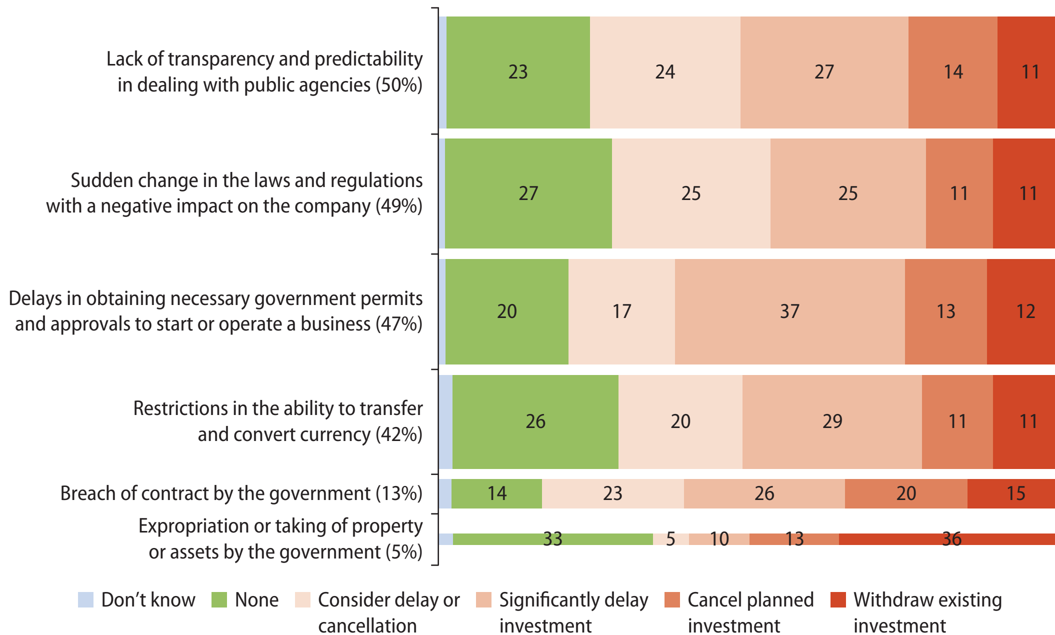
Divestment: Fourth Phase in the Investment Life Cycle

Why Do MNCs Divest from Developing Countries?

Some 29 percent of investors surveyed had shut down at least one of their company's

FIGURE 1.14 Severe Political Risks Are Infrequent but Can Have Highly Negative Effects on FDI

Share of respondents (percent)

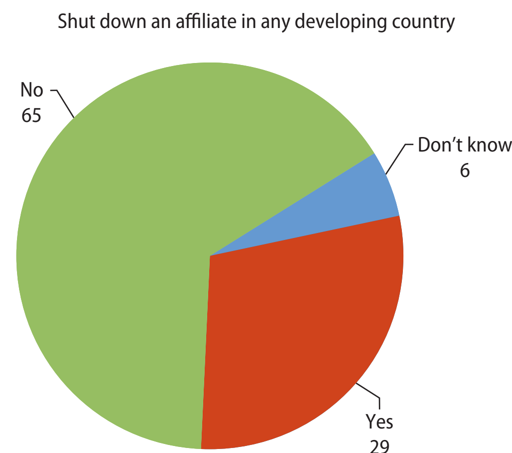


Source: Computation based on the GIC Survey.
Note: The height of the bars reflects the percentage of respondents that experienced disruption in any of their investments owing to the political risk identified. The risks are arranged in descending order from most frequently experienced at the top, to least frequently experienced at the bottom. The numbers across rows do not add up to 100 percent because respondents could select multiple types of disruptions that their companies had experienced. The horizontal bars show the responses of companies, with the darker red bars reflecting more severe reactions. The bars reveal the most severe reactions of companies after experiencing the particular disruption. If, for example, a company experienced withdrawing an existing investment in one country, but only delaying in another, the most severe reaction was considered and the company was included in the *withdraw* bar.

affiliates in a developing country (figure 1.15). The most common reasons were changes in the company's strategy and unstable macroeconomic conditions, including an unfavorable exchange rate. Increased policy or regulatory uncertainty was the third most common reason, which occurred in about a third of the divestment cases (figure 1.16). Arbitrary government conduct, sudden restrictions on currency transfer, and breach of contract by governments are reported as factors by more than 20 percent of investors. These results confirm that companies value transparency and predictability in the conduct of public agencies, as well as investment protections. Foreign investors in services divest more frequently than manufacturing MNCs, possibly because they are more highly regulated and thus vulnerable to political interference. Among the surveyed services companies, 35 percent had shut down an affiliate, versus just 23 percent of manufacturing firms.

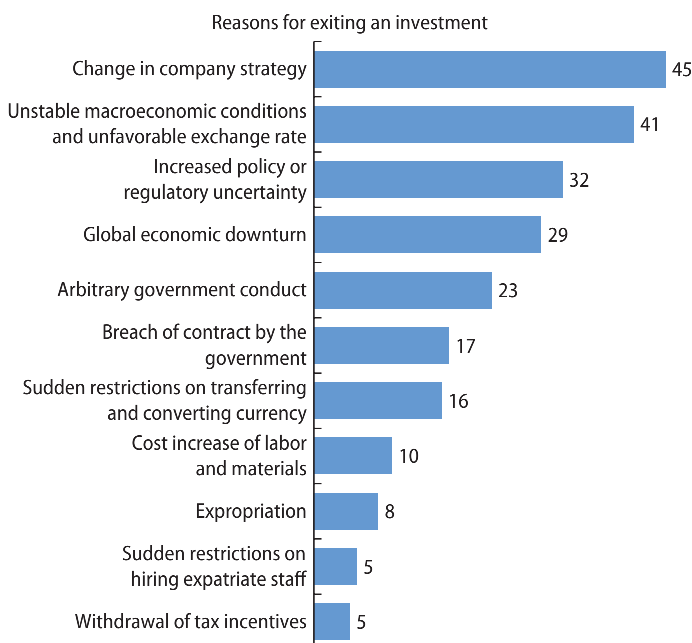
Although some reasons for exiting investments are beyond the control of governments of host countries, many are avoidable. While governments cannot do much about changes in investor firms' corporate strategies or about global economic conditions, they can influence factors in their own countries. In particular, maintaining an appropriately valued exchange rate, managing macroeconomic stability, and ensuring transparent, consistent, and predictable policies and regulations are critical in keeping investors from exiting.

FIGURE 1.15 More than a Quarter of Respondents Had Shut Down an Affiliate in a Developing Country
Share of respondents (percent)



Source: Computation based on the GIC Survey.

FIGURE 1.16 Reasons for Exiting an Investment Are Mixed, Some Controllable and Others Not
Share of respondents (percent)



Source: Computation based on the GIC Survey.
Note: Results are based on 219 respondents that were aware that their companies had shut down an affiliate in a developing country. Shares do not add up to 100 because respondents could select up to five of the most relevant reasons.

What Role Do Investment Promotion Agencies Play across the Investment Life Cycle?

Although MNCs have their own strategic motivations for selecting specific investment locations, the quality of services provided by the host economies can play a key role in MNCs' corporate decisions. The role of investment promotion agencies (IPAs) in facilitating investments can be particularly important in countries with larger physical or cultural distance from the home economies of investors.

IPAs complement rather than substitute for a good investment climate and ecosystem for investment projects. Only 43 percent of the surveyed investors say that IPAs are important or critically important in their decision to invest, the lowest among investment climate variables queried in the survey. Only 12 percent consider quality of IPA services to be deal-breakers, while 14 percent rate IPAs as not at all important. These results suggest that other factors play a more prominent role in firms' decision making. Sound economic fundamentals need to prevail before the services delivered by IPAs become critical for investors.

IPA services thus have great scope for improvement. The relatively low rating of the importance of IPAs does not necessarily suggest that host countries should not strengthen them. The reverse could actually be true—that host countries currently offer poor-quality IPA services for investors, which is why investors' perceptions are not very positive. Only 11 percent of respondents use IPA services in their typical investment, despite 43 percent saying they are important. The proportion of users is somewhat greater for investments in low-income countries than in middle-income countries, suggesting that IPAs provide more value when the business environment is more difficult and information harder to obtain, as is often the case in low-income countries. MNCs involved in efficiency-seeking FDI value IPA services more highly, with 52

percent of respondents identifying IPA services as important or critically important, compared with 37 percent of investors involved in other types of FDI.

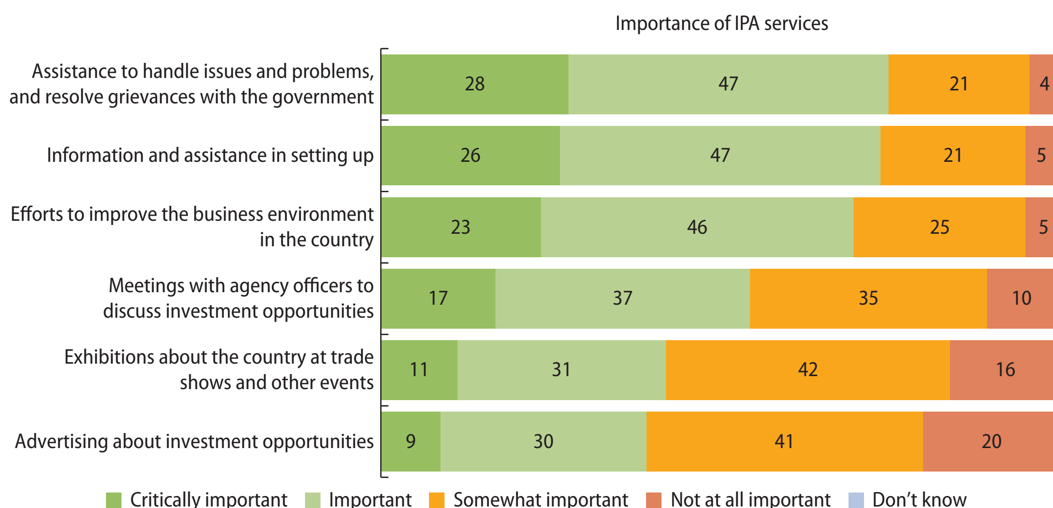
Among investors who do find IPAs to be important or somewhat important, two-thirds highly value help in handling issues and resolving grievances with government, information and assistance in setting up, and business advocacy efforts to improve the business environment. These services are rated more important than investment promotion activities (figure 1.17). Promotion efforts to attract investors—advertising online and in media, and exhibitions at trade shows, investment conferences, and events—are rated as relatively less important. Only about a third of investors find these services important or critically important, the lowest rated among the various factors considered.

Among the 11 percent of investors that did engage with IPAs, their services during entry and establishment were used most frequently. Investors used IPA services for assistance in registering and obtaining permits for a new investment (76 percent), expanding investment (59 percent), exploring locations for a new investment (46 percent), helping address operational issues or problems (41 percent), and finding domestic suppliers (28 percent). These results likely reflect the availability of services offered by IPAs in the first place rather than investors' needs. IPAs often dedicate resources for investment promotion and facilitation, but not many offer additional services after the investment becomes operational. A potential mismatch is apparent—while investors would appreciate assistance with their operations (for example, in resolving issues or grievances with the government), the services they typically receive from IPAs are more focused on the start-up phase.

Some investors value IPA services more than others. In particular, investment promotion efforts—exhibitions, advertising,

FIGURE 1.17 Investors Value IPA Help in Resolving Problems and Setting Up More than Promotion Efforts

Share of respondents (percent)



Source: Computation based on the GIC Survey.
Note: The questions on IPA services were answered by 632 respondents. These respondents answered somewhat important, important, or critically important on the question, "How important are high-quality services and support from the country's IPA in your decision to invest in developing countries?". IPA = investment promotion agency.

and meetings with agency officers—resonate with investors from developing countries more than those from developed countries, and with investors in the services sector more than those in manufacturing. Meetings with agency officers to discuss investment opportunities, information and assistance in setting up an affiliate, and assistance in problem resolution are valued more by firms involved in efficiency-seeking FDI. In general, the ratings remain relatively low, but this suggests that IPA services in attracting investments can be better targeted to those companies that may be more responsive, whenever they align with the country's target sectors and target markets. IPAs often focus on traditional investors from industrialized economies, but as FDI increasingly originates from developing countries, IPAs may well benefit from redirecting their activities accordingly.

Policy Implications

To maximize the gains from foreign investments, developing country governments must adopt effective reform strategies, champion reform at the highest political levels, and strengthen interagency coordination. They must also balance the public interest with investor preferences to ensure that the host country truly benefits from FDI. The results of the survey of MNC executives highlight several priorities for policy makers in developing countries seeking to create a conducive business climate for FDI:

Predictable government conduct is at least as important to MNCs as countries' laws and regulations. Investors cited the importance of transparency and predictability in the conduct of government agencies as the most important among investment climate factors. Investors look not only at policies on paper but also at implementation and administration of those policies. Implementation weaknesses can include bureaucratic inefficiencies, complex regulations and procedures, and unpredictable or arbitrary government conduct. Addressing these weaknesses can not only attract new investments but also prevent divestments by existing investors.

Addressing policy reforms to attract FDI and offering aftercare services are equally important. Policy makers tend to focus on attracting FDI through investment incentives, facilitation, and proactive investment promotion. While these are important, investors say that investment protection is even more critical to them, suggesting that government efforts should also aim to encourage investors to stay in the country and expand their operations. Policy initiatives should include strengthening investor protection guarantees, providing proactive investor aftercare, managing grievances, and promoting linkages.

Targeting policies and reforms to relevant types of investors can maximize effectiveness and cost efficiency. While most investors value some characteristics across the board—such as investment protection guarantees and transparency and predictability—some policy variables are more important for certain investor types. Firms involved in efficiency-seeking FDI seem more responsive to incentives. Manufacturing firms may be more responsive to business-friendly policies on importing inputs, while services firms are more sensitive to adverse government conduct. MNCs from developing countries value IPA services and some types of incentives more than firms from developed economies. These results reinforce the need for targeted policy approaches by governments, keeping in mind the specific types of FDI they wish to attract, retain, and harness for development.

Annex 1A. Survey Methodology and Characteristics

Methodology

The GIC Survey captures perceptions of international business executives on the role of investment climate factors in their FDI decisions. The survey respondents were 754 business executives involved with the

operations of their MNC in developing countries. The sample frame consisted of nearly 8,000 eligible companies in the commercially available Dunn and Bradstreet database. The 754 respondents were executives who were reached by telephone and agreed to participate in the survey. The sample included investors with existing investments in at least one developing country. Respondents were a combination of executives at the global headquarters and executives at a foreign affiliate. The characteristics of their firms are discussed below.

The World Bank Group commissioned a survey firm to conduct 30-minute computer-assisted telephone interviews. The interviews were conducted in 13 languages: Arabic, Bahasa Indonesia, Chinese, English, French, German, Italian, Japanese, Korean, Portuguese, Russian, Spanish, and Turkish. The interviews consisted of a screener phase, to ensure the eligibility of respondents. The interviews were conducted between February and June 2017.

Characteristics

The survey complemented other existing investor surveys by focusing on investment climate variables, such as administrative and legal barriers rather than broader economy-wide factors. These specific investment climate variables were areas actionable for policy makers.

The survey was intended to provide a broad understanding of corporate perspectives and investor behavior and is not intended as a benchmarking tool to compare countries.

The survey was composed of four sections:

1. *General information on the company and respondent*, including sector, number of employees, and position of the respondent in the company.

2. *Importance of factors in investing in a developing country*, where respondents rate the importance of country characteristics and investment policy factors on a scale from 1 to 4 from “not at all important” to “critically important.” “Critically important” means it is a deal-breaker—by itself, it could change the company’s decision about whether or not to invest in a country.

3. *Political risks and investment exit*, where respondents identify experiences of political risks and the company’s course of action. They were also asked whether they had shut down a foreign affiliate in a developing country and their reasons for doing so.

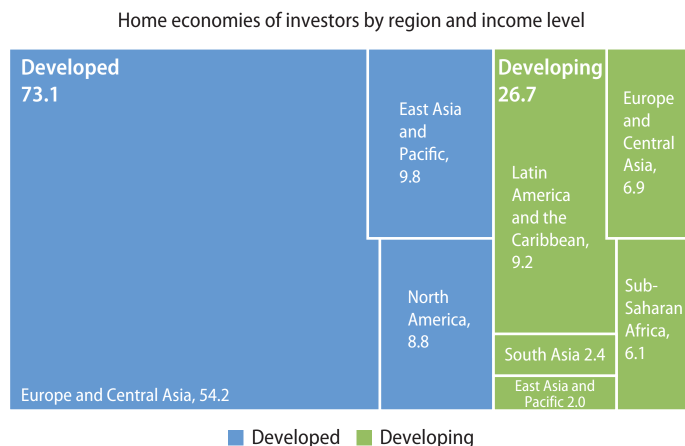
4. *Investment in a specific developing country*, where respondents select a specific developing country where they are most familiar with the process of establishing an affiliate. Questions on the specific investment included sector, activity, motivation, reinvested earnings, efficiency of government agencies, IPA services used, incentives received, sources of inputs, and corporate programs for suppliers.

Annex 1B. Respondent Profile

1. *Location of company headquarters*. Among 754 respondents, 73 percent were headquartered in high-income countries and 27 percent in developing countries. Over half of respondents had headquarters in Western Europe (figure 1B.1).

   The respondents were stratified by source economy of FDI. The sampling method considered whether the source economy was developed or developing but did not aim to make the composition of respondents representative at a country level. Practical considerations such as sample size and translations to local languages precluded the survey methodology from obtaining a representative sample of companies globally. The sampling method also considered that respondents should comprise a large enough sample of developing economies as source

FIGURE 1B.1 MNCs Come from Various Regions and Levels of Development
Share of respondents (percent)



Source: Computation based on the GIC Survey.
Note: Respondents were asked to identify the location of their global headquarters. The classifications of developing and developed are based on the World Bank Group's income level classifications. High-income economies are considered developed economies, while low-, lower-middle-, and upper-middle-income economies are considered developing economies. The analysis for this report is unable to disaggregate into income groups owing to the small sample size. MNC = multinational corporation.

countries of FDI. Table 1B.2 compares the composition of respondents from developed and developing economies with global outward FDI stock in 2016.

2. *Location of respondent*. Of respondents, 401 (53 percent) were executives located at the global headquarters while 353 (47 percent) were executives of an MNC affiliate in a developing country.

3. *Position of respondent in the company*. A large majority of respondents were either the Chief Executive Officer (CEO) or Chief Finance Officer (CFO), or their equivalent (table 1B.3).

4. *Sectoral Distribution*. Some 47 percent of respondents were executives of manufacturing firms, 45 percent were from services, 6 percent were from extractives, and 2 percent were from "other" noncategorized sectors (table 1B.4).

   Table 1B.5 compares the composition of survey respondents with global FDI flows for greenfield investments and mergers and acquisitions (M&A). Data on greenfield investments and M&A are based on data from UNCTAD's World Investment Report, based on the total number of investment projects (not value of investments) over the last five years (2012–16). During this period, there were 15,692 greenfield investment projects and 51,283 M&A purchases.

5. *Number of employees*. Large companies with 1,000+ employees constituted 40 percent of the sample. About one-third (32 percent) of the interviewed companies had fewer than 250 employees, and 26 percent had between 251 and 1,000 employees (figure 1B.2).

6. *Motivation*. Only about a third of companies (33 percent) had one dominant motivation for an investment in a specific developing country. A significant majority (62 percent) had two or more FDI motivations (table 1B.6).

TABLE 1B.1 Location of Headquarters

Developed economies	*No. of respondents*	*Percentage of respondents*	*Developing economies*	*No. of respondents*	*Percentage of respondents*
Germany	111	14.72	South Africa	35	4.64
Spain	80	10.61	Argentina	23	3.05
United States	60	7.96	Turkey	20	2.65
Italy	53	7.03	India	16	2.12
Korea, Rep.	37	4.91	Mexico	14	1.86
Austria	36	4.77	Bulgaria	10	1.33
Japan	32	4.24	Brazil	9	1.19
France	30	3.98	China	8	1.06
United Kingdom	28	3.71	Malaysia	6	0.80
Netherlands	22	2.92	Russian Federation	6	0.80
Sweden	20	2.65	Nigeria	4	0.53
Switzerland	20	2.65	Colombia	4	0.53
Canada	6	0.80	Peru	4	0.53
Belgium	5	0.66	Venezuela, RB	4	0.53
Australia	4	0.53	Belarus	3	0.40
United Arab Emirates	1	0.13	Bosnia and Herzegovina	3	0.40
Uruguay	1	0.13	Guatemala	3	0.40
Chile	1	0.13	Romania	3	0.40
Taiwan, China	1	0.13	Serbia	3	0.40
Iceland	1	0.13	Ukraine	3	0.40
Finland	1	0.13	Kenya	2	0.27
Estonia	1	0.13	Costa Rica	2	0.27
Denmark	1	0.13	Panama	2	0.27
			Egypt, Arab Rep.	1	0.13
			Bolivia	1	0.13
			Botswana	1	0.13
			Ecuador	1	0.13
			El Salvador	1	0.13
			Pakistan	1	0.13
			Saint Lucia	1	0.13
			Sri Lanka	1	0.13
			Swaziland	1	0.13
			Thailand	1	0.13
			Uzbekistan	1	0.13
			Djibouti	1	0.13
			Ghana	1	0.13
			Zambia	1	0.13
			Cameroon	1	0.13

TABLE 1B.2 Composition of Respondents Compared with Global FDI Stock

Percent

Location of headquarters	*Percentage of respondents*	*Share of global FDI stock*
Developed economies	73.21	76.31
Developing economies	26.79	23.69

Source: Computation based on the GIC Survey and UNCTAD.
Note: FDI = foreign direct investment.

TABLE 1B.3 Position of Respondents in the Company

Position	*No. of respondents*	*Percentage of respondents*
CFO/Finance director/Treasurer/Comptroller	336	44.6
CEO/President/Managing director	146	19.4
Head of business unit/Head of department	126	16.7
Other C-level executive	61	8.1
SVP/VP/Director	26	3.4
Board member	24	3.2
Director of global operations or global manufacturing	18	2.4
Other	12	1.6
CIO/Technology director	5	0.7
Total	754	100.0

TABLE 1B.4 Sectoral Distribution of Respondents

Sector	*No. of respondents*	*Percentage of respondents*
Primary		
Agriculture, hunting, forestry, and fishing	22	2.92
Mining, quarrying, and petroleum	26	3.45
Manufacturing		
Refined petroleum products, coke, and nuclear fuel	7	0.93
Agroprocessing, food products, and beverages	24	3.18
Textiles, apparel, and leather	23	3.05
Chemicals and chemical products	24	3.18
Rubber	5	0.66
Plastic products	14	1.86
Pharmaceuticals, biotechnology, and medical devices	26	3.45
Metals and metal products	39	5.17
Nonmetal mineral products	3	0.40
Wood and wood products (other than furniture)	3	0.40
Furniture	2	0.27
Paper and paper products	6	0.80
Printing and publishing	4	0.53
Automobiles, other motor vehicles, and transport equipment	67	8.89
Information technology and telecommunications equipment	6	0.80
Machinery, and electrical and electronic equipment and components	64	8.49
Other manufacturing	36	4.77

table continues next page

TABLE 1B.4 Sectoral Distribution of Respondents *(continued)*

Sector	No. of respondents	Percentage of respondents
Services		
Electricity, gas, and water	20	2.65
Alternative energy	19	2.52
Construction	53	7.03
Wholesale and retail trade	43	5.70
Hotels and restaurants	7	0.93
Other travel and tourism-related services	8	1.06
Logistics, transport, and storage	35	4.64
Telecommunications	13	1.72
Computer and software services	10	1.33
Financial services including insurance	44	5.84
Real estate	4	0.53
Business services	18	2.39
Professional, scientific, and technical services	32	4.24
Health services	8	1.06
Media and entertainment	7	0.93
Other services	15	1.99
Other	17	2.25
Total	754	100.00

TABLE 1B.5 Sectoral Distribution of Respondents Compared with Global FDI Flows
Percent

Sector	Share of global FDI flows for greenfield	Share of global FDI flows for M&A	Percentage of respondents
Primary	**0.5**	**4.7**	**6.4**
Agriculture, hunting, forestry and fisheries	0.0	0.5	2.9
Mining, quarrying and petroleum	0.5	4.1	3.5
Manufacturing	**47.3**	**22.2**	**46.8**
Food, beverages, and tobacco	3.6	2.8	3.2
Textiles, clothing, and leather	8.8	0.6	3.1
Wood and wood products	0.9	0.2	0.4
Paper and paper products	—	0.7	0.8
Publishing and printing	0.1	0.2	0.5
Coke, petroleum products, and nuclear fuel	0.5	0.2	0.9
Chemicals and chemical products	5.0	2.7	3.2
Pharmaceuticals, biotechnology, medical devices	—	1.6	3.5
Rubber and plastic products	2.5	0.5	2.5
Nonmetallic mineral products	1.0	0.8	0.4
Metals and metal products	2.2	1.9	5.2
Machinery and equipment, electrical and electronic equipment	12.4	7.0	8.5
Precision instruments	1.1	—	—
Motor vehicles and other transport equipment	6.7	1.5	8.9
Manufacturing of furniture	—	0.2	0.3
Other manufacturing	2.4	1.2	4.8

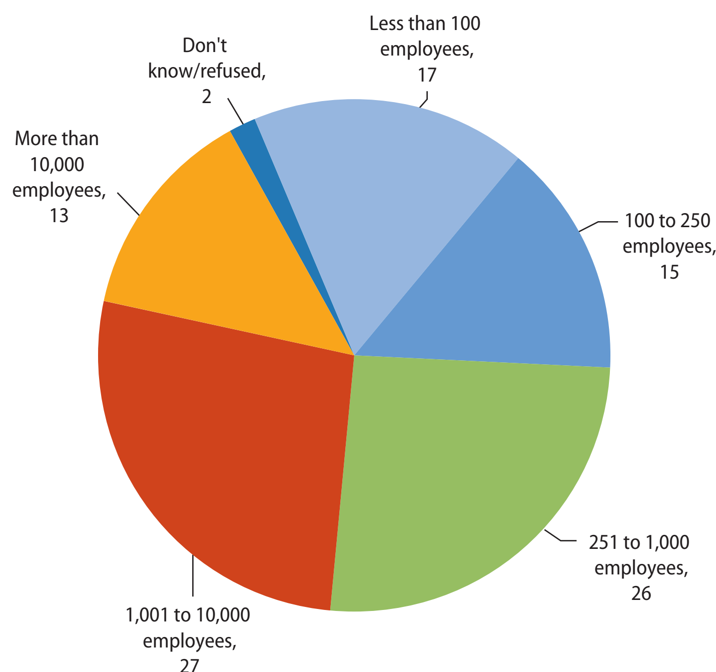
table continues next page

TABLE 1B.5 Sectoral Distribution of Respondents Compared with Global FDI Flows *(continued)*

Sector	*Share of global FDI flows for greenfield*	*Share of global FDI flows for M&A*	*Percentage of respondents*
Services	**52.2**	**73.2**	**44.6**
Electricity, gas, and water	2.2	1.9	5.1
Construction and real estate	1.6	1.1	7.6
Trade	5.3	4.5	5.7
Hotels and restaurants, travel and tourism-related	0.8	3.0	2.0
Transport, storage, and communications	6.4	49.1	6.4
Finance	7.2	11.1	5.8
Business services	26.2	—	2.4
Public administration and defense	—	0.7	—
Education	0.7	0.2	—
Health and social services	0.5	0.7	1.1
Arts, entertainment, and recreation	1.2	0.4	0.9
Other services	0.2	0.3	2.0
Other	—	—	2.3

Source: Computation based on UNCTAD World Investment Report 2017, which sourced its data from UNCTAD M&A database and fDi Markets database, the Financial Times, and based on the GIC Survey.
Note: Sector categories have been slightly adapted to harmonize across the three data sources. Sectors marked with "—" are not in the list of sectors from their original source. FDI = foreign direct investment; M&A = mergers and acquisitions.

FIGURE 1B.2 Size of MNCs by Number of Employees
Share of respondents (percent)



Source: Computation based on the GIC Survey.
Note: MNC = multinational corporation.

TABLE 1B.6 Number of Motivations

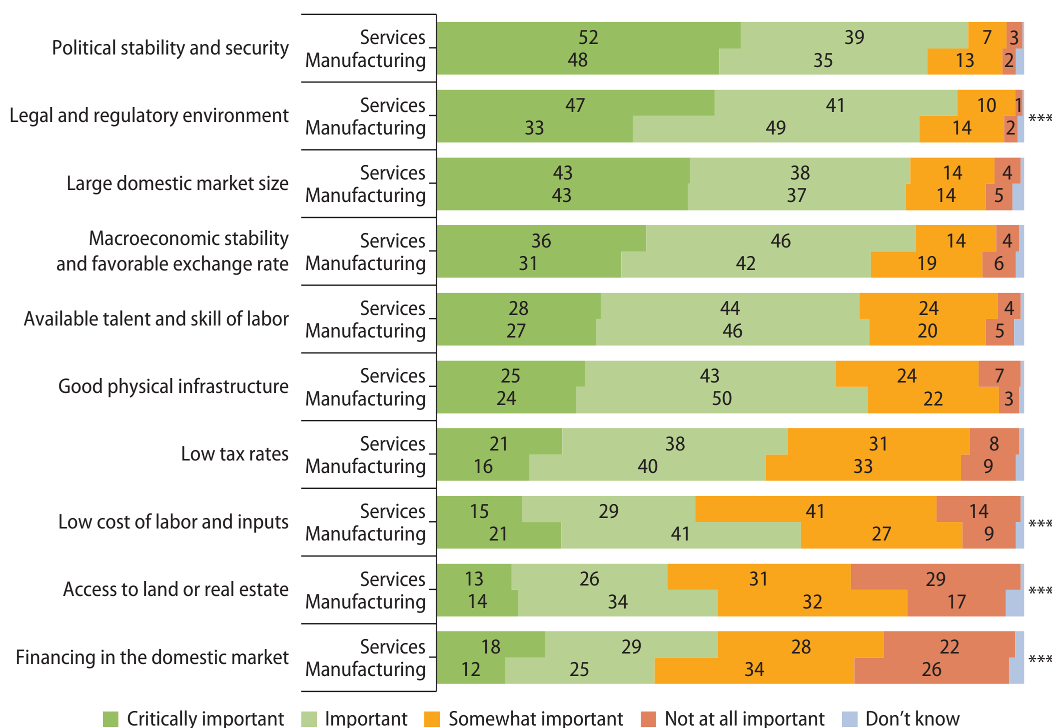
No. of motivations	*No. of respondents*	*Percentage of respondents*
0	34	4.51
1	249	33.02
2	227	30.11
3	159	21.09
4	64	8.49
5	21	2.79
Total	754	100.00

Annex 1C. Differences by Group

The importance of country characteristics varies by sector and source of FDI. Manufacturing firms find cost of labor and other inputs, and access to land or real estate, more important than services firms, probably because the efficiency-seeking motivation is more common in the manufacturing sector than in services. Services firms, on the other hand, are more sensitive to political stability and security,

FIGURE 1C.1 Importance of Country Characteristics by Manufacturing versus Services Firms

Share of respondents (percent)

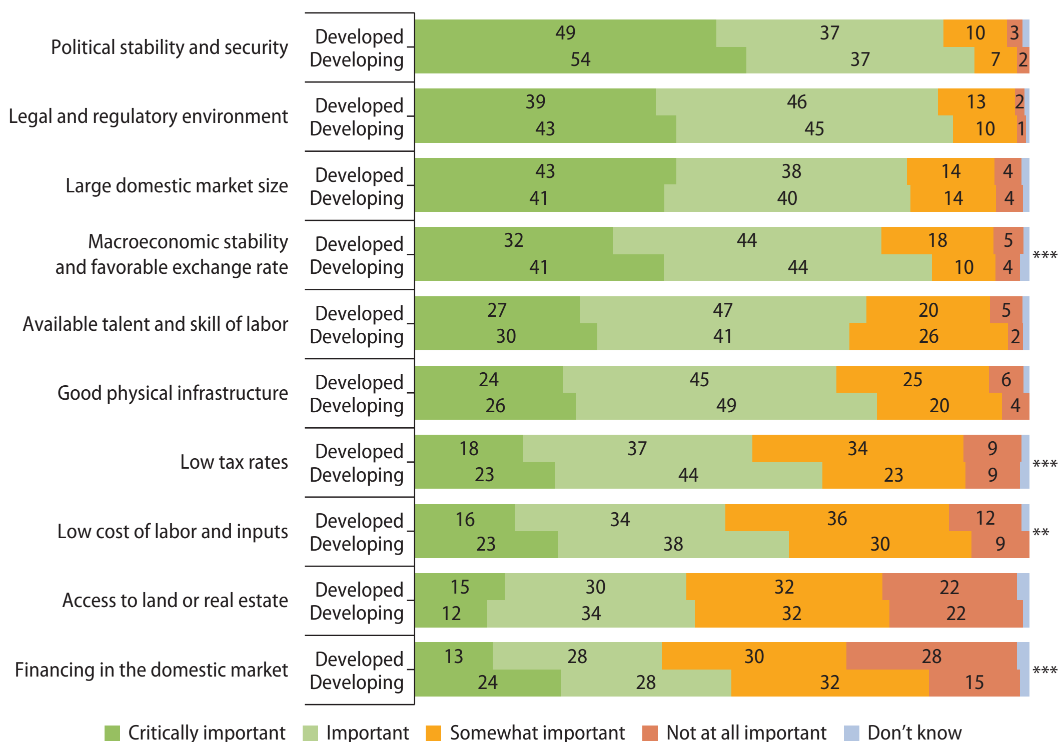


Source: Computation based on the GIC Survey.
Note: The differences between the two groups are significant at ***p<0.01, **p<0.05 and *p<0.1.

the legal and regulatory environment, macroeconomic stability, and financing in the domestic market (figure 1C.1). Many of these services firms offer financial services, retail trade, energy, and telecommunications that are more highly regulated. Investors from developing countries also tend to value many of these factors highly, compared with their counterparts from developed economies—these characteristics include macroeconomic stability, low cost of labor and inputs, low tax rates, and availability of domestic financing (figure 1C.2). Respondents from affiliates located in developing countries tend to rate most characteristics as important compared with respondents based at the companies' global headquarters (figure 1C.3). This suggests that executives on the ground, who are more aware of the challenges in setting up and operating MNC affiliates in developing countries, value more highly factors such as a business-friendly legal and regulatory environment; indeed, almost half said that the absence of such an environment was a deal-breaker, versus only 32 percent of respondents in parent companies.

The importance of investment climate factors also varies by sector. Services firms are more sensitive to transparency and predictability in the conduct of public agencies, investment protection guarantees, and ease of starting a business, likely owing to these industries being more highly regulated (figure 1C.4). Investors from developing countries also seem to value investment climate factors more highly than those from developed economies, but the differences are not statistically significant (figure 1C.5). Respondents from affiliates located in developing countries tend to rate investment

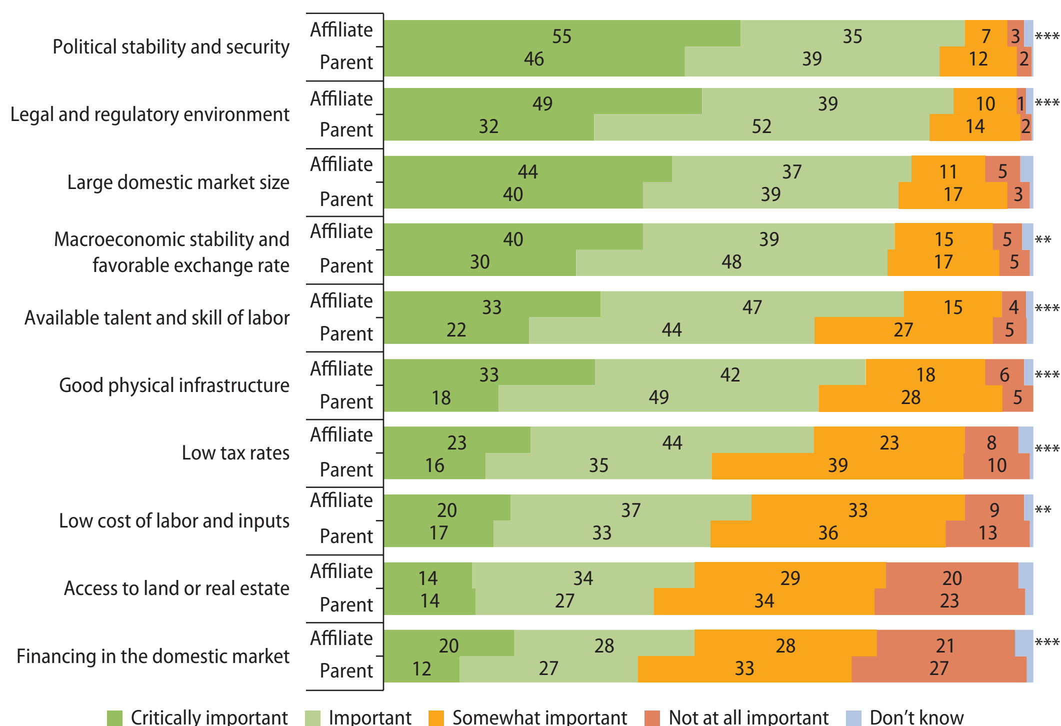
FIGURE 1C.2 Importance of Country Characteristics by Developed versus Developing Source Countries
Share of respondents (percent)



Source: Computation based on the GIC Survey.
Note: The differences between the two groups are significant at ***$p<0.01$, **$p<0.05$ and *$p<0.1$.

FIGURE 1C.3 Importance of Country Characteristics by Parent Company versus Affiliate

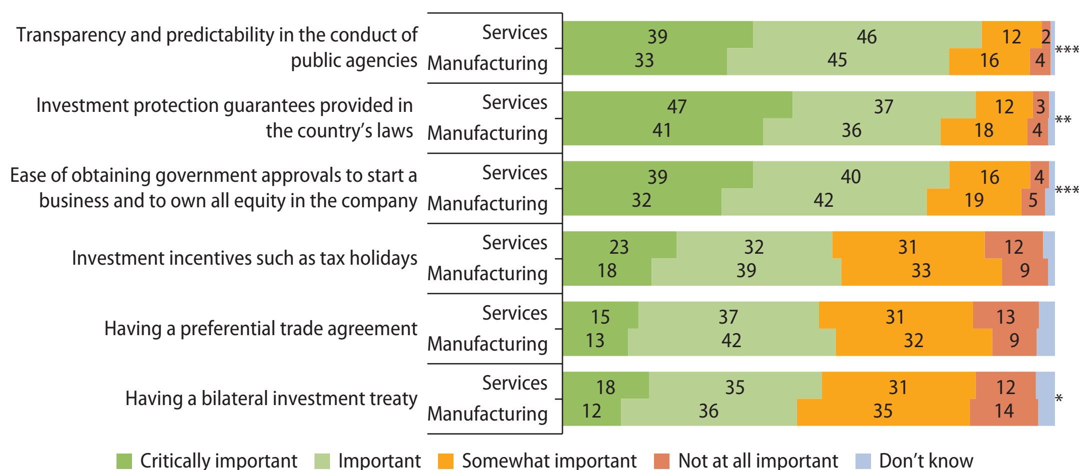
Share of respondents (percent)



Source: Computation based on the GIC Survey.
Note: The differences between the two groups are significant at ***p<0.01, **p<0.05 and *p<0.1.

FIGURE 1C.4 Importance of Investment Climate Factors by Manufacturing versus Services Firms

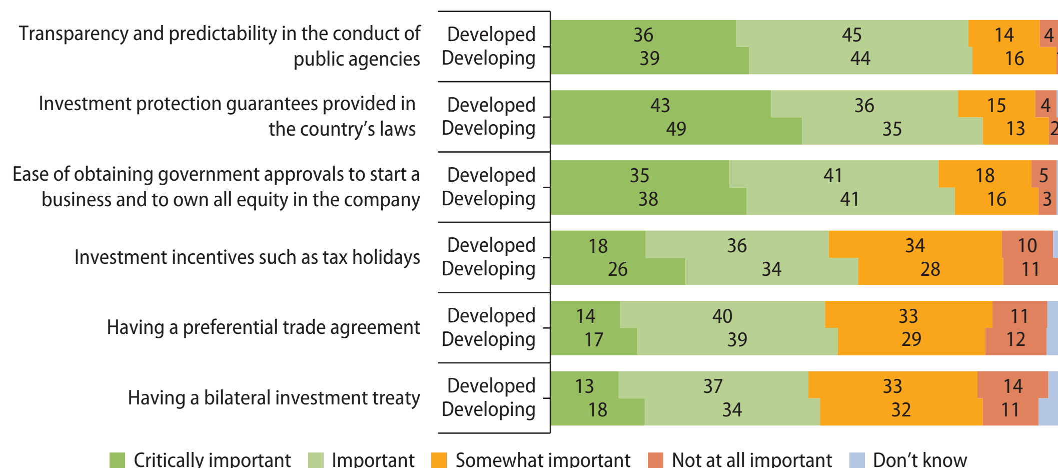
Share of respondents (percent)



Source: Computation based on the GIC Survey.
Note: The differences between the two groups are significant at ***p<0.01, **p<0.05 and *p<0.1.

FIGURE 1C.5 Importance of Investment Climate Factors by Developed versus Developing Source Economies

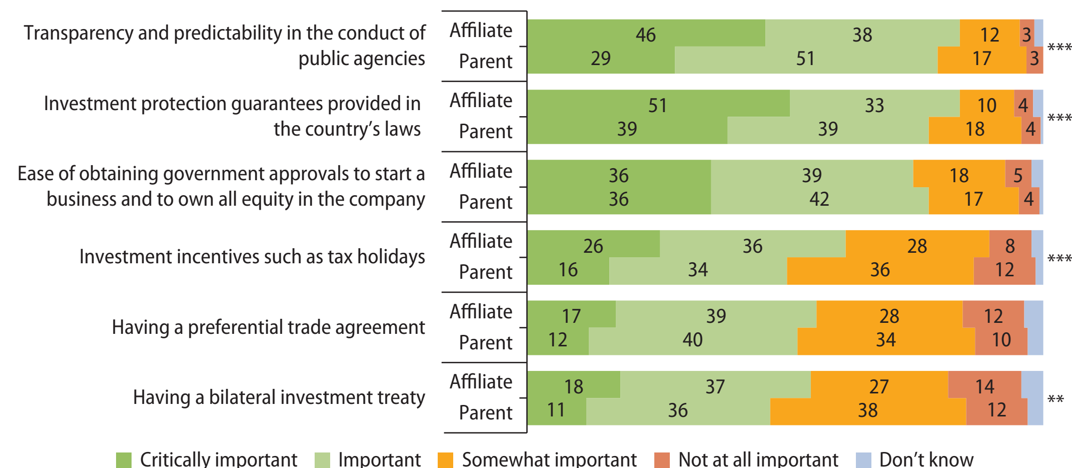
Share of respondents (percent)



Source: Computation based on the GIC Survey.
Note: None of the differences is statistically significant.

FIGURE 1C.6 Importance of Investment Climate Factors by Parent Company versus Affiliate

Share of respondents (percent)



Source: Computation based on the GIC Survey.
Note: The differences between the two groups are significant at ***$p<0.01$, **$p<0.05$ and *$p<0.1$.

climate factors as important compared with respondents based at the companies' global headquarters (figure 1C.6). In particular, these are transparency and predictability in the conduct of public agencies, investment protection guarantees, investment incentives, and having bilateral investment treaties.

Notes

1. This broader definition and use of FDI typology will be further elaborated in a forthcoming World Bank Group publication.
2. In this chapter, "efficiency-seeking" investors are those respondents who said that lowering production costs and establishing a new base for exports was one of their motivations for setting up an affiliate in a developing country.
3. Echandi, Krajcovicova, and Qiang (2015) provide a literature review of local content requirements including studies from UNCTAD (2007), Moran (1998, 2006, 2011), Hufbauer and others (2013).

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