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FDI IN SMALL ISLAND DEVELOPING STATES: ITS LIMITATIONS AND POTENTIAL

HIGHLIGHTS

- *The structural characteristics of Small Islands Developing States (SIDS) limit FDI options.*
  - Their smallness impedes an efficient scale of production thereby discouraging foreign direct investment (FDI).
  - The remoteness of a number of them, mainly those in the Pacific, implies high transport costs which limits exports and, inhibits the establishment of global production networks, affecting the level of FDI.
- *Nevertheless, FDI to SIDS as a group is very high compared to the size of their economies due to fiscal advantages in some SIDS and to large investments in natural resources in others.*
  - The ratio of inflows to GDP during the period 2004–2013 was almost three times the world average and more than twice the average of developing and transition economies.
  - The ratio of stocks to GDP, during the same period, reached 72 per cent, more than twice the world average (30 per cent).
  - FDI flows and stocks per capita are also higher than the world and developing and transition economies averages, but lower than developed economies.
- *FDI to SIDS is concentrated in a few host countries, it comes from a small number of home countries, and it targets a limited number of activities.*
  - FDI to SIDS is concentrated in countries rich in mineral resources, countries offering fiscal advantages, and a few that have a relatively larger market size.
  - A limited number of developed countries, e.g. the United States and Australia, are the main direct investors, although new investor countries are growing.
  - Mineral extraction and related downstream activities, as well as tourism, business and financial services are the main FDI targets.
- *Recent developments have the potential to open new avenues for FDI into SIDS.*
  - China is emerging as a new source of external financing for SIDS.
  - The planned Panama Canal expansion may open new opportunities in transport-related activities in the Caribbean SIDS.
  - The shale gas revolution may encourage investments in small-scale LNG plants, regasification terminals, and power generation.

On the occasion of the third United Nations Conference on SIDS taking place in Samoa in September 2014 that will seek a renewed political commitment to SIDS' development, this Monitor, which also draws upon the World Investment Report 2014, reviews a decade of FDI to the SIDS.[1]

1. SIDS characteristics limit FDI options.

The distinguishing characteristics of SIDS − small market size, narrow resource base, remote location, and high vulnerability to natural disasters − have an impact on the nature and the scope of economic activities that can be developed in these countries. Small markets imply that much economic activity cannot reach the minimum efficient scale of production, resulting in high unit costs. The small size also translates into a high dependence on trade for the development of some activities, both on imports – for the supply of raw materials and intermediate products – and on exports – for the sale of the output. The reliance on trade, added to the limited room for economic and export diversification due to size, exposes SIDS to high risks of exogenous shocks. Air and sea transport are the only options for the movement of goods and people, and the remote location of many SIDS entails high transport costs, which further constrains their ability to expand their economies through trade of goods and to take part in global patterns of specialization. Their high vulnerability to natural disasters increases the risk and volatility of economic activity. These characteristics carry implications for FDI.

The smallness and remoteness of SIDS puts them at a disadvantage when it comes to production for local consumption as well as for exports. This is exacerbated when local production is more dependent on imported goods. This makes SIDS less attractive to market-seeking FDI and to FDI aiming at the export of goods, with the exception of raw materials. In addition, with the liberalization of markets and the reduction of tariff barriers, high transport costs have become a far more restrictive barrier to trade than tariffs. They make SIDS even less attractive to FDI that is dependent on the trade of goods, in particular the global production networks controlled by transnational corporations (TNCs), which imply intensive intra-firm trade and involve export activities with a high import content.

These constraints are reduced when low competitive pressures result in relatively high market shares for market-seeking FDI, mitigating the impact of the small size of the market and making some SIDS – in particular those with relatively high purchasing power – attractive niche destinations for specific services such as retailing, telecommunications, and energy. In the case of efficiency-seeking FDI, the development of information and communication technologies (ICT) has opened up opportunities in new areas that are not sensitive to transport costs, including call centres, data entry, and back offices (such as purchases, logistics, accounting, claims and payment processing), provided a skilled labour force and access to telecommunication and information networks are available.

[1] This study only considers the 29 SIDS that form the informal list used by UNCTAD for analytical purposes, out of the 52 countries and territories presently classified as SIDS by the United Nations Office of the High Representative for the Least Developed Countries, Landlocked Developing Countries and Small Island Developing States (UN-OHRLLS). The 29 SIDS considered in this study are: Antigua and Barbuda; the Bahamas; Barbados; Cape Verde; the Comoros; Dominica; Fiji; Grenada; Jamaica; Kiribati; Maldives; the Marshall Islands; Mauritius; the Federated States of Micronesia; Nauru; Palau; Papua New Guinea; Saint Kitts and Nevis; Saint Lucia; Saint Vincent and the Grenadines; Samoa; São Tomé and Príncipe; Seychelles; Solomon Islands; Timor-Leste; Tonga; Tuvalu; Trinidad and Tobago; and Vanuatu.

2. Despite its limited options, FDI to SIDS is very high compared to the size of their economies.

During the period 2004-2013 FDI to the 29 SIDS was very small in absolute values, – with annual average flows amounting to $6 billion (0.4 per cent of the world's total) and stocks reaching $61 billion (0.34 per cent). Nevertheless, this was very high relative to the size of their economies. This is due to fiscal advantages offered to investors in a number of SIDS, and some large investments in natural resources. The ratio of inflows to current GDP over 2004–2013 was almost three times the world average and more than twice the average of developing and transition economies, while the ratio of stocks to current GDP reached 72 per cent, more than twice the world average at 30 per cent. FDI flows and stocks per capita are also higher than the world and developing and transition economies average, but lower than developed economies (table 1).

Compared to the decade 1994-2003, SIDS' relative ability to attract FDI increased both in terms of current GDP and compared to the world and developing and transition economies. The ratio of FDI flows to current GDP increased from 5 per cent in 1994−2003 to 7 per cent in 2004–2013 whereas it remained the same in the world as a whole. The ratio of FDI stocks to current GDP also registered an increase that was significantly higher than the one recorded at the world level (table 1).

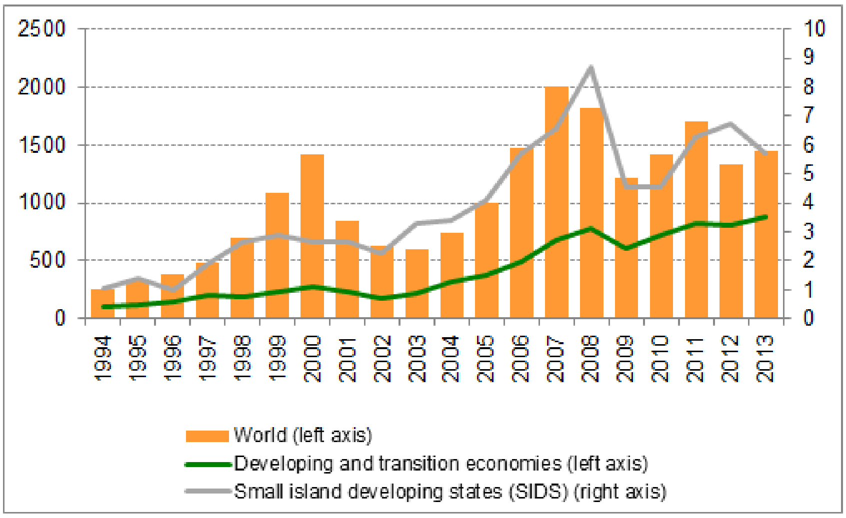
Table 1. FDI flows and stocks in total, per capita and as ratio to GDP in the SIDS in comparison with the world, developed economies and developing and transition economies, 1994–2003 and 2004–2013
(Annual averages)

FDI	SIDS		World		Developed economies		Developing and transition economies	
	1994–2003	2004–2013	1994–2003	2004–2013	1994–2003	2004–2013	1994–2003	2004–2013
FDI flows (in $billions)	2	6	676	1 416	484	767	239	580
FDI stocks (in $billions)	18	61	6 003	18 031	4 541	12 146	1 869	5 314
FDI flows per capita ($)	148	312	113	210	500	751	46	125
FDI stocks per capita ($)	1 215	3 365	1 006	2 668	4 697	11 887	363	1 143
FDI flows per $1 million GDP ($)	53	67	21	24	19	19	29	32
FDI stocks per $1 million GDP ($)	433	719	187	300	182	305	228	294

Source: UNCTAD FDI-TNC-GVC information System, and UNCTAD-Globstat.

However, the global economic crisis took a stronger toll on FDI to the SIDS than to developing and transition economies. While flows to the latter swiftly recovered and surpassed their pre-crisis levels, those to the SIDS registered a much stronger decline and remained – at least until 2013 – well below their pre-crisis level (figure 1). This is one of the reasons why the growth of FDI flows and stocks per capita between 1994–2003 and 2004–2013 was lower in the SIDS countries than in developing and transition economies (table 1).

Figure 1. FDI flows to the SIDS in comparison with the world as a whole and developing and transition economies, 1994–2013
(Billions of dollars)



Source: UNCTAD FDI-TNC-GVC information System.

3. The bulk of FDI into the SIDS is concentrated in a few countries.

Trinidad and Tobago alone accounted for 26 per cent of the total FDI stocks in SIDS in 2013, owing to the presence of large oil and gas resources, coupled with its geographical proximity to North America. The Bahamas, which enjoy the highest GDP per capita among SIDS, accounted for 19 per cent. Jamaica, which has metal mineral deposits and is the second most populated SIDS after Papua New Guinea, received 14 per cent (table 2). Among the ten largest host countries of FDI stock to the SIDS three are rich in mineral deposits (Papua New Guinea, Trinidad and Tobago, and Jamaica), four concentrate the bulk of SIDS' population (Papua New Guinea, Jamaica, Trinidad and Tobago and Mauritius), and some offer fiscal advantages (e.g. Bahamas, Barbados, Mauritius and Seychelles). At the bottom of the ranking, eight countries for which data exist together account for less than 2 per cent of total FDI stock: $1.7 billion or just $215 million per country (table 2). Among these countries, three are low income developing countries, all but three have less than 200,000 inhabitants, none (except Timor Leste) has significant mineral resources, and six are Pacific SIDS, which are among the smallest and most remote.

This suggests that the most attractive SIDS for FDI are those rich in mineral resources, those that offer fiscal advantages to foreign capital, and those that have a relatively bigger market size, while, as predictable, the combination of remoteness, small population, low income, and lack of natural resources is a deterrent to FDI. It is also important to note that the importance of Papua New Guinea and Timor Leste as hosts to FDI stock is probably underestimated. While these two countries host a number of projects in the extractive industries (box 1), they may include non-equity operations. Furthermore it should be noted that countries face insufficient data collection capacities.

Table 2. Real GDP per capita (2012), Real GDP (2012), Population (2013), FDI flows and stocks (2013), and FDI stock per capita (2013) in SIDS

SIDS[1]	Real GDP per capita (base 2005)	Real GDP (base 2005)	Population	FDI flows	FDI stocks	FDI stock per capita
	dollars	$ millions	Thousands	$ millions	$ millions	dollars
Trinidad and Tobago	14 023	18 755	1 341	1 713	23 421	17 463
Bahamas	20 895	7 772	377	1 111	16 667	44 165
Jamaica	4 010	11 102	2 784	567	12 730	4 573
Barbados	14 483	4 102	285	376	4 635	16 284
Papua New Guinea	1 100	7 885	7 321	18	4 082	558
Fiji	3 573	3 126	881	272	3 612	4 099
Mauritius	7 041	8 728	1 244	259	3 530	2 836
Antigua and Barbuda	11 301	1 007	90	138	2 708	30 093
Saint Lucia	5 958	1 078	182	88	2 367	12 987
Seychelles	13 392	1 237	93	178	2 256	24 303
Maldives	6 106	2 067	345	325	1 977	5 729
Saint Kitts and Nevis	10 420	558	54	112	1 916	35 352
Saint Vincent and the Grenadines	5 451	596	109	127	1 642	15 017
Cabo Verde	3 132	1 548	499	19	1 576	3 158
Grenada	6 261	660	106	78	1 428	13 489
Solomon Islands	1 095	602	561	105	1 040	1 854
Dominica	6 052	434	72	18	660	9 168
Vanuatu	2 100	519	253	35	578	2 287
Sao Tome and Principe	1 010	190	193	30	333	1 726
Samoa	2 423	458	190	28	282	1 484
Timor-Leste	3 134	3 491	1 133	20	230	203
Tonga	2 677	281	105	12	132	1 249
Comoros	595	427	735	14	87	118
Palau	7 984	166	21	6	20	966
Kiribati	1 169	118	102	9	14	135
Marshall Islands	2 938	154	53	-	-	-
Tuvalu	2 640	26	10	-	-	-
Nauru	5 573	56	10	-	-	-
Micronesia (Federated States of)	2 467	255	104	-	-	-
Total SIDS	**4 077**	**77 398**	**19 254**	**5 680**	**87 921**	**4 566**

Source: UNCTAD FDI-TNC-GVC information System, and UNCTAD-Globstat.

[1] Ranked according to the magnitude of FDI stocks.

Notes: For detailed sources for stock and flows data, see the methodological note of the World Investment Report 2014 (http://unctad.org/en/PublicationChapters/wir2014chMethodNote_en.pdf)

Box 1. TNCs in the extractive industry of SIDS countries

Four SIDS – Jamaica, Papua New Guinea, Timor Leste and Trinidad and Tobago – have sizeable non-renewable natural resources that have attracted TNC' investment in extractive industries.

Jamaica is rich in bauxite, the ore used to produce alumina. For several years it has been the world's leading producer of bauxite. The island is also endowed with other minerals such as pure limestone calcium carbonate deposits, gypsum, marble and other semi-precious stones. In 2010, the combined value of exports of alumina, bauxite and gypsum accounted for about 42 per cent of the total value of domestic exports.

Around one-third of the bauxite mined each year in Jamaica is shipped unprocessed to the United States by Noranda Jamaica Bauxite Partners, a joint venture between the Government of Jamaica (51 per cent) and Noranda Bauxite Limited (NBL) (49 per cent), a Jamaican company that operates the bauxite mine. The rest is processed in four alumina refineries, three of which are fully or majority-owned (in partnership with the Government of Jamaica) by United Company Rusal (Russian Federation). The fourth refinery – Jamalco – is a joint venture between Alcoa of the United States (55 per cent) and the Government of Jamaica (45 per cent).

In 2009, two refineries owned by Rusal were mothballed because of decreased international prices and the high cost of imported oil to supply energy to the alumina refineries. Rusal is planning to reopen the refineries within three years with a natural gas solution, after entering an agreement with the PACE Group for infrastructure and with British Petroleum (BP) for the supply of gas, which will be delivered as compressed natural gas.

Papua New Guinea has high prospects for oil and gas, with deposits of both found across its territory. The most developed of its projects is the liquefied natural gas (LNG) project led by ExxonMobil,[1] which is expected to begin production in 2014. It will produce 6.6 million tonnes of LNG per year for end users in Taiwan Province of China, Japan and China. The project cost is now estimated at $19 billion, significantly more than the initial cost ceiling of $15 billion. A potential second project is the Gulf LNG project initially driven by InterOil (United States) and now operated by Total (France), which took a majority share in 2013. Oil and gas drilling by foreign companies is continuing apace, with plenty of untapped potential and more gas and oil being discovered each year.

Papua New Guinea is also rich in metal mining, producing both copper and gold. The country is estimated to be the 11th largest producer of gold, accounting for about 2.6 per cent of global production. It also has deposits of chromite, cobalt, nickel and molybdenum. Several international mining companies are majority owners or shareholders in metal-producing operations, including Newcrest Mining (Australia), Harmony Gold Mining (South Africa), Barrick Gold (Canada), New Guinea Gold (Canada) and MCC (China).

Timor-Leste has many oil and gas deposits both onshore and offshore, although most extraction has so far taken place offshore. It also has significant untapped mineral potential in copper, gold, silver and chromite, but the mountainous terrain and poor infrastructure have impeded widespread exploration and development. Major oil and gas discoveries in the Timor Sea in 1994 have led to the development of a large-scale offshore oil industry. ConocoPhillips, Eni, Santos, INPEX Woodside, Shell and Osaka Gas are among the international oil companies operating there.

The energy sector is critical to **Trinidad and Tobago**'s economy. In 2013, oil and gas accounted for 43 per cent of GDP, 85 per cent of merchandise exports, and 50 per cent of Government revenues (fiscal year 2013), but only 3.4 per cent of employment. The sector comprises the exploration and production of crude oil and natural gas (52 per cent of energy sector GDP in 2012), petrochemicals (20 per cent), refining including LNG (17 per cent) and services (11 per cent).

Gas production has come to the forefront since the decline of the oil sector in the 1980s and today gas accounts for almost 90 per cent of the energy sector. Natural gas production is dominated by three foreign companies (BP, British Gas and EOG Resources Trinidad), which together account for about 95 per cent of production. The majority of gas production, 57 per cent, is exported in the form of LNG with the rest used domestically in the petrochemical industry (28 per cent), the electricity sector (8 per cent) and other (7 per cent). Atlantic LNG (owned by British Petroleum, British Gas, France's GDF Suez, Spain's Repsol and Trinidad's State-owned NGC) is the sole producer of LNG. It purchases gas from suppliers and processes it into LNG that is exported. Originally the United States was the largest destination for the country's LNG (99 per cent in 2004) but with the increasing shale gas production in this country, exports are primarily destined for Europe, the Americas and Asia, while those to the United States fell to 19 per cent in 2011.

In addition to natural gas, Trinidad and Tobago produces about 80,000 barrels of oil per day (2012) of which 20 per cent are consumed domestically. About 60 per cent of crude oil is produced by private companies – of which almost 80 per cent is accounted for by three foreign companies (BP, REPSOL and BHP Billiton) – and the remaining 40 per cent by the State-owned Petrotrin. About half of all crude oil produced in the country is refined locally by Petrotrin, which also refines imported crude oil.

Source: Central Bank of Trinidad and Tobago (2014); Humpert, 2013; United States Department of the Interior (2012a); United States Department of the Interior (2012b); IMF, 2012; *Revenue Watch Institute*, "Timor-Leste; Extractive Industries", www.revenuewatch.org; *Jamaica Bauxite Institute*, "Bauxite Industry", www.jbi.org.jm; *Reuters*, "Rusal to reopen Jamaican alumina plants with new energy source", 24 April 2013.

[1] Other partners in the project are Australian Oil Search Limited, Santos, Merlin Petroleum, local landowners and the State-owned Petromin.

4. Mineral extraction and related downstream activities, tourism, business and finance are the main FDI targets in SIDS.

Sectoral FDI data are available for very few SIDS. Only Jamaica, Mauritius, Trinidad and Tobago, and Papua New Guinea make available official sectoral FDI data. These data show a high concentration of FDI in the extractive industries in Papua New Guinea and in Trinidad and Tobago.[2] FDI flows to Mauritius are directed almost totally to the services sector, with soaring investments in activities such as finance, hotels and restaurants, construction and business in the period 2007–2012. FDI to Jamaica, which used to be more diversified among the primary, manufacturing and services sectors, has increasingly targeted service industries during the period 2007–2012 (table 3).

[2] In Trinidad and Tobago, FDI to the services sector increased strongly in 2007–2011 as a consequence of one large acquisition undertaken in 2008 in the financial sector, namely the $2.2 billion purchase of RBTT Financial Group by the Royal Bank of Canada.

Table 3. FDI flows and stock by sector for selected SIDS countries, various years
(Millions of dollars)

Sector/industry	FDI flows (average per year)						FDI stock	
	Jamaica		Mauritius		Trinidad and Tobago		Papua New Guinea	
	2001–2006	2007–2012	2001–2006	2007–2012	2001–2006	2007–2011	2006	2012
Primary	**141**	**71**	**3**	**4**	**768**	**796**	**1 115**	**4 262**
Mining, quarrying and petroleum	141	71	-	-	768	796	991	4 070
Manufacturing	**68**	**36**	**6**	**8**	**10**	**26**	**126**	**187**
Services	**169**	**238**	**78**	**363**	**43**	**487**	**61**	**151**
Business activities	67	133	18	146	..	..	..	..
Finance	..	..	37	114	..	..	43	65
Hotels and restaurants	99	106	10	46	..	..	3	5
Construction	..	..	2	31	..	..	..	..
Other services	3	-	11	26	..	..	14	81
Total	**663**	**587**	**87**	**375**	**876**	**1 344**	**1 350**	**4 656**
Unspecified	285	242	-	-	54	35	48	55

Source : UNCTAD FDI-TNC-GVC Information System

In the absence of sectoral data on FDI for most SIDS countries, information on greenfield FDI projects announced by foreign investors in the SIDS between 2003 and 2013 is used as an alternative method to assess which countries and industries have attracted foreign investors' interest. Upstream and downstream activities in the oil, gas and metal minerals industries[3] have been the focus of most capital expenditures in greenfield projects announced by foreign investors (57 per cent of the total), with Papua New Guinea, Trinidad and Tobago, Timor-Leste and Fiji hosting these projects. Hotels and restaurants are the next largest area of foreign investor interest (12 per cent of total announced investments), with Maldives and Seychelles being their favourite destinations. Other services industries, such as construction, transport and communications, finance, public utilities and business activities, are among the other typical activities for which greenfield FDI projects have been announced in SIDS countries (table 4).

Table 4. SIDS: Announced greenfield FDI projects by sector in total and in top 10 destination countries, 2003–2013
(Estimated total capital expenditures in millions of dollars)

	Papua New Guinea	Trinidad and Tobago	Maldives	Timor-Leste	Mauritius	Jamaica	Fiji	Bahamas	Seychelles	São Tomé and Principe	Others	Total
Primary	**8 070**	**3 091**	**0**	**1 000**	**0**	**0**	**792**	**0**	**0**	**0**	**228**	**13 181**
Mining, quarrying and petroleum	8 070	3 091	0	1 000	0	0	792	0	0	0	228	13 181
Secondary	**7 155**	**3 865**	**78**	**4 010**	**203**	**687**	**59**	**142**	**102**	**351**	**248**	**16 900**
Coke, petroleum products and nuclear fuel	6 650	791	0	4 000	1	0	0	0	0	0	0	11 442
Metal and metal products	228	404	0	0	2	384	0	0	0	0	0	1 019
Chemicals and chemical products	0	2 435	0	0	3	10	0	0	0	0	80	2 527
Food, beverages and tobacco	214	92	0	10	0	258	46	0	59	0	129	808
Other manufacturing	63	143	78	0	197	35	13	142	43	351	39	1 104
Tertiary	**1 113**	**301**	**5 683**	**116**	**4 344**	**3 147**	**551**	**1 079**	**695**	**161**	**2 337**	**19 527**
Hotels and restaurants	0	0	3 153	0	362	504	206	128	476	0	1 171	5 999
Construction	0	0	1 997	0	2 445	1 350	0	0	0	0	0	5 792
Transport, storage and communications	70	23	326	116	362	1 027	70	837	186	150	446	3 613
Finance	162	111	208	0	164	96	248	34	19	11	241	1 295
Electric, gas and water distribution	775	0	0	0	0	0	0	0	0	0	340	1 115
Business activities	48	55	0	0	774	43	27	55	14	0	77	1 094
Other tertiary	59	111	0	0	237	126	0	24	0	0	63	619
Total	**16 338**	**7 256**	**5 762**	**5 126**	**4 547**	**3 834**	**1 403**	**1 220**	**797**	**512**	**2 813**	**49 608**

Source: UNCTAD, based on information from the Financial Times Ltd., fDi Markets (www.fdimarkets.com).

[3] Petroleum, chemical and metal products are among the most relevant downstream activities of the oil, gas and metal minerals industries.

5. Developed countries are the main investors in SIDS, but China is emerging.

Only three SIDS – Cabo Verde, Papua New Guinea and Trinidad and Tobago – provide information from official national sources on the origin of the FDI they receive. These data show, in each of these countries, that developed economy investors are the main source of FDI. They account for at least 69 per cent of FDI stock in Cabo Verde, 79 per cent in Papua New Guinea, and 93 per cent in Trinidad and Tobago. While in Cabo Verde the origin of FDI is more diversified among developed countries, it appears that geographical proximity may play a role in the case of Papua New Guinea – where Australia (58 per cent of FDI stock) is the main foreign director investor, followed by Japan (18 per cent) – and Trinidad and Tobago – where the United States (52 per cent) and Canada (25 per cent) are the main investors (table 5).

Table 5. FDI stocks by home countries in selected SIDS countries, 2012
(Millions of dollars)

	Cabo Verde	Papua New Guinea	Trinidad and Tobago
Australia	0	2 706	0
Bahamas	0	90	0
Bermuda	0	1	0
Canada	0	47	5 396
Germany	0	0	764
Hong Kong, China	0	33	0
India	0	0	349
Ireland	200	0	0
Italy	200	0	0
Japan	0	816	71
Korea, Republic of	0	11	0
Malaysia	0	78	0
Portugal	223	0	0
Singapore	0	78	0
Spain	201	0	0
United Kingdom	205	98	2 827
United States	0	24	11 181
Total world	**1 489**	**4 656**	**21 708**

Source: UNCTAD FDI-TNC-GVC Information System.

Information on greenfield FDI projects announced by foreign investors in the SIDS between 2003 and 2013 confirms that developed countries are the source of almost two thirds of the announced value of greenfield FDI projects. Developed-country TNCs targeted 63 per cent of their capital expenditures in the SIDS at just the three resource-rich countries of Papua New Guinea, Trinidad and Tobago, and Timor-Leste. TNCs from developing and transition economies have focused their interest mainly on four SIDS, namely Papua New Guinea, Maldives, Mauritius and Jamaica, which together accounted for 89 per cent of developing and transition economy TNCs' planned capital expenditure in SIDS (table 6).

Table 6. SIDS: announced value of greenfield FDI projects by top 12 home countries to top 10 destination countries, 2003–2013
(Estimated total capital expenditures in millions of dollars)

Home country	Papua New Guinea	Trinidad and Tobago	Maldives	Timor-Leste	Mauritius	Jamaica	Fiji	Bahamas	Seychelles	São Tomé and Principe	Other SIDS	Total SIDS
United States	3 005	3 094	206	-	569	1 207	554	252	-	-	1 161	**10 046**
Australia	3 535	316	-	4 000	5	-	456	-	-	-	290	**8 601**
China	3 528	-	-	-	-	1 350	8	-	-	-	98	**4 983**
South Africa	3 000	-	-	-	1 320	-	-	-	-	-	-	**4 320**
India	923	171	1 565	-	419	3	3	-	224	-	-	**3 307**
Canada	970	1 205	617	-	121	38	-	-	241	-	63	**3 254**
United Kingdom	139	1 412	42	-	119	367	13	328	7	351	367	**3 145**
France	-	-	13	-	1 732	103	41	550	-	-	-	**2 439**
Thailand	-	-	1 620	10	3	-	-	-	-	-	65	**1 698**
United Arab Emirates	-	23	715	-	72	-	42	-	265	-	64	**1 180**
Italy	8	-	-	1 000	-	-	-	-	-	-	-	**1 008**
Korea, Republic of	959	4	-	-	11	-	-	-	-	-	-	**975**
Others	272	1 032	985	116	178	766	288	90	60	161	707	**4 653**
World	**16 338**	**7 256**	**5 762**	**5 126**	**4 547**	**3 834**	**1 403**	**1 220**	**797**	**512**	**2 813**	**49 608**
Developed economies	***7 705***	***6 967***	***1 302***	***5 108***	***2 686***	***2 441***	***1 115***	***1 131***	***298***	***501***	***2 072***	***31 325***
Developing and transition economies	***8 634***	***289***	***4 460***	***19***	***1 861***	***1 393***	***288***	***89***	***498***	***11***	***741***	***18 283***

Source : UNCTAD, based on information from the Financial Times Ltd, fDi Markets (www.fdimarkets.com).

China is becoming a large investor, coming third place after the United States and Australia as a source of announced greenfield FDI projects. Chinese TNCs have pledged $5 billion in capital expenditures in the SIDS in the period 2003-2013, mainly targeting Papua New Guinea and Jamaica. China has enhanced its economic links with small island developing states since the mid-2000s and this is reflected in the expansion of trade, increased official development assistance (ODA) and more recently the progressive development of FDI (box 2). In the years ahead, China is likely to emerge as a dynamic source of external financial flows, including FDI, to SIDS.

Box 2. China's increasing investment ties with SIDS

China-SIDS ties have increased in the last decade, and this is reflected, among others, in increased ODA and FDI. Development assistance is an important part of the Chinese Government's ‘go global’ strategy, encouraging Chinese companies to gain overseas experience and market access. Chinese overseas investments and development assistance have targeted specific industries, particularly extractive and natural resource-based industries, infrastructure and tourism.

In extractive industries, Chinese companies – such as the China Investment Corporation (CIC) , CNOOC and Sinopec – have a significant presence in Trinidad and Tobago's oil and gas industry, while China Metallurgical Group Corporation (MCC) owns 85 per cent of a $1.5 billion nickel/cobalt mine project in Papua New Guinea that started operation in 2012 (box 1).

In agro-industry, Complant International (China) acquired in 2011 in Jamaica three sugar factories and leased 30,000 hectares of cane fields. In the same year it began an injection of $156 million over four years to improve fields and factories. The company plans additional investment in a new refinery to process 200,000 tons of raw sugar per annum.

The increased involvement of Chinese companies in ***infrastructure projects*** in SIDS is closely linked to the expansion of Chinese development assistance, in the form of grants and – most frequently – loans from Chinese banks. In recent years, two Chinese state-owned banks, China Export-Import Bank (China Exim) and China Development Bank, have pledged/disbursed the majority of China’s loans to SIDS countries. Examples of Chinese financed infrastructure investments in SIDS include sports stadia in Antigua and Barbuda, Bahamas, and Dominica (as well as providing financing to a school and a hospital); roads and shoreline reconstruction in Jamaica, the reconstruction of Tonga's capital destroyed by the 2006 riots; and road upgrading in Fiji. In Papua New Guinea, Chinese firms and investors may well become involved in the government’s new wave of national infrastructure and development projects.

Chinese companies are also involved in ambitious ***port infrastructure*** projects in the Caribbean, possibly in an effort to capitalize on the commercial boost Caribbean ports expect from the Panama Canal expansion. Chinese companies plan to make significant investments in ports in Jamaica, and Trinidad and Tobago. In addition, State-owned China Harbour Engineering Company reportedly plans to invest $1.5 billion in a trans-shipment port in Jamaica, and has expressed interest in developing Trinidad and Tobago's shipbuilding and drydock capabilities. Chinese involvement in port infrastructure in the Caribbean is potentially part of a wider effort to improve Chinese access to transportation routes and markets in the Western Hemisphere. Companies from China are also playing a major part in the $444 million overhaul of Papua New Guinea's Lae Port and national road rehabilitation projects, which are being co-financed by the Asian Development Bank.

Chinese banks have also entered SIDS' ***tourism*** industry poised to become an important conduit for Chinese FDI to SIDS. Investment in the sector is driven by opportunities for attracting tourists from China, which is the fastest-growing source market for tourism in the world and became in 2012 the largest spender on international tourism globally. In 2011, construction began on the 3,800-room Baha Mar, a $3.5 billion resort and casino in the Bahamas, financed by the Export-Import Bank of China, and which is to open in late 2014. China State Construction Engineering Corp (CSCEC) – named as the construction manager/general contractor and investor – has employed some 5,000 Chinese workers for this hotel project.

Source: UNCTAD, based on newspaper accounts.

6. Main locational advantages for FDI in SIDS, and the opportunities and risks they represent for sustainable development.

Despite their common characteristics that significantly limit investment prospects, SIDS have attracted relatively high amounts of FDI, principally in natural resources. However, foreign investors have also increasingly been targeting a number of other industries, such as tourism, financial services and offshore business services that are sometimes linked to the locational advantages of SIDS. At the same time new FDI targets, such as trans-shipment and small scale LNG plants, have the potential to attract greater levels of foreign involvement.

Mining and related activities have been developed in a limited number of SIDS. If properly managed, mineral endowments can provide opportunities for economic development and poverty alleviation. However, exploitation of non-renewable resources poses serious challenges – economic, social and environmental – to prospects for long-term sustainable development. The economic challenges include how to create value from mineral resources, how to capture that value locally and how to make the best use of the revenues created. The social and environmental challenges usually relate to the strong environmental footprint and profound social impacts of the extractive industry.

Tourism has importance as a source of foreign exchange earnings, in view of the constraints faced by SIDS in promoting the exports of goods. Tourism and tourism-related activities in the SIDS have been helped by considerable foreign investments. These activities have become the backbone of the economy in most Caribbean SIDS. By contrast, tourism makes a much lower contribution to national income in most of the African and Pacific SIDS due to poor physical infrastructures, particularly in the smaller countries, isolation from major sources of tourists, and extremely weak aviation and communication links. However there are some notable exceptions including Cabo Verde, Cook Islands, Fiji, Maldives, Samoa, Seychelles and Vanuatu where the industry has attracted significant FDI.

Tourism is often identified as a promising growth sector in SIDS, offering one of the few opportunities for economic diversification through the many linkages it can build with other economic sectors. If adequately integrated into national development plans, it can contribute to the growth of sectors such as agriculture, fishing and services. But if not properly planned and managed, tourism can have negative social and environmental impacts, degrade the environment on which it is so dependent and lead to damage to ecosystems and to traditional activities.

High value-added financial services activities have prospered in many SIDS. A number of them – whether in the Caribbean (for example in Antigua and Barbuda, Barbados, Saint Kits and Nevis, The Bahamas), the Pacific (Vanuatu, Nauru), or Indian Oceans (Mauritius, Seychelles) – have become hosts of offshore financial centres (OFCs). These activities – which are not inhibited by the constraints of small island states – have prospered on the back of strong incentives provided by some countries to TNCs to establish headquarters and financial and trading operations in their jurisdictions and to non-resident wealthy individuals to optimize their tax liabilities. These incentives include favourable tax regimes, efficient business registration, secrecy rules and lax regulatory frameworks. Host countries see these services as a source of growth and economic diversification, with positive spillover effects on other activities, including tourism, hotels and restaurants, telecommunications and transport. However, they could equally be disadvantageous, by making small, open economies vulnerable to sharp and sudden changes in global financial flows and by putting these economies under the scrutiny of countries affected by these services. Renewed focus among main investor home countries on tackling tax avoidance by international businesses may erode FDI-attraction advantages for SIDS in this area.

Offshore business services emerged in the mid-2000s as a new dynamic activity in the Caribbean SIDS that have become an important near shore destination for United States customers. In particular, English-speaking Caribbean countries present a range of advantages for offshoring, among which are the geographical and cultural proximity to the United States and time zone advantages, as well as having English as a first language. This industry is particularly important in Jamaica which hosts large service centres (of more than 1,000 agents) of several top TNCs.[4] Trinidad and Tobago also hosts a number of foreign and local call centres and business process outsourcing (BPO) companies, with several specializing in health-care management services.[5] The presence of offshore banks in a number of Caribbean SIDS – such as Barbados, Saint Kits and Nevis and Saint Lucia – has contributed to the emergence of offshore services, although at a smaller scale.

Offshore business services have not so far attracted large levels of investment, but they are a source of job creation and export earnings. They can potentially become a significant source of technology transfer provided the industry is able to move from low-value-added, low-skilled contact centres and business process services towards higher-value-added, higher-skilled offshore operations, attracting new investment not only on the basis of low costs but also on the strength of technological capacity and skilled human resources.

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[4] These include Affiliated Computer Services (ACS) (acquired in 2009 by Xerox), West Corporation (United States), and AllianceOne (acquired by the French Teleperformance Group in 2007). More recently, the industry in Jamaica received a new boost with the opening in February 2013 of a call center by the Elephant Group (United States), and the launching in December 2013 by Sutherland Global Services (SGS) (United States) of a delivery center that will serve clients across the world. (ECLAC and *Nearshore Americas*, "US BPO Firm Elephant Group Expands Rapidly in Jamaica", 9 January 2014, www.nearshoreamericas.com; *Nearshore Americas*, "Sutherland Launches Global Delivery Center in Jamaica", 9 December 2013, www.nearshoreamericas.com).

[5] In April 2014, telecom capacity vendor Columbus International has chosen Trinidad and Tobago as the site for the company's regional call center while Jamaica will host the customer retention and collections functions (*Nearshore Americas*, "Columbus Launches Two Customer Service Centers in the Caribbean", 3 April 2014, www.nearshoreamericas.com).

New opportunities may arise with the expansion of the Panama Canal, scheduled for completion by December 2015, of which the Caribbean region is well positioned to take advantage**.** For example, transport-related activities in Caribbean ports may increase, as witnessed by the planned expansion of Jamaica's existing container terminal, airports and roads and by the signing by Jamaica's Government of a framework agreement with China Harbour Engineering Co to develop a $1.5 billion trans-shipment and logistic hub in the Goat Islands (box 2). One of Jamaica's main goals is to convince companies to outsource parts of their production there and link the country to global supply chains. There are also expectations that warehousing and manufacturing operations will add value to partly finished products shipped from China that are destined for North America and elsewhere. But the project is encountering local opposition, among others by environmentalists that argue that the Goat Islands, besides being a protected home to wildlife, are inappropriate for development since the Portland Bight area, of which they are a part, is especially vulnerable to hurricanes.

Foreign investment opportunities may also exist in the energy sector, as substituting oil-fired plants for cheaper and cleaner LNG-driven plants becomes viable due to the shale-gas revolution. Projects in this sector are being planned, such as a mid-scale liquefaction LNG plant in Trinidad and Tobago capable of producing 500,000 tonnes of LNG per year to supply the regional market. This plant − a joint-venture between Brighton LNG Gasfin Development SA (Luxembourg-UK-Germany) and the National Energy Corporation of Trinidad and Tobago (NEC) − will facilitate the long-term supply of natural gas to customers in the Caribbean, mainly to feed small-scale power generators interested in shifting to LNG due to the expected cost – saving opportunities.

The Gasfin plant would offer LNG on long-term fixed price contracts to small Caribbean markets below the size needed by traditional large-scale carriers. LNG would be lower-cost and cleaner than traditional diesel or heavy fuel oil. A floating regasification terminal in the receiving market would be an attractive option. Very small scale markets, such as the islands of the Grenadines, could be served separately by containers carried on general shipping. The State-owned National Gas Company of Trinidad and Tobago would be an equity partner in the project, with the potential for participation in the entire value chain including transport, regasification and power generation in the receiving markets. There are also perceived advantages in that the proposal deepens regional integration of the energy market, reinforcing ties among Caribbean countries and other regional partners.

Concluding remarks

FDI flows to the SIDS have tended to target precisely the activities that contribute most to SIDS' growth and from which derive most of the potential for SIDS' development. These activities also constitute the main sources of foreign exchange earnings that are necessary to finance the energy and food imports on which these island countries are often highly dependent. Although FDI represents an important additional source of investment capital in industries that are critical to growth and development, little is known about FDI impacts on SIDS – in particular, how these impacts interact with their structural vulnerabilities.

The small size of SIDS means that development and the environment are closely interrelated and interdependent. There is usually great competition for land and water resources among tourism, agriculture and other land uses (such as mining, in resource-rich countries), and the overdevelopment of any of these sectors could be detrimental to another sector. The challenge for SIDS is to ensure that FDI and its use for economic development do not cause any permanent harm to the sustainable use of land, water and marine resources.

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