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Evaluate Sustainable FDI to Promote Sustainable Development

by
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Prescriptions to increase the role of foreign direct investment (FDI) in promoting sustainable development generally focus on the macro level -- getting policies right and otherwise improving the investment climate. These steps are necessary but not sufficient. Effective implementation processes, especially at the micro project level, are also essential to encourage FDI that matches host country development needs and priorities.

The recent UNCTAD Investment Policy Framework for Sustainable Development[1] offers a set of core principles to guide national and international officials making investment policy. The principles recognize the need to establish development priorities to evaluate FDI projects and a companion FDI contribution index[2] provides a starting point that includes some useful indicators. However, the Framework falls short of providing an integrated and applied mechanism for assessing whether FDI meets sustainability criteria.

Thus, the missing component is a process implementation tool that can help evaluate the multiple, interactive effects of a FDI proposal across economic, environmental, social, and governance objectives.[3] One approach is to use a project assessment matrix to evaluate FDI

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[1] UNCTAD, *World Investment Report 2012: Towards a New Generation of Investment Policies* (Geneva: UNCTAD, 2012).

[2] Ibid., pp. 119-121.

[3] This need was identified by the Millennium Cities Initiative (MCI), a project of Columbia University's Earth Institute, in the course of a Finnish-funded effort to promote sustainable FDI in Africa. MCI devised a ratings format and assessment matrix encompassing a set of 22 important development objectives that can be adjusted to best reflect each country's goals. The matrix was field tested with government authorities and private foreign investors in South Africa and Kenya. Interviews included retrospective evaluations of FDI projects ranging from steel and chemical plants to mattress and molasses production to cut flowers and fish farms.

proposals.[4] A broadly inclusive process would select a top five and second five set of priority goals to receive extra weight. The matrix would assess the impact of FDI projects on value indicators representing a country's development priorities, using a plus-five to minus-five range. After multiplying each indicator by its priority weight, the final score provides a cumulative assessment of its desirability as sustainable FDI.

The assessment would quantify qualitative judgments about non-economic indicators so they can be compared and interactive effects evaluated. Easily quantified economic measures currently dominate FDI evaluations, creating a more-is-better mind-set. Regulations force some environmental assessments of FDI projects, but social and governance effects that lack a similar legal mandate are generally overlooked or undervalued. Ironically, economic measures are really just instrumental values whose ultimate worth is reflected in social indicators that represent how a society's way of life can be enriched. The matrix would curb the disproportionate influence now exerted by economic data in favor of a more holistic evaluation of project impacts.

Adopting an easily understood ratings and assessment system encourages transparency and inclusiveness in the evaluation process. A matrix that incorporates economic, environmental, social, and governance indicators highlights FDI projects deserving promotion, pinpoints areas for improvement and discourages potential corruption by revealing the basis for a project's net benefit assessment.

The scarce resources countries devote to FDI promotion and facilitation should be targeted toward projects that advance priority development objectives. Unless improved evaluation tools assess the full range of project impacts, resource allocation will yield sub-optimal and possibly counter-productive results. FDI promotion dominated by macro-economic measures risks missing social and other impacts that more directly affect people's lives.

Is some FDI always better than no FDI? Perhaps, not. Even least developed countries struggling to attract FDI should assure potential projects produce more than an ephemeral spurt in economic indicators. FDI projects that mobilize capital and create jobs offer measurable economic benefits, but a project assessment matrix would evaluate the investment's environmental, social and governance impacts as well. Projects may pollute or deplete the public water supply, displace populations or strengthen entrenched elites. Such FDI can, on balance, leave the host society less well off, compared to the status quo without the FDI, in terms of inclusive growth and sustainable development.

Each nation sets its own priority development objectives and determines what role FDI should play in their achievement. Host countries should communicate their development priorities to prospective investors, requesting an evaluation of how FDI projects would affect relevant objectives. Investors could evaluate and adjust plans to promote societal benefits, recognizing that sustainable FDI requires a win-win outcome for both the country and the company.

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[4] For the matrix, see John Kline, "Evaluating sustainable foreign direct investment," Working Paper No. 12, Millennium Cities Initiative (New York: Columbia University, 2012), available at: http://mci-admin.ei.columbia.edu/sitefiles/file/Sustainable-FDI-Guidance-Paper-Kline-FINAL.pdf.

Sustainable FDI can contribute to sustainable development, but the outcome is neither automatic nor assured. Within a macro policy framework that encourages FDI, micro process assessments of potential projects are warranted before national resources are committed to their promotion. Both astute policy-making and effective implementation processes are required.

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