Why sustainability cannot be ignored

SUSTAINABILITY GOALS

TOO FEW INVESTMENT PROMOTION AGENCIES AND ECONOMIC DEVELOPMENT ORGANISATIONS INCLUDE SUSTAINABILITY GOALS IN THEIR ACTIVITIES. **DR HENRY LOEWENDAHL, CHRISTIAN KOLLINSKY** AND **DR DOUGLAS VAN DEN BERGHE** OUTLINE A THREE-POINT PLAN TO ATTRACT SUSTAINABLE FDI

Illustration by John Holcroft

During the 1970s and 1980s, the enormous danger of environmental problems was increasingly recognised and the principle of sustainable development was developed. In the following decades, the principle has also been applied to social and economic areas as well as environmental. The UN 2016 Sustainable Development Goals state the wider principles of sustainable development:

- to eradicate extreme poverty and hunger;
- to ensure healthy lives and promote well-being for all ages;
- to achieve universal primary education;
- to promote gender equality; and
- to build resilient infrastructure, promote inclusive and sustainable industrialisation and foster innovation.

It is estimated that \$3500bn to \$5000bn of investment per year is needed to meet the goals' investment needs.

The investor perspective

The OECD guidelines for multinational enterprises and its due-diligence guidance provide advice for companies on standards of responsible business conduct. They are particularly important in countries where domestic policy frameworks remain weak.

Businesses seek to avoid environmental risks that could interrupt operations. They desire access to raw materials that can be sourced reliably over the long term. Many of these factors are influenced by location. The motivation is different, yet sustainable development can still be realised.

Climate change, pollution, dwindling natural resources and economic inequality are changing societies and economies in such a way that businesses will need to consider sustainability during the site-selection process. The workforce also has a growing awareness of sustainable practices. Sustainable investment also contributes to more direct business factors such as infrastructure spending, taxation, government and public relations, and potentially even political stability.

The government perspective

The OECD's policy framework for investment helps governments to put in place conducive and supportive guidelines for sustainable FDI. Organisations such as the Private Investment Corporation in the US or Germany's Investment and Development Corporation have set up sustainable standards for firms they support. Some trade agreements include principles such as strengthening local capacities, protection of labour rights and technology transfer, which contribute to sustainability.

Despite the positive policy frameworks in place, very few investment promotion agencies (IPAs) and economic development organisations (EDOs) have incorporated sustainable development into their investment promotion activities. The World Association of Investment Promotion Agencies conducted a survey of member IPAs around the world in co-operation with the Columbia Center on Sustainable Investment. The results showed that economic development is the highest priority for IPAs, followed by environmental sustainability. Social dimension and governance are the least prominent factors that IPAs consider in their investment strategies.

Recommendations for EDOs and IPAs

1. Sustainable investment should become a part of all investment promotion activities.

Sustainability goals should not be 'window dressing' or box-ticking exercises, but be tangible actions in all phases of investment promotion activities and eventually be embedded into FDI targets, aftercare and policy advocacy activities.

The sector strategy for inward investment should incorporate sustainable development through:

- identifying sectors where FDI can have a direct impact on sustainable development, such as renewable energy investment projects, eco-tourism and organic agriculture;
- identifying sectors where FDI can play an indirect role, especially through technology transfer and specialist services and products that address key sustainable development issues; and
- targeting types of projects within all target sectors that minimise threats caused by pollution, natural resource depletion, intensive agriculture and urban sprawl.

Investor targeting and lead-generation activities should focus on companies that can support sustainable development and growth. Target companies will comprise not only the major multinational enterprises but also smaller specialist companies. The process may also include targeting non-profit organisations and associations who have the expertise and commitment to support sustainable development.

IPAs and EDOs need to consider the type of FDI facilitation services they can offer small companies and non-profit organisations, which may have a high proportion of non-equity mode investments, such as technology transfer agreements.

In the most practical terms, to implement a sustainable FDI programme will require identifying companies that will contribute to sustainable development and targeting these companies to invest in the location.

2. Incentives policies should be aligned with achieving sustainable investment.
If sustainable development is to be an end goal for FDI, business attraction and economic development, the traditional investor attraction tools need to adapt to encourage sustainable investment.

Economic development incentives – tax credits, grants, training programmes, capital investment funds, low-cost loans, infrastructure grants and the like – have been used for decades with the aim of encouraging investment decisions to go to one location or another.

Incentives have rightly come under scrutiny for overuse and misuse. As with any tools, they are only effective for the purpose for which they have been designed. Nonetheless, credits and grants can play an important role in encouraging or enabling sustainable investments.

While most investment incentives have typically been designed to achieve capital investment and job creation objectives, some have been put in place successfully to encourage sustainable development practices. Instead of being used to draw investment away from competitive regions or to areas with economic hardship, these programmes have been instead designed to encourage spending on energy and water conservation measures, local cogeneration and renewable energy, and even to promote workforce use of public or alternative transportation.

The activities most commonly incentivised now focus on energy, recycling and other aspect of environmental sustainability. These are easily measured and include:

- installing pollution control equipment;
- investing in energy-efficient buildings or components;
- manufacturing products from recycled materials;
- investing in systems to capture items from a company's waste stream for recycling or use by others;
- undertaking environmental remediation activities;
- adapting manufacturing or other processes to use alternate energy sources such as solar, wind, geothermal and biomass; and
- producing alternative fuels for vehicles or using alternative fuels to power a company's own fleet.

3. Free zone development should be aligned with achieving sustainable investment.
Many governments have used free zones as an incentive instrument to attract investment to alleviate poverty and achieve substantial economic development. Free zones have successfully tapped into a large pool of multinationals looking to relocate parts of their global value chains to locations with competitive advantages such as preferential market access, generous incentive packages and low-cost labour.

However, several developments have eroded the sources of competitiveness of these traditional free zones since the beginning of this century, including the proliferation of trade agreements and international agreements on incentives reducing the relative benefits of zones; fierce competition putting pressure on labour costs and working standards in some free zones; and stagnant growth in FDI which has led to an oversupply of zone space.

Free zones must move away from tax and cost advantages and lowering standards to remain competitive. They should rather look to maximise 'dynamic' benefits such as economic diversification, skills development, entrepreneurialism, poverty alleviation and policy reform by shifting to alternative and sustainable sources of competitiveness.

Such a shift should be aligned with so-called 'new generation' investment policies. These put a high priority on inclusive growth and sustainable development while strengthening or maintaining the competitiveness of the investment climate. Standards and practices related to sustainable development promoted in such free zones typically include:

- ensuring standards for working hours and benefits;
- giving unions the right to operate in the zone;
- promoting equality;
- reducing emissions by using renewable energy sources, or improved energy efficiency;
- reducing waste;
- protecting the environment with waste disposal;
- ensuring the protection of employee health;
- introducing and monitoring work safety rules;
- introducing and enforcing anti-corruption standards; and
- improving (backward) linkages.

Consequently, free zones may develop as centres of sustainable development in line with international socio-environmental standards and contribute to realising environmental and social policy objectives. ■

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