29 June 2020

Twenty-third Report on G20 Investment Measures[1]

When the Global Financial Crisis broke in 2008 and early 2009, governments around the globe rallied to prevent a repeat of the mistakes of the Great Depression of the 1930s: Avoid protectionism and beggar-thy-neighbour policies as this would lead to a further deepening of the crisis.[2] Their call was followed by a specific and firm commitment to refrain from introducing new barriers to investment or trade and complemented by a mandate for the WTO, OECD and UNCTAD to report publicly on new trade and investment policy measures. So far, 22 reports have been issued under this mandate.[3]

In early 2020, the COVID-19 pandemic broke out. It has led, in addition to dramatic health implications for people around the globe, to an almost immediate and profound economic upheaval in many economies. Governments have been scrambling for responses to limit negative impacts on their societies and economies. G20 Leaders have repeatedly jointly expressed their determination to minimize the negative effects of the pandemic and to remain open to trade and investment.[4]

This 23rd report, jointly prepared by the OECD and UNCTAD Secretariats, covers investment and investment-related measures that G20 Members have taken between 16 October 2019 and 15 May 2020. It documents policy actions that G20 Members have taken in the last months preceding the pandemic and in response to the unprecedented economic crisis that followed, just a decade after the Global Financial Crisis.

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1 This report is issued under the responsibility of the Secretary-General of the OECD and the Secretary-General of UNCTAD. It has no legal effect on the rights and obligations of member states of the WTO, OECD, or UNCTAD. Nothing in this report implies any judgment, either direct or indirect, as to the consistency of any measure referred to in the report with the provisions of any WTO, OECD, or UNCTAD agreement or any provisions thereof. As its previous report, this document distinguishes between measures related to foreign direct investment (prepared jointly by OECD and UNCTAD) and measures related to other international capital flows (prepared solely by OECD).

2 G20 Leaders “Declaration of the Summit on Financial Markets and the World Economy”, Washington, 15 November 2008.

3 Earlier reports by WTO, OECD and UNCTAD to G20 Leaders are available on the websites of the OECD and UNCTAD. A summary table of all investment measures taken since 2008 is also available on those websites.

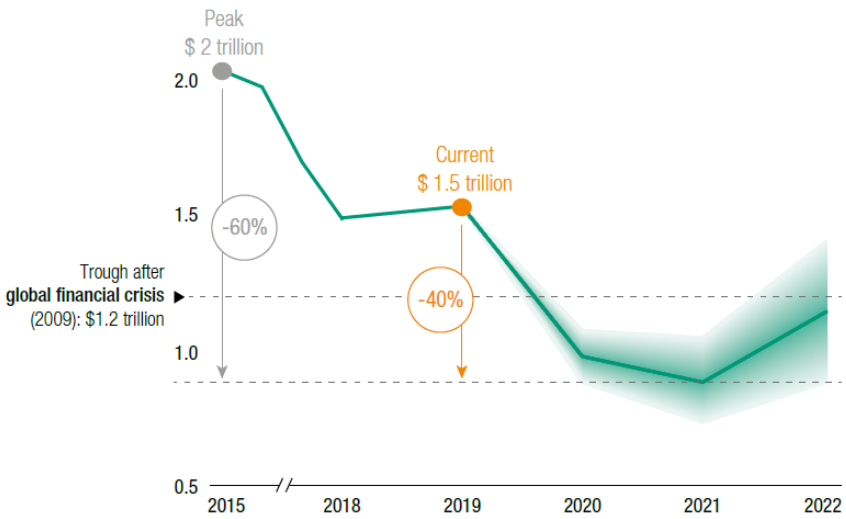
4 Extraordinary G20 Leaders’ Summit “Statement on COVID-19”, 26 March 2020. G20 Trade and Investment Ministers and guest countries statement “G20 Actions to Support World Trade and Investment in Response to COVID-19” , 14 May 2020.

Many countries were still preparing and refining their investment policy responses, when this report was finalised for release; this report takes a snapshot of their actions as of mid-May 2020.

I. Development of Foreign Direct Investment (FDI) flows

Foreign Direct Investment (FDI) has been on a downward trajectory since 2016 and is expected to decline sharply as a consequence of the pandemic and the resulting supply disruptions, demand contractions, and pessimistic outlook of economic actors. Even under the most optimistic scenario – in which the economy begins to recover in the 2nd half of 2020 – FDI flows in 2020 are expected to fall by more than 30% compared to 2019[5] and could plunge by 40% (Figure 1).

Figure 1: Global FDI inflows, 2015 to 2019 and 2020-2022 forecast (USD trillions)



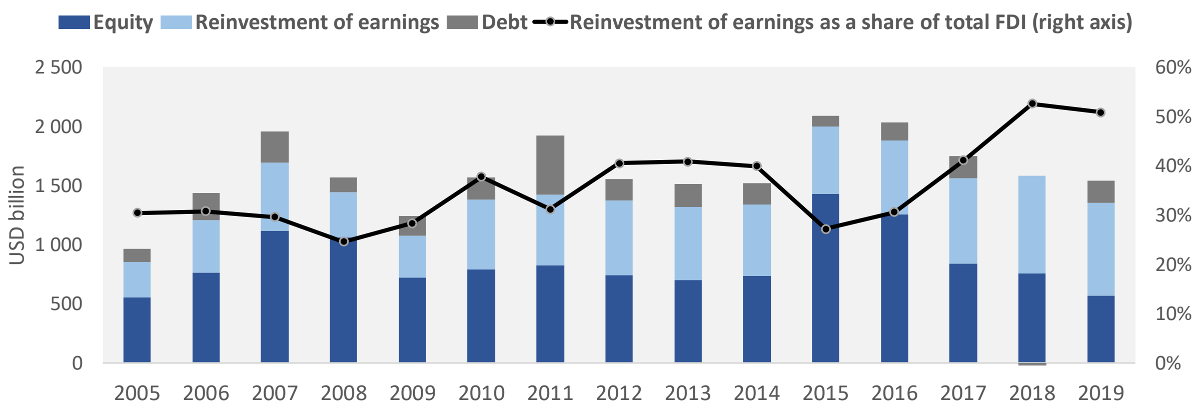
Source: UNCTAD, World Investment Report 2020.

This decrease is accentuating and accelerating the steady decline of FDI flows observed in the past five years (Figure 2). Reinvested earnings – which play an increasingly important role in FDI flows – will drop substantially in the short term, as the crisis will depress earnings and investors are expected to reinvest a smaller share of their earnings than they have done in the recent past. Equity capital flows will also decline as many new investments, both merges and acquisitions (M&As) and greenfield investments, have been put on hold.

Intracompany loans and injections of equity capital from parent companies to their struggling foreign affiliates may offset some decline in reinvested earnings. Such behaviour has been observed during the 2008 Global Financial Crisis and in times of severe currency depreciations; this constitutes an advantage of foreign ownership: financial linkages between investors and their foreign affiliates contribute to the affiliates' resilience to economic crises.

[5] "Foreign direct investment flows in the time of COVID-19", OECD, April 2020.

Figure 2: Global FDI inflows by instrument, 2005 to 2019.



Note: 2019 data are preliminary. Debt in FDI consists of loans between related parties.
Source: OECD FDI Statistics Database.

The pandemic and crisis-response measures are having much greater impacts on some sectors than others, and FDI flows will reflect this. The information and communication sector may see an increase in earnings, while the manufacturing and primary sectors will likely see large drops in earnings, for instance. As some of the worst-hit sectors, including accommodation, food service, and transportation and storage, typically account for relatively small shares of FDI, their suffering will not show proportionately in FDI statistics overall. There will be large cross-country variation. For example, available data show that the primary sector is much more important in inward FDI in some G20 economies, including Australia, Brazil, Canada, Indonesia, the Russian Federation, and South Africa, than in others.

If the public health and economic policy measures do not yield sufficient results, FDI flows may still decline further in the medium term. Divestments could be an additional factor, besides lower earnings and fewer new investments, if financially struggling firms are forced to sell or liquidate some of their foreign operations.[6]

II. G20 Members' investment policy measures

1. Foreign direct investment-specific measures

G20 Members have taken an unusually high number of investment policy measures in the reporting period, mirroring the exceptional economic circumstances that have emerged since early 2020 when the COVID-19 pandemic began to sweep the planet. Australia, Brazil, P.R. China and India took measures before signs of the pandemic emerged, but countries continued to change policies throughout the reporting period. Some of these measures lead to further liberalisation or otherwise more favourable conditions for foreign direct investment:

- *Australia* increased screening thresholds for investors from certain origins under its inward investment screening mechanism through Preferential Trade Agreements and established new rules for financial services licensing of foreigners in Australia;
- *Brazil* rescinded authorisation requirements for foreign investment in financial institutions based in Brazil and henceforth applies the principle of national treatment of foreign investors to this sector;

[6] Projections of FDI flows under different scenarios of the effectiveness of the public health and economic policy measures are set out in the April 2020 issue of *FDI in Figures* and the note on *FDI Flows in the Time of COVID-19*. In the long term, disruptions due to COVID-19 could lead some MNEs to rethink their supply chains, with broader impact on FDI flows. See chapter IV (International Production: A Decade of Transformation Ahead) of the World Investment Report 2020: International Production Beyond the Pandemic for a detailed analysis.

- *P.R. China* relaxed rules on the operation of foreign financial institutions and eased several restrictions on the operation of foreign enterprises in China; and
- *India* relaxed rules for foreign direct investment in the insurance and aviation sectors and clarified rules on local sourcing requirements.

Some other measures have also been observed, including the raising of additional duties for foreign acquirers of residential real estate in some States of *Australia*.

With the breakout of the COVID pandemic, *Australia* and *India* have temporarily adjusted their FDI policies to enable tighter control over inward investment. Australia temporarily lowered the trigger threshold for its foreign investment review mechanism, and India temporarily added additional countries to the list of origins of acquirers who are subject to stricter review rules. Canada has not changed its policies but announced that it will apply heightened scrutiny to the operation of its review mechanism in a Policy Statement – a posture that the EU has also recommended in a Communication addressed to its Member States.

A detailed description of these policy changes is available in Annex 1 of this report.

2. Investment measures related to national security

G20 Members continued to address potential risks that foreign investment could pose to their national security interests and amended their policies to manage these risks. In the reporting period, six countries took policy measures – *France, Germany, Italy, Japan, the Republic of Korea* and the *United States*.

Some of the measures that G20 Members have taken in this regard were unrelated to the COVID pandemic and the economic disruption it created; rather, they had been planned earlier and independently from the pandemic and became effective in the reporting period:

- *France* lowered the participation-thresholds that trigger its foreign investment review mechanism and broadened the mechanism's scope to include additional industries;
- *Italy* made several changes to its investment review mechanism that expand its application, broaden the criteria that apply to the assessment of individual investments under its arrangements and strengthen compliance;
- *Japan* amended the rules governing foreign acquisitions by lowering the capital -threshold that triggers its investment review procedures and modified further procedural rules associated with this step;
- The *Republic of Korea* further enhanced rules that govern foreign investment in areas associated with national core technology; and
- The *United States* issued rules related to the powers of the Committee on Foreign Investment in the United States (CFIUS), following reform legislation passed in 2018, and also introduced new measures to manage national security risks associated with foreign ownership or control in the telecommunications and power sectors.

Supply shortages in the health-sector and the economic disruption that resulted from government action to contain the COVID pandemic led to the introduction of additional measures in some G20 Members, including *Australia, France, Germany, India* and *Italy*. These policy measures were explicitly motivated by factors related to the COVID-pandemic. These policy changes serve one of two distinct purposes:

- Some reforms add health-related industries and associated supply chains that are crucial for the *pandemic response* to the scope of screening mechanisms or strengthen control specifically in this area; and.
- Other measures introduce or enhance FDI screening mechanisms across the board to prevent acquisitions in *any sector* where companies suffer from temporary financial stress and value distortions under the exceptional economic conditions associated with the pandemic.

Measures that focus on companies and activities that are critical for the pandemic response reflect government concerns that production capacity and availability in this area affect essential security interests of societies. *France* and *Italy* added biotechnologies, and *Italy* also critical health infrastructure, to lists to which investment screening applies, and *Germany* and *Japan* henceforth apply tighter procedural rules to these sectors (*Germany*) or companies operating in these sectors (*Japan*).

Australia, France, India and *Italy* introduced temporary adjustments that allow a tighter control over inward investment beyond sectors that are related directly to their pandemic response. *Australia, France* and *Italy* temporarily lowered the trigger conditions for their review mechanisms across the board, and *India* temporarily added additional countries to the list of origins of acquirers who are subject to stricter review rules.

Some G20 members have responded to the exceptional circumstances and challenges that the pandemic has brought for foreign investment screening without resorting to explicit regulatory adjustments. *Canada* has clarified, in a Policy Statement, the heightened scrutiny that it will apply to the operation of its review mechanism, and the EU has likewise called, in a Communication, on EU Member states to pay more attention to transactions that may result in the exposure of Member states' or European Union interests.

These policy measures of G20 Members are part of a broader trend that stretches well beyond G20 Membership.[7] Governments around the world are becoming more concerned about risks to their national security interests, and ever more countries are introducing or strengthening mechanisms that allow for an upfront review of certain investment proposals to manage these risks. These efforts have accelerated significantly since 2016, and the pandemic and its fallout has merely accelerated, rather than triggered this trend.

The protection of national security interests is a legitimate role and indeed obligation of governments. International investment law recognises this legitimacy and allows for policy space for this purpose. The limited transparency over the application of these rules, often an imperative given the sensitivity of information for governments and involved businesses alike, makes investment review mechanisms potentially prone to misuse for purposes other than the protection of national security interests.

To avoid that these tools are used as an avenue to introduce restrictions that are not mandated by national security interests, agreement on good policy and common principles, transparency and peer-pressure are paramount.

G20 Members have made good progress in this regard:

- **Common principles** for this policy area have been agreed as part of the G20 Guiding Principles for Global Investment Policymaking (2016)[8] and, earlier and in somewhat greater detail, in the OECD Guidelines for Recipient Country Investment Policies relating to National Security (2009). UNCTAD's Investment Policy Framework for Sustainable Development (IPFSD) also provides guidance.[9]
- **Greater transparency** is achieved, collectively, through public reporting on policy changes in this policy area under the present exercise and through notification requirements that many G20 Members have taken on in other contexts.[10] In addition, many individual G20 Members have significantly increased efforts to generate greater transparency and access to public information on their implementation practice, either at the occasion of individual decisions or in different levels of aggregate.

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[7] See for a broader analysis "*Acquisition- and ownership-related policies to safeguard essential security interests – current and emerging trends, observed designs, and policy practice in 62 economies*", OECD, March 2020 and UNCTAD, "National Security-Related Screening Mechanisms for Foreign Investment: An Analysis of Recent Policy Developments", IPM Special Issue, November 2019 and UNCTAD, World Investment Report 2019: Special Economic Zones, June 2019, and the UNCTAD report on "National-Security-Related Screening of Foreign Investment, IPM Special Issue, November 2019.

[8] Endorsed in September 2016 at the G20 Leaders Summit in Hangzhou, China.

[9] See paragraph 2.1.2 of the National Investment Policy Guidelines, in: UNCTAD, Investment Policy Framework for Sustainable Development, 2015.

[10] Countries that have adhered to the OECD Declaration on International Investment and Multinational Enterprises are required to notify any new policies area to the OECD under the Third Revised Decision of the Council concerning National Treatment. Policy changes taken by the thirteen G20 Members that have adhered to these instruments are available publicly through the OECD.

- Greater transparency, policy dialogue on policy practice, extensive analysis by international organisations[11] and other actors, and involvement of stakeholders have increased **peer-pressure** on governments that helps discipline their policy-making. Governments have actively given more room for the involvement of stakeholders, and some G20 Members that do not routinely seek public input on policy proposals or make such feedback on proposals publicly available have recently enhanced their efforts and transparency in this policy area.

Despite these elements of progress, vigilance remains critical to avoid an excessive expansion of mechanisms and their implementation beyond what is necessary to protect countries' national security interests.

3. Investment policy measures not specific to FDI[12]

In the reporting period, eight G20 Members – *Argentina*, *Brazil*, *P.R. China*, *India*, *Indonesia*, *Republic of Korea*, the *Russian Federation* and *Turkey* – took measures that affect international capital flows but are not specific to FDI. These measures relate to the degree to which economies are integrated in global financial markets.

Some of the measures that were recorded in the reporting period and are set out in greater detail in Annex 2 of this report sought to respond to the disruption in financial markets that the COVID-19 pandemic caused and that impacted international portfolio flows heavily.[13] Emerging market economies as well as some advanced economies including Italy, Japan, and the United States experienced very large drops in portfolio investment inflows (Figures 3 and 4).

The sudden stop of portfolio flows was faster and more incisive than observed during earlier events of significant outflows in recent years, including during the 2008 Global Financial Crisis. As a consequence of the pandemic and the steep oil price fall, exchange rates of emerging market G20 Members, including Brazil, Indonesia, Mexico, Russian Federation, and South Africa depreciated substantially in March 2020, while currencies of advanced economies, and most notably the US dollar, have generally strengthened over the period.

Capital flows have stabilized in many countries in April and May 2020, non-resident portfolio flows to emerging market economies have grown, and currencies have rebounded in several but not all G20 Members affected by the steep exchange rate drop. While the shock has been common to many countries in the first stages of the crisis, the follow-up has seen greater country differentiation, which will likely continue depending on the evolution and handling of the health crisis in emerging market economies in the coming months.

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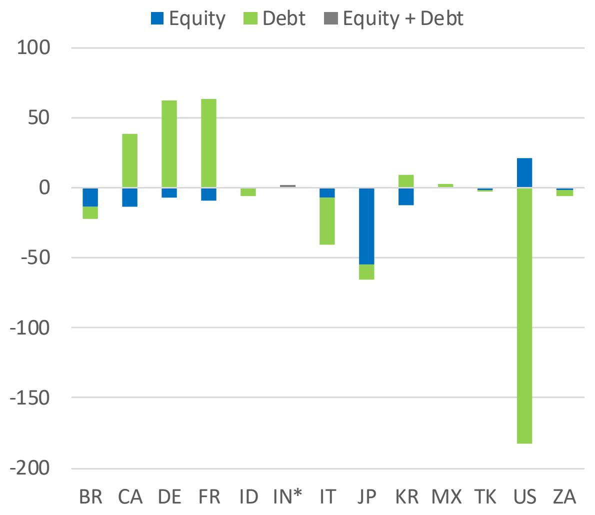
[11] "*Acquisition- and ownership-related policies to safeguard essential security interests – current and emerging trends, observed designs, and policy practice in 62 economies*", OECD, March 2020; UNCTAD, World Investment Report 2020, June 2020; "*OECD investment policy responses to COVID-19*", OECD, June 2020; "*Investment screening in times of COVID – and beyond*", OECD, June 2020; UNCTAD, "Investment Policy Responses to the COVID-19 pandemic", Investment Policy Monitor, Special Issue, May 2020

[12] This section on "Investment policy measures not specific to FDI" has been prepared by the OECD Secretariat under the responsibility of the Secretary-General of the OECD. Annex 2 provides information on the coverage, definitions and sources of the information contained in this section.

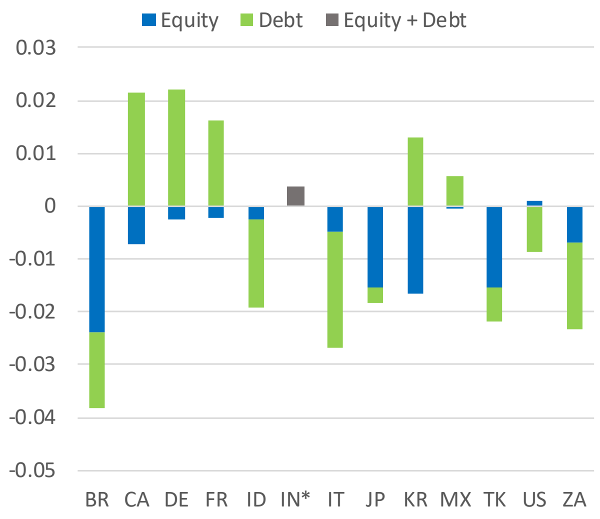
[13] "*COVID-19 and Global Capital Flows*", OECD, June 2020, provides information on major trends in global capital flows during the COVID-19 shocks and description of selective policy responses in OECD countries and non-OECD G20 countries.

Figure 3. Portfolio inflows to selected G20 members –2020Q1 (bln USD)



Note: Net incurrence of portfolio liabilities. Data for Mexico's portfolio debt not available and March data for India not available.
Source: OECD compilation from national sources.

Figure 4. Portfolio inflows to selected G20 members – 2020Q1 (% Portfolio liabilities as of 2019Q4)



Note: Net incurrence of portfolio liabilities, scaled by IIP Portfolio liabilities as of 2019Q4. Data for Mexico's portfolio debt not available and March data for India not available.
Source: OECD compilation from national sources, IMF International Investment Positions.

Governments have used a variety of tools to respond to these developments and have notably made important adjustments in currency-based and residency-based policies beyond FDI. Such responses were with some exceptions in the direction of easing liquidity constraints on inflows, notably:

- *P.R. China* eased a ceiling on cross-border financing;
- *India* eased limits on foreign portfolio investments in corporate and government bonds.
- *Indonesia* and *Turkey* loosened foreign exchange reserve requirements;
- The *Republic of Korea* eased foreign exchange FX derivative caps, while *Turkey* tightened their caps;
- The *Republic of Korea* also eased its foreign exchange liquidity ratio and its levy on foreign exchange liabilities.

No G20 member introduced new restrictions on capital outflows over the period. *Argentina* eased some outflow controls.

4. *International Investment Agreements*

During the reporting period, G20 Members concluded two new bilateral investment treaties (BITs),[14] and one new "other IIA".[15] Furthermore, during the reporting period, eight BITs concluded by G20 Members

[14] The Brazil-India BIT (signed on 25 January 2020) and the Japan-Morocco BIT (signed on 8 January 2020).

[15] The China-Mauritius Free Trade Agreement (signed on 17 October 2019). "Other IIAs" encompass a variety of international agreements with investment protection, promotion and/or cooperation provisions – other than BITs. They include free trade agreements (FTAs), regional trade and investment agreements (RTIAs), comprehensive economic partnership agreements (CEPAs), cooperation agreements, association agreements, economic complementation agreements, closer economic partnership arrangements, agreements establishing free trade areas, and trade and investment framework agreements (TIFAs). Unlike BITs, "other IIAs" may also cover plurilateral agreements.

were effectively terminated.[16] As of 15 May 2020, there were 2897 BITs and 390 "other IIAs". Data on G20 Members' IIAs is available in Annex 3.[17]

III. Overall policy implications

Until the COVID-19 pandemic struck in early 2020, investment policy making in G20 members had slowed down further, with some measures oriented towards greater openness for international investment and most policy measures concerning the reform of investment policies designed to safeguard national security interests against threats associated with international investment. Even though this is a continuation of a trend that had taken root around 2016 these measures have been accelerated due to the pandemic. They need to be monitored and international dialogue should be strengthened to find the right balance between managing risks while taking advantage of the opportunities that FDI brings to countries.

As some governments have achieved first successes in containing the pandemic and bringing the health crisis under control, measures to support a swift and sustainable recovery from the economic crisis are crucial. FDI can play a central role in achieving this objective – provided governments embrace the potential of international investment. The recourse to national security-related screening mechanisms for foreign investment that has gained momentum during the pandemic must not result in an overstretch. Favourable investment policies, embedded in a sound and transparent regulatory framework, are a key component to enable this potential, especially if other factors that weigh on the global economy – in particular increasing trade tensions – are also mitigated and addressed. It is vital that G20 Members remain committed to their recently confirmed goal to "realize a free, fair, non-discriminatory, transparent, predictable and stable trade and investment environment, and to keep our markets open".[18]

Close monitoring of policy developments and continuous multilateral dialogue, as is taking place at the OECD and UNCTAD, can make important contributions to tackling the enormous challenges. Such dialogue also contributes to inform design of investment policies that allow countries to navigate the uncertainties brought about by the COVID pandemic and establish conditions that usher in a sustainable recovery.