

POLICY UNCERTAINTY IMPEDES INVESTMENT

SIDE EVENT AT UNCTAD WORLD INVESTMENT FORUM, 2014

SPEAKING NOTES OF PRADEEP S MEHTA FOR OPENING SESSION

- The world FDI inflows breached the USD 2 trillion mark for the first time in 2007. They have since fallen by more than a fourth and are currently hovering around 1.5 trillion mark. Obviously, the financial meltdown caused the immediate slump, but can it solely be attributed for impeding the recovery even after half a decade?
- The way the crisis spread like a wildfire, quickly engulfing real sector, and breaching geographical boundaries, from US to EU to emerging economies, it brought with itself a heightened sense of distrust, insecurity and uncertainty. This increased the worldwide interest in relationship between uncertainty and investment and how one impacts other.
- Baker, Bloom and Davies, developed an economic policy uncertainty index and found evidence of substantial increases in policy uncertainty in the United States and worldwide since 2007. Julio and Yook observed that uncertainty related to election outcomes in the US leads economic agents to postpone private investment abroad until some degree of the uncertainty is resolved. Gulen and Ion estimated that approximately two thirds of the 32 percent drop in corporate investments during the 2007-2009 period could be attributed to policy-related uncertainty.
- Given that uncertainty negatively impacts investment inflows, in order to contain it, and revive investment, one needs to understand what causes uncertainty.
- In early 2014, Anand and Tulin found that uncertainty in India was primarily driven by its domestic policy challenges, and not by global uncertainty factors. The 2014 World Investment Report also noted that

policy uncertainties surrounding the FDI policy in retail sector in India has dampened the investment climate.

- In Nepal, political instability and post conflict transitional phase has resulted in uncertainty. Weak enforcement of the rule of law in Bangladesh generates operational and contractual uncertainty for investors, and raises the overall cost. Speaking of Africa, lack of clear and detailed transfer pricing regulations in Mozambique has not only constrained its ability to fight tax evasion, but also generated uncertainty. In Tanzania, institutional weaknesses in form of overlapping government responsibilities have created uncertainty. Delay in dispute resolution is a cause of uncertainty in Kenya. Lack of clarity in regulations and procedures relating to accounting and taxation have led to uncertainty in Ethiopia.
- All these point to domestic policy instability as a critical component of uncertainty. However, it is not the only factor.
- Ambiguous interpretation of investment treaties is also a source of uncertainty. Obligations under treaties are generally vaguely stated, leaving much room for interpretation. Details regarding awards are not publicly available, hindering the ability of national and local government officials charged with implementing the treaties to understand just how treaties are being interpreted and applied.
- Johnson and Volkov pointed out that the long term nature of investment agreements, differing interests of the public and private sector contracting parties, and a range of uncertainties and changing circumstances affecting the expected costs and benefits of the relevant transaction stresses on the contractual relationship between investors and states.
- There could be various other causes of uncertainty. There is a need for deeper research for understanding such causes, finding solutions,

developing action plan to implement such solutions, and involving stakeholders in all such activities.

- CUTS already has the experience of implementing country specific and multi-country research led advocacy, which involved stakeholders throughout the process, and resulted in positive policy changes. We believe the success can be repeated in this area as well.
- The objective of this event is to help us in developing an actionable programmatic agenda to work towards reducing uncertainty and reviving investment. We, along with our event partners, Institute of Economic Affairs, Kenya, have already developed a background paper which is available for your reference.
- We look forward to the ensuing panel discussion, and trust it dwells on the issues of relationship between uncertainty and investment, various causes of uncertainty, such as domestic policy unpredictability and ambiguous investment treaties, approach to address the problems identified, and highlighting critical sectors and countries which should be prioritised, for interventions.
- We believe that such focused approach is necessary, and look forward to your co-operation.
