

# Investment Trends and Prospects in ASEAN

## Executive Summary

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*The views expressed in this report are those of the authors, and not necessarily those of the ASEAN Secretariat and/or the Australian Government.*

## *Executive summary*

### *Greater intra-ASEAN foreign investment can benefit all Member States*

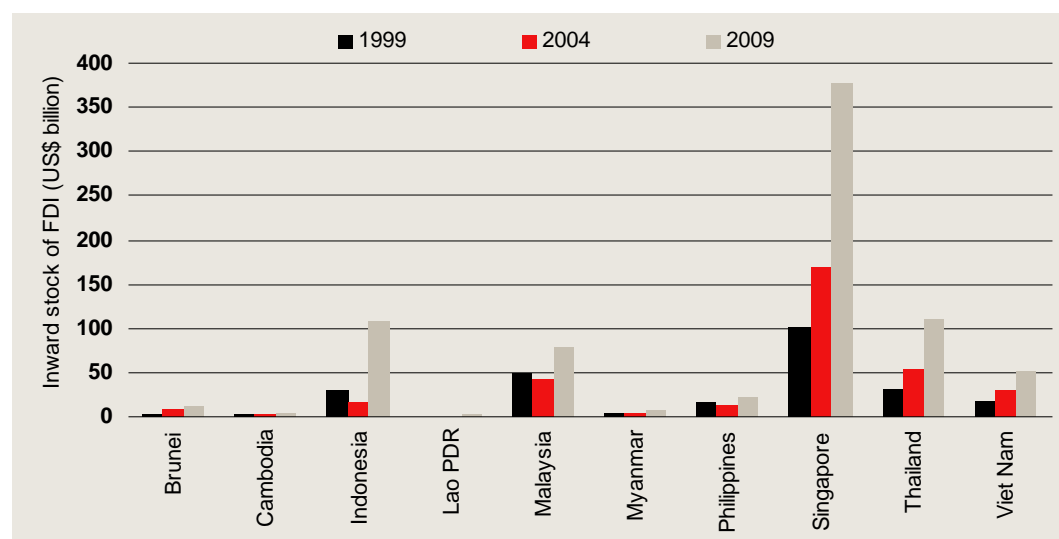
- **Greater intra-ASEAN foreign direct investment flows could benefit all ASEAN Member States, but in different ways. The benefits for each AMS are likely to depend on the level of development and domestic savings and investment patterns.**
  - High-income AMS generate significant excess savings. Reforms that make the lower and middle income AMS a more attractive place to invest would increase intra-ASEAN investment flows by attracting a greater share of the outflows from the high-income Member States. These reforms would be of significant benefit to investors from the high-income Member States.
  - The middle-income AMS also generate significant excess savings. However, evidence suggests that this is at least partly due to under-investment in those economies, relative to their level of development. Improving the domestic investment climate in these Member States would attract more of the foreign direct investment outflows from the high-income AMS, thereby increasing intra-ASEAN investment flows, as well as attracting more of the domestic savings pool.
  - The lower-income AMS have a significant savings shortfall. These Member States need to attract more of the foreign direct investment outflows from the high and middle-income Member States. Foreign direct investment from these Member States is also likely to bring the additional benefits of transferring technology and know-how.

### *Foreign direct investment in ASEAN Member States*

- **As of (the end of) 2009, the stock of foreign direct investment in AMS was valued at US\$772 billion, an increase of around 200 per cent over the 1999 figure of US\$255 billion. As can be seen from Figure 1 Singapore is the destination for the majority of FDI in the ASEAN region.**

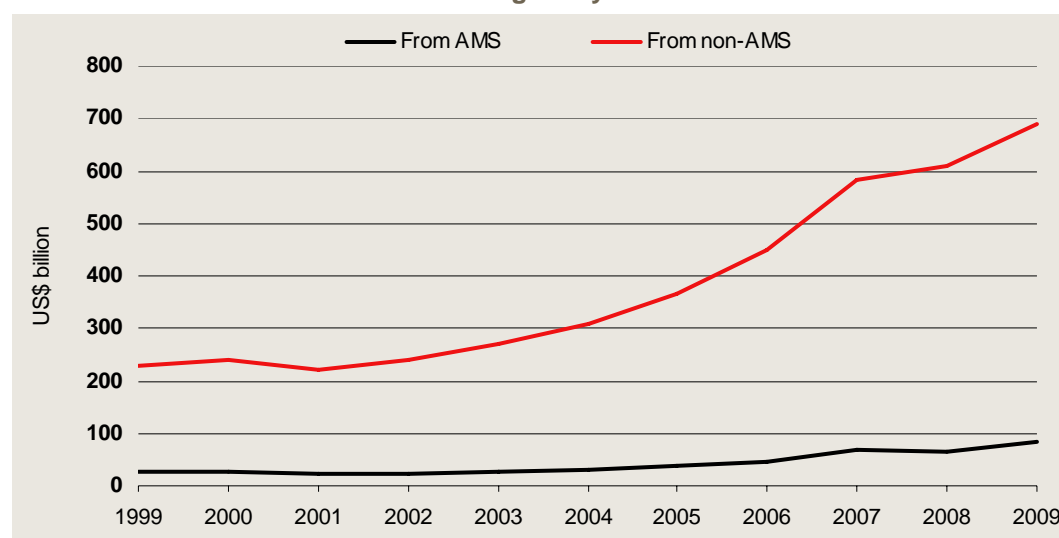
- The stock of FDI in AMS has primarily been sourced from countries outside of the ASEAN region, with the intra-ASEAN versus extra-ASEAN sourcing shares staying relatively constant over 1999 to 2009. From Figure 2 it can be seen that in 1999 some US\$27 billion (11 per cent) of the ASEAN region's FDI stock was sourced from AMS. By 2009 AMS accounted for US\$83 billion (11 per cent) of the region's FDI stock.

## 1 Value of the FDI stock in ASEAN Member States



Data source: Inward FDI positions as reported by Central Banks, Statistical Agencies or Investment Promotion Agencies of ASEAN Member States and CIE calculations.

## 2 Stock of inward FDI into ASEAN region by source

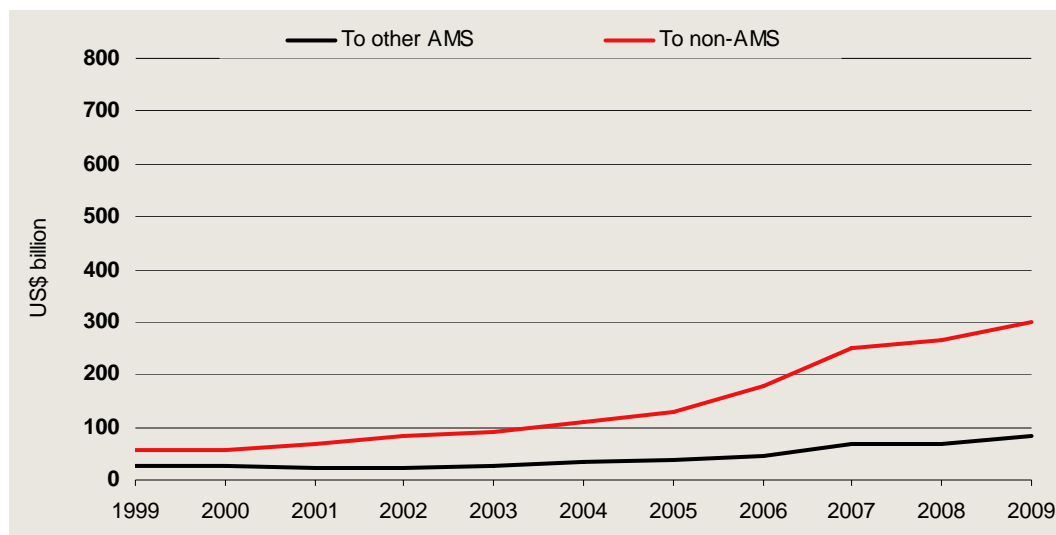


Data source: Inward FDI positions as reported by Central Banks, Statistical Agencies or Investment Promotion Agencies of ASEAN Member States and CIE calculations.

- While the majority of the ASEAN region's FDI stock has been sourced from non-AMS, as can be seen from Figure 3 the AMS are themselves sending a greater share of their outward FDI to

non-AMS. In 1999 AMS held FDI stocks worth US\$27 billion in other AMS, accounting for around 33 per cent of the region's outward FDI stocks. By 2009 AMS held FDI stocks worth US\$83 billion in other AMS, representing 22 per cent of the region's stock of outward FDI. Hence over time the AMS are directing a greater share of their outward FDI to non-AMS.

### 3 Stock of outward FDI from ASEAN region by destination

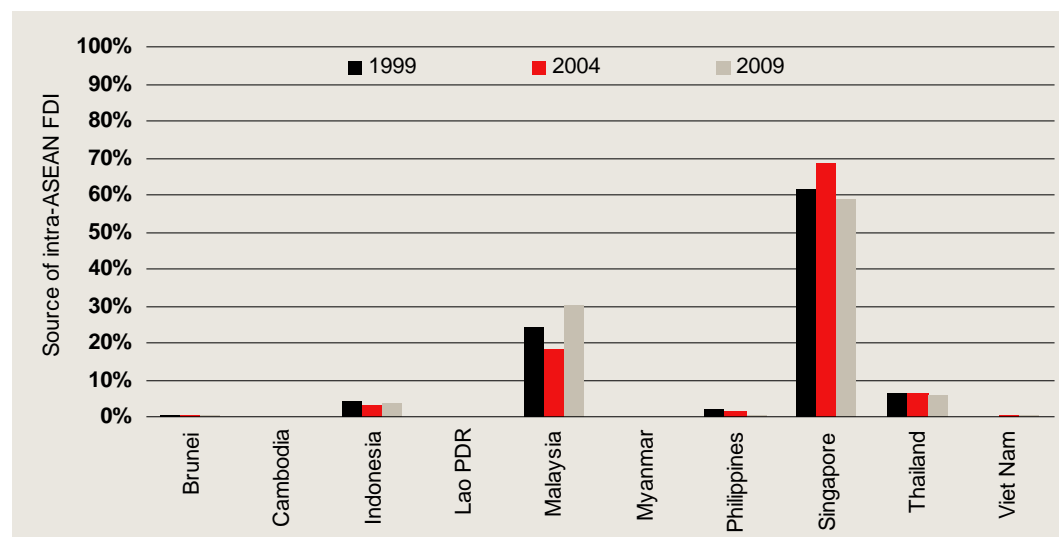


Data source: Inward FDI positions as reported by Central Banks, Statistical Agencies or Investment Promotion Agencies of ASEAN Member States and CIE calculations.

#### *Intra-ASEAN foreign direct investment*

- As can be seen from Figure 4, the intra-ASEAN FDI that is occurring is typically sourced from 2 Member States – Singapore and Malaysia. In 2009 these 2 Member States were the source of US\$74 billion of the US\$83 billion of intra-ASEAN FDI. If intra-ASEAN FDI is to be encouraged, and at least in the short term until the other AMS have further developed, then it will likely be a matter of encouraging Malaysian and Singaporean investors to invest in other AMS as opposed to investing in non-AMS.

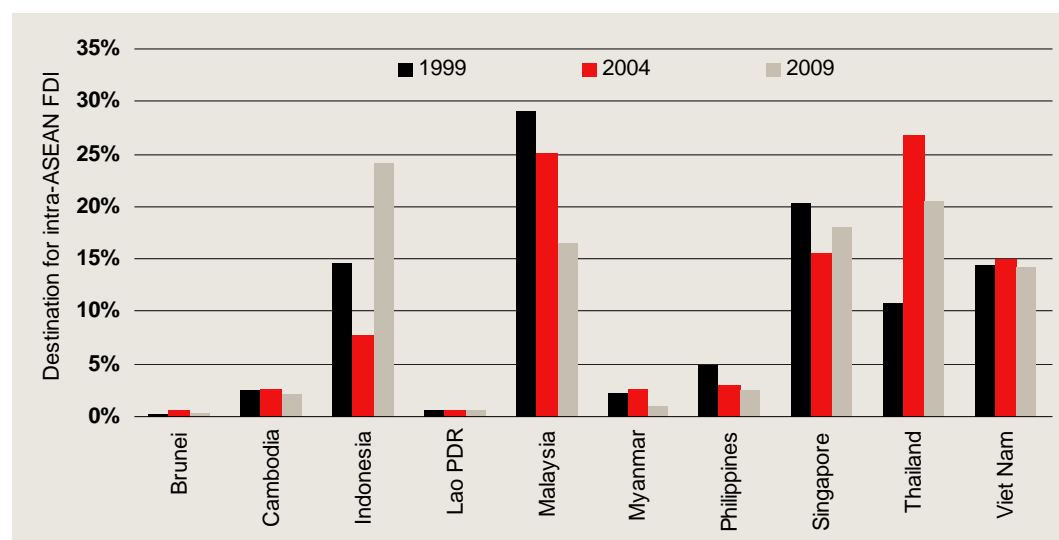
#### 4 Source of intra-ASEAN FDI stock



Data source: Inward FDI positions as reported by Central Banks, Statistical Agencies or Investment Promotion Agencies of ASEAN Member States and CIE calculations.

- While intra-ASEAN FDI is largely sourced from Malaysia and Singapore, the destination of that FDI is much more diversified. As can be seen from Figure 5, in 2009 the destinations of Indonesia, Malaysia, Singapore, Thailand and Viet Nam each accounted for (at least) 15 per cent of the intra-ASEAN FDI stock.
- There is currently very little ASEAN investment in Brunei, Cambodia, Lao PDR, Myanmar or the Philippines.

#### 5 Destination for intra-ASEAN FDI stock



Data source: Inward FDI positions as reported by Central Banks, Statistical Agencies or Investment Promotion Agencies of ASEAN Member States and CIE calculations.

### ***Stakeholder views on foreign direct investment***

- **Government agencies in all AMS consulted appear to have a highly favourable attitude towards FDI and were actively seeking foreign investors.**
  - The lower income Member States see attracting FDI as a key to economic growth and development, with the focus being on how they can attract as much investment as possible.
  - The middle income Member States tended to focus more on the quality of investment, as well as the quantity. This is likely to reflect that these Member States generate sufficient domestic savings to fund all of their investment opportunities, but could nevertheless benefit from better technology and know-how that can be accessed through FDI.
  - As a significant source of savings, stakeholders in Singapore tended to focus more on what other AMS could do to improve their investment climates.
- **Private sector investors generally reported that the investment climate in the ASEAN region was improving gradually over time. Investors were also impressed with the efforts of governments to engage with the private sector.**
- **The barriers to investment identified by stakeholders tended to vary, reflecting each Member State's unique political and economic circumstances. There were nevertheless some common themes. Often cited problems included (in no particular priority):**
  - poor transport infrastructure (extending to poor logistics);
  - poor/unreliable, or high cost, electricity infrastructure;
  - problems with implementing and enforcing contracts/laws (poor legal infrastructure);
  - high transaction costs arising from bureaucratic impediments and administration burden;
  - either a lack of transparency in regulations/laws, or a failure to implement said laws correctly (questionable conduct of bureaucracy);
  - corruption;
  - low productivity of the labour force and an absence of sufficiently skilled workers to undertake higher value-adding activities; and
  - long Sensitive Lists.
- **In general, the perception of government agencies in each Member State as to the greatest problems faced by investors broadly aligned with private sector views. This suggests that governments in the region have an understanding of the main barriers to investment in their country.**

### *Factors influencing the investment location decision making process*

- Survey results suggest that, ASEAN-wide, the 5 most important location offer factors influencing the investment location decision are the presence of suitably skilled/educated labour, economic stability, political stability (and an absence of sovereign risk), the availability of adequate utilities (power, water etcetera) at acceptable cost, and a well functioning investment incentive regime.
- The ASEAN region appears to get moderate location factor scores (6–7 out of a possible 10) in terms of those areas directly impacting on businesses — the availability of skilled labour, labour cost, access to export markets, openness to trade, adequacy of infrastructure etcetera. However, the region does not rate so well in terms of the institutions underpinning/supporting business activities and property rights. The legal system, law and order, local laws and regulations/red tape, and transparency in decision making all recorded averages scores of 5.3 or lower.
- Despite their cited importance, investment incentives are not a long term substitute for fundamental reform and correction of location offer shortfalls. Indeed, it may be a more cost-effective use of government funds to directly address investor cited deficiencies in the location offer rather than compensating investors for supposed deficiencies. Reform has the added advantage of aiding all sectors of the economy, and not just those select firms receiving incentives.

### *Impediments to getting investment operational*

- Even if the location offer is adequate, foreign investment may still be limited if investors experience difficulties in getting FDI approval and/or the investment operational.
- Nearly one-third of surveyed investors reported difficulties in getting their investment approved or operational. The top 3 reported impediments comprise difficulties associated with obtaining necessary operating licenses, interacting with government agencies, and corruption. For those investors experiencing difficulties in obtaining necessary operating licenses and

dealing with other government agencies, the problems experienced were severe (average scores of 7.7 and 7.4, respectively, out of a possible 10).

- Nearly two-thirds of survey respondents were able to identify (sometimes numerous) areas of needed improvement so as to enhance the investment environment. The most often cited needed improvements comprised better infrastructure (quality and cost), better government support, a reduction in administration burden and red tape, better transparency and reduced corruption, and better policy coordination and implementation.
- Investor knowledge of the various ASEAN integration measures was mixed. ASEAN-wide, investors appear to have quite good knowledge of the Trade in Goods Agreement and the ASEAN Economic Community initiative, but only moderate to poor knowledge of the other integration measures.
- Only 20 per cent of survey respondents believe that the AEC will be fully implemented by 2015. However, a large 56 per cent of investors believe that once implemented, the AEC will benefit their business while 65 per cent believe that it will improve the attractiveness of the region to FDI.

### *Initiatives to improve the environment for foreign investment*

- Initiatives to be undertaken over the short term so as to address impediments to getting FDI approved and operational would see the AMS (in order of priority):
  - reducing the difficulty associated with investors obtaining necessary operating licenses. This should extend to reviewing the need for some licenses in the first place;
  - reviewing the approach taken by other government agencies in their dealings with investors with the objective of improving interactions; and
  - improving the transparency in decision making by moving to a rules based approach to decision making and eliminating the ability of public officials to make discretionary/ad hoc decisions, in so doing reducing the opportunity for corruption.
- A fully implemented AEC appears to be highly valued by investors, yet investors are pessimistic about the AEC being implemented by the planned 2015. Given this, a priority of the AMS and Secretariat should be to ensure that the AEC is fully implemented by 2015, or sooner if possible.



- **Not all location offer reforms are suited to being addressed by ASEAN on an ASEAN-wide basis, rather, some reforms can only be addressed through a Member State acting alone. It is thought that ASEAN could play a role in implementing reform in the location offer factors of:**
  - access to regional and other export markets
  - openness to trade and investment
  - size of investment incentives provided
  - transparency in decision making, absence of corruption
  - access to cheap labour
  - access to labour with necessary skills/education
  - access to raw materials and production inputs.
- **Other location offer improvements are better suited to individual Member State initiatives.**
- **Matching prioritised location offer reforms with those seemingly best placed to be addressed at the ASEAN level suggests that ASEAN should initially be targeting reforms/measures to address:**
  - improving access to materials and openness of the region to trade and investment;
  - improving transparency and moving towards rules based decision making; and
  - improving the free flow of skilled labour.
- **There are several no regrets reforms/measures that AMS and the Secretariat should consider implementing irrespective of reforms elsewhere. These include:**
  - measuring progress in implementing signed agreements and outcomes actually achieved (an initiative that can be done over the short term);
  - establishing a process for the formal review of sectors placed onto Member States' Sensitive Lists (a medium term initiative); and
  - a best practice investment incentive regime (a longer term initiative).