

WORLD INVESTMENT REPORT 2013

Global Value Chains: Investment and Trade for Development

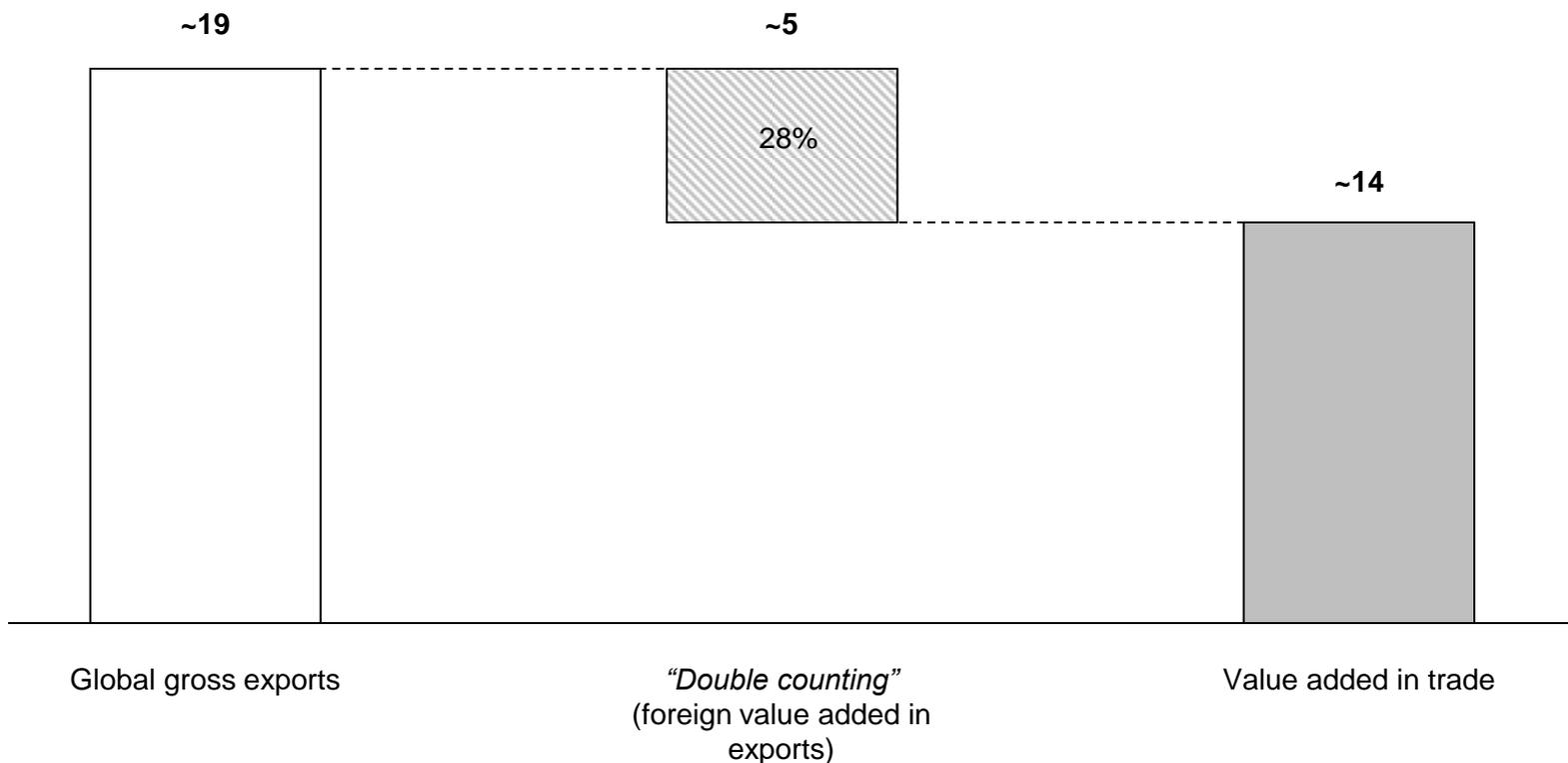
UNCTAD
Division on Investment and Enterprise

Presented:
New York, 6 November 2013
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Trade is increasingly driven by global value chains (GVCs), leading to a significant amount of double counting

Value added in global trade, 2010
(Trillions of dollars)

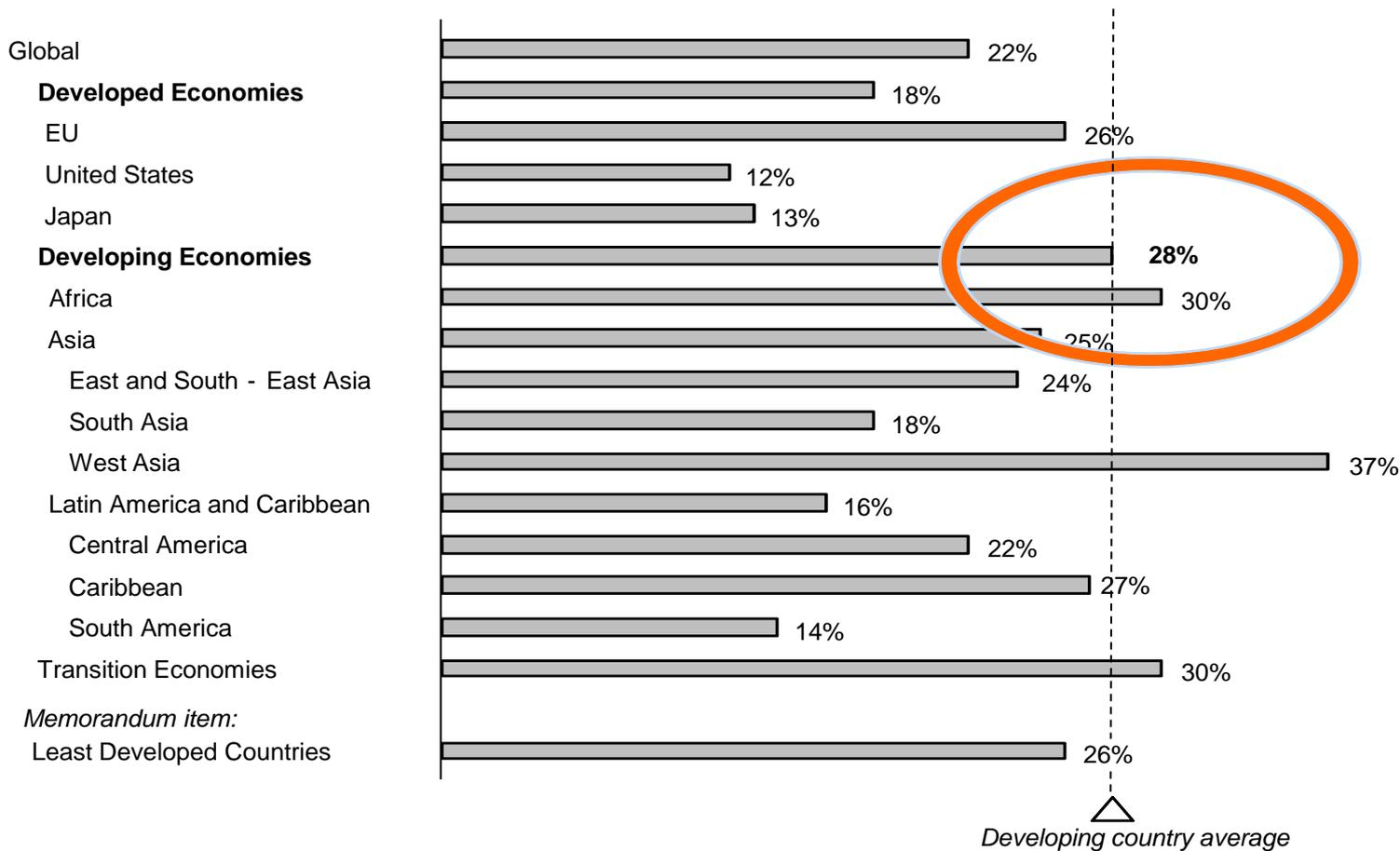
ESTIMATES



The contribution of GVCs to the economy can be significant

Domestic value added in trade as a share of GDP, by region, 2010

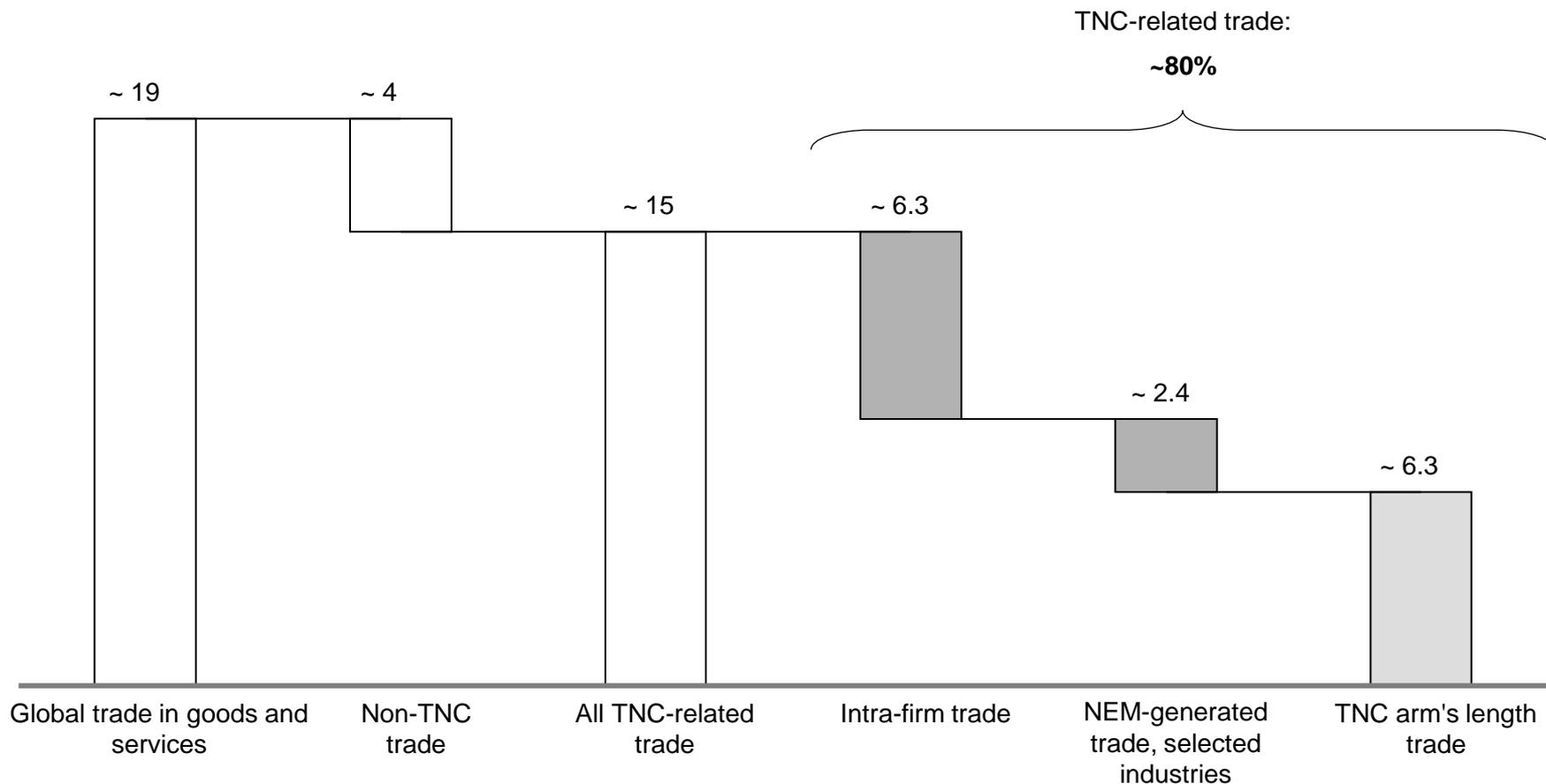
(Per cent)



GVCs are typically coordinated by TNCs

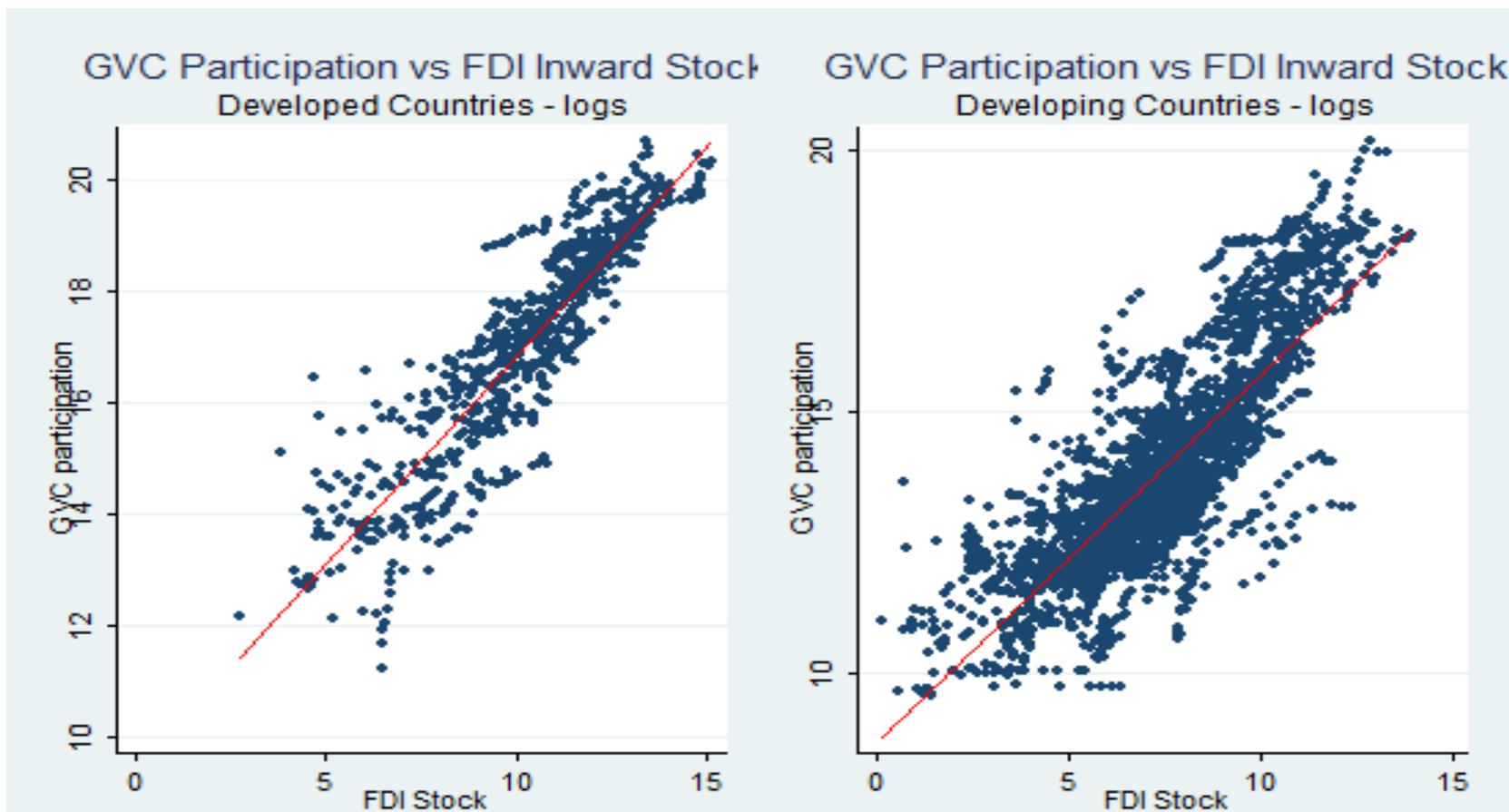
Global gross trade (export of goods and services), by type of TNC involvement, 2010
(Trillions of dollars)

ESTIMATES



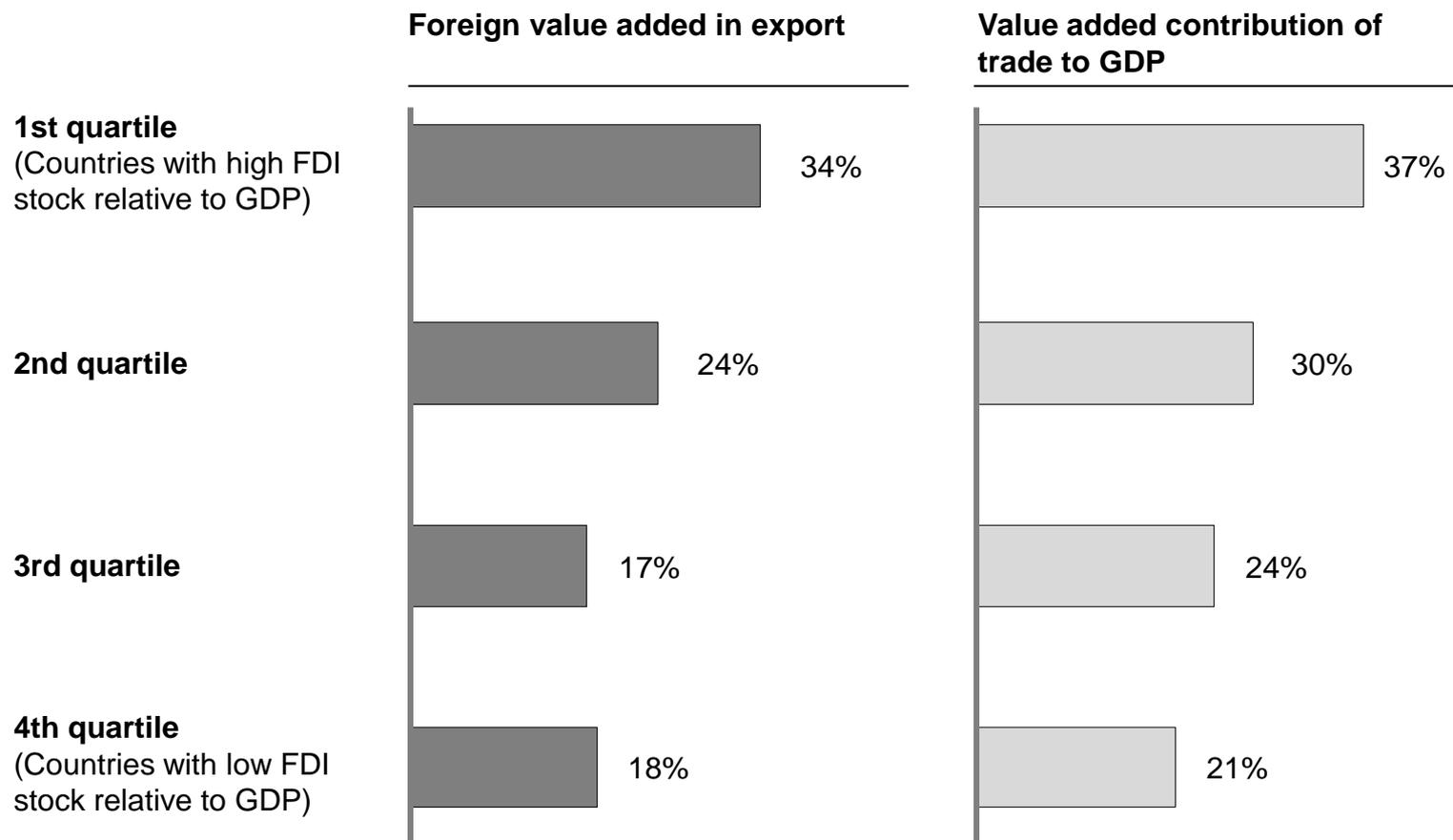
The presence of TNCs drives GVC participation

Correlation between inward FDI stock and GVC participation, 187 countries, 1990 – 2010



FDI shapes patterns of value added in trade

Key value added trade indicators (median values), by quartile of FDI stock relative to GDP, 2010



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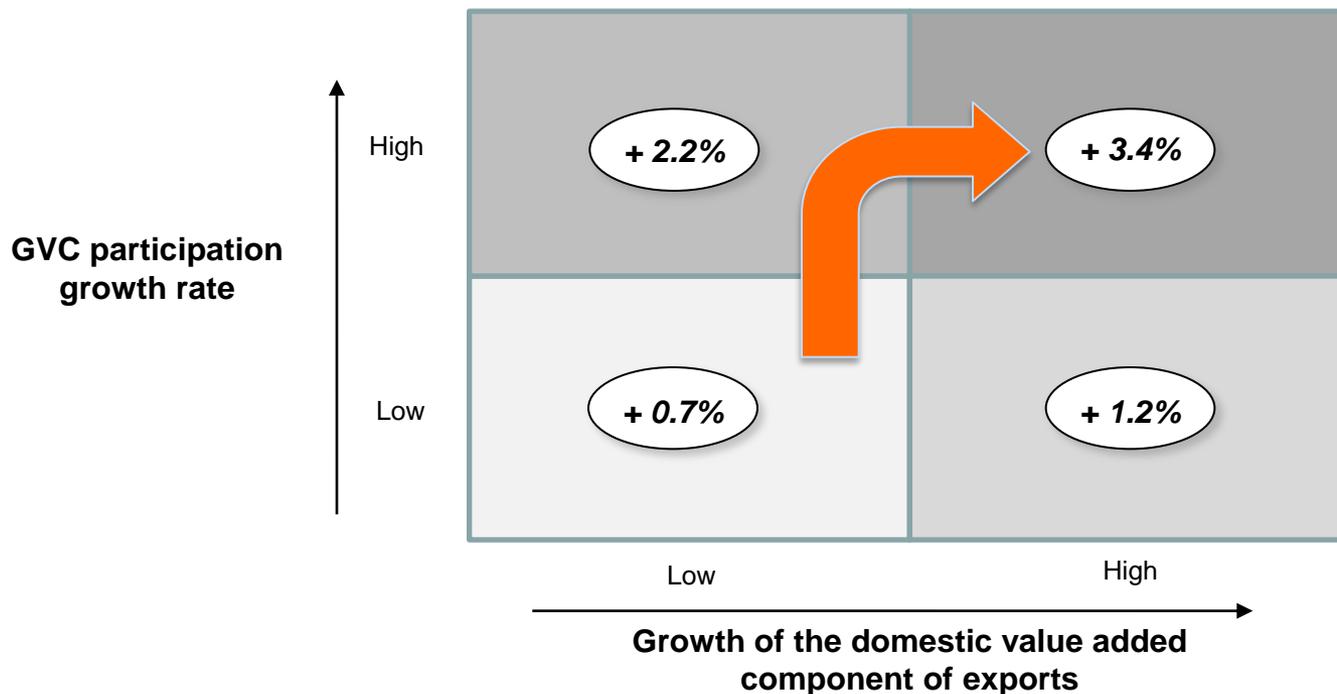
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Longer term, the ideal development path involves not just participation but also domestic value added creation

GDP per capita growth rates for countries with high/low growth in GVC participation, and high/low growth in domestic value added share, 1990-2010

+ n.n% = median GDP per capita growth rates



A number of factors and conditions may facilitate ‘climbing’ the GVC development ladder

(ii) Share of exports by level of technological sophistication



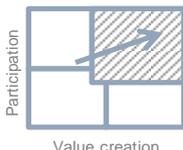
(i) Participation/ value creation archetypal moves

GVC development stages

Upgrading

(Focus on functional and chain upgrading)

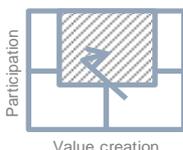
- Move to (or expand to) higher value segments in GVCs
- Move to (or expand to) more technologically sophisticated and higher value GVCs



Upgrading

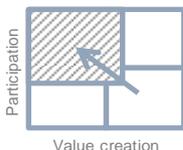
(Focus on product and process upgrading)

- Increase productivity and value added produced within existing GVC segments



Integrating

- Enter (increase relative importance of) more fragmented GVCs
- Increase exports of intermediate goods and services



Facilitating factors and conditions

- Effective national innovation system, R&D policies, and intellectual property rules
- Presence of TNCs capable of GVC coordination and a domestic and international supplier base
- Pool of highly trained workers

- Presence of domestic supplier base fully integrated in multiple GVCs (reduced reliance on individual GVCs)
- Absorptive capacities at higher technology levels, capacity to engage in R&D activities
- Pool of relatively low-cost skilled workers

- Availability and absorptive capacities of domestic supplier firms and partners
- Reliable basic infrastructure services (utilities and telecommunications)
- Pool of relatively low-cost semi-skilled workers

- Conducive investment and trading environment
- Basic infrastructure provision
- Pool of relatively low-cost workers

The contribution of GVCs to development can be significant, however participation in GVCs also involves risks



- Value added trade contributes nearly 30 per cent to developing countries' GDP on average
- There is a positive correlation between participation in GVCs and growth rates of GDP per capita
- GVCs have a direct economic impact on value added, jobs and income
- Participation in GVCs can help countries' acquisition and dissemination of technologies and skills, and spread international best practices, including on social and environmental issues, e.g. through the use of CSR standards
- GVCs can also be an important avenue for developing countries to build productive capacity, opening up opportunities for longer-term industrial upgrading



- GDP contribution of GVCs can be limited if countries capture only a small share of the value added created in the chain
- Also, a large part of GVC value added in developing economies is generated by foreign affiliates of TNCs, which can lead to relatively low "value capture", e.g. as a result of transfer pricing or income repatriation
- Technology dissemination, skill building and upgrading are not automatic. Developing countries face the risk of remaining locked into relatively low value added activities
- Environmental impacts and social effects, including on working conditions, occupational safety and health, and job security, can be negative
- The potential "footlooseness" of GVC activities and increased vulnerability to external shocks pose further risks

Countries need to make a strategic choice whether or not to promote GVCs

- Countries need to carefully weigh the pros and cons of GVC participation, and the costs and benefits of proactive policies to promote GVCs or GVC-led development strategies, in line with their specific situation and factor endowments
- Some countries may decide not to promote GVC participation. Others may not have a choice: for the majority of smaller developing economies with limited resource endowments there is often little alternative to development strategies that incorporate a degree of participation in GVCs . The question for those countries is not so much *whether* to participate in GVCs, but *how*. In reality, most countries are already involved in GVCs one way or another
- Promoting GVC participation requires targeting specific GVC segments, i.e. GVC promotion can be selective. Moreover, GVC participation is only one aspect of a country's overall development strategy

Policies matter to make GVCs work for development

A policy framework for GVCs and development

Embedding GVCs in development strategy

- Incorporating GVCs in industrial development policies
- Setting policy objectives along GVC development paths

Enabling participation in GVCs

- Creating and maintaining a conducive environment for trade and investment
- Putting in place infrastructural prerequisites for GVC participation

Building domestic productive capacity

- Supporting enterprise development and enhancing the bargaining power of local firms
- Strengthening skills of the workforce

Providing a strong environmental, social and governance framework

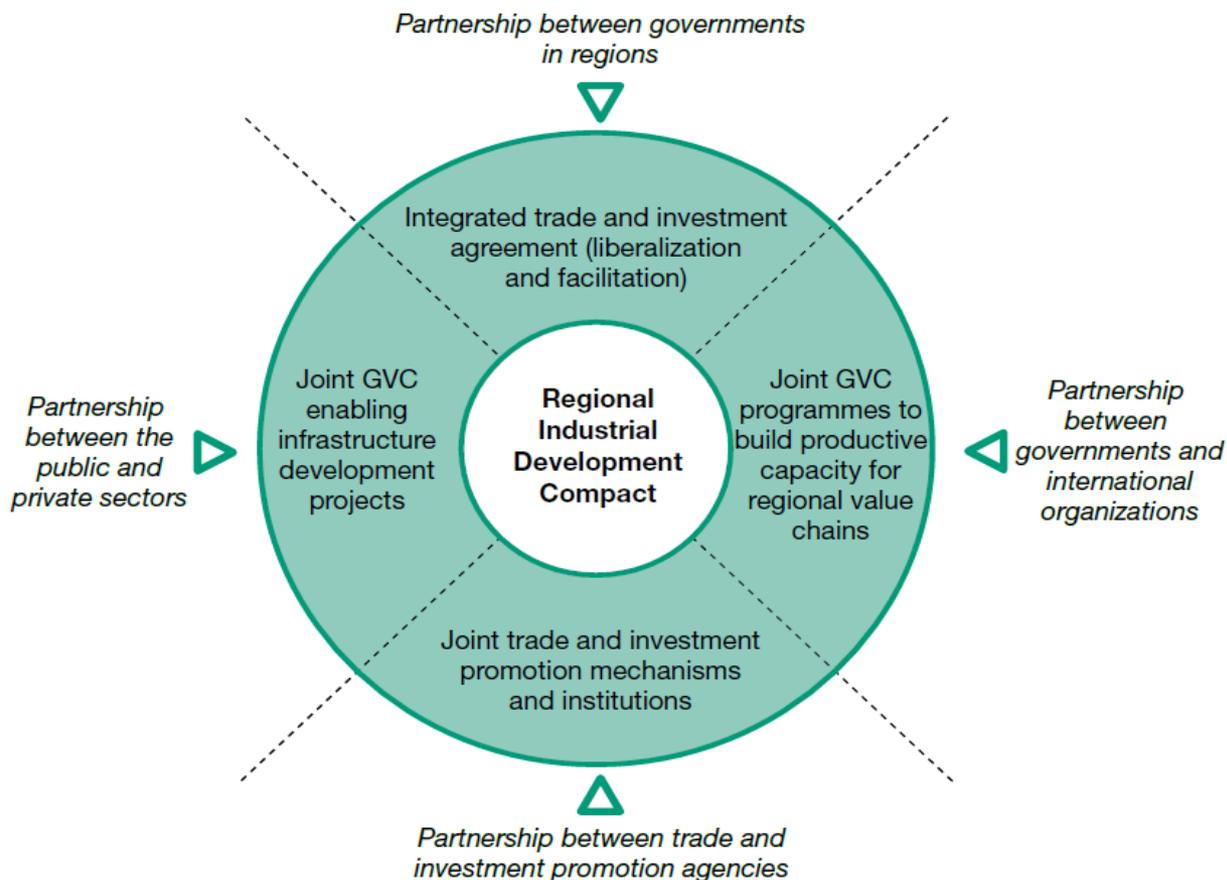
- Minimizing negative effects and risks associated with GVC participation through regulation, public and private standards
- Supporting local firms in complying with international standards

Synergizing trade and investment policies and institutions

- Ensuring coherence between trade and investment policies
- Synergizing trade and investment promotion and facilitation
- Creating 'Regional Industrial Development Compacts'

Regional trade and investment agreements could evolve into *regional industrial development compacts*

Regional industrial development compacts for regional value chains



The internationalization of state owned enterprises (SOEs) and sovereign wealth funds (SWFs) maintains pace

Number of state owned TNCs increased from 650 in 2010 to 845 in 2012

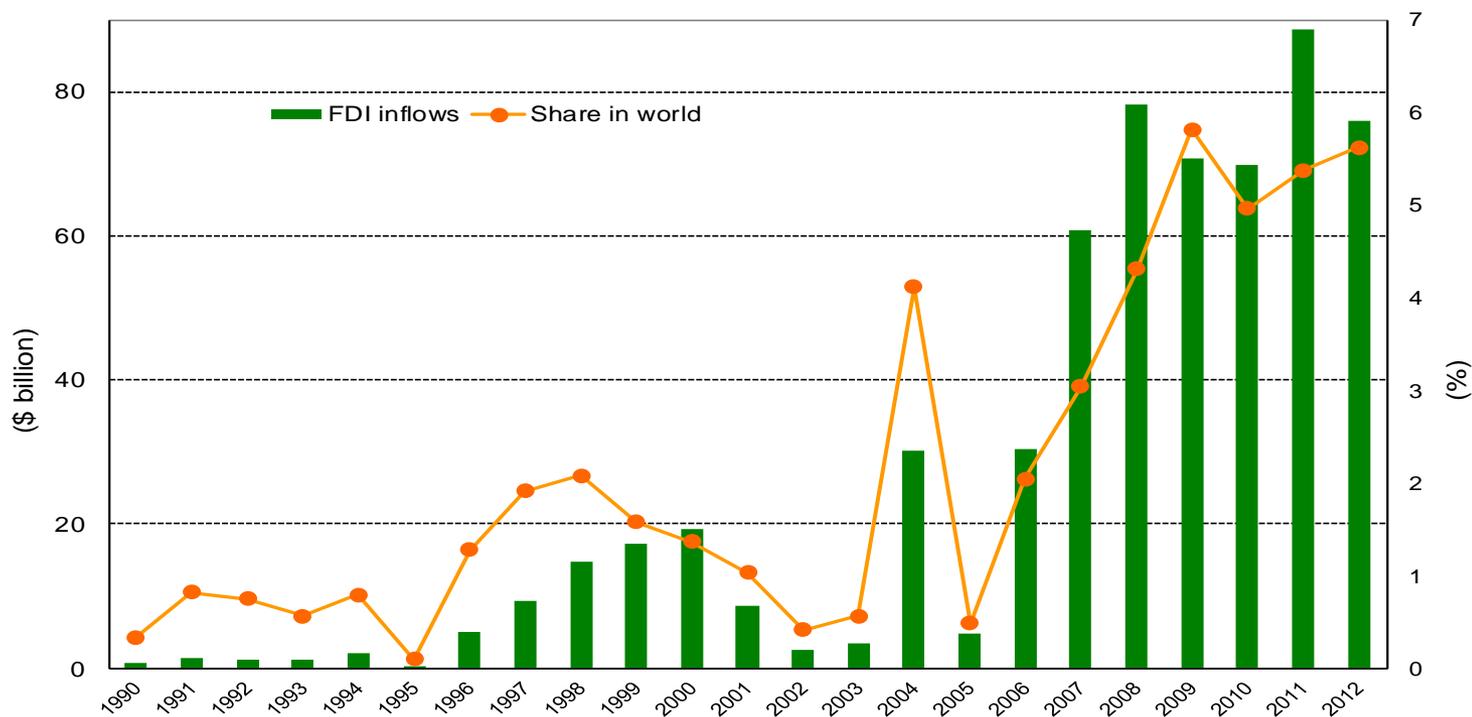
FDI by SOEs amounted to \$145 billion in 2012, almost 11 per cent of global FDI, despite a contraction of 23% vs. 2011

FDI by SWFs doubled in 2012, reaching \$20 billion

The number of net M&A deals by private equity remained at historically high levels, although value fell by 34%

Investments in offshore financial centres (OFCs) remain at historically high levels

Value and share of OFCs in global FDI flows, 1990 – 2012
(Billions of dollars and per cent)



However special purpose entities (SPEs) play an even larger role

Estimated investment flows to SPEs and OFCs, 2011

(Billions of dollars)

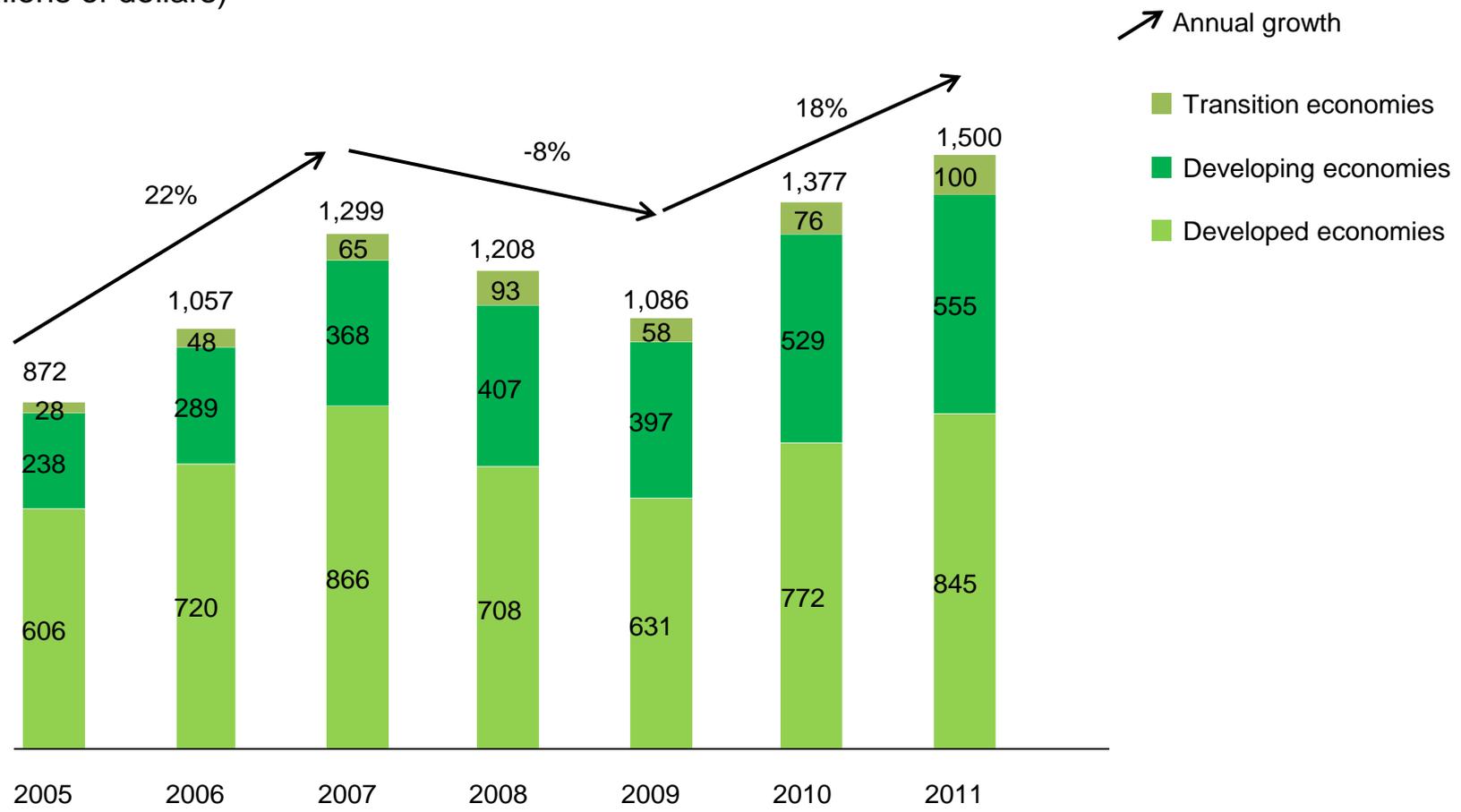


* Includes only flows to SPEs based in Hungary, Luxembourg and the Netherlands. UNCTAD does not include flows to SPEs in these countries in FDI statistics

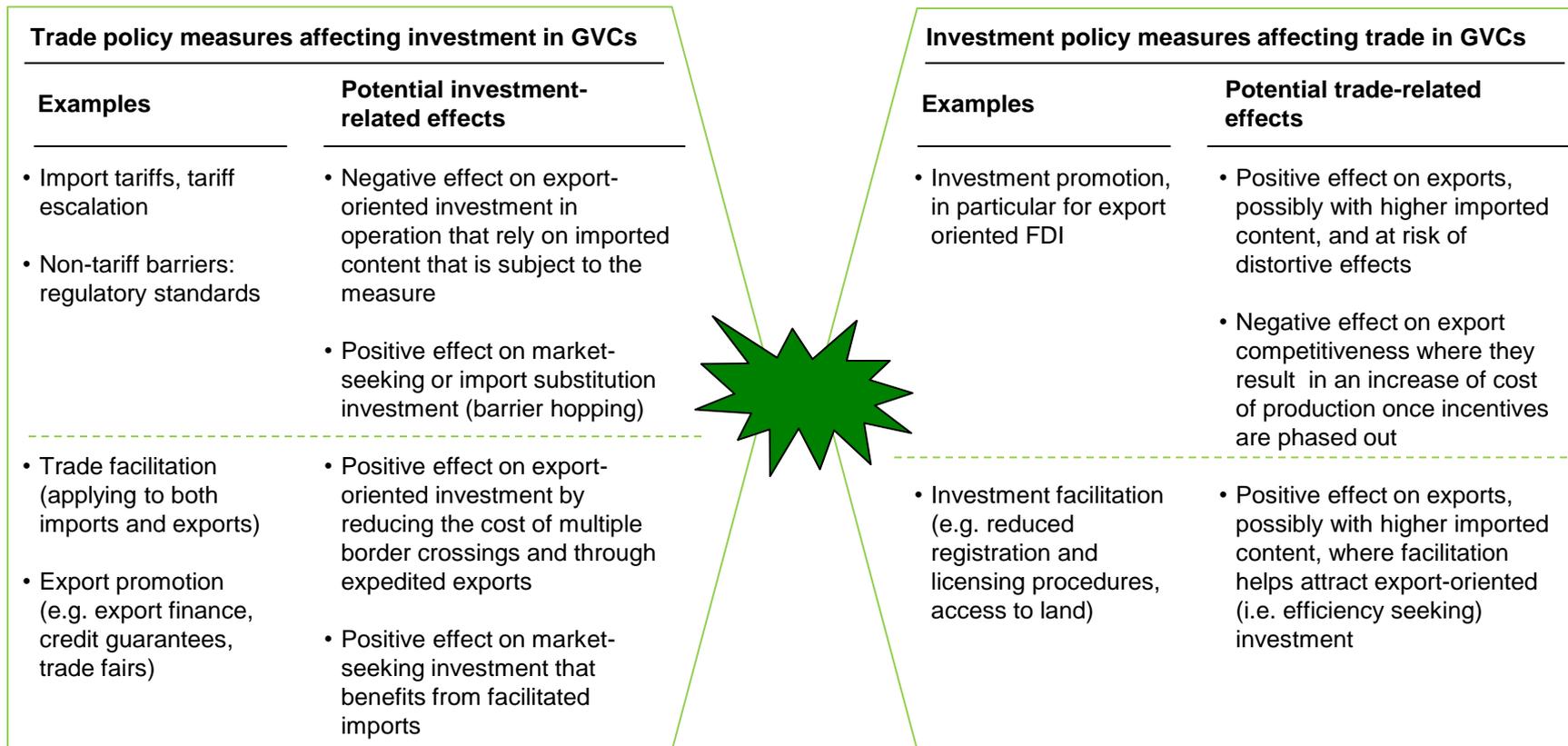
Global FDI income reached \$1.5 trillion in 2011

Trend of FDI income by economic group, 2005 – 2011

(Billions of dollars)



Policymakers need to make sure that investment and trade policy measures work in the same direction



Extensive list of examples in WIR

Export processing zones could evolve into centres of excellence for sustainable business

‘Sustainable export processing zones’

Rationale

- Respond to the **obligation** (inherent to the governmental or quasi-governmental nature of EPZs) **to protect human rights and promote environmental best practices**
- Enhance EPZs’ **ability to attract and retain investment** by providing social and environmental standards demanded by TNCs, also in view of the potential regulatory challenges deriving by WTO’s Agreement on Subsidies and Countervailing measures

Key elements

- Build a comprehensive **regulatory framework** and provide **infrastructure and services** to promote sustainable business practices **across multiple areas of sustainability**:
 - Responsible labour practices
 - Environmental sustainability policies
 - Employee occupational safety and health
 - Good governance: combatting corruption

Advantages for firms

- **Share the cost** of sustainability-related services, leading to economies of scale
- **Standardize and harmonize** CSR practices, leading also to a reduction in the number of on-site inspections
- Benefit from **reputational gains** deriving from positive “branding” of zones