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EQUITABLE GROWTH, FINANCE & INSTITUTIONS INSIGHT

Divestment Drivers and FDI Retention

Priyanka Kher and
Carlos Griffin



WORLD BANK GROUP

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1818 H Street NW
Washington DC 20433
Telephone: 202-473-1000
Internet: www.worldbank.org

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Acronyms

CEO	chief executive officer
CFO	chief financial officer
FDI	foreign direct investment
HQ	headquarters
IPA	investment promotion agency
LSS-ILG	Industry Leadership Group of Life Sciences Scotland
MIGA	Multilateral Investment Guarantee Agency
MNE	multinational enterprise
OECD	Organisation for Economic Co-operation and Development
OEM	original equipment manufacturer
RDB	Rwanda Development Board
WBG	World Bank Group

Acknowledgments

Priyanka Kher (pkher@worldbank.org) is a Private Sector Specialist in World Bank Group's Global Investment Climate Unit. Carlos Griffin is a Senior Investment Promotion Consultant in the same unit. The authors are grateful to Armando Heilbron (Senior Private Sector Specialist, World Bank Group) for his valuable inputs and support through the publication process. The authors are grateful for valuable inputs and comments from Soujanya Chodavarapu (Senior Private Sector Specialist, World Bank Group), Zenaida Hernandez (Senior Private Sector Specialist, World Bank Group), Eloise Obadia (Senior Consultant, World Bank Group), Jesica Torres Coronado (Economist, World Bank Group), Peter Kusek (Senior Economist, World Bank Group), David Bridgman (Senior Consultant, World Bank Group), Mark Hallan (Director, Global Investment, Scottish Development International), Paul Lewis (Senior Investment Promotion Consultant, World Bank Group), Eduardo Antonio Jimenez Sandoval (Consultant, World Bank Group) and Yan Liu (Economist, World Bank Group). The note was prepared under the guidance of Asya Akhlaque (Practice Manager, World Bank Group) and Ivan Nimac (Lead Private Sector Specialist, World Bank Group).

Thanks to Marcy Gessel of Publication Professionals LLC for professional editing services and to Diego Catto Val for design and production services.

This publication was made possible through the financial support of the United Kingdom's Foreign, Commonwealth and Development Office.

Contents

EXECUTIVE SUMMARY	1
1. INTRODUCTION	3
2. DRIVERS OF DIVESTMENT DECISIONS	7
Type 1: Planned Market Exit	12
Type 2: Worsening of an Affiliate's Performance	14
Type 3: New/Heightened Risks for Affiliates	15
Type 4: Change in HQ Circumstances	16
3. ACTING ON DRIVERS OF DIVESTMENT FOR GREATER INVESTMENT RETENTION	19
Step 1: Set Strategic Parameters for Retention Efforts	20
Step 2: Actively Monitor and Assess Divestment Risks	22
Step 3: Facilitate Solutions to Investor Problems	24
Step 4: Escalate and/or Advocate before Others in the Government to Take Timely Action	27
4. CONCLUSION	29
REFERENCES	31

Figures

Figure 1: Biggest Obstacles Cited by Foreign Affiliates Around the World in WBG Enterprise Surveys	9
Figure 2: A Typology of Divestment Drivers	10
Figure 3: Effects of COVID-19 Lockdown Policies on Global Value Chains	12
Figure 4: Changes in the Number of Japanese Companies, Electronics Firms, and Residents in Malaysia, 1990-2010	13
Figure 5: Trends among Top Three Divestment Motives in Recent Years	16
Figure 6: A Systematic, Four-step Approach for Optimal Retention	19
Figure 7: JVC Video Malaysia's Transition from Analog to Digital Products	26

Box

Box 1: Public-Private Collaboration for Company and Sector Growth: Life Sciences in Scotland	28
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Tables

Table 1: Types of Issues Potentially Leading to Divestment	8
Table 2: Illustrative Investor Retention KPIs – Year 1	21
Table 3: Characteristics of Firms and Sectors Indicating Increased Likelihood of Divestment	22
Table 4: Illustrations of Creative Problem-solving Applied to a Range of Divestment-threatening Issues	24



Executive Summary

Affiliates of foreign multinationals offer potential growth and benefits through years of successful operation and successive expansions, including through job creation, new skills and technologies, and deeper participation in global value chains. In fact, reinvestment has become an increasingly important part of global foreign direct investment flows. This is evidenced by the share of reinvested earnings in global FDI¹ growing from 30 percent in 2005 to more than 40 percent since 2018.²

However, these benefits can also be lost with a multinational's divestment from affiliates. An analysis by the Organization for Economic Co-operation and Development (OECD) of 62,000 foreign affiliates around the world shows that one in five was divested during the period of 2007-2014,³ which is supported by recent analysis showing that the number of divestitures completed globally in 2021 had more than doubled from 2020 (Deloitte 2022). On the other hand, in some cases divestment is needed -for example, to transition to energy efficient production and to decarbonize supply chains. In this context, governments are challenged to systematically implement effective investment retention and expansion strategies.

The need to address the issue of divestment is made more urgent by extraordinary crises. The COVID-19 pandemic, the war in Ukraine, inflation, growing geopolitical tension, volatile energy prices, climate change, an acceleration in the emergence of disruptive technologies,⁴ resurgent protectionism and related challenges in global value chain integration, the possibility of a global minimum corporate tax, have led to disruptions in business plans of multinationals. The beginning of 2020 saw the second largest annual decline in global FDI flows. Dropping 35 percent, FDI fell below US\$1 trillion for the first time since 2005. Several countries saw net divestment. Although FDI flows recovered in 2021, much of that growth was in developed economies, driven by stimulus spending in infrastructure and large outlier projects. Latest data shows that FDI declined by 12 per cent in 2022, to \$1.3 trillion (UNCTAD 2023).

While much research has been done regarding how political and regulatory risks — such as arbitrary, unpredictable, and non-transparent government actions, breach of contract, and expropriation — can lead to divestment (MIGA 2009-13; World Bank 2019, 2020; Kher and Chun 2020), much less has been done on how operational issues can lead to divestment and what governments can do to avoid them. As such, this note aims to serve as a starting point, synthesizing literature and World Bank experience on the topic, to explore three questions: What

1 As opposed to equity or intra-company loans.

2 <https://www.oecd.org/coronavirus/policy-responses/foreign-direct-investment-flows-in-the-time-of-covid-19-a2fa20c4/>

3 The study highlights the impact on the divested affiliate. For example, the divested affiliates experience on average 28 percent lower sales, 24 percent lower value-added, and 13 percent lower employment as compared to firms that stay foreign-owned.

4 Evidence from multiple sectors and countries overwhelmingly points to accelerated digital adoption since the pandemic. Survey evidence from the World Bank's Global MNE Pulse Survey finds a large and persistent increase in the share of firms reporting new or increased use of digital platforms due to the pandemic in developing countries. Perception surveys also suggest most businesses plan to continue using digital technologies once the immediate crisis is over (Riom and Valero 2020, BTB/Lloyds 2020). On the other hand, growing international gaps in technology adoption could further disadvantage emerging market and developing economies, making it harder for them to attract or retain foreign affiliates.

are the drivers of divestment decisions? Are there any early warning signs of divestment likelihood that could be discernible to retention agencies?⁵ How can retention agencies leverage this knowledge to enable better FDI retention?

There are no comprehensive, publicly available datasets from global surveys of firms concerning their reasons for divestment. Nonetheless, the breadth of variables studied in the existing literature, divestment cases for which details are publicly known, and the World Bank's experience working with client governments to strengthen their investment institutions show that, at the highest level, the drivers of divestment may be classified into four broad types: (i) planned market exit; (ii) worsening of affiliate's performance; (iii) new/heightened risks for an affiliate; and (iv) a change in the headquarters' circumstances. Among these, the one which appears to be the most significant divestment driver is the worsening of the affiliate's performance (that is, reduced revenues, increased costs, and/or worse performance than other affiliates in its corporate network). This typology is primarily intended to highlight factors and situations that can help with the timely detection and monitoring of divestment risks.

To detect and reduce risks of divestment, effective retention measures need to be implemented by a lead agency in close coordination with the institutions responsible for technical areas and other stakeholders. The lead agency may be an investment promotion agency (IPA) mandated to perform investor aftercare and retention services, an investment ombudsman office, or a focal point within a ministry. What is critical is that the lead agency is legally mandated for retention, suitably empowered with access to high-level government authorities, adequately resourced (both with financial and human resources), able to secure effective collaboration from other agencies, and trusted by the investor community. Even these ideal characteristics and great knowledge of divestment drivers do not automatically translate into greater retention. The breadth of the investor community, their varied and ever-changing circumstances, and a government's limited time and resources mean that retention officials are never able to attain a comprehensive inventory of divestment risks or do something about every risk of which they are aware. Indeed some divestments may be planned and needed. Optimizing risk identification and retention requires a systematic approach. Retention agency officials can follow a four-step approach, entailing (i) setting strategic parameters, (ii) risk assessment, (iii) problem-solving, and (iv) escalation and advocacy (Kher, Obadia, and Chun 2021; World Bank 2019). Using this approach, officials can identify, assess, and monitor high-risk situations where there could be potential divestment.

In terms of setting strategic parameters, individual divestment threats should be prioritized on the basis of their significance for the government's development goals, retention agency's strategy, and the ability of retention officials to influence outcomes. This, in turn, requires that officials who would optimize their retention efforts ask and answer additional questions about the rationale for undertaking retention, objectives, target audiences, activities, resources, and monitoring and evaluation.

Knowledge of divestment risks can come either directly from firms or indirectly from other sources. It may be possible to confirm divestment threats to individual affiliates, or to observe heightened divestment risks at a sector or national level. While most of the divestment drivers represent changes in a firm's circumstances, some firms and sectors may also have inherent characteristics that indicate a higher likelihood of divestment. Officials may choose to act based only on confirmed divestment threats from specific companies. Alternatively, they may do so based on officials' perceptions of heightened divestment risk among a pool of investors as defined by, for example, sector, region, firm characteristic, market dynamic, and government action. Once risks are identified, agencies need to engage in effective problem-solving. Problem-solving can be through provision of information, assistance, advocacy or other services.

At the root of each divestment driver is a change to revenue, cost, or risk — either actual or projected. These changes may arise from firm circumstances, market dynamics, and government actions, with each demanding a different form of problem-solving. What is critical for effective problem-solving is the recognition of this possibility of divestment, timely identification of such a risk, as well as proactive engagement with stakeholders based on an analysis of divestment risk. Investor issues requiring the government to make a change can either be completely within the authority of one agency, or they can require a lengthy, formal, inter-ministerial, deliberative process. At the simpler end of this spectrum, the services provided by the retention agency require consideration and cooperation from another agency. At the more complex end, it requires advocacy to persuade multiple, influential stakeholders to support and/or accept a particular course of government action with wide-ranging effect, such as the changing of laws and national policies. Retention agencies must accordingly lay the groundwork in the form of relationship-building and awareness-raising with the institutions from which they are likely to seek cooperation.

5 For the purpose of this note, agencies leading government efforts to better retain investment are referred to as "retention agencies." These typically include units within ministries, IPAs, ombudsman offices, and/or other agencies.

Introduction

At the beginning of the COVID-19 pandemic in 2020, the world witnessed the second largest annual decline in global FDI flows. Dropping 35 percent, FDI fell below US\$1 trillion for the first time since 2005. Twenty-three countries — as diverse as Italy, Qatar, Thailand, Trinidad and Tobago, and Ukraine — saw net divestment, the largest number of countries in any year since 1986.⁶

Although FDI data for 2021 shows an annual increase of 77 percent, this recovery was highly uneven. Nearly two-thirds of that growth was in developed economies, driven by stimulus spending in infrastructure and large outlier projects. Meanwhile, greenfield investment in industrial sectors remained 30 percent below pre-pandemic levels globally, with some developing regions experiencing further double-digit declines in 2021.⁷ Quarter (Q)2/2020 had the lowest number of new FDI projects since 2015, that is, almost half of the pre-pandemic peak in 2019. 2022 started with a strong recovery, but Q3 and Q4 saw the number of projects fall back to below pre-pandemic levels. Latest data shows that FDI declined by 12 per cent in 2022, to \$1.3 trillion (UNCTAD 2023). As part of the World Bank's quarterly Global Multinational Enterprise (MNE) Pulse Survey for March-June 2022, 28 percent of respondents indicated that they would reduce investment in the host country as compared to 23 percent indicating an intention to increase investment.

Alongside, the share of reinvested earnings in global foreign direct investment (FDI)⁸ has grown from 30 percent in 2005 to more than 40 percent since 2018.⁹ Foreign affiliates present great opportunities for FDI growth, global value chain participation, job creation, and knowledge spillovers. However, these benefits can be lost with divestment. An analysis by the Organization for Economic Co-operation and Development (OECD) on 62,000 foreign affiliates around the world shows that one in five affiliates was divested during the period of 2007-2014 (Borga and others 2020).¹⁰ Recent analysis also shows that the number of divestitures completed globally in 2021 had more than doubled from 2020 (Deloitte 2022). Indeed, in some cases divestment is needed -for example, to transition to energy efficient production and to decarbonize supply chains. In this context, FDI policy and promotion efforts of governments need to systematically include effective retention and expansion strategies.

6 <https://unctadstat.unctad.org>

7 https://unctad.org/system/files/official-document/diaeiainf2021d3_en.pdf

8 As opposed to equity or intra-company loans.

9 <https://www.oecd.org/coronavirus/policy-responses/foreign-direct-investment-flows-in-the-time-of-covid-19-a2fa20c4/>

10 The study highlights the impact on the divested affiliate. For example, the divested affiliates experience on average 28 percent lower sales, 24 percent lower value-added, and 13 percent lower employment as compared to firms that stay foreign-owned.

The need to address the issue of divestment is urgent, given the extraordinary crises and trends that now present investors and policymakers with extreme economic uncertainty. Chief amongst these developments are the COVID-19 pandemic, the war in Ukraine, inflation, growing geopolitical tension between the world's two largest economies, volatile energy prices, climate change, an acceleration in the emergence of disruptive technologies,¹¹ resurgent protectionism and related challenges in global value chain integration, and the possibility of a global minimum corporate tax. Further, the relationship between nearshoring/reshoring and divestment is a close one. Indeed, divestment from one location can be based on a decision to relocate elsewhere for reasons of nearshoring/reshoring. Retaining and encouraging expansions from existing investments has become all the more important, as global, regional, and national crises, along with substantial fiscal constraints, reduce investment prospects (Ruta and others 2022).

Much research has been done regarding how political and regulatory risks — such as arbitrary, unpredictable, and non-transparent government actions, breach of contract, expropriation — can impact retention and expansion of investment (MIGA 2009-13; World Bank 2019, 2020; Kher and Chun 2020). However, relatively little has been done recently concerning how other issues faced by investors in their operations can lead to divestment. Thus, the aim of this note is to fill that gap and ultimately help host country investment agencies with more timely identification of potential divestment risks. Based on a literature review and the World Bank's operational experience, this note explores the following three questions:

1. What are the drivers of divestment decisions, including the cancellation of expansion plans?
2. Are there any early warning signs of divestment likelihood that could be discernible to retention agencies? (that is, agencies leading government efforts to better retain investment).
3. How can retention agencies leverage this knowledge to enable better FDI retention?

The topic of divestment broadly needs more research. As such, this note aims to serve as a starting point, documenting available literature on the topic. It ultimately aims to support retention agencies in taking more informed steps and decisions to better retain investment.

Indeed, during this time of multiple crises, many agencies in charge of FDI, such as investment promotion agencies (IPAs) have responded by prioritizing retention services. A World Bank Group (WBG) survey of 41 national IPAs in April 2020 found that a large majority intended to contact all established firms in their respective countries. Their aim was to systematically collect information about issues faced by investors, solve individual investor issues, and advocate before government for emergency policy responses or reforms.¹² The experiences of countries such as Brazil, Ethiopia, Rwanda, and Vietnam also show that systematic efforts to support retention and expansion of investment can lead to concrete results (Kher, Obadia, and Chun 2021).

Services to enable better FDI retention and expansion include addressing investor issues, advocating investment ecosystem reforms, and collaborating for sector development. These services are typically provided through aftercare, retention, and grievance management programs (Heilbron and Aranda Larrey 2020; World Bank 2019; Kher, Obadia, and Chun 2021). Such services and programs are often provided by IPAs, ministries of economy, ombudsman offices, special economic zone authorities, business development offices of subnational governments, and other public offices tasked with private sector development. These “retention agencies” require a deep knowledge of what it takes for firms to grow, as well as what can threaten their success and survival. The challenge usually faced by governments is that they typically find out about divestments when it is too late to remedy a situation. The earlier officials can identify a potential divestment, the better their chance of successfully preventing it.

For the purpose of this note, all divestments (that is, business sales or liquidations) can be understood as occurring through one of the following modes:

1. **An established project is sold to another foreign investor.** In this case, the project is still viable. Specific FDI benefits, such as local sourcing, jobs, skill/technology spillovers, and international connections, could change. In addition, there is a potential for downsizing or for upgrading in the near term.
2. **An established project is sold to a domestic investor.** Here as well, the project is still viable, and some level of jobs and tax collection continues. However, broader FDI benefits could be lost.

11 Evidence from multiple sectors and countries overwhelmingly points to accelerated digital adoption since the pandemic. Survey evidence from the World Bank's Global MNE Pulse Survey finds a large and persistent increase in the share of firms reporting new or increased use of digital platforms due to the pandemic in developing countries. Perception surveys also suggest most businesses plan to continue using digital technologies once the immediate crisis is over (Riom and Valero 2020, BTB/Lloyds 2020). On the other hand, growing international gaps in technology adoption could further disadvantage emerging market and developing economies, making it harder for them to attract or retain foreign affiliates.

12 <https://pubdocs.worldbank.org/en/917561588958415090/WBG-IPA-Response-to-COVID-19.pdf>

- 3. An established project is closed (liquidated or relocated abroad).** This is the most harmful type, representing direct and indirect losses. From the host country's perspective, both liquidation and relocation represent a total closure and direct loss of jobs, taxes, and other development benefits. A possible weakening of suppliers, customers, and the sectoral ecosystem could also occur, sending a signal to potential investors about the declining attractiveness of the location.
- 4. A planned expansion is cancelled.** This is the next most harmful case. It is not technically a divestment. However, the cancellation of a planned expansion still means that the investor was prepared to create jobs, generate tax revenues, and produce other FDI benefits but was dissuaded. This may also have the power to dissuade other potential investors.

The rest of this note is organized as follows: Section 2 presents a typology of divestment drivers, Section 3 presents a systematic approach for retention agencies to apply this knowledge for effective retention, and Section 4 presents the conclusions.





Drivers of divestment decisions

No comprehensive model has yet been developed to explain voluntary divestment (i.e., divestments not caused by expropriation or other similar government measures) (Steenhuis and Bruijn 2009). Much research has been done on divestments caused by purely government measures (such as breach of contract, expropriation, and other regulatory risks), but literature on the topic of divestments due to other reasons — what is being referred to here as operational issues — is relatively limited.¹³

Based on World Bank surveys (MIGA 2009-13; World Bank 2020a) and operational experience, Table 1 presents an illustrative list of the types of political risk issues and other operational issues that can potentially lead to divestment, as well as those that can be influenced by proactive efforts of retention agencies.

13 One reason for the limited extent of research literature on divestments may be that they are associated with job losses and negative economic impacts. As such, they may be perceived as failures of the company and/or host government. This can make the stakeholders involved reluctant to publicize details of divestment reasons and processes. See also Grunberg (1981).

TABLE 1. Types of Issues Potentially Leading to Divestment

Topic	Examples of Investor Issues Potentially Leading to Divestment ^a	
	Political risk issues (These put investments at risk of divestment and can lead to investor-state disputes.)	Operational issues (These may not lead to investor-state disputes but can still put investments at risk of divestment.)
Legal and Regulatory Environment	<ul style="list-style-type: none"> Sudden changes in policies, laws, and regulations; compliance feasibility Abusive refusal of renewing permits/licenses Changes in the terms of a contract Non-transparent and inconsistent application of laws, regulations, and policies Discriminatory treatment against foreign investors Any other government policies, laws, regulations, and other actions that could lead to investment disputes Systemic regulatory and policy issues affecting a group of investors or sector 	<ul style="list-style-type: none"> Unreasonably lengthy delays in renewing permits and licenses (for example, work permits, visas, construction permits; environment permits, inspection) Systemic regulatory and policy issues^b affecting a group of investors or sector (for example, local content requirements), as well as compliance feasibility
Infrastructure/ Utilities/Inputs	<ul style="list-style-type: none"> Government actions that could lead to a breach of contract Unpredictable and arbitrary change in policy/law affecting the continuity of the infrastructure project Non-transparent awarding and termination of a contract Expropriation 	<ul style="list-style-type: none"> Serious issues regarding infrastructure reliability, utility quality or consistency, thus affecting investment sustainability Change in infrastructure, utility rates that renders the project unfeasible
Labor	<ul style="list-style-type: none"> Discriminatory, unreasonably burdensome, and/or improperly implemented labor rules 	<ul style="list-style-type: none"> Difficulty in obtaining urgent access to foreign workers (due to quotas, visa process, speed, transparency, and/or a lack of information concerning available skills) Labor/social unrest, strikes, road blockages Inadequate skills
Finance		<ul style="list-style-type: none"> Difficulty in finding access to affordable rescue finance^c
Capital Transfer	<ul style="list-style-type: none"> Restrictions on international transfers, repatriation (ad hoc arrangements leading to discrimination) 	<ul style="list-style-type: none"> Restrictions on international transfers, repatriation (weekly limits on banks for foreign currency transfers)
Taxes	<ul style="list-style-type: none"> Unpredictable changes Retrospective taxation Non-transparent awarding of taxes Abusive penalties Undue and persistent targeting and harassment of particular investment projects and/or sectors by the tax administration 	<ul style="list-style-type: none"> Tax and incentive predictability, transparency Sudden and excessive tax increases for a sector
Customs	<ul style="list-style-type: none"> Unpredictable changes Retrospective application of duties Discriminatory, unreasonable requirements Abusive penalties 	<ul style="list-style-type: none"> Customs lockdowns, trucking, port, customs strikes causing significant delays for imports and exports Customs clearance (speed of import of inputs and capital goods, issuance of tax and duty exemptions for investors in special regimes, and transparency at customs clearance)
Land	<ul style="list-style-type: none"> Unilateral cancellation or change of terms of a land lease contract Confiscating land of an investor or making it unusable (amounting to expropriation) 	<ul style="list-style-type: none"> Title security and speed, lease process speed, transparency
Courts		<ul style="list-style-type: none"> Speed, predictability, transparency, enforcement, and access to mediation/arbitration/dispute resolution
Crisis/Force Majeure	<ul style="list-style-type: none"> Contract non-performance due to crisis/force majeure Sudden regulatory and policy changes due to crisis/force majeure 	<ul style="list-style-type: none"> Issues stemming from a global, country, or sector crisis affecting investment sustainability Delays in approving emergency licensing or registration to rapidly change line of business (for instance, personal protective equipment, health supplies or medical devices)
Country's International Policies		<ul style="list-style-type: none"> Sudden trade restrictions, sudden currency restrictions
Market Dynamics		<ul style="list-style-type: none"> Consumer preferences change, competition is increased, or technological innovation leads to a competitive disadvantage.
Firm Circumstances		<ul style="list-style-type: none"> Change in direction of corporate strategy (for example, nearshoring, diversification), weaker performance than sister affiliates, limited embeddedness in the host economy

Source: World Bank Group.

a There could be other factors that can lead to divestments, for example, macroeconomic challenges related to exchange rate volatility, inflation, and political instability. These may require more long-term, structural reforms and are not covered in this table.

b Such systemic concerns could arise from both political risk and operational issues.

c Financing needed for urgent or emergency situations, such as to remedy default under a debt financing agreement or to support liquidity needs.

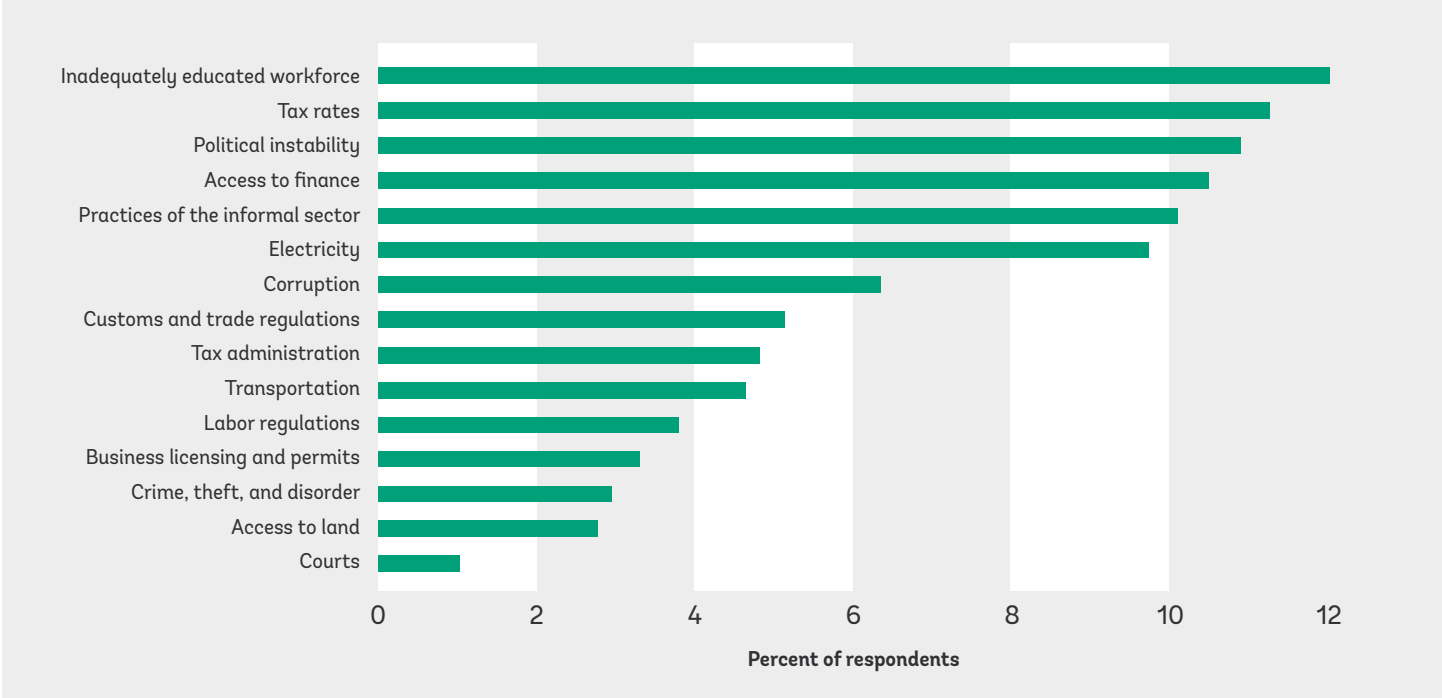


The World Bank’s quarterly Global MNE Pulse Survey for the second half of 2021, 28 percent of respondents indicated that they would reduce investment in the host country. Half the respondents indicated that country diversification and the local legal and regulatory environment were top reasons for such a reduction. Near-shoring, re-shoring, and a change in sourcing decisions were other reasons identified by a third of the respondents.

There are no comprehensive public datasets for global surveys of firms concerning their reasons for divestment, including a good range of factors across the firm circumstances, market dynamics, and government actions. However, the WBG’s Enterprise Surveys provide insight into areas where one would expect the government to exert constructive influence. Figure 1 shows these “biggest obstacles” (risks), as cited by foreign affiliates in 155 countries. These are based on each country’s most recent enterprise survey.

> > >

FIGURE 1. Biggest Obstacles Cited by Foreign Affiliates around the World in World Bank Enterprise Surveys



Source: World Bank Enterprise Surveys in 155 countries between 2006 and 2021 and authors’ calculations.
 Note: This figure includes the percentage of respondents citing each obstacle as their most significant.

The breadth of variables studied in existing literature and the divestment cases for which basic details are publicly known indicate that divestment monitoring and retention measures are likely to vary according to a project's divestment visibility (for example, planned versus unanticipated), leverage point (affiliate versus headquarters), as well as the most influential actors (for example, the multinational itself, other market players, the government, and the workforce). It should also be noted that much of the existing literature has been prepared with at least an implied goal of helping businesses make better business decisions. However, this note aims to contribute towards helping governments keep existing businesses healthy and competitive.

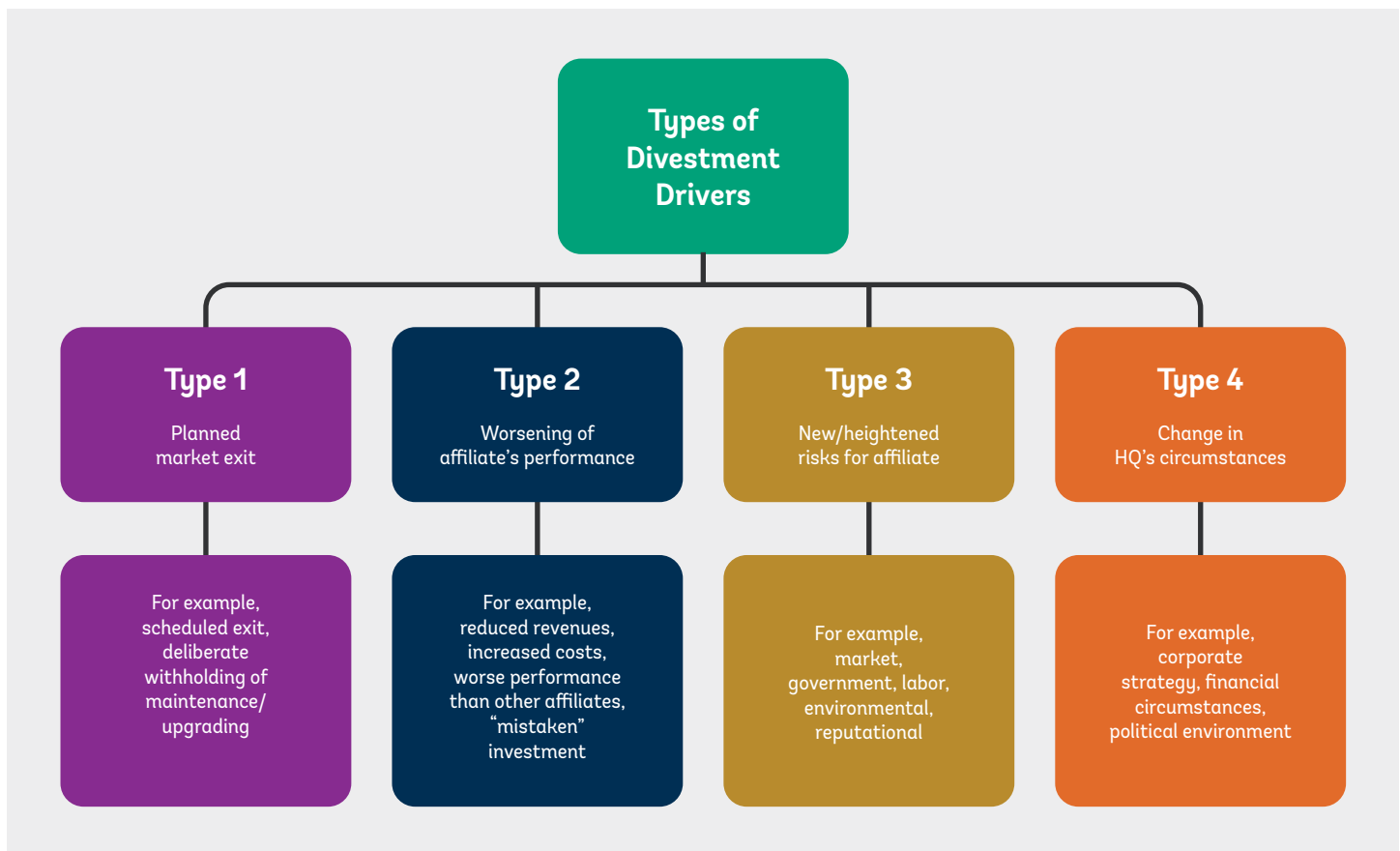
If divestment is the opposite of investment, one can think of the decision to divest as occurring only when the initial reasons for investing are lost. For example, Dunning (1988) hypothesized that three advantages determined FDI location: (i) the investment strengthening the company's competitive advantage, (ii) the

host location possessing some advantage over other locations, and (iii) ownership of the foreign operations providing some advantage over outsourcing the operations through licensing, contract manufacturing, and so on. Operational challenges or issues commonly faced by foreign affiliates are presented in Table 1 above. Each of these can be thought of as diminishing one or more of Dunning's three advantages. When the advantages for FDI location are lost, the rationale for investment may become a rationale for divestment¹⁴.

As noted, the topic of divestments is under-researched, especially in recent years. However, as a starting point, and with the investor perspective in mind, World Bank experience of working with client governments in strengthening their investment institutions shows that at the highest level, the drivers of divestment may be classified into four broad types: (i) planned market exit; (ii) worsening of affiliate's performance; (iii) new/heightened risks for an affiliate; and (iv) a change in the headquarters' circumstances (Figure 2).

> > >

FIGURE 2. A Typology of Divestment Drivers



Source: Authors' Analysis

Note: The typology does not speak to the relative impact, frequency, or interplay of the drivers globally, historically, or in the cases of individual companies where multiple drivers are likely at play simultaneously. Of course, the status and circumstances of a company can change at any time, and a factor driving divestment today may cease to do so tomorrow.

14 McDermott 1989; Wilson 1980

Type 1 has to do with planned divestments, such as those coinciding with product life cycles and contract end dates. Types 2-4 all have to do with changes in circumstances, or, at least, a changed understanding of circumstances. The changes in circumstances leading to divestment come down, directly or indirectly, to three factors. They may hurt actual and projected profitability in the following ways:

- Decreased revenues
- Increased costs
- New or heightened risks which worsen projections for future revenues and/or costs¹⁵.

In recent years, the notion that business decisions should be made on any basis other than profit maximization has gained some credence at the executive level. For example, in 2019, 181 Chief Executive Officers (CEOs) who are members of the United States (US) Business Roundtable signed a revision to its Principles of Corporate Governance, stating that the purpose of a corporation was not just to serve shareholders, but to also deliver value to all stakeholders, including customers, employees, suppliers, communities, and shareholders.¹⁶ Multinationals enterprises are increasingly facing pressure to commit to climate change reforms due to climate-conscious consumers, regulations, environment-social-governance guided investors.¹⁷ While specific climate considerations are gradually shifting the calculus for MNEs in their assessment of their business strategies, long-term profitability continues to be an important lens to present environmental, social and governance considerations to shareholders.¹⁸

Among the four types identified, the one which appears to be the most significant divestment driver is the worsening of the affiliate's performance (that is, reduced revenues, increased costs, and/or worse performance than other affiliates in the corporate network). According to EY's 2021 Global Corporate Divestment Study,¹⁹ two-thirds of companies reported that their most recent divestment was triggered by suboptimal returns in the divested business.²⁰ Wilson presents a model for making a divestment decision on this basis²¹. He applies a cash-flow model to his study of divestments, describing divestment as the rational

course of action when the value to headquarters (HQ) of the affiliate's future cash flows falls below the current value of sale or liquidation. This implies that the most responsible company does not wait until an affiliate is losing money to sell it; at that point, the affiliate is worth much less. Rather, when that company projects dwindling profitability, it should either invest in strengthening the company or plan for divestment at the optimal time.

The typology takes an investor-centric view, that is, examining how investors may rationalize decisions to divest. Often government officials tasked with retention and working in close cooperation with policymakers, regulators, and public administrators may, by default, tend to approach their work from areas of clear government responsibility or regulation, such as: licensing and permitting and access to land. However, factors affecting revenues, costs, and risks arise not only from government action, but also from firm circumstances and market dynamics — that is, circumstances that the government is also in a position to help with. Indeed, these kinds of broad categories (based on government areas of responsibility) seem to be a simpler way to categorize issues. However, following a more investor-centric approach would allow retention agencies to provide more comprehensive services (that is, information, assistance, and advocacy) to investors to tackle the issue of divestment. For example, support needed may include navigating the local market, accessing new markets, finding local input sources, and maintaining good labor relations.²²

Some shocks that may be popularly discussed as individual factors — particularly during times when the need for retention efforts is magnified — can be seen through the lens of this typology as a bundle of several divestment drivers. The COVID-19 pandemic, for example, does not fit under a single type of driver. Rather, it manifests itself as several forms of divestment pressures under Types 2, 3, and 4, depending on the circumstances of the firm. This can include reduced affiliate revenues, increased affiliate costs, a worse position relative to other affiliates, an increased labor risk for affiliates, a shift in corporate strategy, and/or a worse corporate financial situation (Figure 3).

15 A recent report makes complementary observations, suggesting that the reasons for divestment can be driven by internal, firm specific, or external factors. Internal factors occur largely when a company's investment returns do not meet the expectations of its shareholders. A key cause of divestment decisions is that investors' expectations do not meet the reality on the ground. It mentions two main sources for this: first, the lack of knowledge about the local markets resulting in higher-than-expected operating costs; and second, when an investor's expectations are unrealistically high due to over-enthusiastic attraction and promotion efforts. (Arriagada Peters et al., 2021).

16 <https://www.businessroundtable.org/business-roundtable-redefines-the-purpose-of-a-corporation-to-promote-an-economy-that-serves-all-americans>

17 This will gain further ground as countries start putting in place laws and regulations to mandate actions by enterprises to address sustainability issues. For example, Germany's Act on Corporate Due Diligence Obligations in Supply Chains (Gesetz über die unternehmerischen Sorgfaltspflichten in Lieferketten) took effect on January 1, 2023. The Act imposes due diligence obligations that includes the requirement to establish a risk management system to identify, prevent or minimize the risks of human rights violations and damage to the environment. The Act sets out the necessary preventive and remedial measures, makes complaint procedures mandatory and requires regular reports. The due diligence obligations apply to an enterprise's own business area, to the actions of a contractual partner and to the actions of other direct or indirect suppliers. This means that an enterprise's responsibility no longer ends at its own factory gate but applies along the entire supply chain. See World Bank, Investment Facilitation for Development Guide, Forthcoming.

18 Recent research shows that less than a third of the most-emitting MNEs have formally established a commitment to have net-zero GHG emissions by 2050. Large MNEs are most likely to have long term ambitions like net-zero GHG emissions by 2050, yet share of such firms having long, medium and short term strategies and a capital allocation strategy drops markedly (Steenbergen and Saurav 2023).

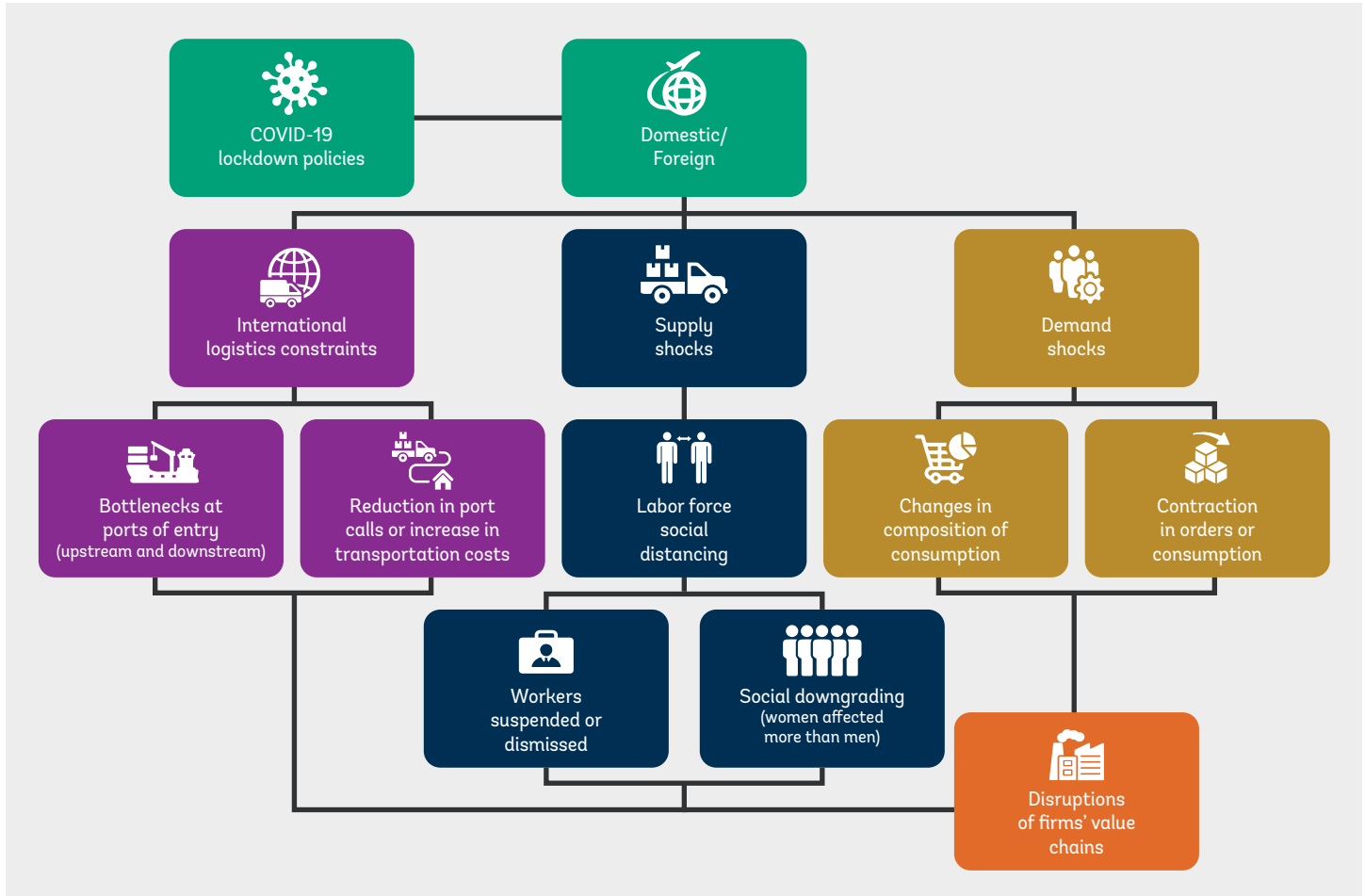
19 According to EY, "Results are based on an online survey of 1,040 global corporate executives and 27 global activist investors (conducted between January and March 2021), including companies from 11 industries, with 88 percent of respondents holding the title of CEO, Chief Financial Officer (CFO) or other C-level executive."

20 https://assets.ey.com/content/dam/ey-sites/ey-com/en_gl/topics/divestment/2021/pdfs/ey-global-corporate-divestment-study-2021-report.pdf

21 Wilson, Brent D. 1980. *Disinvestment of Foreign Subsidiaries*. Ann Arbor, MI: UMI Research Press.

22 Of course, any such efforts would have to be neutral from a competition perspective to avoid tilting the level playing field toward one or a few firms.

FIGURE 3. Effects of COVID-19 Lockdown Policies on Global Value Chains



Source: Brenton, Ferrantino, and Maliszewska (2022).

Type 1: Planned Market Exit

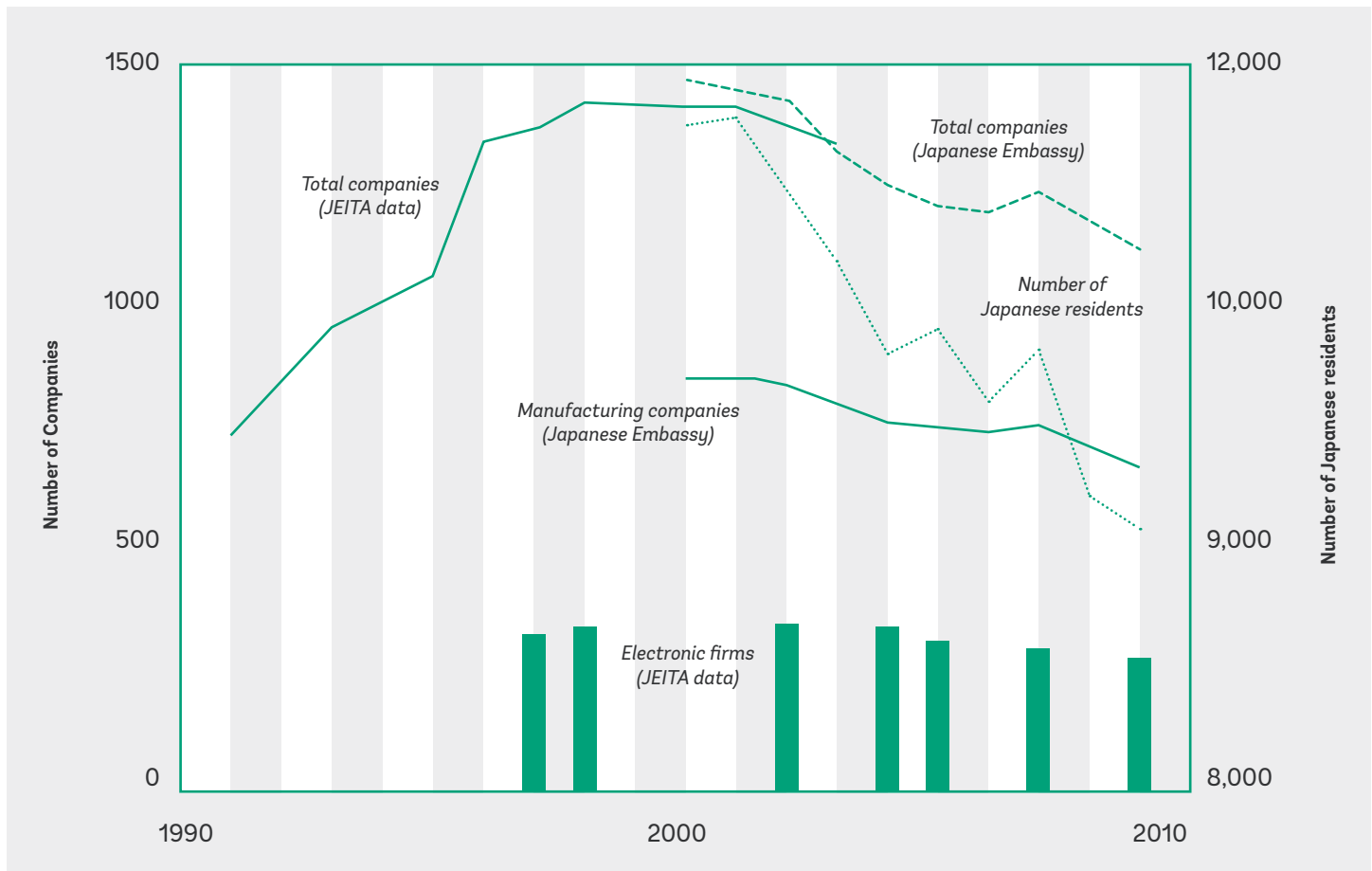
This type of driver can be thought of as consisting of a long-planned market exit as part of a larger strategy, for example, for older products using older technologies, or for a less strategic, even casual, divestment arising from a choice to withhold reinvestment for upgrading or maintenance.

Scheduled exit

Not all divestments represent failures. For example, some are planned to coincide with the expected obsolescence of a technology, such as eReaders and many digital cameras.

Others may relate to the end of a government concession or contract, as with the end of a build-operate-transfer agreement for a hydroelectric dam. Another example may be a garment company's plans to switch back from pandemic-era production of personal protective equipment to garment manufacturing. In one specific example, Figure 4 shows a trend among Japanese electronics manufacturers of divesting from Malaysian affiliates. This occurred in the years after Malaysia's peak as a hub for analog TV and VCR assembly, as these technologies became obsolete. They were then replaced by digital technologies whose production required skills and production technologies not well established in Malaysia.

FIGURE 4. Changes in the Number of Japanese Companies, Electronics Firms, and Residents in Malaysia, 1990-2010



Source: Edgington and Hayter (2013).
 Note: JEITA= Japan Electronics and Information Technology Industries Association

While a government need not necessarily view this as a failure of its investment climate and could conceivably let the investor go without being blamed for the loss of jobs, helping the investor find a business case for extending or repurposing its project could lead to more positive outcomes (See Section 3’s description of how the Japanese company JVC upgraded its production to make its Malaysian factories relevant for the digital era rather than divest). Exits may also be planned in the context of transitioning to more ‘green’ and energy efficient businesses - for example retiring existing coal power plants before they complete their life cycle (Steenbergen and Saurav 2023). Energy companies in the ranking of the top 100 MNEs are divesting fossil fuel assets at a rate of about \$15 billion per year (UNCTAD 2023).

Gradual exit

Divestment is generally thought of as occurring in a relatively short timeframe, whether by the sale of the firm or by asset

liquidation. However, it may also happen gradually when an affiliate is allowed to atrophy over time, especially by withholding the investments that might otherwise go to maintaining and upgrading the business. Profits may be repatriated instead of reinvested. In this case, product innovation and market development at the affiliate are not supported by HQ. Machinery is not upgraded and may not be well maintained. Some refer to this decrease in financial and managerial commitment to an affiliate as “disinvestment” rather than divestment. Within the present typology, disinvestment to the point of eventual divestment is labeled “gradual exit.”

Gradual exit differs from a scheduled exit in that it is less deliberate, with HQ not making a decisive plan to divest up front. Rather, it makes a series of explicit or implicit decisions over time to prioritize other affiliates, products, or markets over those of the gradually divested affiliate. The changed

circumstances comprising the divestment drivers of Types 2-4 may still be behind the headquarters' attitude toward the disinvested affiliate. However, the worsening circumstances may be so gradual or of such a vague origin that they escape close scrutiny and decisive action — whether remedial or divestment — by the multinational's HQ or affiliate.

As discussed further under Type 2, foreign affiliates may be one among many affiliates jockeying for internal priority and investment funds. Local managers who year after year find only middling success in that internal competition may find themselves avoiding closure, but not winning new investment funds or being allowed to reinvest earnings. Furthermore, some firms only become foreign affiliates when they are acquired by other firms for their strategic assets, and their long-term strategy or survivability may be only secondary concerns to the new HQ. This sort of gradual divestment may also be common as a reaction to a substantial, “government-induced” worsening of the investment climate, particularly when the company is unable to obtain redress from the government.

Type 2: Worsening of an Affiliate's Performance

The worsening of an affiliate's performance comes down to factors hurting the affiliate's absolute or relative performance, whether directly or indirectly, through the following factors:

- Decreased revenues
- Increased costs
- Either of the above, not in absolute terms, but relative to sister affiliates with which the affiliate finds itself in competition for HQ attention or resources.

Reduced affiliate revenues

Problems affecting revenues concern the decreased ability to produce, price, and sell one's products, as needed, to maintain or grow revenues. These are both internal and external to the affiliate. Internally, this includes problems with strategy, product design, production engineering, labor, machinery, utilities, marketing, and management. Externally, this includes changes in consumer tastes, increased competition, reduced disposable income of consumers, disrupted distribution, and reduced availability and/or quality of material inputs, utilities, and additional labor.

Increased affiliate costs

Sharp increases in production costs — such as labor, raw materials, utilities, land and facility leases, transportation, taxes, and licenses — may likewise reduce profits or generate losses. For example, rising wages and other production costs in Costa Rica led Intel to close its semiconductor assembly and test plant after 17 years.²³ In another example, Turkey's steady, severe currency devaluation has led to much higher costs for imported inputs and fears of a general economic crisis.

Cost increases caused by government action — such as regulatory changes with high marginal costs for compliance and increases in taxes, utility tariffs, import duties, wage and benefit requirements, and public land fees — are within the government's power to address. While government actions leading to cost increases may have been taken with full knowledge of the impact they would have on businesses, this is often not the case. Of course, even if there is a knowledge of the potential impact, governments may have little or no options, especially with burgeoning deficits currently faced by many countries.

Cost increases caused by market players can sometimes be countered by the government, at least in part. However, the challenge is to do it cost-effectively (that is, in such a way that the development impact is worth the fiscal expenditure) and without distorting markets. Most governments already have policies meant to promote investment through reduced costs. For example, a special economic zone with a dedicated power supply may offer concessional lease rates and save investors the cost of operating their plants with diesel generators.

Some of these costs tend to move in unison internationally, such as energy, commodity inputs, and international transportation. Therefore, a local price increase for such costs does not necessarily create a competitive disadvantage that would induce a multinational to move or divest from its foreign affiliate.

Worse position relative to other affiliates

As a single affiliate within a multinational corporation consisting of many, the affiliate's interests are subordinate to those of the corporation. In this context, the affiliate is just one of many levers through which the corporation executes its global strategy. The importance of affiliates within that strategy is not equal, and that inequality is reflected in the different levels of investment and long-term commitment. To some extent, an affiliate's strategic importance is dictated by the fit of its activities into the corporation's core business and strategic plans. However,

23 In 2020, with consistent support and attention to the investor, Costa Rica was able to attract reinvestments by Intel.

among affiliates having similar strategic purposes (for example, attempting to grow retail sales in new markets), one affiliate's higher performance in Region A or HQ's strategic reorientation towards Region A may cause the affiliate in Region B to lose favor and, therewith, investment. In this sense, affiliates are in constant competition with one another, such that even a well-performing affiliate may be disinvested when its position relative to another affiliate worsens.²⁴

Reversal of an investment mistake

The site selection process by investors typically begins after a thorough collection of information from several candidate locations. They then make comparisons according to a cost-benefit analysis that leads to a single location as objectively, the best location for that company's expansion. While this approach may be generally applied, processes and information are not perfect, time and budget are limited, and there are many ways in which subjectivity may lead to imperfect site selection.

In cases where such a miscalculation comes with options to remedy the issue, IPAs may be able to help the investor. However, some mistaken investments may be difficult to remedy. For example, the US discount retailer, Target, opened 124 stores in its first two years in Canada by taking over the leases of a defunct retailer. In retrospect, these locations were too remote for Target's urban clientele, and Target was never able to establish a proper supply chain system. Profitability was originally expected after one year. However, after two years of operation, management's projected profits were still six years away. Therefore, Target chose to close all its Canadian stores and exit the country.²⁵

Type 3: New/Heightened Risks for Affiliates

Whereas Type 2 is concerned with an affiliate's actual performance to date, Type 3 covers new or heightened risks which may turn previously positive projections to ones characterized by operating losses, lost markets, or other adverse results, thus justifying divestment. Examples include the advent of disruptive technologies, an emerging trade war, and new and unexpected climate realities.

These can come from market actors (customers, competitors, and suppliers), governments, the local workforce and

population, and the physical environment. It can also come from the affiliate itself when it creates a reputational risk for the multinational.

Increased market risk for the affiliate

In this note, market risk is defined as risk that the number, preferences, and/or capacities of customers, competitors, and/or suppliers will change in such a way as to reduce the affiliate's profitability, market share, and/or strategic position. These new or heightened risks can occur at the firm level, with the entry of a new competitor, a supplier going out of business, or a new trend moving consumer preferences toward features unique to the affiliate's competitor (for example, a political push to "buy domestic"). They may also arise from larger economic changes, such as a recession, or sectoral supply chain disruptions, as with the pandemic and invasion of Ukraine. In addition, they may arise from technological changes, such as the Internet of Things and artificial intelligence.

Increased government risk for the affiliate

Firms can divest in response to political instability and institutional weakness (Soule and Swaminathan 2014). World Bank research shows that government risks — such as breach of contract, sudden and adverse regulatory changes, lack of transparency and unpredictable actions — can cause investors to divest or cancel expansion plans (Kher and Chun 2020; World Bank 2019; World Bank 2020a). In fact, most recently, the 2019 Global Investment Competitiveness Survey finds that two-thirds of existing investors (foreign investors) would consider withdrawing investments or cancelling planned investments in the face of political risk exposure in host countries. Indeed, the risks of expropriation and government breach of contract evoke particularly negative investment reactions. When faced with such risks, about 50 percent of investors would consider withdrawing existing investments, and 40 percent of investors would consider cancelling planned investments. Such risks add an additional threat of liability for countries due to investors suing states for violation of their investment law, treaties, and/or contracts.

Increased labor risk for the affiliate

An increase in labor-related risks occurs when the anticipated availability, cost, or skill level of workers becomes less favorable. Some examples of how a development may unexpectedly threaten one firm, sector, or economy more than others include labor unrest, higher turnover or the lower availability of workers resulting from a sector boom, a loss of training capacity or support, or more restrictive pandemic restrictions. Such

²⁴ Grunberg 1981

²⁵ <https://digital.hbs.edu/platform-rctom/submission/targets-failed-entry-in-to-canada/>

labor risks may worsen anticipated profitability. For example, for decades, investors operated in China to benefit from low-cost labor. As the Chinese government shifts to a more consumption-driven economy, wages have increased across several Chinese provinces, thereby presenting a heightened labor risk (Arriagada Peters et al. 2021).

Increased environmental risk for the affiliate

Extreme weather events may damage infrastructure. For example, erosion may threaten the foundation of a building; recurring flooding may damage crops and buildings; or a local river drying up may deprive an affiliate of water for production or a transportation method for goods. Increased temperatures may increase energy costs for cooling. Climate change may change consumption patterns, where workers live, and what raw materials are available at a given time or cost. A change in environmental projections brings new risks, leading many investors to reconsider their location options. An OECD study finds that a 10 percent increase in a country's stringency of environmental protection can also increase the probability of divestment by 0.5 percent (Borga and others 2020). From the perspective of the host country, this calls for a balancing act between the possibility of divestment and environment considerations. Thus, governments could perhaps consider systematic regulatory impact assessments when preparing new regulations and broad-based investor consultations.

Increased reputational risk at the affiliate

The risks described above are risks experienced by the affiliate. Another kind of risk concerns reputational risk, that is, a risk to the parent corporation caused by the affiliate. Improper or even simply unpopular behavior by a company has the potential to damage its reputation, and that reputational damage has the potential to spread to other parts of the corporate network. This could depend on many unpredictable factors acting across distant and varied geographies, including public perceptions, news reporting, the actions of local managers, and the corporate ability to detect and remedy such problems. If such a reputational risk makes it difficult to operate, the company may decide to divest.

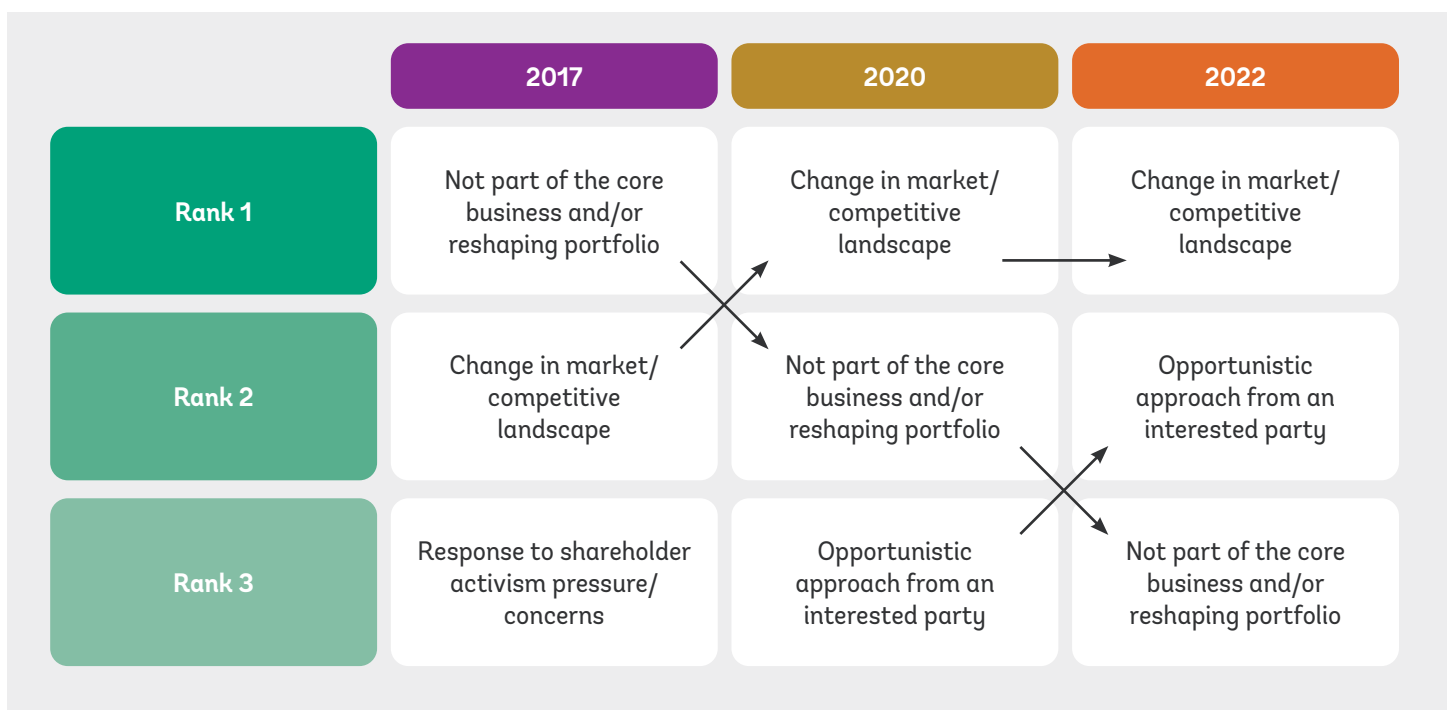
Type 4: Change in HQ Circumstances

Shift in corporate strategy

With changes in technology, net-zero related commitments, companies are increasingly streamlining models so that they can pivot more quickly towards new growth opportunities and stay competitive. In this context, divestments are being used to fund new investments in technology, products, markets and geographies.²⁶ In fact, in two recent global surveys concerning divestment, this was the number one motive for divestment at the HQ level, as shown in Figure 5.

> > >

FIGURE 5. Trends among Top Three Divestment Motives in Recent Years



Source: Deloitte (2022).

²⁶ https://assets.ey.com/content/dam/ey-sites/ey-com/en_gl/topics/divestment/2021/pdfs/ey-global-corporate-divestment-study-2021-report.pdf



Rapid technological change alone is expected to be a tremendously disruptive force on the competitive landscape and investment location patterns. A 2021 divestment study found that “94% of global companies say changes to the technology landscape are influencing divestment decisions, up from 59% pre-pandemic.”²⁷ Honda provides an example of this, specifically, with its new strategy to sell only electric cars by 2040, and its consequent announcement in 2021 that it would close an engine parts plant in the town of Mooka, Japan in 2025.

Worsened corporate financial situation

Multinational corporations experiencing poor performance or other financial strain may come under pressure to improve performance through cost cuts, a change in management, a shedding of non-core business lines, a commitment to a different strategy, a merger with a synergistic partner, and other measures. All such measures can directly or indirectly translate into divestments. In these situations, foreign affiliates may find themselves trying to convince HQ of their long-term value. An affiliate may be divested even when it is well-performing, simply because it no longer fits with the corporate strategy, or because its sale would generate much-needed cash.

Shift in HQ’s political environment

Apart from factors, such as strategy and finances, which are internal to a multinational’s management, pressures may arise that are external to management. Such pressures could lead to cuts or realignment that threaten foreign affiliates with divestment. New or evolving regulations can all affect the way a company’s management sees the suitability of an affiliate to its future plans. These regulations could include those pertaining to governance or environmental and social aspects of business, vocal stakeholders demanding particular actions, or political risk at home. For example, the US-China trade tensions have raised the risk for US-based companies of opening Chinese affiliates and vice versa.

The typology described above is primarily intended to highlight factors and situations that can help with the timely detection and monitoring of divestment risks. Building on this, Section 3 provides steps that retention agencies can take for detecting and addressing divestment risks, including through active monitoring of divestment risks.

27 https://assets.ey.com/content/dam/ey-sites/ey-com/en_gl/topics/divestment/2021/pdfs/ey-global-corporate-divestment-study-2021-report.pdf



Acting on drivers of divestment for greater investment retention

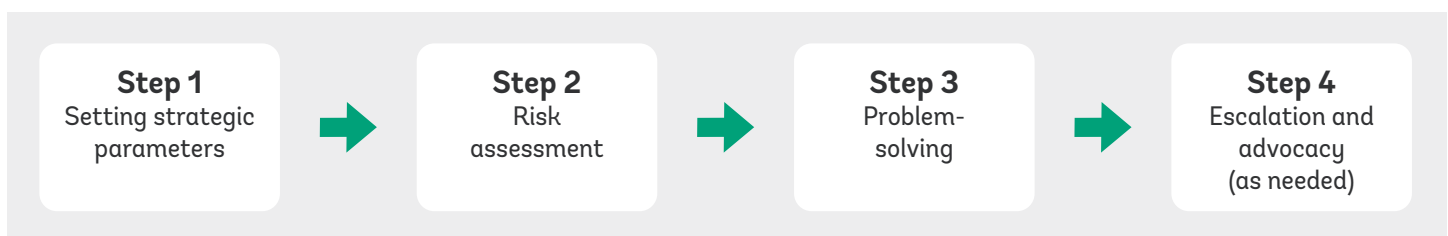
Effective retention measures should be implemented by a lead agency in close coordination with the institutions responsible for specific technical areas and other stakeholders. As noted, the lead agency may be an IPA mandated to perform investor aftercare and retention services, an ombudsman office, or a focal point within a ministry. What is critical is that the lead agency is legally mandated, suitably empowered with access to high-level government authorities, adequately resourced (both with financial and human resources), able to secure effective collaboration from other agencies, and trusted by the investor community (Heilbron and Whyte 2019; Kher, Obadia, and Chun 2021; World Bank 2019).

It should be noted that even these ideal characteristics and a greater knowledge of divestment drivers do not automatically translate into greater retention. The breadth of an investor community, their varied and ever-changing circumstances, and a government's limited time and resources mean that retention officials are never able to attain a comprehensive inventory of divestment risks or do something about every risk of which they become aware.

Optimizing risk identification and successful retention requires a systematic approach. This section guides retention agency officials through a four-step approach, as depicted in Figure 6 (Kher, Obadia, and Chun 2021; World Bank 2019). Using this approach, officials can identify, assess, and monitor high-risk situations where there could be potential divestment, based on the earlier discussion on drivers of divestment. Indeed, an appreciation of these drivers can allow for early recognition of signals of divestment. Experience also shows that concerted and organized efforts by lead agencies can lead to improved investment retention.²⁸

> > >

FIGURE 6. A Systematic, Four-step Approach for Optimal Retention



Source: World Bank Group

²⁸ For example, efforts by Scottish Enterprise and the town council supported a kitchen sink manufacturing company and helped retained 23 logistics jobs. <https://www.scottish-enterprise-mediacentre.com/news/carron-phoenix-23-jobs-retained>.

Step 1: Set Strategic Parameters for Retention Efforts

Not all divestments are “bad” divestments, as demonstrated in the case of planned divestments. In some cases, it represents a natural market evolution. Furthermore, not all revealed divestment threats can be stopped. Even when a divestment can be stopped by government action, it may not always be worth the price, and it can set an undesirable precedent. In addition, it can open the government to accusations of untransparency and favoritism. Furthermore, temporary or one-time incentives cannot guarantee permanent retention.

Negotiating on behalf of investors can be a valuable service with a strong contribution to retention efforts. During the pandemic, for example, the Moldovan IPA identified and negotiated on behalf of healthcare providers for the use of hotels to accommodate doctors and health workers.²⁹ When an investor believes that a government will fully support the investor in resolving its concerns, it builds a sense of comfort and loyalty.

Strategizing for effective retention ultimately requires officials to answer this question: Which (undesirable) divestments can I identify and dissuade based on my organization’s capacity, authority and partnerships?

Individual divestment threats should be prioritized on the basis of their significance for the government’s development goals, the retention agency’s institutional strategy and its ability to influence outcomes. This, in turn, requires that officials who seek to optimize their retention efforts, answer additional questions about their institution’s rationale for undertaking retention, objectives, target audiences, activities, resources, and monitoring and evaluation.

- **Rationale:** “Why” is the retention agency engaging in investor retention? Indicate 2-3 reasons for its importance to the location, for example, key sectors, segments, or specific investors suffering to the point of permanently closing operations, increasing unemployment and/or social unrest, as well as possible legal disputes.
- **Objectives:** “What” is investment retention aiming to save — investment projects and respective jobs in general, or specific sectors, segments, and/or regions at risk? Specific indicators can be included in a table, as illustrated in Table 2 below.

- **Target audience:** The retention agency should consider which investment is both strategic in normal times and at risk of divestment. Key criteria to consider include the following:
 - » Employment numbers, including for women and youth
 - » Strategic region/location
 - » Current priority sector
 - » Anchor companies that link to many domestic suppliers
 - » Risk of closure
 - » Opportunity of expansion
 - » Revenue/sales/exports
 - » Signaling effect to other investors
 - » Support green transition

Ultimately, prioritization by agencies will greatly depend on the overall development goals, priorities for FDI, and the agency’s ability to influence outcomes.

- **Activities:** This requires the retention agency to tailor its activities to suit its objectives, for example, as many IPAs did in helping investors adapt to the circumstances of the COVID-19 pandemic.³⁰ Some key steps in revising one’s activities might include:
 - » Reviewing the adequacy of existing structures for issue identification, such as meetings with investors to collect information about their issues; the appointment of focal points for collaboration with other agencies; the availability of online platforms for submission of investor requests for support, mapping of typical issues investors are facing from existing reports, surveys, meetings with chambers and associations, and so on
 - » Mapping of key stakeholders to contribute to the solution for each issue and protocols for engagement, such as the appointment of focal points, service level agreements, and memoranda of understanding
 - » Developing capacities, including staff skills, as well as systems and tools, such as investor and stakeholder databases, an investor relationship management system or other tracking tools. Such tools could include an issue management or service ticket feature, a website, and so on. This also includes undertaking research, analysis and preparation of materials to bridge information asymmetries regarding new opportunities for investors to re-direct/route their investment towards - for example, green businesses/activities.

29 <https://thedocs.worldbank.org/en/doc/917561588958415090-0130022020/original/WBGIPAResponsetoCOVID19.pdf>

- **Resources:** Importantly, a strategy requires making decisions as to what resources would be required and where they would come from. For instance, deciding whether new or reallocated personnel would be doing the retention work. A seasoned aftercare account manager could take care of about 50-60 investor engagements per month in normal times, including dealing with some problem resolution. Staffing decisions should also take into consideration any

sectoral priorities and technical areas that most frequently cause investor issues.

- **Monitoring and Evaluation:** This helps the retention agency to monitor progress, evaluate and adapt the program as necessary. Table 2 provides an illustration of how retention agencies might set targets for goals and track progress over time.

> > >

TABLE 2. Illustrative Investor Retention Key Performance Indicators – Year 1

Indicator	Measure	Target (Illustrative)	Actual	Progress %
Impact				
Investment retained	US\$ Millions	10		
Jobs retained	Number	500		
Of which women and youth	Number	200		
Outcome				
Investment projects retained	Number	5		
Investment issues solved	Number	15		
Activity/Output				
Investment retention calls/visits	Number	300		
Investment issues identified	Number	60		
Investment issues being managed	Number	45		
Baseline				
Projects at risk	Number	9		
Jobs at risk	Number	1000		

Source: World Bank Group

Note: Investments and jobs retained refers to investments and jobs that were at risk of divestment due to a specific investor issue. These could be retained due to effective resolution of the specific issue.

As part of monitoring and evaluation for investor retention, officials should consider: (i) how often to measure and report, (ii) sources of information, such as official figures, surveys, investor relationship management system or other tracking system, interviews, site visits, (iii) reporting mechanisms, (iv) evaluation and distillation of lessons learned, and (v) program modifications.

With the proper strategic approach, the lead agency can more effectively perform and sustain their retention functions.

However, in times of crisis when retention efforts often become a priority, adjustments may be needed. For example, during the COVID-19 pandemic, agency resource needs increased tremendously, both in terms of staffing and finances. With restricted travel and a much greater need for virtual communication, prompt resource adjustments were needed to provide stronger broadband, online communications, and virtual meetings hardware/software. In addition, a more robust investor relationship management and tracking system was required.³¹

30 World Bank, World Association of Investment Promotion Agencies (WAIPA), Initial Response of IPAs to Covid 10, https://waipa.org/waipa-content/uploads/WBG_IPA_Response_to_COVID-19.pdf

31 See for example, Invest India's Business Immunity Platform.

Step 2: Actively Monitor and Assess Divestment Risks

Knowledge of divestment risks can come either directly from firms or indirectly from other sources. It may be possible to confirm divestment threats of individual affiliates, or to observe heightened divestment risks at a sector or national level. Also,

while most of the divestment drivers discussed in Section 2 represent changes in a firm's circumstances, some firms and sectors may also have inherent characteristics that indicate a higher likelihood of divestment. As a subset of divestment research, the body of research concerning firm characteristics associated with divestment is even more limited. However, Table 3 offers several insights drawn from existing literature that can help retention agencies with the monitoring of divestment risks.

> > >

TABLE 3. Characteristics of Firms and Sectors Indicating Increased Likelihood of Divestment

Characteristic	Effect on the Likelihood of Divestment
Acquisition versus greenfield	Acquired affiliates may be more likely to be divested than greenfield investments (Benito 1997, Li and Guisinger 1991), as new owners may seek to streamline the acquired affiliate's operations within their global network or even to keep only strategic assets, such as intellectual property, and liquidate the rest. Officials who monitor investment projects and become aware that a project has been acquired may wish to check in with the local and corporate managers to better understand the acquisition motive and long-term plan.
Relatedness of industry	Foreign affiliates working in industries unrelated to those of their parent companies may be more susceptible to divestment than affiliates working in related industries (Benito 1997). This has been well-illustrated by the LG Corporation in the spin-off of five companies, which occurred when its management was handed off to a new generation in 2018. Citing the intent to focus on its core businesses of electronics, chemicals, and telecommunications, the company to spin off companies involved in trading, manufacturing of interior parts for automobiles, manufacturing of chips for car and phone displays, and others. ³² Therefore, officials might want to more closely monitor affiliates of more diversified corporations (such as 3M, which makes "everything from Post-It notes to semiconductors" ³³). This would be especially true when the affiliate is further away from the corporation's core business.
Driven by access to low-cost production factors	Foreign affiliates whose purpose within the corporate network is to act as "source plants" or provide the network with access to low-cost production factors may be more susceptible to divestment (Vereecke, De Meyer, and Van Dierdonck 2008). Therefore, officials may suppose that a foreign-invested company is likelier to divest if it was established for the sole purpose of extracting or purchasing commodities to be used by other companies in its corporate network. Low-end garment manufacturers or other firms whose business cases depend heavily on low-cost labor might also need closer monitoring for this reason.
Corporate interdependence	Foreign affiliates may be more likely to divest, the more independent the affiliates' activities are from those of their corporate networks. For example, a food manufacturer set up in a foreign country to serve that market using local inputs is more independent. As such, it is more likely to be divested than an auto parts or consumer electronics manufacturer feeding into a global supply chain (Wilson 1980).
Diversity of product base	Foreign affiliates may be more likely to divest, the less diverse their product bases are (Wilson 1980). Therefore, an official may need to more closely monitor a local Proctor and Gamble (P&G) plant that produced only a few items than another plant that produces the company's full range of consumer products.
Recent change in management at HQ	A foreign affiliate's divestment may be more likely shortly after a change in the CEO (Torneden 1975) because changes in the CEO and shedding of under-performing affiliates both occur more often after a period of overall poor corporate performance range of consumer products (detergents, diapers, shampoo to over the counter healthcare products). Therefore, officials would be well-advised to keep abreast of leadership changes at the HQs.
HQ problems in managing an international network, including culture and language issues	This characteristic may include factors such as language and culture. It is less observable to someone outside of the company. However, it may be something that can be learned from the affiliate, if officials have established a trusting, collaborative relationship with them.
Level of product innovation	Foreign subsidiaries are less likely to be sold off when they are characterized by high levels of product innovation performance, human capital, or have introduced organizational innovations (Konara and Ganotakis 2020).

³² <https://www.reuters.com/article/us-lg-corp-restructuring-idUSKBN2860NX>

³³ <https://www.thebalance.com/the-most-diversified-companies-in-the-stock-market-4169730>



The earlier officials know about potential divestments, the better their chance of successfully intervening. Waiting until divestment plans are already publicly known is generally too late. Therefore, officials need to maintain a deep understanding of developments, trends, and prospects of individual firms, products, and sectors. The channels by which they can typically do this include the following:

- Conversations with individual affiliates and HQs, for example through an IPA's aftercare support
- Surveys of affiliates and sector associations, whether conducted by retention officials, their partners (for example, chambers of commerce), or public sources (for example, international organizations)
- Reporting on individual affiliates, HQs, products, and sectors by general and sector-specific news outlets and journals
- Sector conferences and seminars
- In places where project monitoring is legally required, a review of periodic project status reports
- Review of public-private partnership project terms for planned market exit or conditions under which the private partner is permitted to exit
- Research and analysis, including public, paid/bespoke, or in-house, concerning shifting costs, market dynamics, and risks in priority sectors. Public research may come from government offices, academia, sector associations, and international organizations. Where these are inadequate, officials may be able to do the research in house, including through their own conversations with investors. Alternatively, they may pay market research companies for sector trend reports.

During the COVID-19 pandemic, many governments were faced with a sudden, widespread surge of severe divestment risks. Each company's situation could be quite different. As such, company-specific intelligence and support was needed,

but on a much larger scale and at a faster pace than any government agency was accustomed to.

Monitoring priority investors and sectors in these ways can yield useful warning signs of divestment plans. Retention officials can focus on the issues of highest strategic priority. For example, a systematic assessment of observed divestment risks may help score each risk for likelihood of divestment, as well as for the anticipated impact of the divestment (for example, one company or many, closure or sale of affiliate, critical blow to an ecosystem or negligible). Although this may sound straightforward, it requires that officials set up a system consisting of the following:

1. An internally unified set of definitions and measures for sectors, products, company importance, company status, and signs of divestment
2. A database of existing investors
3. Personnel charged with implementation and supervision of monitoring, assessment, service provision to investors, coordination with partners, and advocacy
4. Standard operating procedures for monitoring signs of divestment, assessing the likelihood and impacts of divestments, and evaluating the government's options for addressing them, including the responsible offices, anticipated costs of intervention, anticipated benefits, and likely obstacles
5. Partnerships with similarly interested stakeholders (for example, sector associations, office of an investment ombudsman, or grievance management unit) to coordinate information collection and advocacy steps
6. A monitoring schedule (for example, company visits/calls, surveys, and public-private dialogue meetings on the sidelines of periodic sector-specific events)
7. A tracking system to record issues raised by individual investors and analyze them in aggregate

Step 3: Facilitate Solutions to Investor Problems

Officials may choose to act based only on divestment threats from specific companies. Alternatively, they may do so based on officials' perceptions of heightened divestment risk among a pool of investors as defined by, for example, sector, region, firm characteristic, market dynamic, and government action. The services rendered by retention officials to investors may fall under the same headings of information, assistance, and advocacy, as all services under the WBG's Comprehensive Investor Services Framework. However, the specific services

provided are not fixed or finite. In fact, the ability to tailor services is critical for effective retention.

Table 4 presents a sample of the types of services that have been deployed globally, as illustrations of how particular services are suited to specific divestment drivers. As noted, at the root of each divestment driver is a change to revenue, cost, or risk — either actual or projected. These changes may arise from firm circumstances, market dynamics, and government actions, with each demanding a different form of problem-solving. What is critical for effective problem-solving is the recognition of this possibility of divestment, timely identification of such a risk, as well as proactive engagement with stakeholders based on an analysis of divestment risk.

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TABLE 4. Illustrations of Creative Problem-solving Applied to a Range of Divestment-threatening Issues

	Firm Circumstances	Market Dynamic	Government Action
Revenue	<ul style="list-style-type: none"> During the COVID-19 pandemic, the governments of Ethiopia and Haiti helped investors cut through red tape to repurpose production lines from garments and pharmaceuticals to make hygienic masks, medical robes, and hand sanitizer.³⁴ 	<ul style="list-style-type: none"> In a shrinking market, the IPA shares, at no cost, market intelligence generated by the Ministry of Commerce concerning disposable incomes, consumer preferences, and domestic production capacity, thus improving firms' abilities to adjust with the market. 	<ul style="list-style-type: none"> A new tax stamp rule requires beverage bottlers to place a stamp on each bottle, necessitating a major reconfiguration of factory floors, thus pushing businesses with razor-thin margins toward unprofitability and divestment. The retention agency provides an objective impact assessment to the government and advocates a modified measure. This accomplishes the government's goal, without pushing firms out of business.
Costs	<ul style="list-style-type: none"> The retention agency introduces the firm to local suppliers and helps the latter understand how to obtain certification from the firm, thereby allowing it to avoid more costly, time-consuming imports. 	<ul style="list-style-type: none"> The retention agency advocates for relief of a sector constraint, thereby bringing down costs sector-wide (for example, establishing a water purification plant close to garment manufacturers in a special economic zone, thus allowing timely and lower-cost access to high quality water that is needed for more competitive production). 	<ul style="list-style-type: none"> A new auto policy extends incentives to new Original Equipment Manufacturers (OEMs) only, leaving existing OEMs at a competitive disadvantage. The retention agency advocates for inclusion of existing OEMs in the new incentives.
Risks	<ul style="list-style-type: none"> The IPA has a standing mechanism for receiving and mediating labor complaints, thereby reducing firm-specific labor risks. 	<ul style="list-style-type: none"> Greater consumer demand for sustainability increases the risk that firms will lose market appeal with existing practices or face unprofitability with the changes demanded. The retention agency provides information and assistance in accessing support for greening buildings, industrial symbiosis, adding green business lines, and so on. 	<ul style="list-style-type: none"> A new government comes into office promising a variety of increased business regulations. The retention agency advocates for a consultative process inclusive of the private sector.
Relations with other affiliates and HQ	<ul style="list-style-type: none"> The retention agency helps the affiliate to build a business case for expansion, diversification, or greater integration within the corporate network, thus positioning the affiliate to be of greater long-term strategic importance. 	<ul style="list-style-type: none"> An affiliate's sales are in its host country market A. The affiliate's HQ is in country B, with a worsening reputation in the host country A, thus weakening the affiliate's market position. The retention agency helps the affiliate understand how it is perceived and why. It advises the affiliate on potential actions that might bolster its domestic image. 	<ul style="list-style-type: none"> Tensions have been rising between the governments of the affiliate's host country A and home country B. The retention agency can continue to convey its non-political, non-discriminatory commitment to the investor community, including the affiliate, which remains a highly valued client.

34 <https://thedocs.worldbank.org/en/doc/917561588958415090-0130022020/original/WBGIPAResponsetoCOVID19.pdf>

Poor performance is the leading reason for divestment. As such, any retention agency that can systematically help affiliates avoid poor performance will significantly reduce the risk of potential divestments. Governments may help investors avoid poor performance by providing support to them in dealing with the factors affecting revenues, costs, their position relative to other affiliates, as well as other risks.

In the normal course of their duties, many public offices produce data and analysis of great value to firms, providing insights into local markets and the business environment. This can help firms find new customers; enter new markets; find cheaper, higher quality, or more reliable inputs; take advantage of cost-saving or capacity-building services provided by the government; and better understand their risks.

Broad-based initiatives to identify economy-wide issues, for example, as part of a reform or crisis response initiative, may simultaneously reveal many company-specific issues that present the opportunity for concrete retention through individualized problem-solving. For example, a survey of 41 IPAs found that a majority had contacted all established investors during the pandemic, and 59 percent had stated they were working to solve individual investor issues related to the pandemic, with another 20 percent planning to do so in the two weeks that followed the survey. In several cases, these efforts led IPAs, such as South Africa's InvestSA, to deliver company-level problem-solving on a large scale. InvestSA, which had strategically focused its pandemic retention efforts on producers of essential goods and services — such as pharmaceuticals, medical devices, food, and critical manufacturing inputs — was able to identify and quickly address threats to their supply chains. InvestSA then maintained constant communications with nine provincial IPAs through a WhatsApp working group in order to continuously monitor the effects of its retention work, as well as any shifts in divestment risks among this essential constituency. This also enabled good intergovernmental coordination and ground-level support for implementation across the country.³⁵

Regardless of the government's chosen approaches to investment retention (proactive/reactive, continuous/periodic, or targeted/broad), the provision of information is important. Globally, most IPAs would claim to provide information. However, in fact, much of that information is patchy and driven by what is available at the time of an investor request. It is not strategically developed, maintained, and disseminated with the explicit goal of influencing, targeted investors, as well as other public stakeholders in the problem-solving process.

Even more useful than telling an investor where they can find good domestic supply of raw materials or how to take advantage of some government incentive is the provision of assistance in meeting suppliers or navigating the bureaucracy, for example. Officials who become aware of a likely divestment early enough might find a way to address the divestment drivers. Also, if divestment is going to nonetheless proceed, officials may be able to help the company to find a buyer so that the firm can remain open, thus preserving jobs and sectoral strength.

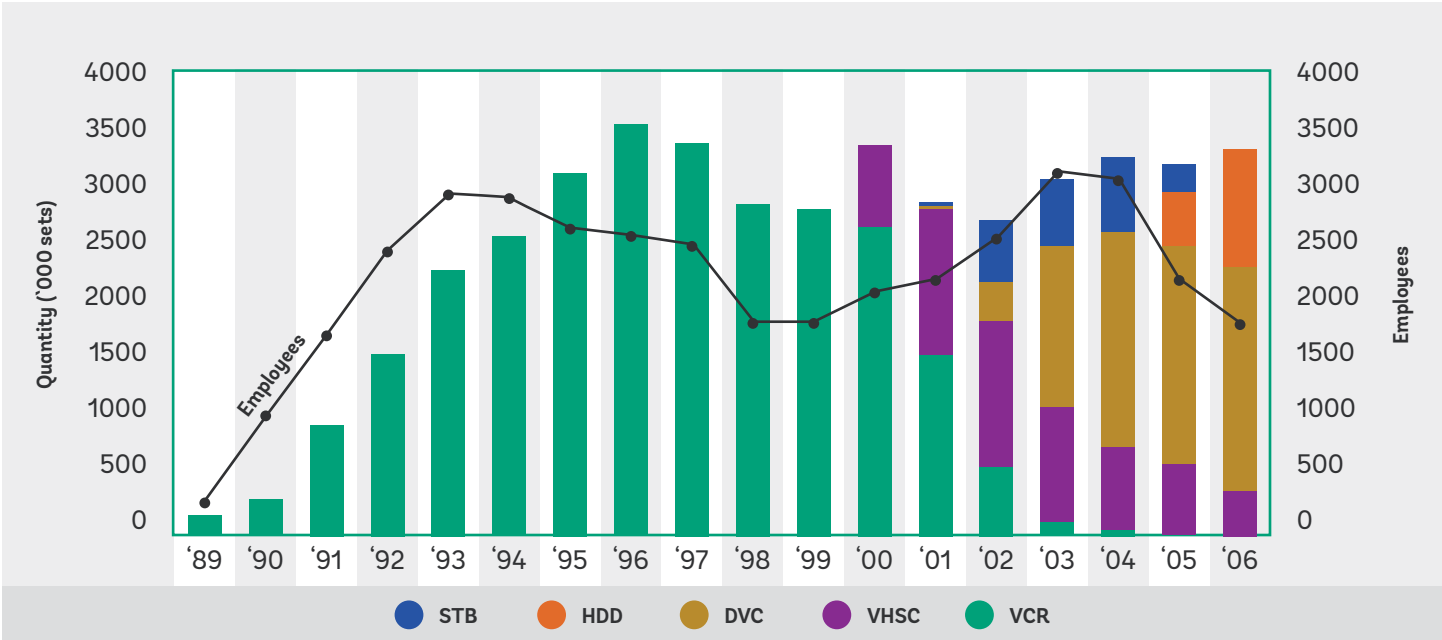
The example of the analog electronics manufacturing sector being phased out in Malaysia was discussed earlier. However, several Japanese corporations that were generally tending to shift production to lower cost locations, such as China and Vietnam, were able to work with the Malaysian national and state governments to create better conditions for a transition to digital electronics manufacturing within Malaysia. This included support from the governments towards: (i) cluster infrastructure and support; (ii) a relaxation of restrictions on skilled immigrant labor, which was needed for HQ-based technicians to train local engineers and oversee the transition; and (iii) set up of industry-specific training centers, such as the Penang Skill Development Centre. Figure 7 shows how one corporation, rather than divest from its Malaysian factories, was able to completely transition from analog products to digital products in six years. In so doing, it kept total output at comparable levels and shed some jobs. However, this was primarily due to productivity gains.³⁶

35 World Bank Group 2020

36 <https://www.sfu.ca/content/dam/sfu/geography/People/Faculty/roger-hayter/edgington-and-hayter-upgrading-malaysia-2013.pdf>



> > >
FIGURE 7. JVC Video Malaysia's Transition from Analog to Digital Products



Notes: Analog production: VCR = video cassette recorder; VHSC = analog camcorder.
 Digital production: DVC = digital camcorder; HDD = hard disk drive; STB = set top box.
 Source: Edgington and Hayter (2013).

With labor and environmental risks, too, the government is likely to have a critical role in resolving any problems that may arise. Officials can do much to assuage investor concerns by openly and preemptively identifying potential risks, making firms feel well consulted, as well as making firms understand what the government is willing to do to mitigate risks. For example, the government may engage labor unions in a constructive dialogue or make plans to undertake public works to protect companies from environmental risk.

Officials can also proactively support investors divest from polluting activities and divert their investment to more green activities. For example, to leverage the very substantial oil and gas supply chain in Scotland (given 50 years of North Sea O&G exploration) and to ensure a just transition to net zero policy goals, Scottish Development International (SDI) has recently taken specific steps.

SDI put together a policy to reposition its support for companies in a way that would enable the shift to a low carbon economy with initiatives such as:

- a. Focusing its assistance to existing overseas inward investors in the oil and gas supply chain, to incentivize them to invest in diversification into low carbon opportunities (such as supporting new products and services for these new market opportunities). This also meant moving away from directly incentivizing further investment purely into the oil and gas sector.
- b. A similar approach was taken on trade support, where net zero transition market opportunities were prioritized rather than traditional oil and gas events.
- c. A program of environmental aid (state aid approved) is put in place to incentivize existing investors to reduce their carbon outputs from their current facilities. This aims to improve the carbon efficiency of existing operations.

These interventions sit alongside work of Scottish Enterprise (the nation's wider economic development agency) to support innovation within the O&G supply chain (building on a strong subsea technology base) and deployment of offshore wind (and future wave and tidal) generation.

Step 4: Escalate and/or Advocate before Others in the Government

Investor issues requiring the government to make a policy change are more complex than others. They can either be completely within the authority of one agency to address, or they can require a lengthy, formal, inter-ministerial, deliberative

process. At the simpler end of this spectrum, the services provided by the retention agency require consideration and cooperation from another agency. At the more complex end, it requires advocacy to persuade multiple, influential stakeholders to support and/or accept a particular course of government action with wide-ranging effect, including the changing of laws and national policies. Retention agencies must accordingly lay the groundwork in the form of relationship-building and awareness-raising with the institutions from which they are likely to seek cooperation.

A clearly defined institutional set up and empowered retention agencies can potentially facilitate systemic advocacy efforts, as well as escalate issues to higher authorities as needed. Such is the case in Rwanda, where a new law confirmed the mandate of the Rwanda Development Board (RDB) to address investor complaints arising from government action. An inter-ministerial committee called the Private Investment Committee was set up to discuss investor issues and propose acceleration measures to resolve them. This is particularly relevant when there is a high chance of the investor disinvesting and/or the government being held liable for breach of contract or law. This mechanism provides for four stages of escalation, depending on the complexity and gravity of the problem. It starts with the RDB's investment office, moving up to the RDB's cabinet-level CEO, then the Private Investment Committee (comprising RDB's CEO, the Minister of Finance, and a representative of the Presidency), and finally the cabinet. In the first few months of operation, the office had registered 17 issues portending a high risk of divestment or litigation in a range of sectors. It resolved eight, mostly by reaching agreement on new payment modalities in the case of a government agency or the investor not providing contractually obligated payments. From these eight resolved issues, investments representing US\$26.5 million and 761 jobs were retained (Kher, Obadia and Chun 2021).

In the same way that one may argue "the best defense is a good offense," one may contend that the best way to prevent divestments is to promote expansions and other actions, thus deepening a company's roots in a location. Globally, IPAs and governments best regarded for their success in fostering FDI are those that strategize and plan to grow sectoral ecosystems in close collaboration with the private sector and critical stakeholders, such as academia and labor representatives. These collaborative groups are often at the cutting edge of their sectors, staying ahead of the curve and leading growth, thereby, supporting the revenue side of investors' profit equations. Box 1 presents a good example of this type of collaboration from the Scottish life sciences sector.



BOX 1. Public-Private Collaboration for Company and Sector Growth: Life Sciences in Scotland

Companies and publicly funded research institutions are well abreast with, what technologies are emerging, how these may interact with evolving consumer preferences, what new products are feasibly commercialized, and what areas of research are most profitably funded next. Companies and publicly funded educational institutions both want to invest in workforce development, but each depends on the other to provide levels of education (for example, multi-year biological engineering degrees at public universities and weeks-long trainings on proprietary technologies and processes at life sciences companies). Without the public universities, companies would have a human resource shortage; without the companies hiring, public universities would be educating people, but without job prospects. These two sides can invest more efficiently in workforce development when they do it together.

“[T]he Life Sciences sector in Scotland is defined as a priority sector of economic significance by the Scottish Government and is, therefore, fast becoming one of the most effective places to develop innovations and commercial enterprises. The Life Sciences Scotland Industry Leadership Group (LSS ILG) works in partnership with Scottish Government, academia and health professionals to create an ecosystem where scientific endeavour leads to economic growth across the Life Sciences spectrum, producing more companies of scale with international growth potential.”

“[LSS ILG], is a joint industry, enterprise of agencies and government strategy teams. Their remit is to develop, drive and deliver the Life Sciences strategy in Scotland. By developing an environment where ingenuity and innovation can create jobs and wealth for Scotland, they aim to benefit the global community.”

“The LSS ILG is chaired by...Director of Government Affairs at Medtronic and co-chaired by...Minister for Trade, Innovation and Public Finance, and supported by...Minister for Public Health and Sport.”

“The LSS ILG consists of senior representatives from stakeholders across the spectrum of the Life Sciences community: CEOs and Directors from pharmaceutical, biotechnology, medical devices and diagnostics companies; research organisations and academic institutions; Scottish Enterprise, Highlands and Islands Enterprise, the Scottish Government and Scotland’s National Health Service.”

“The LSS-ILG has focused on tackling key issues important to the sector and industry. Theme subgroups across Business Environment, Innovation and Commercialisation, Sustainable Production and Internationalisation with additional representation from colleagues across the sector have come together to address these challenges.”

Source: Excerpted from the Life Sciences Scotland website (www.lifesciencesscotland.com) on July 9, 2022.

4

Conclusion

Most of the economic benefits from FDI have always come over the many years of each project's life, and not at the instant of announcement or start-up. With FDI, governments are seeking decades of wages, tax revenues, procurement from domestic companies, export earnings, skill and technology spillovers, and stimulation of sector development. The benefits come from the sustained successful operation of affiliates, which governments should nurture through robust retention and expansion support.

This note categorizes drivers according to their visibility (for example, planned versus unanticipated), leverage point (affiliate versus headquarters), and most influential actors (for example, the multinational itself, other market players, government, and the workforce). In this way, government officials can use them to identify divestment risks and approach the most influential players with tailored retention activities. A strong understanding of what drives divestments and an ability to discern harmful ones is a prerequisite to effective retention. Investment retention efforts should be strategic and systematic, with a combination of both proactive and responsive elements. The earlier a divestment risk is identified, the more time and options a government will have to do something about it. Governments need to have a suitable institutional set up, as well as a systematic approach and operating procedures to address the drivers of divestment, thereby retaining and perhaps expanding investment.

Indeed, the topic of divestment remains under-researched. Thus, more updated insights are needed through investor surveys and empirical research. Some ideas needing further exploration include: (i) the relative importance of factors that drive divestment; (ii) firm characteristics that can impact divestment decisions; and (iii) in the current context of multiple parallel crises, how these different crises have impacted divestment in host countries.



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