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Please find attached the presentation by Mr. Edilberto Segura, SigmaBleyzer Foundation,
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In 1999, SigmaBleyzer initiated the International Private Capital Task Force (IPCTF) in Ukraine. Its objective was to benchmark transition economies to identify best practices in government policies that improve the investment climate and attract private capital. An Action Plan was developed and presented to the Ukrainian government, which identified the economic policy actions necessary to improve the investment and business climate in Ukraine, attract additional flows of private capital to the country, support economic growth, and improve the quality of life for their citizens. In 2001, this effort was expanded to all countries of the FSU, and IPCTF ratings for all 15 countries of the FSU were developed. They are available from SigmaBleyzer and The Bleyzer Foundation.

The Bleyzer Foundation was established in 2001 in order to promote the IPCTF framework and help countries implement the policies necessary to successfully complete transitions to market economy.

The Foundation's Managing Director is Mr. Victor Gekker, who is supported by a team of economists and business analysts. The Advisory Board of The Bleyzer Foundation is chaired by Dr. Edilberto Segura and provides advice and guidance to the activities of the Foundation.

Survey of International Foreign Investment Promotion Practices

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Introduction

It is widely recognized that foreign direct investment (FDI) plays an important role in worldwide economic development. A large number of developing countries and transition economies have benefited from FDI inflows, which bring into the recipient countries not only capital, but also modern technology and know-how. With the wave of globalization, FDI inflows help developing countries and transition economies integrate into the world economy by making them more competitive and by improving their living standards. By acknowledging the advantages of foreign investments for the recipient economy, governments in many developing and transition countries put forth great efforts to attract FDI flows into their economies. Therefore, investment promotion by these governments has become an increasingly important tool for improving the investment climate and attracting FDI into their countries. Growing competition among developing and transition countries in their efforts to attract FDI gave rise to the establishment of specially designed investment promotion agencies on both national and sub-national levels in many countries. Presently, there are more than 160 investment promotion agencies (IPAs) worldwide that deal with attracting foreign investments. According to the research findings, economies in transition can attract more FDI when they have effective agencies that assist foreign investors.

This report reviews the international experience of IPAs' operation and organizational structures in order to assess what makes these agencies effective in promoting a country for foreign investments (in influencing foreign investors' decisions to enter a particular market.) Based on the results of analytical surveys and research performed by international organizations (particularly the Foreign Investment Advisory Service (FIAS) of the World Bank/IFC and United Nations Conference on Trade and Development (UNCTAD)), and our own assessments of IPA operations in the CEE region, we can define the best practices in the promotion of foreign investment. The conclusions made as a result can be instrumental and have useful implications for the development of an investment promotion strategy for Ukraine.

Investment Promotion Agencies: A Review of International Experience

Investment promotion may be defined as activities that disseminate information about or attempt to create an image of the investment location and provide investment services for prospective investors. Targeted investment promotion activities implemented by the government may be instrumental for not only the attraction of foreign capital to the country, but also significant improvements in the domestic business environment with corresponding benefits for both domestic and foreign entrepreneurs.

There are three major roles for an IPA. One is to communicate and disseminate information about the business environment and opportunities among prospective investors. Such information is considered a public good, and there should be free access for all interested parties. However, in emerging economies, information is a scarce resource, partly because companies operating in the private sector may restrict information flows to prevent entry of new competitors into the market. Another role is the coordination of activities aimed at improving the business environment in the country, which may range from providing assistance to potential and existing investors in their day-to-day problems, to lobbying for key policy and legal reforms. A third role undertaken by many IPAs is investment generation; that is, activities aimed at identifying potential investors and targeting specific sectors and companies in order to create investment leads.

Although it is difficult to measure the effectiveness of investment promotion efforts, the major indicator of an IPA's performance is the amount of FDI attracted. Major empirical studies that investigated the issue [1,3] found significant positive correlation between the investment promotion efforts and FDI flows to emerging economies. In addition, the effectiveness of the agency's operations may be evaluated by exploring data on foreign investments attracted with the help of the agency in relation to the total flow of investments, although data on IPAs performance is scarce. For instance, the investment promotion agency in the Czech Republic (CzechInvest) was involved in about 22% of total FDI flows into the country since its establishment in 1993 till 2001. The agency also showed significant progress in attracting foreign investments during the period. In the first years of its operation, CzechInvest attracted relatively small amounts (up to \$100 million in FDI or about 8% of the total inflow.) But as the agency gained experience and credit among investors, its performance improved. In 2000–2001, CzechInvest mediated about 36% of the total FDI flows into the country. This reflects significant progress, especially taking into account that volumes of FDI inflow increased more than 5 times

between 1993 and 2001. A similar agency in Hungary (ITDH) reported that in 2002, it managed to attract about 25% of the total FDI inflow over the period. However, research carried out by FIAS and UNCTAD suggests that the effectiveness of investment promotion activities crucially depends on the status, organization, personnel, and budget of an IPA, and also the functions it performs.

For effective investment promotion, the organizational and functional structure of an IPA should be business-oriented in order to develop strong links with the private sector, and should have support from the highest political level to perform its objectives in a cost-effective manner. Thus, it is important to consider the IPA's functions, organization and management in more detail to determine best practices.

A. Functional Structure of an IPA

Investment promotion includes four types of activities — image building, investment generation, investment servicing, and policy advocacy (see Table 1.) Most investment promotion agencies usually

Table 1. Major Functions of An Investment Promotion Agency

Function		Objective	Activities
Image Building		To create the perception of a country as an attractive site for international investment	<ul style="list-style-type: none"> • advertising • PR events • mass media campaigns abroad • investor forums • maintaining relationships with journalists and business partners • developing the agency's website
Investment Targeting/ Generation		To create investment leads that target investment into specific sectors, development areas, or companies.	<ul style="list-style-type: none"> • identification of potential investors • matchmaking • direct mailing, telephone campaigns • seminars for targeted investors
Provision of Investment Services	Pre-Investment Services	To facilitate a foreign investor's entry into the economy; to assist in analyzing investment decisions	<ul style="list-style-type: none"> • information provision • "one-stop-shop" registration/approval service • sectoral analyses • various assistance in obtaining sites, suppliers etc.
	Post-Investment or Aftercare Services	To assist a foreign investor in maintaining his business in a good standing, facilitating reinvestment decisions in the future	<ul style="list-style-type: none"> • legal or other advisory support to on-going foreign investment projects • dealing with bureaucracy etc.
Policy Advocacy		To improve an investment climate by establishing an effective feedback between a foreign investor and government	<ul style="list-style-type: none"> • surveys of private sector • participation in task forces • policy and legal proposals to authorities • lobbying

Source: based on Wells and Wint, 2000

implement these activities, although the degree of importance that they grant to each type of activity varies greatly. Some agencies also deal with promotion of privatization.

One of the important missions of IPA is to create a positive international image for a country or specific area within the investor community. Image-building activities constitute an important part of agency operations, especially in the initial stages of investment promotion. In particular, these include various kinds of advertising in financial and industry- or sector-specific international media, generation of favorable news stories about the progress in reforms and other positive changes occurring in the country. It also includes other public relations events like participation in investment exhibitions and fairs, conferences, and organization of investment opportunity seminars. Image building is particularly important for a country with a poor investment climate and low levels of FDI in order to generate investment interest.

Investment generation entails targeting specific sectors and source countries to generate investor interest in specific developmental objectives of the country or area. Activities include organization and implementation of road shows and seminars focused on special audiences, which are targeted at specific countries, sectors, industries and even companies. Conducting general investment missions to the country is also a part of investment generation activities. Within this category of services, a number of agencies also organize country visits that envisage meetings with government officials, suppliers of infrastructure and other services, representatives of public think-tanks, embassies, chambers of commerce and scientific institutions. The logic behind targeting foreign investment into specific sectors lies in the diversification of economic activities of the particular country in order to reduce the country's susceptibility to external shocks. Presently, IPAs in transition economies of Central and Eastern Europe target foreign investments into sectors that are currently not a particular strength of the economy. Usually these are high-tech sectors like engineering, information technology, etc. In many countries, governments provide specific investment incentives to such priority development sectors or areas, which are often used for investment generation.

The overwhelming majority of IPAs around the world put a great emphasis on investment servicing and facilitation, which is an integral part of investment promotion. Investment servicing entails a wide range of services to assist investors in analyzing investment decisions, establishing a business and maintaining it in good standing. All investors' services that IPAs usually provide can be divided into two broad categories: pre-investment and post-investment (aftercare) services. Virtually all existing IPAs provide services in the

pre-investment decision stage. These include giving interested investors information about the country, its macroeconomic situation, major industries, legislation and procedures required of investors, investment incentives, costs of doing business and other information that can facilitate an investor's decision to launch a business or set up a joint venture in the country. IPAs usually assist investors with the process of launching their investment projects. They may act as a "one-stop-shop" for expediting the registration or approval process, obtaining sites, utilities, suppliers, etc. These agencies also may have the discretion to grant investment incentives to foreign investors, although most IPAs only provide information about them and guide them through the application procedure. However, the issue of investment incentives should be discussed in more detail.

Growing competition for foreign investments among emerging markets make governments invent different incentive schemes to stimulate FDI. However, the nature of incentives offered by governments to foreign investors has changed significantly over the last decade. Developing and transition countries tend to depart from the practice of granting distortionary tax incentives to investors because they failed to deliver the desired outcomes and turned out to be extremely costly for the economy as a whole. International experience suggests that in addition to creating market distortions and hindering competition, tax breaks and other tax privileges for foreign investors gave rise to various rent-seeking activities in the public sector, which contributed to corruption and reform delays. Still, some countries provide investment incentives in the form of tax relief, but they are limited to the specific priority development sectors or areas and are granted for a limited time period. In the Czech Republic, for example, corporate tax relief is granted to enterprises with foreign participation in the manufacturing sector only, while in Poland, only investors operating in special economic zones are eligible for income tax relief. At the same time, the major emphasis in modern investment incentive schemes is on job-creation and training grants, grants for infrastructure development, discounts for purchase of land and property, and partial reimbursement of initial investment costs. Such investment schemes are considered non-distortionary for the economy as a whole, but can facilitate an investor's decision to invest, especially if assisted by an IPA.

Reinvestments by the foreign business community make up a substantial part of FDI inflow into the country. Thus, provision of post-investment services is based on the belief that satisfied investors will ultimately expand their operations and help attract foreign investors to a country. Post-investment services include assistance to foreign investors in overcoming problems that arise while they

are operating, such as advice and consultation in dealing with bureaucracy. Nearly 70% of IPAs around the world encourage investment through post-investment (or aftercare) services. These kinds of services also help to identify administrative and other barriers to foreign investments, and thus facilitate implementation of the other important function of an IPA — policy advocacy.

Because of day-to-day contacts with private sector representatives, an IPA could be considered a bridge between the private sector and the government. An IPA may often know where improvements in the investment regime are required. This includes a wide range of actions, from amendments to legislation to small improvements in administrative procedures that can facilitate investor operation in the country. While being either part of the government or having close connections with high-level government officials, an IPA has the ability to advocate changes in investment policies, and to play a key role in the preparation of new investment legislation and regulations. According to a recent UNCTAD study, 80% of IPAs indicated that they engage in policy advocacy services.

The mix of different services offered by an IPA should correspond to the existing business environment in which the agency operates, and its priority objectives. According to an FIAS survey of IPA performance, 35% of all IPA's activities are devoted to image building, 33% to investment servicing (out of which 75% entails pre-investment services), 22% to investment generation, and only 10% to policy advocacy. Although it is important for an IPA to provide a full range of services in each particular environment, it is hardly a cost-effective approach. For instance, in countries that experience temporary domestic unrest, such as a turbulent political situation or other instability that may scare off new investors, image-building and investment generation activities are likely to be very ineffective, if not counterproductive. During such periods, post-investment activities and policy advocacy associated with efforts to improve the investment climate can be the principal activities of an IPA. Results of empirical research conducted by Morisset [1] imply that those IPAs that devote more resources to policy advocacy are more effective because this activity provides benefits to both foreign and domestic investors. At the same time, investment-targeting activities turn out to be quite expensive and risky, especially in countries with a poor investment climate.

A recent study by FIAS (The Effectiveness of Promotion Agencies at Attracting Foreign Direct Investments) attempted to measure the effectiveness of the various functions of an IPA in attracting FDI. The study concluded that policy advocacy was the most effective activity to attract FDI. Image-building and investor services were also

important. On the other hand, the study showed that investment generation was not associated with higher FDI flows, even though it absorbed the greatest share of most IPAs' budgets. The report recommended that most IPAs should dedicate a larger portion of their budget to policy advocacy, particularly to improve the country's business environment.

B. Organizational structure of an IPA

The effectiveness of an IPA crucially depends on its organizational structure. According to the studies performed by FIAS and UNCTAD, certain organizational characteristics of an IPA are associated with better performance in delivering the desired outcomes. Because of the public good nature of investment promotion activities, IPAs are government entities in most countries. About 80% of the IPAs surveyed by the UNCTAD were government agencies. However, investment promotion agencies have responsibilities and functions that differ from other government agencies and, correspondingly, need a different organizational structure. Traditional government processes usually deal with regulation and control, creation and enforcement of laws, exercising authority, operating as a custodian, and so forth. However, investment promotion agencies should perform activities that are typical of the private sector. And this requires the flexibility to quickly respond to investors' needs, adjust to changing market conditions, and the autonomy to generate and implement investment promotion strategies that are consistent throughout a long period, disregarding the political environment in the country.

Therefore, many agencies have appealed for more independence from their governments to increase the effectiveness of investment promotion activities. A more autonomous status gives IPAs the chance to create corporate office cultures and to attract experienced staff from the private sector by offering competitive salaries. Over 25% of the IPAs surveyed by the FIAS and UNCTAD are autonomous public institutions, and about 35% of the IPAs are semi-autonomous state bodies with private sector involvement (when private sector is represented in the supervisory or steering boards of IPAs.) The share of IPAs that are units of Ministries represents less than 20%. Research studies also provide evidence in favor of a more autonomous nature of IPAs [1, 3]. It was found that FDI flows were significantly lower in countries where the IPA was part of a ministry, in contrast to those that were either an autonomous or semi-autonomous public institution. Also, the effectiveness of IPAs was found to be greater when the agency reported to a supervisory board that included representatives of the private sector, and it reported directly to highest-level officials (either a country's President or a

Prime minister). Thus, an autonomous or semi-autonomous institutional structure of an IPA can be more effective in a transition economy, because such an organization can contribute to strengthening the government's commitment to market reforms as well as reinforce the agency's credibility and visibility in the business community. Out of 14 national IPAs operating in the CEE and CIS region (information about which is presented in Table 2 in the Appendix), 7 are either autonomous or semi-autonomous government agencies.

Due to the peculiarities of IPA's functions mentioned above, the issue of the agency's staff and management personnel is the second most important after the institutional structure of the agency. An IPA's staff should include people that are comfortable with both business operations and investment decisions, and government procedures. To run an effective image-building campaign, an IPA should be staffed with experienced marketing people that usually earn high salaries in the private sector. Thus, it is not surprising that 60% of IPA staff around the world has private sector experience, and 41% of IPAs offer salaries that are competitive with those of the private sector. According to the UNCTAD study [2], 30% of IPA staff has an educational background in economics, 20% in business administration, and 12% in public administration. Special attention should be given to the choice of agency director or chief executive officer. On the one hand, for successful IPA performance, the director should be able to communicate regularly and effectively with government officials, maintain political neutrality, and lobby for money with home and, perhaps, donor governments. On the other hand, the director must be able to get along with domestic and foreign businesses and fit into their social activities.

In many countries, IPAs also have steering or advisory boards, the composition of which is also important for the agency's performance. In most cases, boards are composed of representatives from both the public and private sector. Government board members, especially high-level officials, provide access to the bureaucracy, which can be extremely valuable when the agency is trying to help investors solve problems with the government. Meanwhile, private sector members are likely to emphasize and monitor the agency's performance (ensuring transparency), improve the agency's understanding of how decisions are made in the private sector, and provide information on barriers to investment in the country. For instance, private sector representatives are included in the steering boards of IPAs in the Czech Republic, Bosnia and Herzegovina, and Estonia. In addition, close connections of the agency with the Ministry of Foreign Affairs brought about an effective use of the country's diplomatic service for implementation of image-building activities. UNCTAD has even launched a special series of training

workshops in investment promotion for mid- and senior-level diplomats from developing and transition countries that offers significant savings for IPAs overseas image-building activities. The World Association of Investment Promotion Agencies (WAIPA) also offers different trainings and conferences for IPA staff. IPAs in transition economies employ on average 26 people, including three people on support staff.

The public good nature of investment promotion envisages financing of the IPA with public funds. Although investment promotion agencies have alternative sources of financing, public funds account for about 70% of their total budgets. Alternative sources of funding, such as private or external sources, have been inconsistent or weak complements because of the public nature of investment promotion. According to the FIAS survey, agencies operating in CEE transition countries rely on foreign assistance to finance their activities by almost 30%. Indeed, foreign aid appeared quite handy in the first years of the IPA's establishment, but as an agency expands its activities it should not be dependent on aid money because they tend to disappear over time and donors usually attach strict reporting requirements to aid money. For instance, the Foreign Investment Promotion Agency (FIPA) in Bosnia and Herzegovina enjoyed World Bank and UNDP support at the initial stages of its development, and it also has been advised by FIAS on the organizational and functional structure of the FIPA.

The European Union also provides financial and technical assistance to investment promotion agencies in the CEE region. A UNCTAD study on investment promotion practices, which captured a broader sample of IPAs, reveals that international aid is the third largest source of financing for IPAs (9%), while revenue earned from chargeable services accounts for 10% of IPAs budgets. Despite this fact, most government agencies provide their services for free to foreign investors (see Table 2 in the Appendix). If the agency charges money for its services, it should be able to compete on the price and quality with private companies offering similar services, and by doing so the agency runs the risk of losing its credibility as a government representative. Some agencies have tried to raise funds through charitable donations from corporations already operating in the country (in the form of membership fees), but the results have not been encouraging [3].

The scope of IPA's financing differs greatly across different countries. It is natural that higher-income countries usually spend more on investment promotion than lower income countries. According to the UNCTAD study, the average operational budget of an IPA was \$1.1 million per annum in 1999. Transition economies tend to spend on average \$800,000 a year on investment promotion

activities. Research findings presented by Morriset (2003) suggest that the size of an IPA's budget does have an effect on the effectiveness of investment promotion efforts. In particular, a 10% increase in the annual budget of an IPA within \$60,000–\$2 million range is associated with a 7.5% increase in FDI inflows into the country. For instance, in the Czech Republic, government expenditures for investment promotion efforts have increased from \$200,000–\$300,000 in the first years of CzechInvest's operation, to almost \$4 million in 2001. For comparison, the Estonian government allotted \$450,000 or almost 20% of its budget expenditures to the Estonian Investment Agency's needs in 2003. These agencies seem to be quite efficient given their small budgets. In 2001, CzechInvest managed to attract slightly over \$2 billion of FDI, while the Estonian Investment Agency mediated \$160 million of FDI inflow in 2002.

Conclusions and recommendations

The analysis presented in this paper supports the view that investment promotion agencies can be effective in influencing the decision to invest in a country, and their operation may bring substantial increases in FDI inflows. Judging by international investment promotion practices, several implications for the establishment of an effective investment promotion agency in Ukraine can be made.

First, the agency implementing investment promotion activities should have clear objectives that correspond to its primary mission — to increase the quantity and quality of FDI flows into the country. The agency should effectively disseminate information about the business environment and opportunities among prospective investors and coordinate activities aimed at improving the business environment in the country.

Second, the agency must be transparent and must be trusted by the investment community, including foreign investors already operating in the country. Satisfied foreign investors are likely to not only expand their own operations in the country given favorable market conditions and positive changes in the investment climate, but also to facilitate the arrival of new investors.

Third, the agency's effectiveness is influenced by its organizational structure and reporting mechanisms. To be effective, the agency should have a business orientation, strong links with the private sector, and simultaneously, be supported by the highest levels of the government (President or Prime Minister.) Private sector participation in the management of the IPA would also contribute to the

efficiency of the agency's performance. Therefore, it would be desirable for the agency to be either autonomous or semi-autonomous of the government.

Fourth, the agency should perform all the basic functions of a typical investment promotion agency. The mix of different services offered by an IPA should correspond to the existing business environment in which the agency operates and its priority objectives. Even taking into account the poor investment climate and low FDI level in Ukraine, an agency promoting foreign investments should pay attention to image-building activities to communicate positive shifts in economic policies in order to attract new investors into the country. Also, the agency should focus on policy advocacy activities by establishing tight links with foreign investors currently operating in the country, in order to address administrative and other barriers to FDI flows to Ukraine. However, investment generation activities should not be relied upon because international experience has shown that implementation of these activities is not associated with higher FDI flows, even though it requires substantial financing [1]. It is also important that the agency's basic services are provided free of charge.

Fifth, an effective IPA should rely mostly on government financing. Investment promotion agencies operating in CEE transition countries relied on foreign assistance to finance their activities as alternative sources of funding by almost 30%, especially in the early years of its establishment. Ukraine is also eligible to get foreign assistance for the establishment of an investment promotion agency. In transition economies, the size of an IPA annual budget range from \$400,000–\$4 million, with an average of \$800,000.

References:

- [1] Morisset, Jacques. 2003. Does a Country Need A Promotion Agency to Attract Foreign Direct Investment? *World Bank Policy Research Working Paper #3028* (April)
- [2] UNCTAD. 2001. A World of Investment Promotion at a Glance. A Survey of Investment Promotion Practices. *Advisory Studies #17*
- [3] Wells, Louis T., and Alvin G. Wint. 2000. Marketing a Country: Promotion as a Tool for Attracting Foreign Investment. *FIAS Occasional Paper #13* (March). The World Bank, Washington, DC.
- [4] Websites of various investment promotions agencies.

Appendix. Table 2. Summary on IPAs performance in CEE and NIS region

Country	Name of the Agency	Investment Promotion Services provided by the Agency					Are Agency's services free of charge?	Status of the Agency	Date of Establishment
		Image-building	Pre-Investment Services	Post-Investment Support	Do Investment Incentives for Foreign Investors Available?	Policy Advocacy			
Poland	Polish Agency for Foreign Investment (PAIZ)	Yes	Yes	Yes	G, T	No	Yes	A	1992
Czech Republic	CzechInvest (CI)	Yes	Yes	Yes	G, T	Yes	Yes	SA	1993
Slovak Republic	Slovak Investment and Trade Development Agency (SARIO)	Yes	Yes	Yes	G	No	Yes	A	2001
Slovenia	Slovenian Trade and Investment Promotion Agency (TIPO)	Yes	Yes	Yes	G	Yes	Yes	NA?	?
Serbia	Serbian Investment and Export Promotion Agency (SIEPA)	Yes	Yes	Yes	G, T	No	Yes	NA?	?
Hungary	Hungarian Investment and Trade Development Agency (ITDH)	Yes	Yes	Yes	?	No	Yes	NA	1993
Bulgaria	Bulgarian Foreign Investment Agency (BFIA)	Yes	Yes	No	?	Yes	Yes	A	1995
Bosnia & Herzegovina	Foreign Investment Promotion Agency (FIPA)	Yes	Yes	Yes	?	Yes	Yes	SA	1998
Estonia	Estonian Investment Agency (EIA)	Yes	Yes	No	G	No	Yes	SA	1994
Latvia	Latvian Development Agency (LDA)	Yes	Yes	No	G, T	Yes	?	A	1993
Lithuania	Lithuanian Development Agency (LDA)	Yes	Yes	Yes	—	No	?	NA	?
Russia	National Agency for Foreign Investments (NAFI)*	No	Yes	Yes	—	Yes	?	NG	1998
Moldova	The National Agency for Attracting Investments (NAAI)	Yes	Yes	No	?	Yes	Yes	A	1997
Kazakhstan	KazInvest	Yes	Yes	Yes	?	No	?	NG	2000

Notes to the table:

* — NAFI is not the only investment promotion agency in Russian Federation, there is also other agencies, but the information about them is scarce.

Investment incentives: G — investment grants; T — tax incentives;

Status of the Agency: A — autonomous government agency; SA — semi-autonomous government agency (with private sector representatives in steering board); NA — non-autonomous (agency is either unit of ministry or the Cabinet of Ministries); NG — non-government agency (public sector representatives are included in the board).