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The Evolving Role of Southeast Asia in Global FDI Flows

Stephen Thomsen, Misuzu Otsuka and Boram Lee

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Center for Asian Studies

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Executive summary

This paper traces the evolution of FDI in ASEAN and discusses future prospects for the region as a host – and increasingly home – to FDI. Southeast Asia has long been a focal point for FDI by OECD-based firms. Some prominent countries in the region were among the first to pursue a strategy of export-led development based partly on FDI. They were in the right place at the right time – and with accommodating policies – to welcome firms from Japan and the newly industrializing economies such as Chinese Taipei as these firms faced currency appreciation and rising wages at home. They also attracted investment from the rest of the OECD, notably the United States and Europe. As a result, in the 1990s Southeast Asia was collectively among the world's largest recipients of FDI.

Attention shifted away from Southeast Asia following the regional economic collapse of 1997-1998 and the slow recovery that ensued. Other emerging economies also began to imitate the successful policies of the take-off period in Southeast Asia as part of a more general shift worldwide from import substitution to export promotion. Fear of losing investment to other countries, notably China, has been one of the drivers of further regional integration within ASEAN.

Policy reforms implemented at the national level after the Asian crisis have made many ASEAN states much more resilient against shocks, as evidenced by the relatively good performance of parts of Southeast Asia during the recent global economic crisis. ASEAN as a group has also stepped up efforts to improve the regional investment climate. ASEAN member states signed the ASEAN Comprehensive Investment Agreement in 2009 and have been working to establish the ASEAN Economic Community by 2015, which promises to transform ASEAN into an integrated region with free movement of goods, services, investment, skilled labor and a freer flow of capital.

Compared to the trends in the 1980s and 1990s, recent FDI flows are increasingly more diversified in terms of host and source countries. Not only have traditional investors in ASEAN such as Japan spread their investment more widely in the region, but as relatively advanced ASEAN countries have upgraded their technologies, gained more experience in the international market and built up foreign reserves, they are also emerging as outward investors, especially at the regional level. Although lagging behind the progress in intra-ASEAN trade flows, intra-ASEAN FDI has been growing gradually since the Asian crisis. Perhaps somewhat surprisingly,

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ASEAN economies have invested a larger amount abroad over the past decade than either China or India.

At the same time as it is possible to detect a major positive trend in FDI inflows to Southeast Asia and in the region's overall economic development, it is important to bear in mind that this trend is not uniform. Not all countries in the region are equally coveted as investment destinations by multinational enterprises and many of those which are on investors' radar screens could potentially receive even more FDI.

An analysis of investment trends by itself gives little idea of how investment in the region is evolving. Other information on the activities of foreign investors in ASEAN suggests that they are increasingly focusing on the regional market. Local markets still account for the largest share of sales of affiliates, but regional sales are growing faster than exports to the home country of the investor. This suggests that competition for global FDI will in the future depend as much on the appeal of the ASEAN market itself as it will on the costs of production and related factors.

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Introduction

The countries of Southeast Asia were among the first to pursue a strategy of export-led development based partly on foreign direct investment (FDI). They were in the right place at the right time – and with accommodating policies – to welcome firms from Japan and the newly industrializing economies such as Chinese Taipei, as these firms faced currency appreciation and rising wages at home. They also attracted investment from the rest of the OECD, notably the United States and Europe. As a result, in the 1990s Southeast Asia was collectively among the world's largest recipients of FDI.

Attention shifted away from Southeast Asia following the regional economic collapse of 1997-1998 and the slow recovery that ensued. Having gained a reputation for sound economic policies and rapid growth before the crisis, the shock of 1997 left a legacy of negative perceptions about the region's growth potential. Other emerging economies also began to imitate the successful policies of the take-off period in Southeast Asia as part of a more general shift worldwide from import substitution to export promotion. Fear of losing investment to other countries, notably China, has been one of the drivers of further regional integration within the Association of Southeast Asian Nations (ASEAN)[1].

Policy reforms implemented at the national level after the Asian crisis have made many ASEAN states much more resilient against shocks as evidenced by the relatively good performance of parts of Southeast Asia during the recent global economic crisis. In those countries most affected in terms of FDI inflows by the global crisis, Singapore and Malaysia, recovery has been as swift as the initial decline. Having rejected a "beggar thy neighbor" protectionist option in 1997-1998, Southeast Asian countries have continued to resist such temptations during the recent crisis. They are now pursuing further economic reforms, including improving their investment environments. This process, already under way before the current global economic crisis, has intensified as countries compete for FDI to help them maintain growth.

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[1] ASEAN includes Brunei, Cambodia, Indonesia, Laos, Malaysia, Myanmar, Philippines, Singapore, Thailand and Vietnam.

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ASEAN as a group has also stepped up efforts to improve the regional investment climate. ASEAN member states signed the ASEAN Comprehensive Investment Agreement in 2009 and have been working to establish the ASEAN Economic Community by 2015 which promises to transform ASEAN into an integrated region with free movement of goods, services, investment, skilled labor and a freer flow of capital.

A return to growth that has proved resilient in the face of the recent global economic crisis, among those countries most affected by the 1997-1998 crisis, together with continuing efforts to enhance regional integration, suggests that a reassessment of the region's potential as both a recipient and also increasingly a source of FDI is now in order.

This study uses recent FDI statistics to trace the revival in the region's fortunes as an attractive environment for foreign investment. Data on multinational enterprise (MNE) activities in the region are also used to assess the degree of integration already achieved both within the region and with the global economy more generally. Multinational enterprises from OECD countries have invested over USD 320 billion in ASEAN – more than the same firms have invested in China and India combined. Their activities in the region provide insights into the evolving role of ASEAN in global production networks.

Compared to the trends in the 1980s and 1990s, recent FDI flows are increasingly more diversified in terms of host and source countries. Not only have traditional investors in ASEAN such as Japan diversified their investment destinations, but as relatively advanced ASEAN countries have upgraded their technologies, gained more experience in the international market and built up foreign reserves, they are also emerging as outward investors, especially at the regional level. Although lagging behind the progress in intra-ASEAN trade flows, intra-ASEAN FDI has been growing gradually since the Asian crisis. This study also looks at the emerging tendency of Southeast Asian countries to become sources of capital, initially on a regional basis but ultimately to the rest of the world. Perhaps somewhat surprisingly, ASEAN economies have invested a larger amount abroad over the past decade than Brazil, China, and India.

At the same time as it is possible to detect a major positive trend in FDI inflows to Southeast Asia and in the region's overall economic development, it is important to bear in mind that this trend is not uniform. Asia is the most diverse continent in the world, including in terms of cultural differences, level of economic and social development, political and institutional regime, and hence income disparities, and Southeast Asia is a microcosm exemplifying that diversity.

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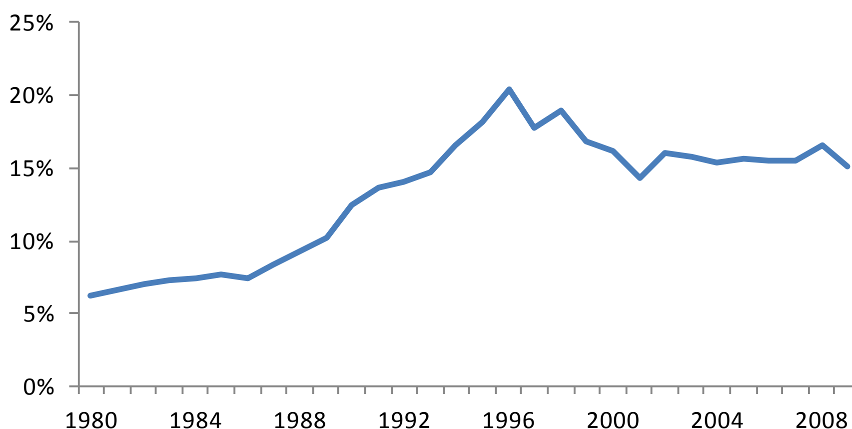
Southeast Asia's long-term performance in attracting FDI

ASEAN countries have never fully recovered from the shock of the Asian financial crisis in terms of their share of total FDI flows to developing countries, but they have continued to see rising levels of both investment and employment by foreign investors. In Indonesia, for example, FDI inflows reached historic levels in 2010, at a time when global flows are still heavily affected by the recent crisis.

Southeast Asia's early success in attracting FDI was primarily as an export platform for markets elsewhere. With the possible exception of Indonesia, markets were too small to attract much market-seeking investment, particularly Singapore and Malaysia. Regional integration at the time was also insufficient to entice investors on the basis of a regional market. In spite of these drawbacks, the export platform strategy was immensely successful. The region has become well integrated into the world economy by becoming a global production platform, and there has been a rising influx of FDI since the late 1980s in export-oriented and primary industries. The ASEAN share of the total stock of FDI in developing countries (excluding tax havens in the Caribbean) grew without interruption from under 8% in 1986 to over 20% in 1996, even with the emergence of China after 1991 (Figure 1). The Asian crisis put this process into reverse, but the ASEAN share of developing country FDI quickly stabilized at around 15%.

Figure 1: ASEAN share of inward stock of FDI in developing countries*



*Excluding Caribbean tax haven countries.

Source: UNCTAD.

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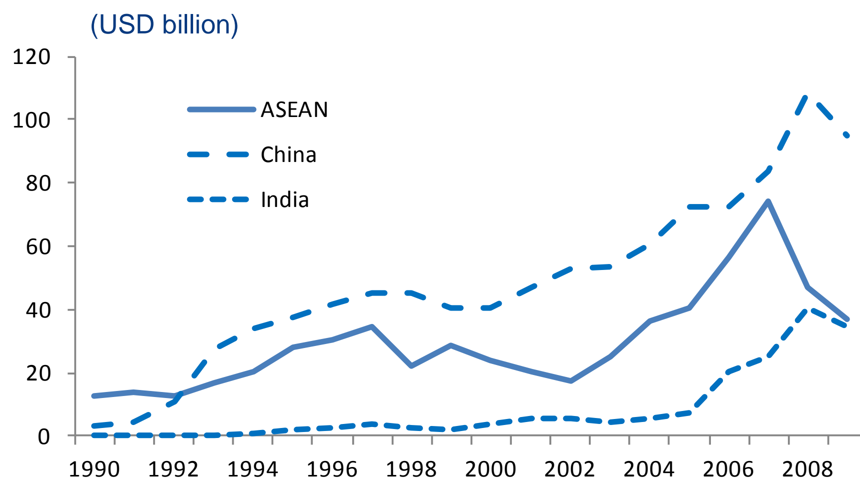
As part of their crisis management in 1997-1998, ASEAN countries initiated reforms in FDI laws and regulations as they opened further to foreign investment, albeit often on a selective basis. When international investment activity started to increase again in 2003, ASEAN countries were ready to attract foreign capital. Foreign direct investment in the region has nevertheless failed to return to its leading role as a host for FDI among developing countries. Meanwhile, the ASEAN countries' share of world GDP has recovered to the pre-Asian crisis position, reaching 2.5% of world total GDP.

The rise of China and India and its impact on FDI in ASEAN

China is often seen within ASEAN as a competitor for FDI. Indeed, total FDI inflows into China since the early 1990s have exceeded by a wide margin those going to ASEAN (Figure 2). China emerged in the 1990s as a magnet for FDI with its large and dynamic market and low costs of production. In terms of FDI trends, rising inflows to both China and India have been matched by growing FDI inflows to ASEAN. Only the 1997-1998 crisis and then again the global crisis after 2007 appear to have had any adverse effect on inflows into the region. Although many ASEAN countries saw a decline in flows in 2008-2009, much of the downturn can be explained by the fortunes of Singapore and Malaysia, the two countries in the region most affected by the global crisis. Some countries such as Vietnam in 2008 and Indonesia in 2010 saw record FDI inflows.

Figure 2: FDI inflows to ASEAN, China and India from all investors



Source: UNCTAD.

There are many reasons why China's rapid rise as an attractive FDI destination is not likely to have crowded out FDI into ASEAN. In the first place, much of the investment in China has come from

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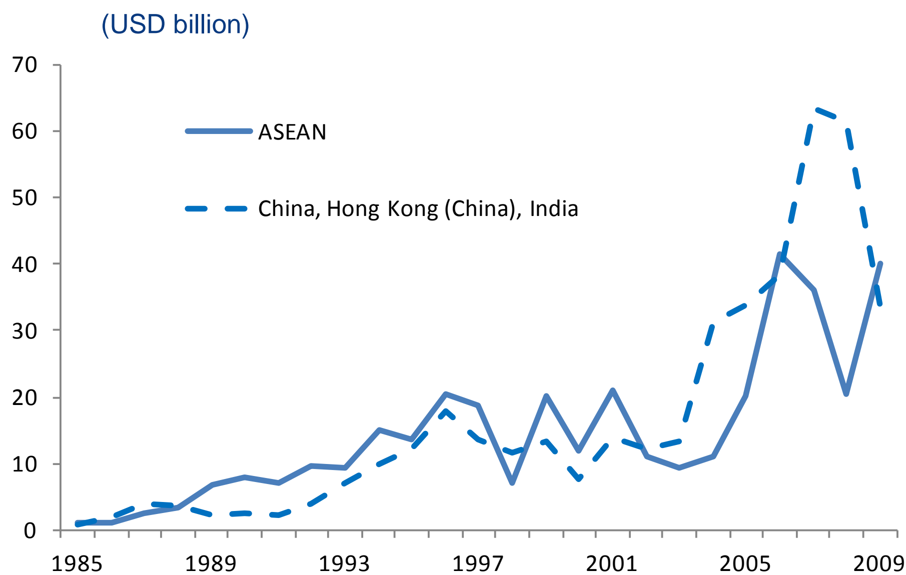
Hong Kong (China) and Chinese Taipei where cultural similarity and geographical proximity lower transactions costs for investors. For some of these firms, the choice is not between China and ASEAN but between producing at home or in China. For OECD investors, the evidence suggests that, at least until 2007, FDI flows to ASEAN and to other emerging economies have largely been synchronized. This in itself does not prove that investment diversion has not occurred, but it does put its potential importance in perspective. Figure 3 compares total FDI inflows into ASEAN from OECD countries with that going to China, Hong Kong (China) and India.

Figure 3: FDI flows to countries in Asia by OECD-based investors

(USD billion)



Source: OECD International Investment Statistics Yearbook.

Econometric studies such as Plummer and Lee (2004) and Cheong and Plummer (2009) reject the hypothesis that China has had any statistically-significant bearing on outward investment from OECD countries to ASEAN. Rather, they conclude that "China's success in attracting FDI has actually helped ASEAN (and other Asian) countries by attracting complementary FDI"[2]. As argued in Thomsen (2004, p. 82), "FDI is not a zero sum game, with one country gaining at the expense of all others. Investment in China can stimulate greater FDI throughout East Asia, acting like a regional magnet for investors much as Singapore has done within ASEAN."

Both China and ASEAN have invited investment projects complementary to each other and have joined the same global production networks of MNEs. As China strives to shift towards a more domestic demand-driven economic model and Chinese wage levels increase, new opportunities may present themselves to ASEAN in terms of both

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[2] Cheong and Plummer (2009), p. 14.

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attracting global FDI flows and investing in China. To capture these opportunities and utilize FDI towards its developmental goals, ASEAN has to adjust its economic policies and develop beneficial linkages between MNEs and local enterprises.

The trend in Figure 3 is not the result of any group of OECD investors but tend to be common to individual OECD countries as well. Figure 4 shows FDI flows from the United States, Japan and Korea to both ASEAN and China. All three OECD member countries are actively involved in China, but in each case investments in ASEAN are also growing, particularly over the past few years.

For Korean firms, ASEAN is the third largest investment partner after China and the United States. In late 2005, the governments concerned announced a plan to launch Korea-ASEAN FTA negotiations. This helped to trigger increased interest by Korean investors in ASEAN countries. Figure 4 shows a sharp upturn in Korean direct investment in Southeast Asia from 2005, similar to the rise in FDI flows from Korea to China four years earlier. Traditionally, Korean investors have focused on labor-intensive manufacturing and the primary sector, accounting for about 60% of total FDI from Korea to ASEAN in 2008. While both sectors still dominate Korea's FDI inflows into ASEAN, these are now becoming more diversified to include real estate, services (finance and insurance, information technology services) and construction. This shows that Korean companies, including the large conglomerates (*Chaebol*), have now started focusing on market-seeking investment in ASEAN countries.

To convey a greater sense of what these OECD investments represent in tangible terms, Figure 5 shows total employment in majority-owned, non-bank affiliates of US MNEs and in affiliates of Japanese MNEs in ASEAN, China and India. Employment in China by US MNEs is growing most quickly, but it is also growing in both India and ASEAN – rising by 400,000 over two decades in ASEAN as a whole. As a percentage of the total labor force, US investors employ far more workers in ASEAN than in either China or India. Japanese MNEs employ more workers than their US counterparts in both China and ASEAN which is not surprising given the greater geographical proximity. Employment by Japanese MNEs in ASEAN has risen by roughly 50% since 1998, while more than tripling in China.

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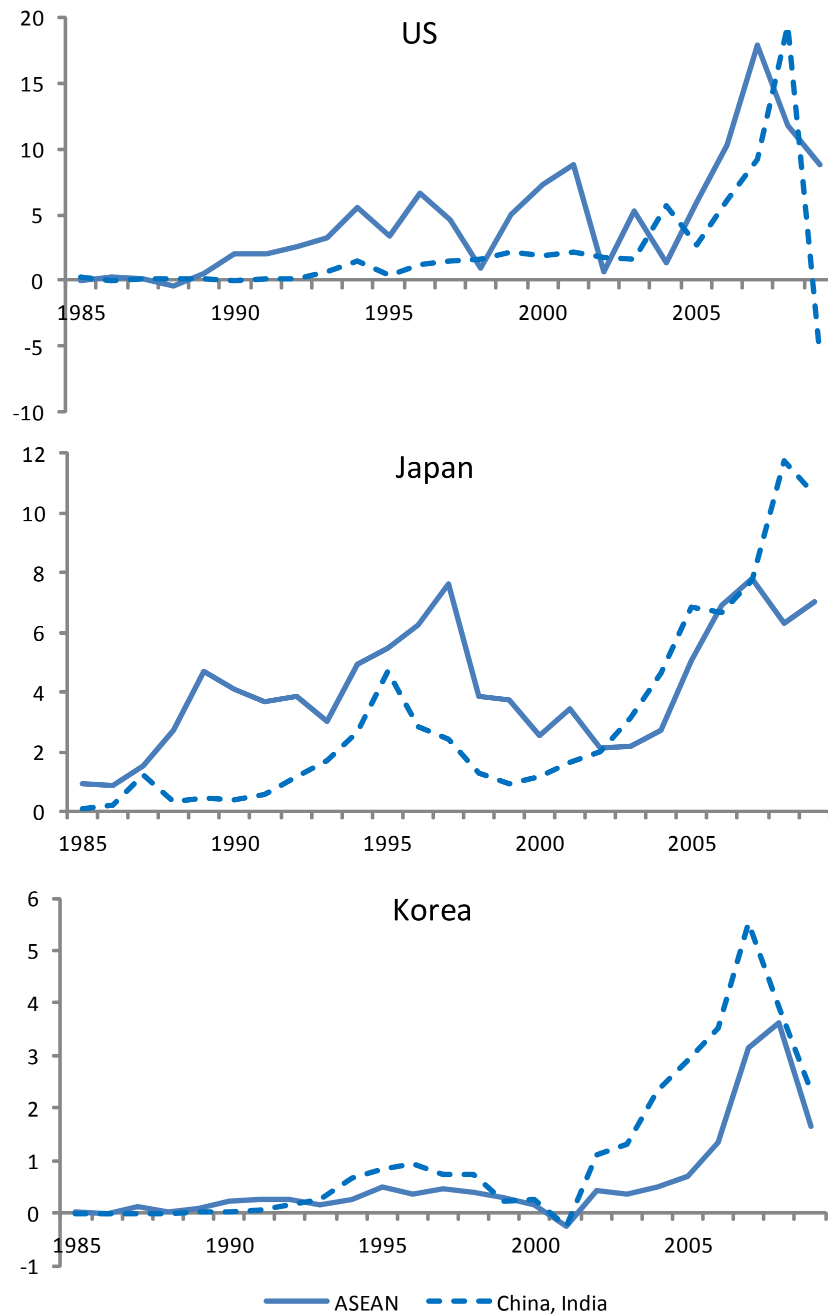
Figure 4: FDI in ASEAN, China and India from selective OECD countries (USD billion)



Source: OECD.

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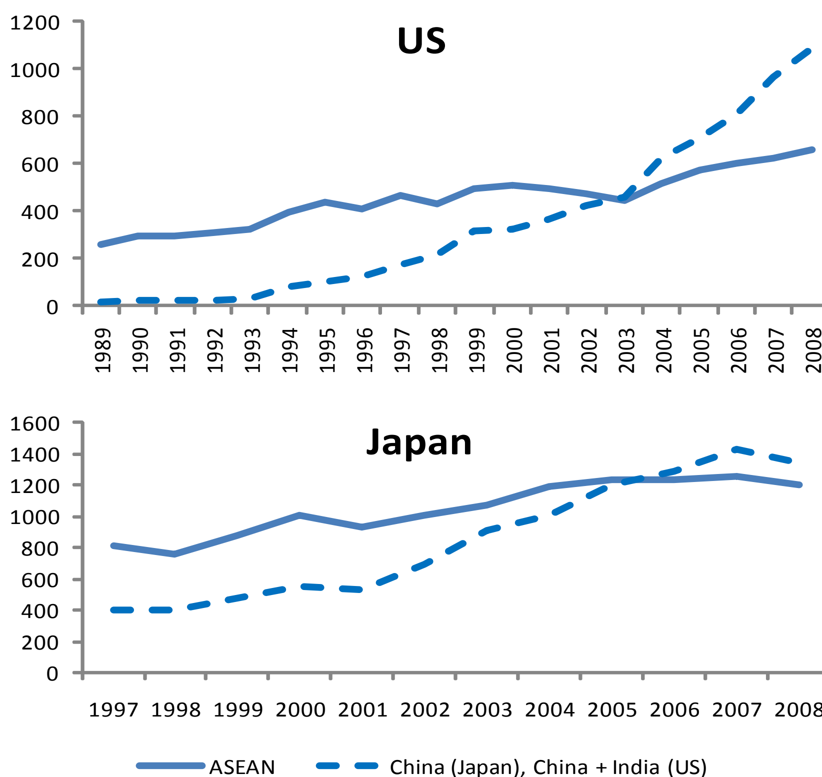
Figure 5: Employment by US and Japanese MNEs in Asia
(thousands)



Source: Bureau of Economic Analysis, US Department of Commerce.

FDI plays a larger role in ASEAN than in other emerging economies

FDI has been a particularly important source of capital and technology to the ASEAN region and has played a leading role in promoting sustainable economic development. The share of FDI in gross fixed capital formation (GFCF), generally between 15% and 23% since the Asian crisis, has been far larger than in other developing countries (Figure 6). For both China and India, for example, FDI shares in GFCF have remained well below 10% over the past decade. Furthermore, the share in China has been in secular decline since the mid-1990s, as inflows have not kept pace with the expansion of the economy.

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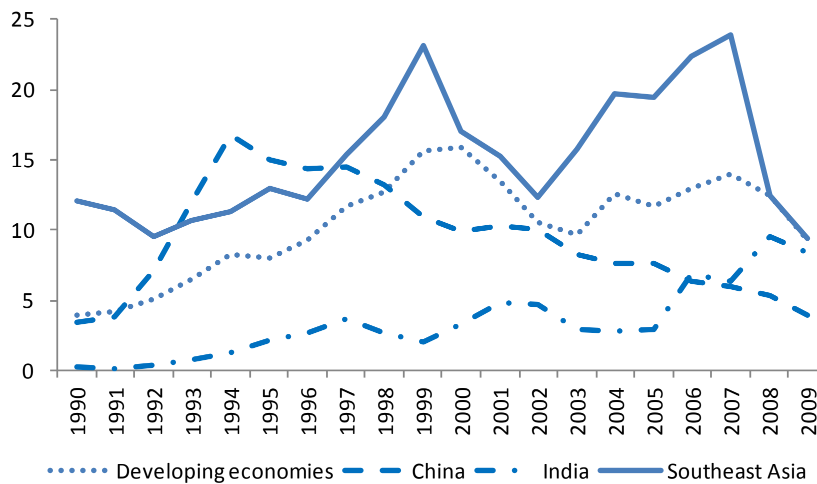
Figure 6: FDI inflows in ASEAN, China and India

(% of gross fixed capital formation)



Source: UNCTAD.

Singapore's unique role

Singapore has received 45% of total inflows to ASEAN since 1990, followed far behind by Thailand and Malaysia and then Indonesia and Vietnam (Figure 7). The Philippines continues to receive a smaller share of the total than its population size would lead one to expect. Cambodia and Laos take in a very small share of the total, although these investments may be significant relative to the size of their economies.

Some of the investment into Singapore is then channeled to other countries in the region. Looking instead at employment by US MNEs in ASEAN, it can be seen that both Singapore and Malaysia have seen little change in employment levels since the early 1990s, while Indonesia, Thailand and the Philippines have seen sharp and continuous growth (Figure 8). Surprisingly given its importance in recent inflows in ASEAN, Vietnam has not seen a similar takeoff in US affiliate employment. The important point is that rising employment by foreign affiliates in these countries does not appear to have come at the expense of employment in other ASEAN member states. To the extent that there has been an impact, it appears to be on *growth* in employment in the richer countries.

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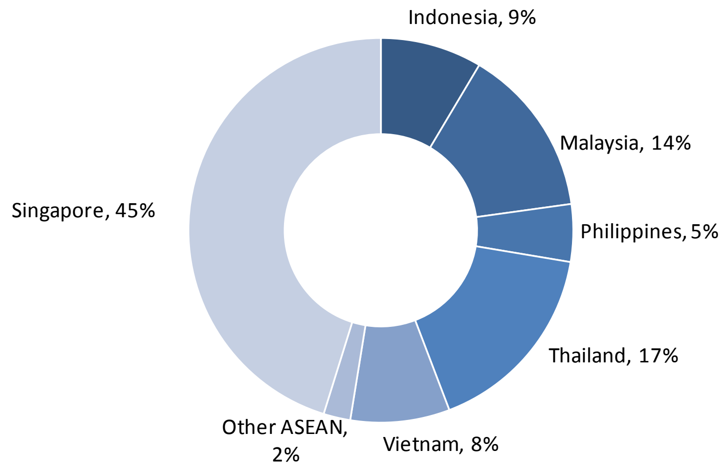
Figure 7: Cumulative FDI inflows in ASEAN 1990-2009, distribution by country

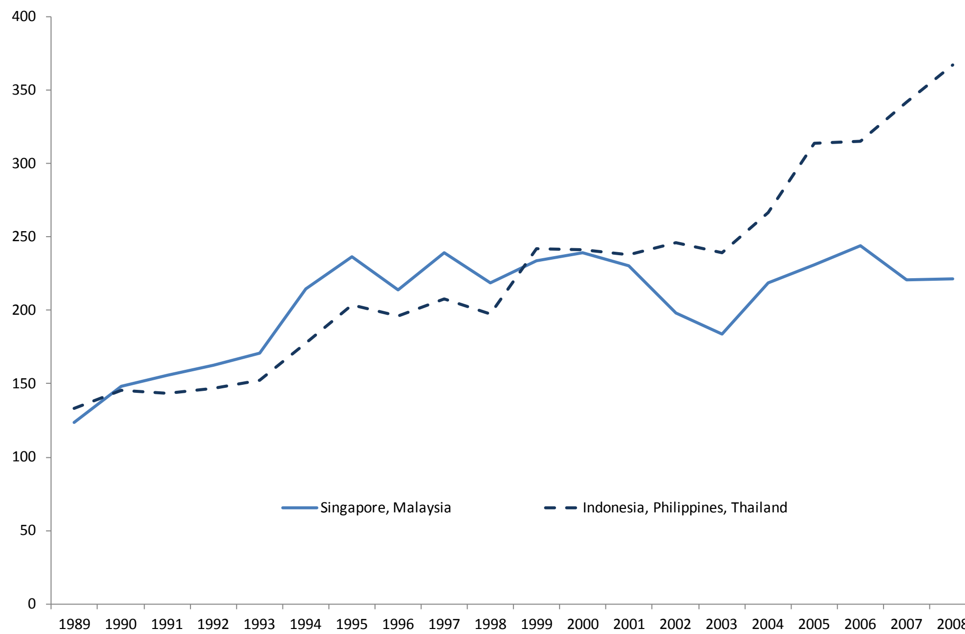
(share of total inflows to all ASEAN member states)



Source: World Bank.

Figure 8: Employment by US non-bank MNEs in ASEAN

(thousands)



Source: Bureau of Economic Analysis, US Department of Commerce.

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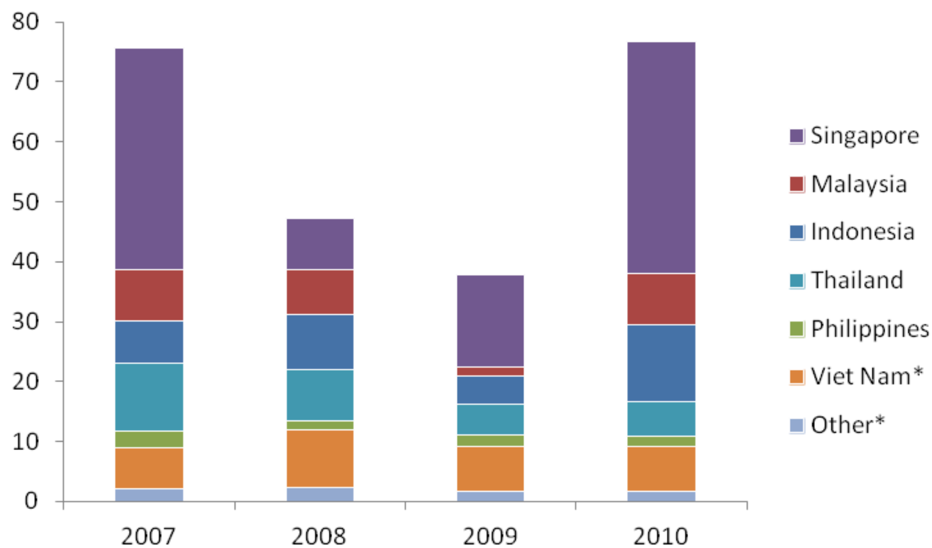
Southeast Asia's performance during the most recent global crisis

The subprime crisis began in mid-2007 in the United States and then developed into a global economic recession. As a result, world FDI flows plunged from their 2007 peak by 14% in 2008 and 39% in 2009[3] As a result of the varying degrees of external economic dependency and market liberalization within the region, ASEAN countries experienced uneven shocks from the global crisis. Economies depending more on external demand such as Singapore and Malaysia suffered from a larger loss in FDI inflows while relatively large economies depending more on internal demand such as Indonesia, the Philippines and Vietnam were less adversely affected (Figure 9). Recovery was swift: the sharp drop in FDI inflows into ASEAN in 2008-2009 was matched by a dramatic rebound in 2010. Total inflows in 2010 have returned roughly to the level in 2007 which itself had been an historic peak for inflows. Indeed, even cautiously assuming that inflows into Vietnam and the smaller ASEAN members remained unchanged in 2010, ASEAN may well have received historic FDI inflows, at a time when global flows are still recovering from the global crisis. It is already apparent that Indonesia, Malaysia and Singapore all received record inflows in 2010.

Figure 9: Recent FDI Inflows to ASEAN Economies (USD million)



*2010 estimates for Vietnam and Other are based on the assumption of no change with 2009.

Source: ASEAN and national sources.

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[2] UNCTAD, World Investment Report.

In spite of these variations in the response to shocks, the region's economies do have some common features. ASEAN FDI flows as a whole collapsed in 2008 because of ASEAN's (1) relatively high integration with the global economy in terms of both trade and investment, (2) high reliance on developed countries' external demand as a result of export-oriented policies and (3) the impact of the global crisis on Singapore, which absorbs the lion's share of ASEAN's FDI inflows and is the largest source of intra-ASEAN FDI flows. Despite some anecdotal evidence of rising protectionism and economic nationalism globally, ASEAN countries have not resorted to further restrictions in their FDI.

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The future prospects for ASEAN as a location for FDI

Foreign investment in ASEAN is evolving: new destinations within the region are appearing on investors' radar screens; ASEAN-based investors are starting to invest in other markets within the region; new investors are arriving from other emerging markets; the sector of investment is becoming more diversified; and the strategies of investors are evolving away from simple export platform strategies towards a more sophisticated approach which places greater emphasis on the regional market. This section reviews these trends before turning to a discussion of how regional integration and bilateral investment agreements are helping to shape the policy environment. Differences in FDI performance within ASEAN are discussed in Annex.

FDI flows to ASEAN by country of origin

Most FDI in ASEAN originates in OECD countries, but inflows from Asia, including from within ASEAN itself, are growing. Somewhat compensating for the negative impact of the external shock, ASEAN countries have deliberately strengthened their mutual economic cooperation to diversify their sources of inward FDI. As a result, intra-ASEAN investment has recently increased, becoming the second largest source of FDI in ASEAN in 2007 and the largest in 2008. The ASEAN share of inflows declined in 2009. Firms based in Singapore and Malaysia, in particular, have become major foreign investors within the region.

Ascertaining the exact origin of FDI inflows into ASEAN is difficult for two reasons. First, a significant amount of investment is reported as originating in offshore financial centers and tax havens: firms from the Cayman Islands and Bermuda have together invested over USD 18 billion in ASEAN over the past four years. This investment usually originates from third countries or sometimes even the host country itself. Second, intra-ASEAN investment includes an unknown portion of flows from ASEAN-based affiliates of MNEs from OECD countries. These firms might, for example, invest in the region through their regional headquarters in Singapore, which would often show up as investment in Singapore rather than in the final destination. This can be seen, for example, from the fact that

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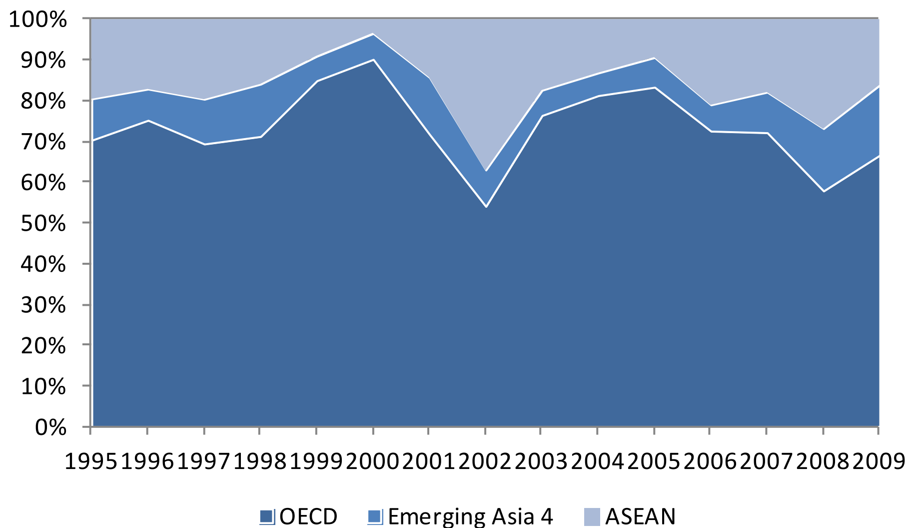
Singapore receives almost two thirds of total US FDI in ASEAN but accounts for only one third of the value added of US-owned affiliates in the region.

Figure 10 shows the origin of inflows, excluding offshore financial centers and countries not shown separately. In spite of fluctuations over time, there is very little discernible trend in the shares of investment coming from OECD, Asian and ASEAN countries since 1995. Over the whole period, OECD investors have contributed 73% of total inflows, with the rest coming from non-OECD Asia (10%) and ASEAN itself (17%). Among new investors, FDI from China and India is growing rapidly and has averaged almost USD 3 billion annually since 2007.

Figure 10: FDI flows to ASEAN by country/region

(share of total inflows, excluding offshore financial centers)



Emerging Asia: China, Chinese Taipei, Hong Kong (China), India.

Source: ASEAN.

Among OECD investors, firms from EU countries have invested almost twice as much as US and Japanese firms combined since 1995, but firms from all three regions are major and long-standing investors in ASEAN. Unlike in other emerging regions, where FDI inflows tend to be dominated by the closest OECD country or region, Southeast Asia has always been a crossroads for investors, much as it was for traders in earlier centuries. This diversity is a source of both stability and strength.

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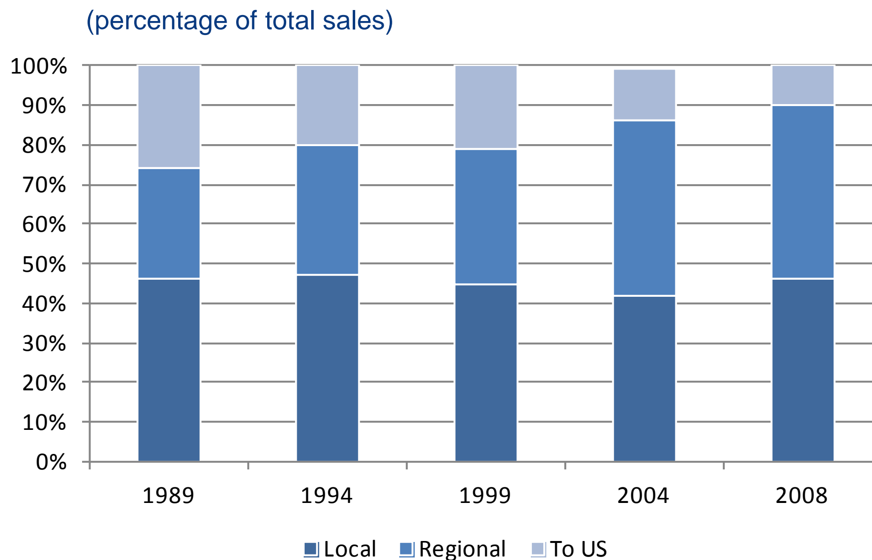
Evolving MNE strategies in Southeast Asia

Although Southeast Asian countries are considered to be among the earliest and most successful cases of export platforms within global MNE value chains, their appeal has always been partly based both on national markets and on the regional market itself. Over time, national markets remain important, but the fastest growing segment of sales is to the region itself, reflecting the growing degree of integration within ASEAN.

Figure 11 shows sales patterns of US affiliates in ASEAN over two decades. Local sales (to the national market) represent just under one half of sales, a share which has changed very little over time. What has evolved is the distribution of exports. In 1989, exports were evenly divided between the home US market and the rest of the world. By 2008, only 10% of sales were back to the US market; the rest were to other countries, principally within the region itself.

Figure 11: Destination of sales of US majority-owned affiliates in ASEAN*

(percentage of total sales)



Source: Bureau of Economic Analysis, US Department of Commerce.

Affiliates of Japanese MNEs in ASEAN show a similar sales pattern, with almost one half of sales going to the local market. Of affiliate exports, a higher share is sent back to the home market than was the case for US MNEs, as can be expected given the closer proximity of Southeast Asia to the Japanese market. But twice as many exports are sent to third markets, with presumably a high share going to other countries in the region. The export propensity of affiliates varies by country, and is particularly high in the Philippines,

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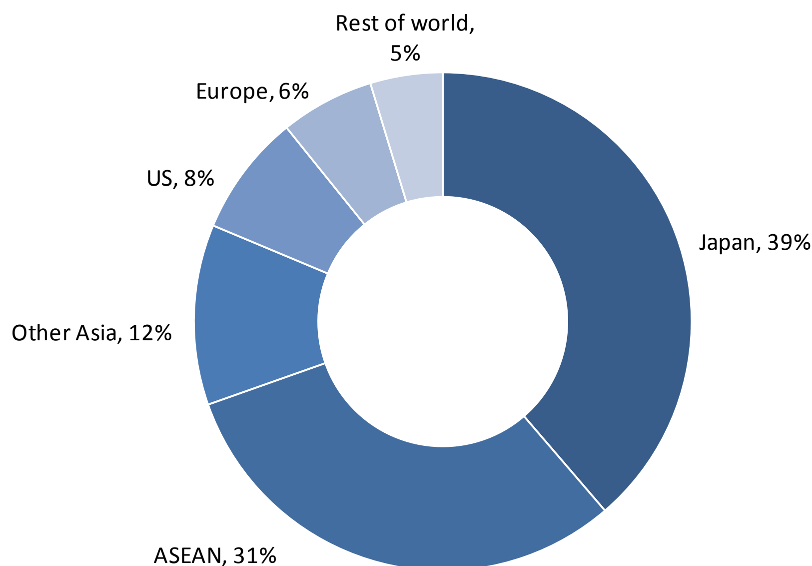
followed by Singapore and Vietnam. Japanese investors in other major ASEAN countries are more interested in the local market.

Figure 12 shows the destination of export sales by Japanese manufacturing affiliates in ASEAN. Export propensities tend to be higher in manufacturing than in other sectors, with one half of affiliates surveyed exporting 70% or more of their output. The largest export market is Japan, particularly for affiliates in Vietnam, the Philippines and Indonesia. Almost one third of exports are to other ASEAN countries or 45% for affiliates in Singapore – demonstrating once again the key role that Singapore plays within the ASEAN market for foreign investors. With only 14% of exports flowing to the European and US markets, Japanese manufacturing firms are clearly not yet using ASEAN as an export platform to supply these OECD markets. For both US and Japanese investors, ASEAN-based affiliates supply predominantly the regional (including local) market and to a much lesser extent the home market but not the global one.

Figure 12: Exports of Japanese manufacturing affiliates in ASEAN by destination



Source: JETRO.

The growing role of the regional market and the importance of further economic integration

Given the growing importance of the regional market, it is instructive to compare the size and characteristics of the ASEAN market with those of other emerging markets. Figure 13 shows the importance of ASEAN as an economic bloc and in terms of wealth, exports and FDI inflows compared to other major emerging economies. Its economy is roughly the size of the Russian one, and between those of Brazil and

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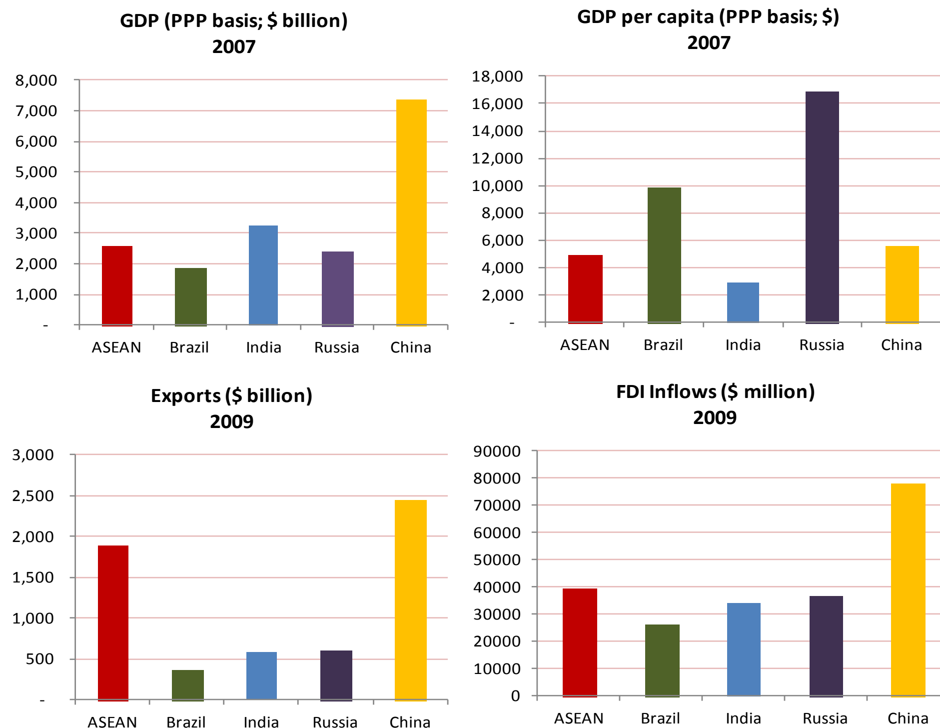
India, and its GDP per capita is similar to China's on a purchasing power parity (PPP) basis. It is also second after China in terms of both exports and FDI inflows. The ASEAN market is large, with a growing middle class and a high degree of integration with the global economy. The region's population is reaching 600 million (7% of the world total) with a collective GDP of USD 1.5 trillion at current prices and exchange rates set to rise rapidly: in 2010, GDP growth in ASEAN countries is estimated to be within a range of 3%-8%.

ASEAN has a middle class population of about 300 million, hence about half of the total population has an income level between USD 2-20 per person per day on a 2005 PPP basis. The middle class in ASEAN is expected to grow at a rapid pace, increasing the purchasing power of ASEAN households.

Figure 13: ASEAN vs. BRICs



Myanmar is not included in GDP and export statistics for ASEAN.

Source: IMF and World Bank.

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International co-operation to expand FDI flows

ASEAN countries have stepped up international co-operation, both amongst themselves and with other countries and regions. This latter group includes free trade agreements (FTAs) and economic partnership agreements signed between ASEAN and other countries, as well as bilateral trade agreements and investment treaties signed by individual ASEAN member states.

ASEAN is promoting regional economic integration

The Association of Southeast Asian Nations (ASEAN), established in 1967, has made progress in moving towards regional economic integration. The ten member countries have signed several trade and investment agreements amongst themselves since the mid-1980s with varying degrees of sectoral coverage (Table 1). Each new agreement has tended to supersede or combine earlier approaches. In 2009, ASEAN states replaced the two existing investment related agreements by signing the ASEAN Comprehensive Investment Agreement (ACIA) which consolidates and strengthens the provisions under the two agreements. The implementation of ACIA is a critical element in the process of establishing the ASEAN Economic Community by 2015. Compared with the former regional investment agreements, ACIA will provide more transparency and predictability for investors, offer more liberalization commitments and grant immediate benefits to ASEAN investors and ASEAN-based foreign investors by 2015.[4]

Table 1: ASEAN approaches towards integration

		Launched	*Implemented*
Trade			
ASEAN Industrial Projects	AIP		
ASEAN Industrial Complementarity	AIC		
ASEAN Industrial Joint Ventures	AIJV	1987	
Brand-to-Brand Complementation Scheme	BBC	1988	
ASEAN Free Trade Area (ASEAN 6)	AFTA	1992	
ASEAN Framework Agreement on Services	AFAS	1995	
ASEAN Industrial Cooperation Scheme	AICO	1996	
ASEAN Economic Community	AEC	2003, 2007	Originally 2020, moved to 2015
ASEAN Trade in Goods Agreement	ATIGA	2010	
Investment			*Amended*
ASEAN Agreement for the Promotion and Protection of Investments	IGA	1987	1996
ASEAN Dispute Settlement Mechanism		1996	
ASEAN Investment Area	AIA	1998	
ASEAN Comprehensive Investment Agreement	ACIA	2009	

[4] Detailed information can be found on the ASEAN Secretariat website: www.aseansec.org

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Trade and Investment Agreements in ASEAN countries

After the Asian Crisis, ASEAN governments realized the importance of more economic co-operation within the region and of comparatively stable long term investment from foreign countries rather than depending on short-term loans and portfolio investments. The mismatch of maturities as well as currencies between short-term borrowing from abroad for long-term domestic projects had been a major contributor to the crisis.

One of the efforts of ASEAN governments to improve domestic investment prospects is aggressively to pursue bilateral trade and investment negotiations with both developed and developing countries (Table 2). The process escalated in the 1990s. Bilateral investment treaties (BITs) and FTAs have improved ASEAN's investment position by boosting confidence on the part of foreign firms in the host economies regarding ASEAN's policies towards FDI. In their investment agreements, ASEAN countries focus on guaranteeing an internationally standard level of investment protection. Indonesia, Malaysia and Singapore first started promoting BIT negotiations, followed by Vietnam, the Philippines and Thailand.

As an export-oriented grouping of economies, ASEAN bilaterally and regionally has engaged in many FTA negotiations with non-ASEAN members. So far, ASEAN has signed five regional FTAs with six countries (including four OECD countries) namely Japan, China, Korea, Australia and New Zealand, India as well as an FTA within ASEAN itself. ASEAN-EU negotiations on a possible FTA started in 2007. All these agreements include an investment section. Among 95 signed free trade agreements, more than half of them include an investment chapter.

Table 2: Number of Signed Agreements on FDI in ASEAN

	BIT	Signed FTA	Signed FTA with Investment Clauses	DTT
ASEAN		6	6	
Brunei	5	8	7	10
Cambodia	17	6	5	15
Indonesia	63	8	6	53
Laos	23	6	5	9
Malaysia	34	10	7	60
Philippines	41	7	6	37
Singapore	35	21	16	68
Thailand	39	10	8	58
Vietnam	55	7	5	50

Source: Government websites; OECD (2009).

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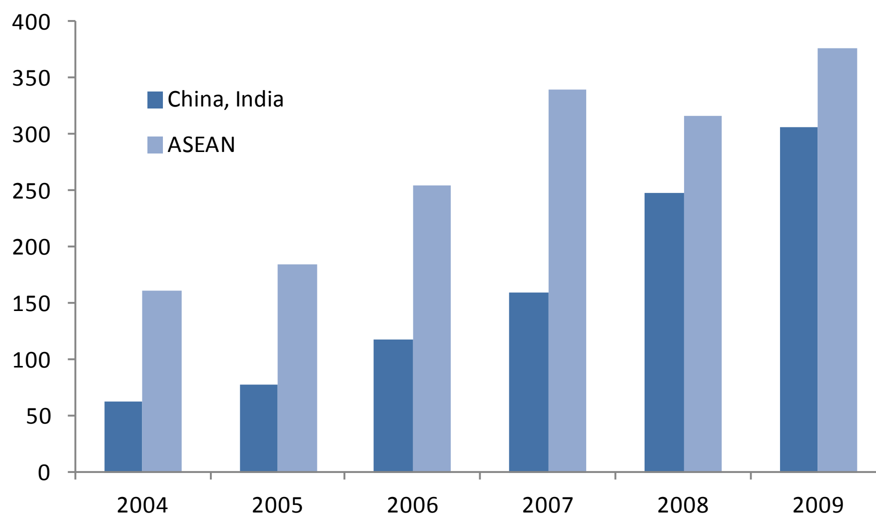
Growing FDI outflows from ASEAN

ASEAN members may account for a mere 1% of total world FDI outflows, but among emerging economies they are among the most active outward investors. Their stock of outward investment still exceeds that by Chinese and Indian firms (Figure 14), and ASEAN firms are much more prominent investors in OECD economies than firms from either China or India (Figure 15). High saving rates, technological sophistication and lower barriers to cross-border transactions have contributed to FDI outflows from several ASEAN countries.

Almost all of this investment emanates from Singapore and Malaysia, accounting for 72% and 21% of the total ASEAN outward stock respectively. In terms of annual flows, firms from Indonesia, Thailand and the Philippines have also invested significant amounts abroad recently (Figure 16).

Figure 14: Outward stock of FDI from ASEAN, China and India

(USD billion)



Source: IMF.

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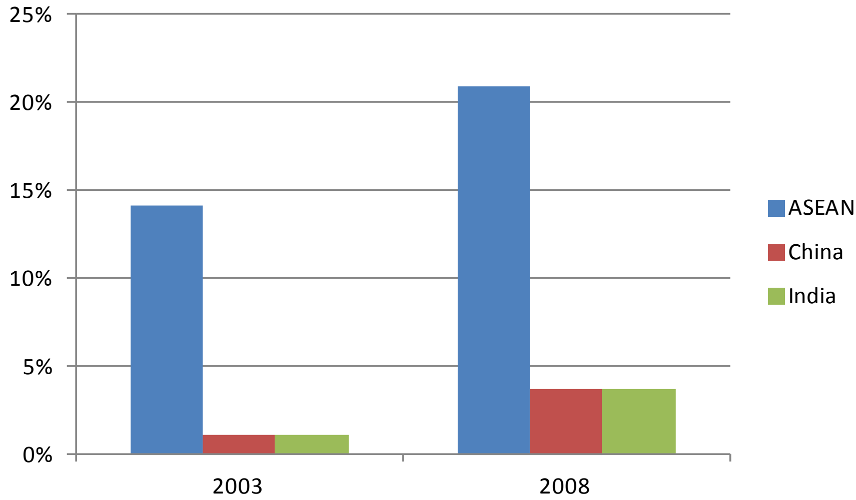
Figure 15: OECD countries as hosts to FDI from ASEAN, China and India

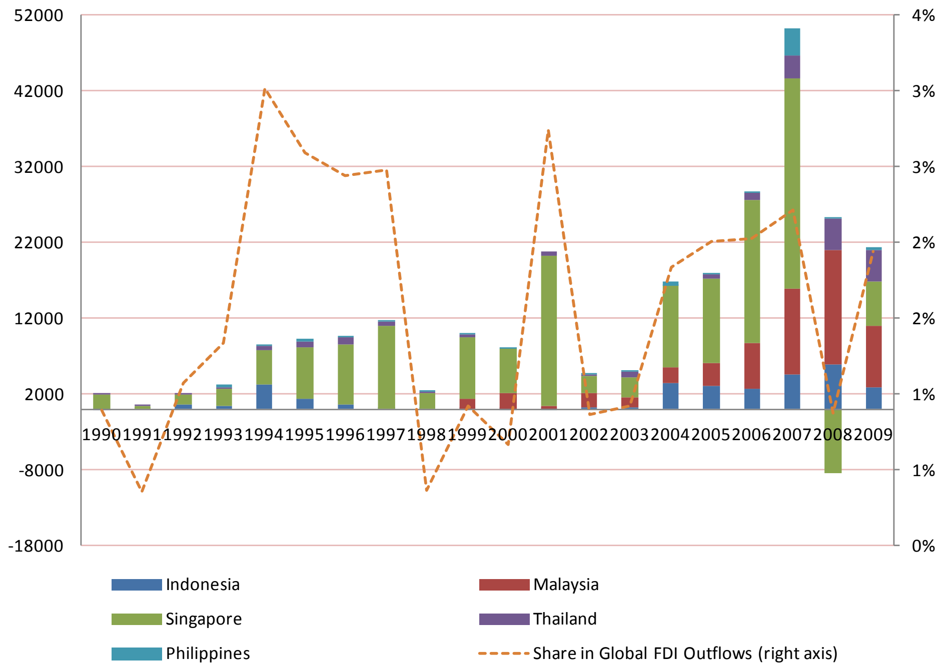
(Share in stocks held by non-OECD member countries in OECD)



Source: OECD.

Figure 16: FDI outflows from ASEAN 5

(USD million)



Source: IMF.

While there is marked difference in the scale and pattern of outward FDI between ASEAN countries, some common features are also present: (1) an increase in the share of services in outward FDI particularly from Singapore and Malaysia, (2) an expansion in over-

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seas business by ASEAN companies from the region to the world as a whole and (3) rising outward investments largely driven by home government FDI policy with an important role of government-linked enterprises.

Some of the most important ASEAN MNEs and their largest acquisitions abroad are listed in Table 3. State-owned enterprises and sovereign wealth funds (SWFs) figure prominently.

Table 3 : Recent Outward FDI by ASEAN MNEs

(2005-2009)

Company Name (Country)	Industry	Overseas Activity	Specific Targets
Temasek Holdings (Singapore)	SWF	Extensive global investments	- Merrill Lynch (US; banking): USD 4.9bn for 9% stake (2007) - Standard Chartered Bank (UK; banking): 18.8% stake worth USD 357 million - Chennai branch office of the DBS bank (India; banking) (2009) - Shin Corporation (Thailand; telecom): 49.6% share for USD 1.88 billion (2006)
Petronas (Malaysia)	Oil and Gas operations (Government owned)	Extensive overseas (recently focusing on Africa, Asia)	- FL Selenia (EU; lubricant blend and marketing): USD1.4 billion - Cairn India Limited (India; oil): stake purchased from Cairn UK
Maybank (Malaysia)	Financial services	Embracing Islamic Finance	- PT Bank International Indonesia (Indonesia; banking): USD1.1bn for 55.6% stake (2008) - MNC Bank (Pakistan; banking): USD 687mn for 15% stake
Bangkok Bank (Thailand)	Financial services	21 overseas activities mainly in Asia, but also US/UK	- People Insurance of China (China; insurance): 10% share (2005)
Charoen Pokphand (Thailand)	Agro-business and food industry/ Diversified (e.g. restaurants in China)	Extensive overseas activities (Mainly in Asia)	- Marine business (Philippines) - Restaurant chain (China) - Marine and animal feed business (UK and Turkey)
Salim Group (Indonesia)	Conglomerate	Mainly in Asia (China/India)	- New Kolkata International Development (India; real estate): 50% stake increase - LAB Plant (China; chemical): USD 97mn via a joint venture with Korean Great Orient Chemical Pte. Ltd. (2008)
Lippo Group (Indonesia)	Conglomerate	Global network mainly in Singapore/ Malaysia	- Robinson and Company Ltd. (Singapore; retail): EUR 100 million for 29.9% stake - Overseas Union Enterprise (Singapore; hotel and real estate): stake raised by 88.5% worth USD 957mn - First REIT (Singapore; hospital and real estate): USD 111 million
San Miguel (Philippines)	Food and beverages	Mainly ASEAN countries/ China for market seeking and cost reduction	- Brewery operations (China and ASEAN) - Packaging facilities (China, Viet Nam, and Malaysia) - Meat processing plants (Indonesia and Viet Nam) - Feed mill and hog farm (Viet Nam)
Petrovietnam (Viet Nam)	Mining and quarrying	20 projects in 17 countries mainly in Russia and Venezuela	- Rusvietpetro Joint Venture (Russia): 49% stake in 2008 - joint venture with Petroleos de Venezuela - projects in Algeria and Malaysia

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Motives for outward investment differ by firm, sector, country and ownership. They include many of those typically associated with outward investment by OECD-based MNEs: market access, technology sourcing, low cost labor or resource seeking, and asset diversification.

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Conclusion

As hosts to international direct investment, ASEAN countries have emerged from the recent global crisis in relatively good shape. Inflows are at record levels in some countries, and the prospect for future flows is good. Although many regions have followed the path breaking development strategy of ASEAN in welcoming inward investment, ASEAN member states are holding their own against this competition – including from China. ASEAN offers a large and dynamic market, as well as a diversity of investment environments to appeal to almost all potential investors.

Southeast Asian countries, with few exceptions, also have a well-established track record of openness to FDI. Neither in the 1997 Asian financial crisis, nor in the most recent global one, did governments in the region resort to protectionism. On the contrary, governments in some crisis-affected economies in 1997-1998 actually opened further to foreign investors in key sectors such as banking. But governments are continuously being tested by incumbent firms, often but not always local ones, eager to protect or increase their quasi-monopoly rents. It is essential to ensure that the renewed ease in attracting global investors does not give way to backtracking in investment policies. It is also important that ambitious plans to create an integrated ASEAN market do not come at the expense of economic relations with the rest of the world.

An analysis of investment trends by itself gives little idea of how investment in the region is evolving. Other information on the activities of foreign investors in ASEAN suggests that they are increasingly focusing on the regional market. Local markets still account for the largest share of sales of affiliates, but regional sales are growing faster than exports to the home country of the investor. This suggests that competition for global FDI will in the future depend as much on the appeal of the ASEAN market itself as it will on the costs of production and related factors.

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ANNEX I. FDI trends in ASEAN by country

Inflows

Singapore

Singapore plays a pivotal role within ASEAN, as both an *entrepôt* for trade and a hub for foreign investment. As argued by Cheong and Plummer (2009, p. 6), "while Singapore apparently does extremely well by almost any measure in attracting FDI, its destiny in many ways is linked to economic performance in the region." The Singapore economy serves as ASEAN's manufacturing export, trade, and financial hub. Many global corporations including ASEAN-based MNEs have established their regional headquarters in Singapore to service international trade and financing and to penetrate more effectively into emerging Asian markets.

The global crisis hit Singapore – the most open economy in ASEAN – the hardest. US and EU MNEs have together provided more than 50% of the total FDI stock in Singapore. The occasional sudden decline of Singapore's FDI inflows closely matches periods of developed-country economic downturns, such as in the early 1990s and 2000s and in the most recent crisis (Figure A.1). The current global crisis has been no exception: inward FDI in Singapore declined by USD 23 billion in 2008 from the peak level of USD 32 billion in 2007. By 2010, inflows had rebounded to almost USD 37 billion. Indeed, following each downturn, the recovery has been even more dramatic.

Supporting Singapore's economic position in the region, FDI in Singapore is concentrated in financial and insurance services (40%, including investment holding companies), manufacturing (23%) and wholesale and retail trade, hotels and restaurants (19%) (Figure A.2). FDI in the pharmaceuticals sub-sector has greatly increased its share from 22% of FDI in manufacturing in 2001 to 33% in 2008. Most recently, leading pharmaceutical and biotech companies are expanding their operations in Singapore and locating their strategic regional headquarters there. The traditionally leading FDI sub-sector, electronics, declined from 44% of FDI in manufacturing in 2001 to 26% in 2009, while the petroleum products sub-sector has remained stable at roughly 14% in 2008, reflecting the importance of Singapore as the

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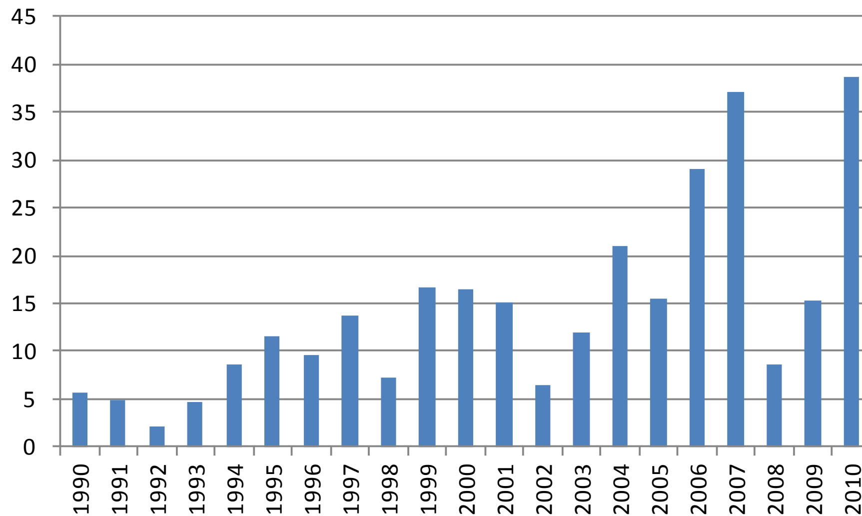
region's main oil refining center. This sectoral trend in FDI has been actively supported by the government's industrial policy, including the Biomedical Science Initiative beginning in 2000.

Figure A. 1.: Singapore FDI inflows, 1990-2010

(USD billion)



Source: Statistics Singapore and ASEAN Secretariat.

By source country, the largest share of FDI comes from Europe (40%), followed by Asia (26%). Some of the share attributed to the Caribbean may involve pass through investments and hence the geographic origin is largely unknown. Investment in Singapore comes from all regions, including within ASEAN itself, but the total amount is nevertheless dominated by only a handful of countries. The Netherlands, the US, Japan and the UK represent 41% of total inflows. Many new investors such as India and China are neverthe-less expanding rapidly in Singapore.

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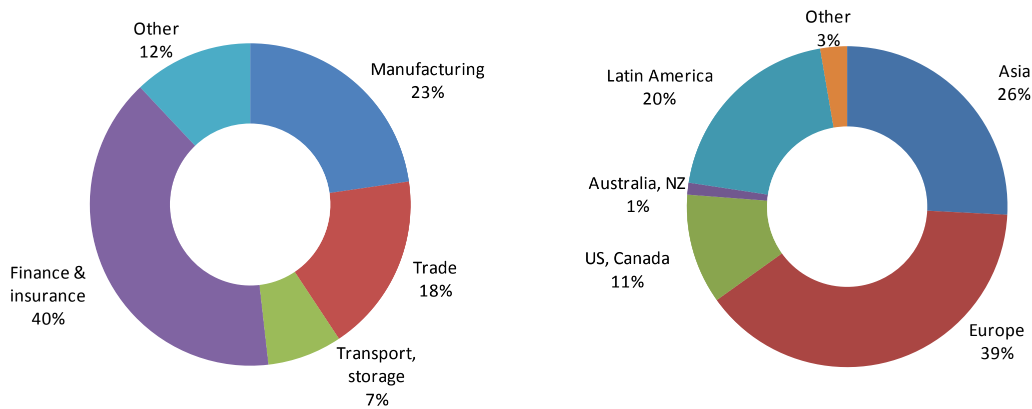
Figure A. 2.: Singapore FDI Stocks by Investor Country/Sector

(Share as of end 2009)



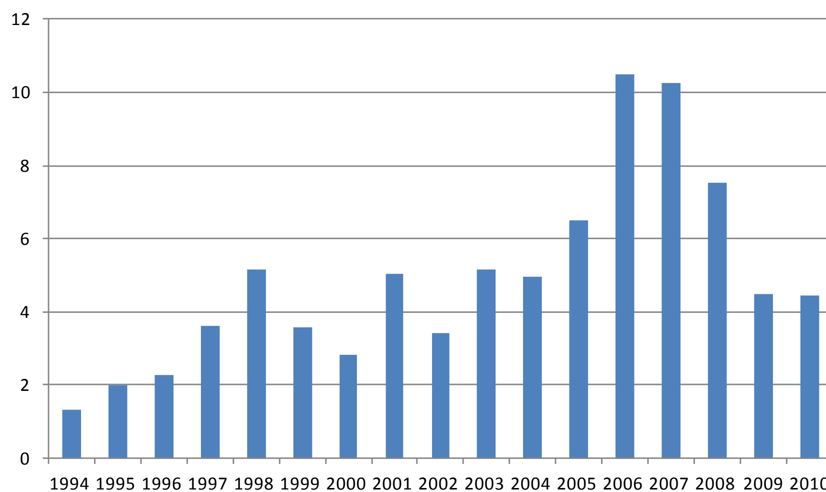
Source: Singapore Department of Statistics.

Thailand

Thailand has traditionally been one of the preferred destinations for FDI in the region and was the second largest FDI destination among ASEAN countries throughout most of the past decade. Foreign investors have been attracted by Thailand's relatively strong manufacturing sector, along with its status as the second largest domestic market in the region (18% of total ASEAN GDP in 2009) with 67 million consumers. Owing to political instability since 2005, Thailand has been gradually losing its share of FDI inflows to other ASEAN countries. The global crisis caused FDI flows to drop for two consecutive years in 2008 and 2009, with no signs yet of recovery (Figure A.3).

Figure A. 3.: Thailand FDI Inflows, 1990-2010

(USD billion)



Source: Bank of Thailand (non-bank sector only).

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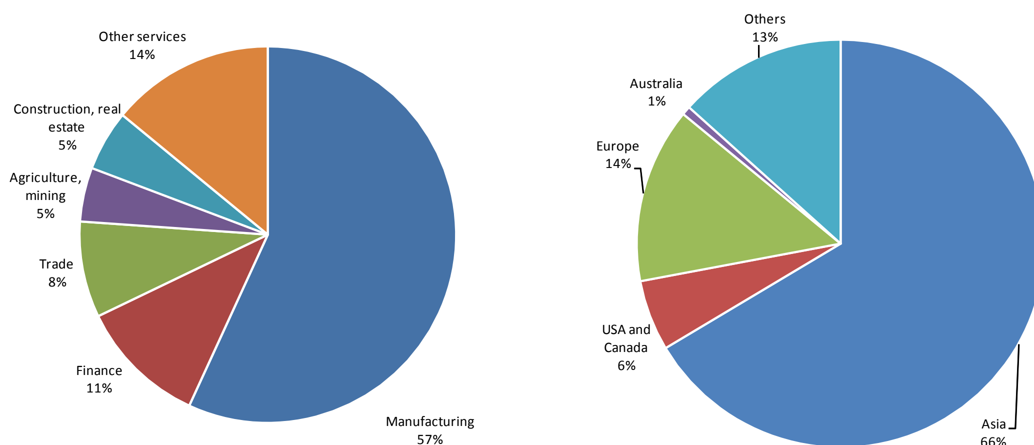
Most FDI in Thailand comes from the rest of Asia, accounting for 66% of total FDI in 2000-2010 (Figure A.4). Japan is the largest investor in Thailand, particularly in the manufacturing sector (automobiles and components), while ASEAN now ranks second, mainly in trading and telecommunications and mostly from Singapore. The EU follows in third place, mainly providing FDI in the trading sub-sector. A marked drop of FDI by US MNEs has taken place over the past decade.

More than 50% of inward FDI is in manufacturing, especially electrical appliances, chemical and machinery and transport equipment, but there has been an increase in the share of FDI in services from 2005 onward. The financial sector led this increasing trend following the Bank of Thailand's Financial Master Plan in 2004. Before the global financial crisis, FDI in financial institutions (but not including banks) accounted for 40% of total FDI in the services sector followed by the investment (18%), other services (14%) and trade sub-sectors (12%). After the onset of the current global crisis, FDI in financial institutions declined to 16%, with real estate and trade expanding to fill the gap.

Figure A. 4.: Thailand FDI Stocks by Investor Country/Sector

(Share of cumulative flows from 2000 to 2010)



Source: Bank of Thailand (non-bank sector only).

Malaysia

Malaysia played an early leading role in export-oriented industrialization and FDI promotion. Since the Investment Act in 1986, Malaysia has experienced a huge influx of foreign capital into its economy and the government has successfully channeled this into export manufacturing. The country exhibits a high degree of specialization in electronics and electrical products.

Like Singapore, Malaysia experienced a dramatic drop in FDI in the most recent global crisis, as it had earlier following the Asian

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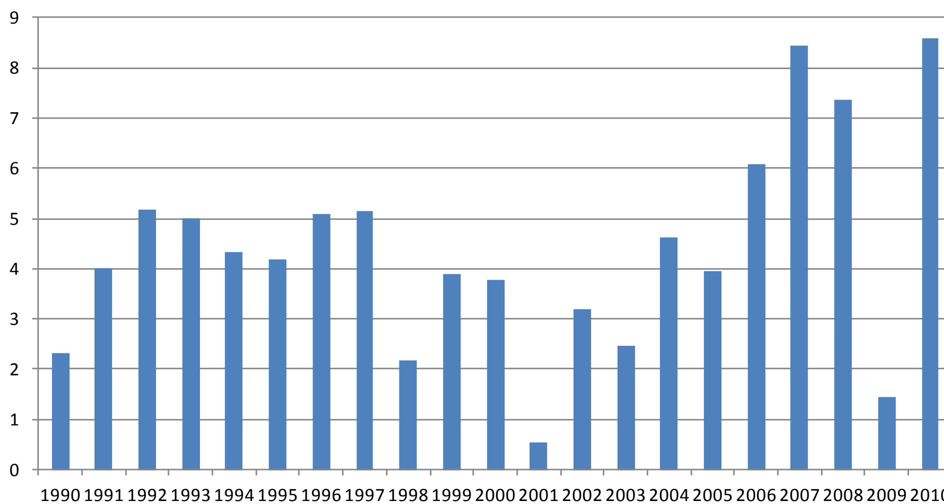
crisis of 1997-1998 and the dot com crash of 2000-2001 (Figure A.5). Although recovery in 2010 was swift, there are nevertheless concerns that Malaysia might slowly be losing its competitiveness as an attractive investment destination. Three main reasons may be adduced for this phenomenon: (1) increasing competition with other developing countries in labor-intensive manufacturing, especially from China, Vietnam, and Indonesia, (2) the successful completion of large-scale public sector infrastructure projects with no immediate following projects of a similar scale, and (3) the government's effort to effect an economic transformation to attract high-value added activities with advanced and less labor-intensive, technology, which may not mesh with foreign investor perceptions of Malaysia's suitability for such investments.

Figure A. 5.: Malaysia FDI Inflows, 1990-2010

(USD billion)



Source: IMF and Bank Negara Malaysia.

FDI in Malaysia has been largely funded by retained earnings. Asian and European investors hold almost the same amount of FDI stocks in Malaysia accounting for one third each of the total stock as of end 2009 (Figure A.6). Japan and Singapore are the two largest Asian investors in Malaysia, focusing on chemicals and electronics respectively. The country also has a strong economic relationship with the United States (12% of total FDI stocks).

By sector, Malaysia has traditionally been strong in manufacturing (light manufacturing, electronics, logging, and petroleum production) and agriculture (rubber, palm oil processing). From the 1980s onwards, Malaysia has been a preferred manufacturing base of MNEs such as Samsung. The manufacturing sector (basic metal products, electronic and electrical products) still receives almost half of Malaysia's total FDI and is expected to continue to attract FDI in new growth areas such as solar energy and medical equipment. FDI in services has increased sharply, reaching 42% of total FDI flows com-

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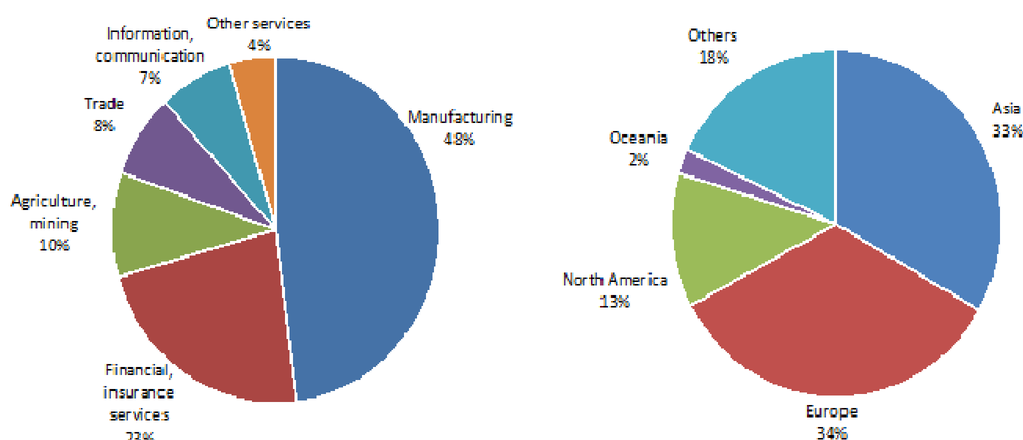
pared to only 15% in the 1990s. Among services, financial services (including Islamic finance) received the most foreign investment (RM 42 billion of net FDI inflows in 2000-2009), followed by communications, transport, hotels and wholesale and retail trade sectors. As of April 2009, the government had liberalized 27 services sectors with no equity condition imposed.[5] Further investment in services is expected, judging by the experience of other developing countries and Malaysia's stated commitment to liberalize its service sector further. There are steady FDI inflows into oil and gas, mostly undertaken through production sharing contracts in joint ventures with Petronas.

Figure A. 6.: Malaysia FDI Stocks by Investor Country/Sector

(Share of FDI stocks as of end 2009)



Source: Bank Negara Malaysia.

The Philippines

The Philippines has a high potential to attract investment. The country's geographic location, abundant resources and population of nearly 100 million (similar to Mexico's) provide a competitive advantage to the Philippines. The country has been hampered in its attempts to realize this potential by *i.a.* the perception of high levels of corruption in government (such as in the Corruption Perceptions Index of Transparency International[6]), restrictive foreign ownership rules and uncompetitive labor compliance costs.

Inward FDI in the Philippines has been relatively stagnant compared to its ASEAN peers. The global crisis caused a 47% decline in inflows in 2008, but an early recovery took place in 2009, led by investment in infrastructure (Figure A.7). The United States and Japan have been the leading investors, accounting for nearly half

[5] These sub-sectors are in the areas of health and social services, tourism services, transport services, business services and computer and related services. (MIDA)
[6] The Philippines ranks 134 worldwide in terms of corruption perceptions, well behind most of the other larger ASEAN countries.

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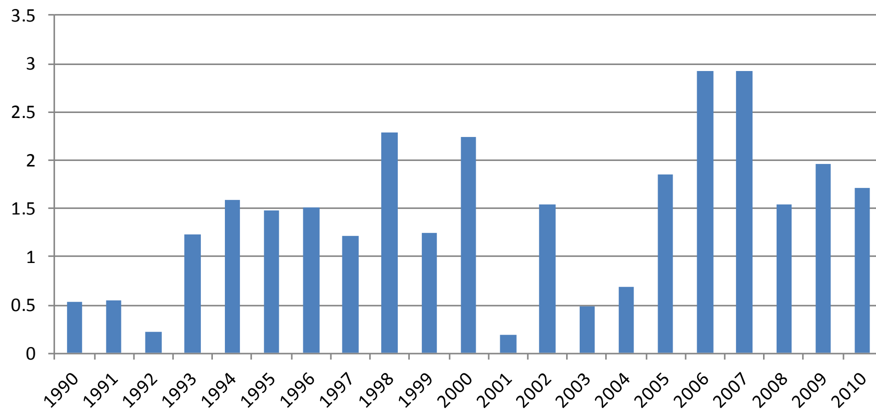
of FDI inflows to the Philippines over the past decade. The high volatility of FDI inflows suggests that the Philippines may need to make stronger efforts to lure long-term, sustainable investment projects to the country.

Most FDI in the Philippines is in manufacturing, but FDI in services has increased noticeably since 2007 (Figure A.8). As part of the government's effort to develop the country's infrastructure, investments in electricity, gas and water led the increase of FDI in services in 2007 and accounted for 20% of FDI in services since 2000. Real estate and construction ranked second (16%) followed by financial services (10%). Acknowledging the importance of FDI for sustainable growth, the central government, together with 11 government investment promotion agencies, has launched another Philippine Investment Promotion Plan (IPP) for 2010-2014.

Figure A. 7.: Philippines FDI Inflows, 1990-2010

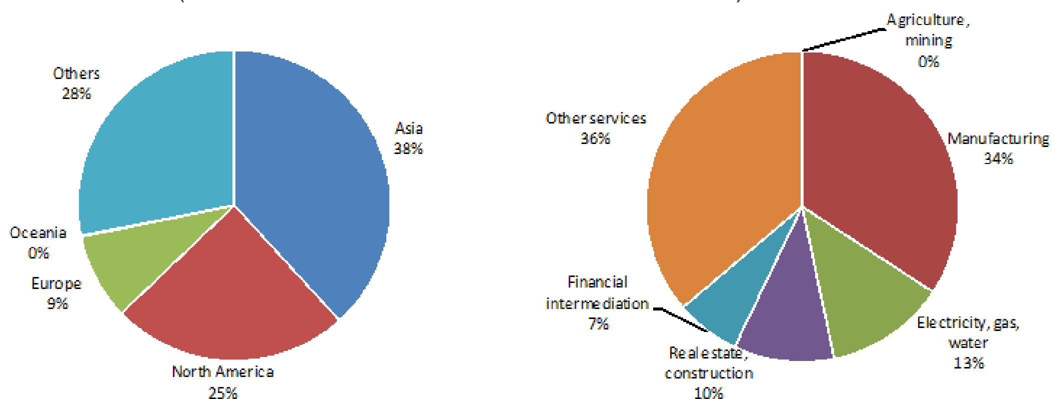
(USD billion)



Source: IMF and Central Bank of the Philippines.

Figure A. 8.: Philippines FDI Stocks by Investor Country/Sector

(Share of accumulated flows from 2000 to 2010)



Source: Central Bank of the Philippines.

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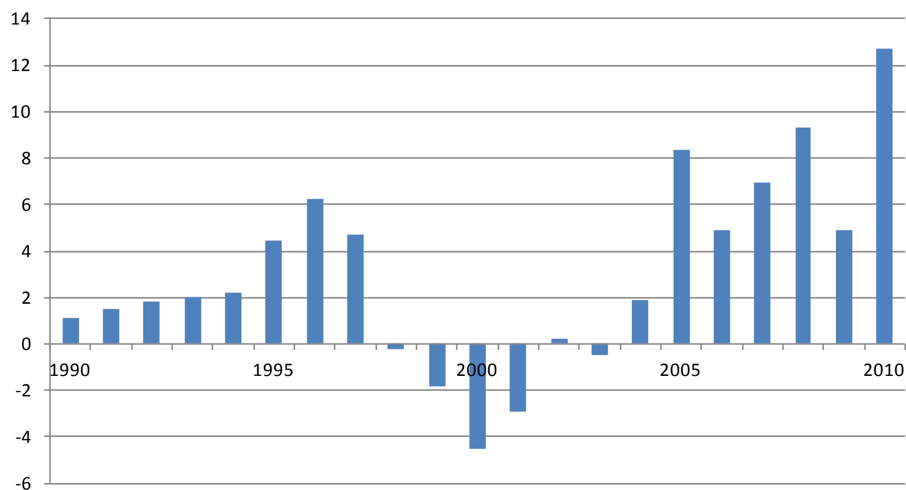
Indonesia

The largest economy in the region, Indonesia experienced a dramatic recovery after 2003 following massive capital outflows in 1998-2003 totaling USD 10 billion (Figure A.9). No doubt in part attracted by the improved investment climate resulting from greater economic and political stability, FDI inflows in Indonesia have grown rapidly over time, reaching an historic peak in 2010 (OECD 2010). As in the cases of Malaysia and Thailand, Asian investors play a leading role in Indonesia (Figure A.10). While Japanese firms (16% of total FDI) have been the most consistent investors, a recent significant increase of FDI from ASEAN countries (36% mostly from Singapore and Malaysia) is noteworthy. The EU accounted for 18% and the United States 7% of total FDI inflows in 2000-2010.

Figure A. 9.: Indonesia FDI Inflows, 1990-2010

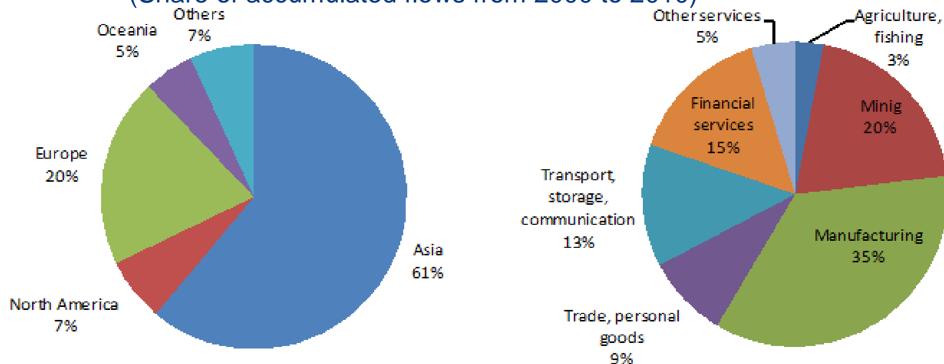
(USD billion)



Source: Bank Indonesia.

Figure A. 10: Indonesia FDI Stocks by Investor Country/Sector

(Share of accumulated flows from 2000 to 2010)



Source: Bank Indonesia.

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Since 2000, services have constituted the largest share of FDI flows (41%), followed by manufacturing (35%), mining (20%) and agriculture, forestry and fisheries (3%). Metal, machinery and electrical goods are the largest sub-sectors in the manufacturing FDI, followed by the chemicals and pharmaceuticals. In the services sector, a sudden increase in investment in infrastructure recently occurred, particularly investment in transport, storage and communications which increased significantly from USD 133 million in 2008 to USD 1.8 billion in 2009.

Vietnam

Vietnam is the most dynamic destination for foreign investment within the region, becoming the second largest host of FDI inflows among ASEAN after Singapore in 2008 and 2009. In 2008 FDI was equivalent to 11% of Vietnam's GDP and 20% of its gross fixed capital formation. WTO accession in January 2007 has been a turning point for Vietnam, resulting in major economic reforms (Figure A.11).

Asian investors, mainly Japan, the NIEs, and Malaysia have been the dominant source of FDI in Vietnam (Figure A.12). Better prospects for FDI in Vietnam result from rapid economic growth – Vietnam is now a USD 96 billion economy – and its abundant workforce. Intel is expected to open a $1 billion chip assembly and test plant near Ho Chi Minh City.

Manufacturing is the main beneficiary of FDI, accounting for 46% of total inward FDI in 1988-2009, while FDI in the services sector has been led by hotel, tourism, construction and real estate. The government has prioritized FDI in infrastructure, with its USD 8 billion stimulus package heavily tilted towards infrastructure spending. Steady FDI inflows in mining and quarrying can partly be explained by the government's policy to take advantage of booming oil prices in 2006 and 2007.

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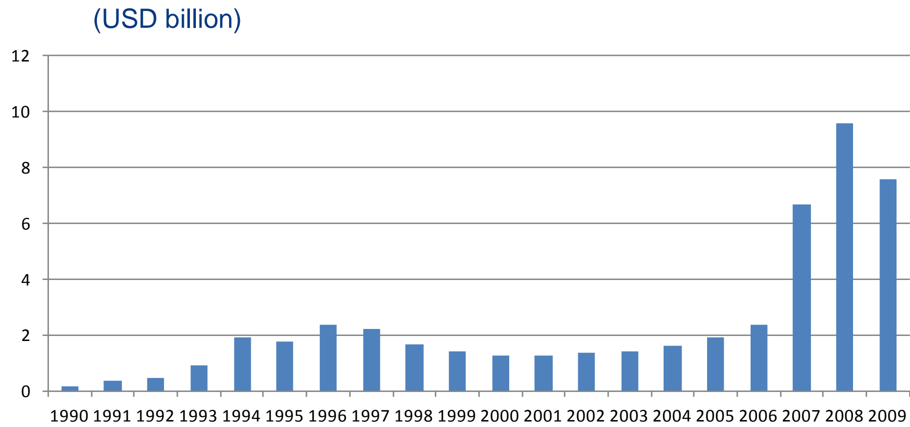
Figure A. 11.: Vietnam FDI Inflows, 1990-2009

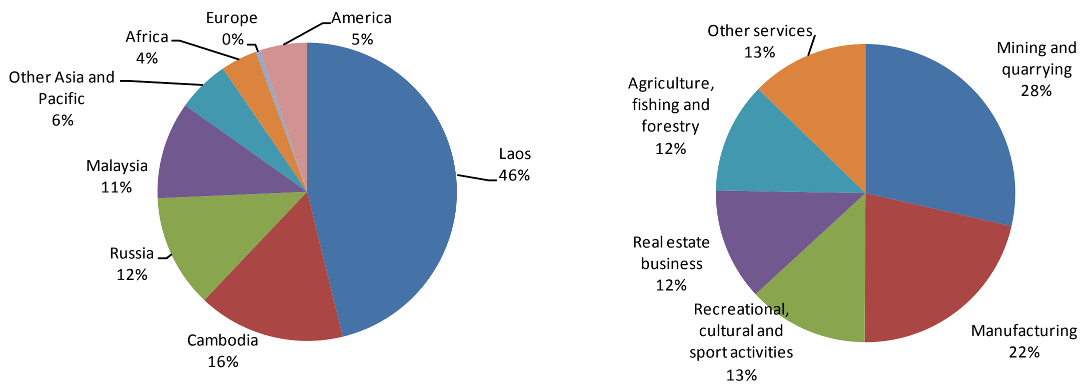
(USD billion)



Source: IMF and UNCTAD.

Figure A. 12: Vietnam FDI Stocks by Investor Country/Sector

(Share of accumulated flows from 1988 to 2009)



Source: Ministry of Planning and Investment (based on realized investment).

Smaller ASEAN economies[7]

FDI inflows into the smaller economies of ASEAN (Cambodia and Laos are both classified as least developed countries by the UN) have not been important in comparison with flows into the larger ASEAN economies because of their small domestic markets. FDI inflows to the three smaller ASEAN economies accounted for only 3% of total flows into ASEAN during 2000-2009. However, the small size of each of these economies also means that a single large FDI project can result in a substantial impact on the entire economy.

[7] This section considers Brunei, Cambodia and Laos but not Myanmar.

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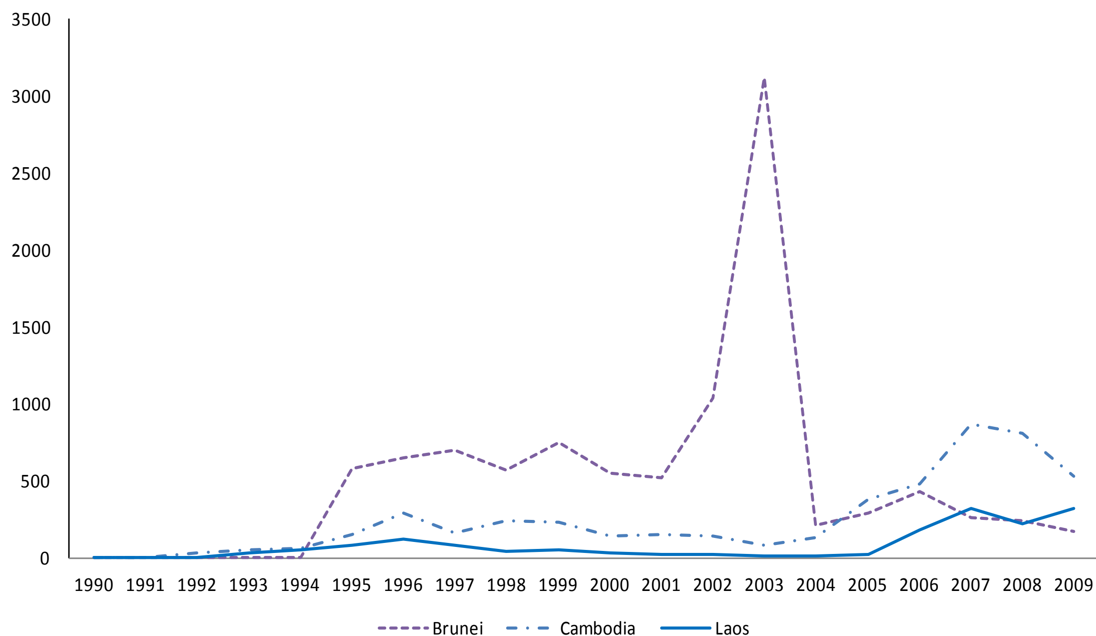
FDI in these three countries is largely concentrated in those few sectors where perceived resource strengths and comparative advantages exist. Brunei's economy is highly dependent on oil and gas, Laos on hydropower and Cambodia on unskilled labor-intensive projects and tourism.

Figure A. 13.: FDI flows to smaller ASEAN economies

(USD million)



Source: IMF, International Financial Statistics.

Brunei Darussalam

Brunei Darussalam has a small GDP (USD 11 billion) and population (400,000) but ranks second highest in ASEAN in terms of per capita income, with the primary sector (oil and gas production) accounting for 70% of GDP. Brunei's FDI trend is highly volatile as a result of large plantation projects and the world oil market.

FDI inflows into Brunei have been dominated by a small number of foreign investors. The United Kingdom and the Netherlands have been the two largest investors followed by Japan, Singapore and Malaysia. For instance, the Royal Dutch Shell group holds equal shares with the Brunei government in the joint venture Brunei Shell Petroleum (BSP), the top oil and gas producer in Brunei. Mitsubishi is a joint venture partner with Shell and the Brunei Government in Brunei LNG, Brunei Coldgas, and Brunei Shell Tankers, which together produce LNG and supply it to Japan.

Recently, a number of projects have emerged to diversify the economy. As part of the diversification effort, Japanese firms, Mitsubishi and Itochu, became joint venture partners with Petroleum

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Brunei and established the Brunei Methanol Company in 2006, Brunei's first petrochemical manufacturing company.

Cambodia

Cambodia's economy has enjoyed a comparative advantage in its low unit labor costs, export quotas, which formerly favored the country as a location for exports to the US and EU markets, and its abundant tourism resources. There has been a 12-fold increase of FDI into Cambodia since 2004 due to macroeconomic stability and the country's open FDI policy. FDI in Cambodia peaked in 2007 with a net inflow of FDI of USD 868 million, a sharp rise from USD 483 million in 2006. Based on FDI approval data from 2007 to 2009, China has been the leading source of FDI, followed by Korea and the United States. Investment in tourism was the main beneficiary of FDI, accounting for over 70% of total FDI, followed by industry (energy, food processing and garments, together 12% of total FDI) and services (12%) and agriculture. The traditional FDI beneficiary, garment related projects, has greatly declined due to the evolution of export quotas to the United States since 2005.

Laos

Laos has pursued an open door policy since shifting from a planned to a market economy in the late 1980s. There has been a marked increase in the country's FDI inflows from 2005 onward. From 2000 to 2007, Thailand and China together constituted the largest source of FDI in Laos, followed by Vietnam and France. A large share of FDI went to the natural resources sector, especially to hydroelectricity generation from the country's abundant water resources, and this sector made up 30% of total FDI in 2003-2007. It is estimated that the Mekong River in Laos, for example, has an electricity generation potential of over 18,000 MW. FDI also flowed into agriculture and mining.

Outflows from ASEAN economies

Singapore

Singapore has traditionally been the largest source of FDI from the ASEAN region. While Malaysia exceeded Singapore in terms of net FDI outflow in 2008, Singapore accounted for 62% of the total ASEAN FDI outward stock in 2009 (USD 213 billion), much larger than Malaysia's 22% (USD 76 billion).[8] Government support has been important for Singapore's OFDI performance starting with the International Direct Investment Programme in 1988 and has been involved in setting up industrial parks and infrastructure projects in developing Asia and facilitating acquisition of technology in advanced markets.

[8] UNCTAD World Investment Report (2010)

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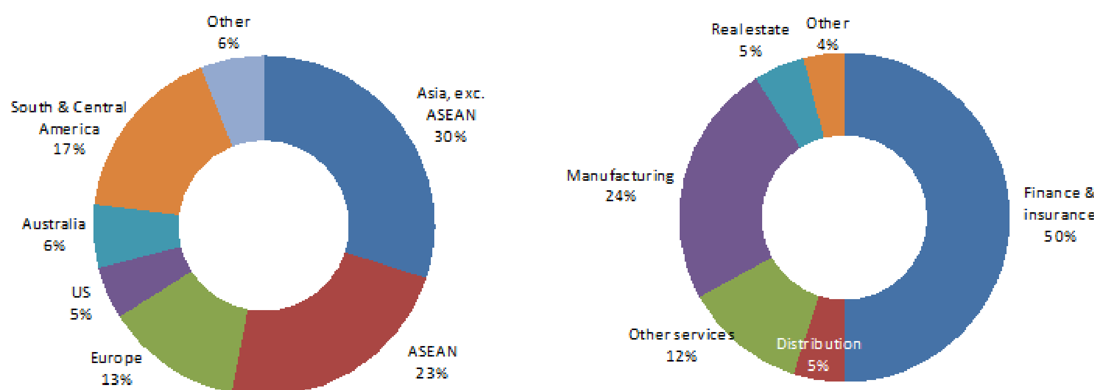
Government-linked companies, including Temasek holdings, continue to be the dominant overseas investors from Singapore. Half of Singapore's capital was invested in Asian countries including China (the top destination of Singapore's investment, primarily in manufacturing), Malaysia, Hong Kong (China), Thailand, and Indonesia, in that order. This was followed by the South and Central America (British Virgin Islands being the second largest destination) and Europe (the UK being the third largest destination).

The bulk of Singapore's capital is invested in the financial and insurance services (for market access) and manufacturing (for market access and low-cost labor seeking). These two sectors account for more than 70% of total OFDI from Singapore. Singapore's investment in ASEAN countries has been quite steady, accounting for slightly above 20% of Singapore's total outflows in 1998-2008. But ASEAN's share has declined from 30% in 2000 to 23% in 2008, mostly explained by a decreasing share of FDI flows to Malaysia. Singapore's investment in China has compensated for the decreased ASEAN portion. Part of this outward FDI has been made by foreign-invested companies based in Singapore, indicating Singapore's role as regional headquarters or investment hub.

Figure B. 1.: Singapore FDI outflows by country and sector

(Stock as of end 2008)



Other Services includes information & communications (5%), transport & storage (4%), hotels & restaurants (1%), professional support services (2%) and construction (0%).

Source: Singapore Department of Statistics.

Malaysia

Malaysia's outward FDI has gained momentum since 2006, encouraged by structural constraints in the domestic market (high labor costs and limited market size), as well as government support over more than two decades. Fully 78% of the country's total direct investment abroad during the past ten years (2000-2009) occurred after 2006. In 2007, outward FDI exceeded inflows and in 2008 and 2009 the country became the region's top outward investor, with total FDI outflows of USD 23 billion.

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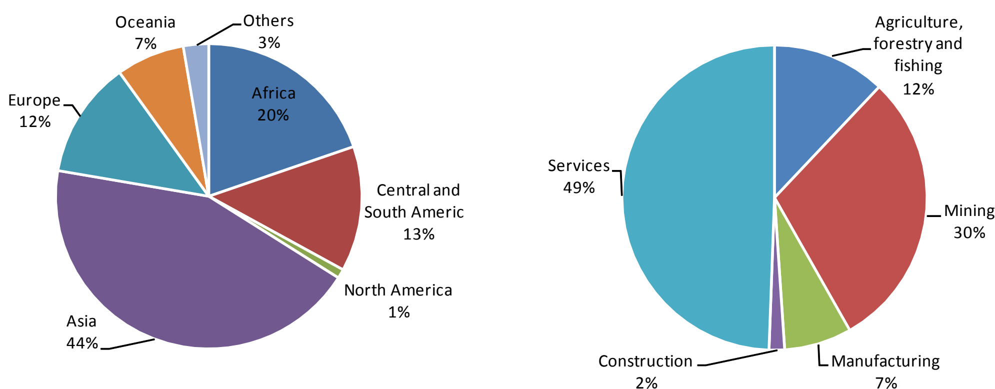
During the initial stage of Malaysia's overseas investment, as in the case of Singapore, Petronas and the government-linked companies (Khazanah Nasional Berhad, Telekom Malaysia) took the lead, investing in oil and gas as well as in agriculture. Over time, however, private firms such as Sime Darby, which was in top position among MNEs in agribusiness ranked by foreign assets (UNCTAD 2009), also gained sufficient competitiveness to start investing abroad. The Malaysian government provides incentives to encourage enterprises to go global.

As a result, FDI in services (i.e. financial services, telecommunications, utilities and business services) has greatly increased, accounting for 70% of total outward FDI in 2000-2009. This was followed by the oil and gas sector (10%) mainly from Petronas' activities in Africa, Central Asia and Vietnam and the manufacturing sector (7%). Excluding the Labuan International Offshore Financial Centre, most of Malaysia's investment was undertaken in the Asian region especially in ASEAN, Korea, Chinese Taipei, Hong Kong (China) and China, while some asset-seeking FDI occurred in Europe and the US, including the national automotive company Proton's acquisition of the Lotus Group in the UK in 1996 to upgrade its engineering capabilities. In 2002, Proton acquired a British automobile company which has acted as an R&D center (Hiratsuka 2006). KNM group's acquisition of Borsig (Germany) in 2008 is another noteworthy example of investment to acquire new technology and gain a foothold in the EU market.

Figure B. 2.: Malaysia FDI Outflows by Country and Sector



The data (by country) exclude retained earnings which are often an important component of total flows and thus may understate net outward FDI from Malaysia.

Source: BNM.

The share of Malaysia's OFDI in ASEAN has decreased from 32% in 1995 to 23% in 2004 while its investment in the US and in Africa has expanded considerably (from 9% to 14% in the United States and from 1.2% to 4.5% in Africa in 2006). However, based on

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the outward FDI stock, the share stayed almost unchanged at around one third in 2000-2006.[9]

Malaysia's OFDI is expected to stay positive in the future judging by the rising profits and dividends accruing to the Malaysian companies from their operations abroad. (BNM, 2008: RM 14.4 billion profit; 2001: RM 0.2 billion loss).

Indonesia

In Indonesia's case, outward FDI increased markedly from 2004 onward. A high share of Indonesia's capital targeted the financial and insurance services sector and storage and transport facilities sector in Singapore, Indonesia's preferred investment destination. This was also accompanied by a strong preference for the real estate sector due to the property boom in Asia (primarily in China and India) and labor-intensive industries such as textiles, garments and footwear in Cambodia, China, Sri Lanka, Thailand and Vietnam.[10] The major source of Indonesia's OFDI is understood to be from ethnic Chinese Indonesians, who dominate much of the country's modern business sector[11] and whose political vulnerability leads them to diversify their asset holdings abroad. Indonesia has shown a strong preference for investing in Singapore (86%) and Malaysia (6%), which together account for almost all of Indonesia's outward investment.[12] Although only a small share of total outflows, some manufacturing investment in poorer ASEAN countries may have been encouraged by the country's relatively rigid and expensive domestic labor system in terms of the cost of hiring and firing employees, compared with its regional peers.

Thailand

Thailand's outward investment is not yet significant compared with Singapore and Malaysia. During 1980-2008, Thailand's FDI outflows accounted for only 5% of GDP or USD 11 billion while Singapore and Malaysia accounted for 104% and 30% of GDP respectively.[13] The Asian crisis caused a sharp decline in Thailand's OFDI from the peak recorded in 1996. The main reason for this contraction was the lack of strong ownership advantages of Thai investors who had expanded abroad due to ample liquidity and inflated asset prices (Hill and Jongwanich, 2009). As Thai companies struggled for survival at home, OFDI activities remained low for several years, but the recent strong economic growth and the launch of the Thai direct investment policy to promote cross-border operations and profitable opportunities by relaxing approval requirements or foreign exchange regulations in

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[9] Hiratsuka (2006) and Pananond (2008).
[10] Siregar and Gunawan (2007)
[11] In the late 1990s, the ethnic Chinese controlled over 80% of corporate assets and 160 of the 200 largest businesses in Indonesia (Yeung (1999, p. 104)).
[12] Pananond (2008).
[13] Bank of Thailand

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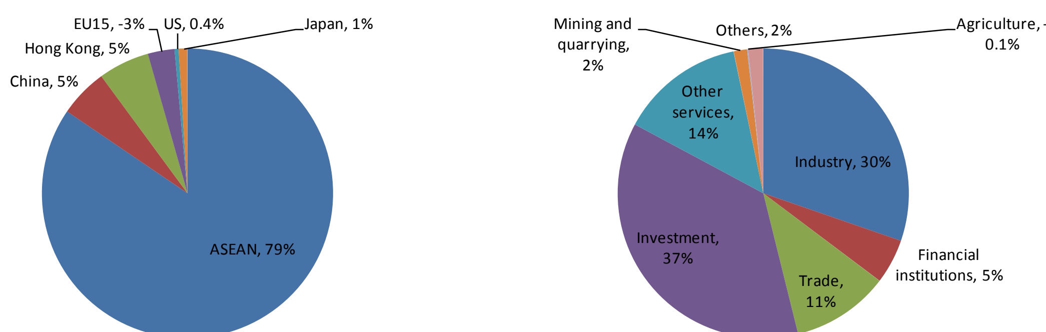
activities related to outward investment[14], have helped Thailand's OFDI to take off since 2005.

Most overseas investments are undertaken by large, often publicly listed, companies such as Bangkok Bank, Thai President Foods, Banpu, Loxley, Jasmine, Siam Cement and Charoen Pokphand, a large food-based conglomerate.

The destination of Thailand's outward FDI is mainly Asian countries (ASEAN accounts for nearly 80% of Thai total equity investment abroad, China and Hong Kong (China) around 5% each in 2005-2009). The recent surge in Thailand's outward FDI is mostly explained by outflows to ASEAN. Thailand's OFDI share in ASEAN increased from 54% in 2000 to 90% in 2009 in terms of equity investment[15], and Thailand is becoming an important regional investor. Thailand's outward FDI by sector has shown a preference for financial institutions, food and sugar, trade and mining and quarrying in that order. While most of Thailand's OFDI is in the form of greenfield investment, M&As also take place.

Figure B. 3.: Thailand (non-bank) FDI outflows by country/sector

(Equity basis; cumulative 2005-2009)



Source: Bank of Thailand.

The Philippines

Residents' net investments abroad from the Philippines started to turn positive in 2002 and increased significantly in 2004. While the positive trend was generally led by portfolio investment, direct investment abroad increased significantly in 2007, reaching a peak of USD 3.5 billion but declining quickly again thereafter during the global crisis. The bulk of residents' equity investments have gone to the US, China, Argentina, Singapore and Hong Kong (China). Hotels and restaurants, transport, storage and communications and manufacturing (food and beverage in particular) were the preferred targets of Philippines capital. For example, San Miguel, which ranked 35th in the

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[14] Examples of the policy include relaxation of capital outflow measures, a capital flow liberalisation road-map, and several tax incentives. (Bank of Thailand)
[15] This figure from Bank of Thailand does not consider OFDI in banking sector.

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world's largest food and beverage MNEs in 2007 according to UNCTAD has expanded its business to operate breweries in Vietnam, Australia and Indonesia and it also maintains four breweries in China including Hong Kong (China). Overseas packaging facilities include a glass plant and metal plants in China and Vietnam as well as plastic plants in China and Indonesia.[16]

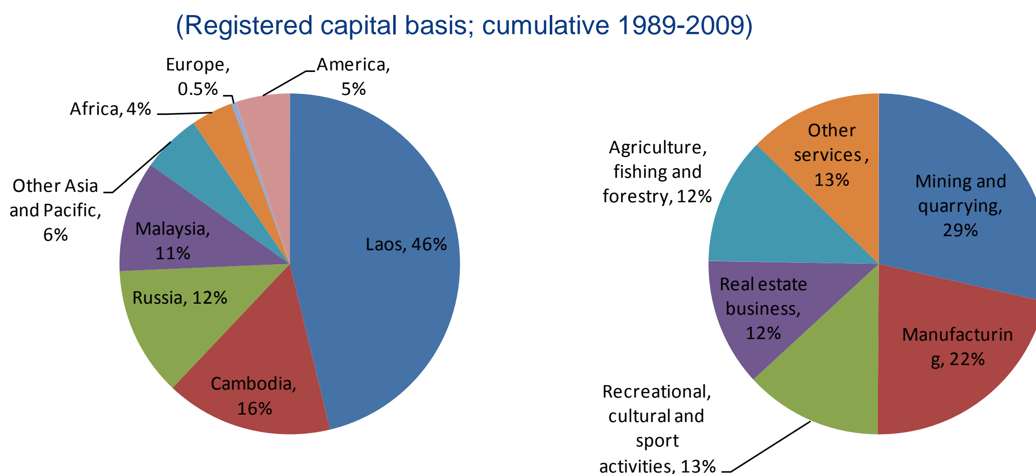
Vietnam

Vietnam's OFDI began in 2005 but the amount is still small compared with OFDI from its regional peers. With increasing integration into the world economy, rapid economic growth and continued market liberalization, Vietnam's OFDI is expected to increase in the near future. Since the establishment of a Laos-Vietnam Joint Venture in 2000 to extend loans to Vietnamese firms to invest in Laos, Laos has become Vietnam's preferred investment destination, accounting for nearly one third of the total registered FDI flows in 1989–2009.

In 2009, despite the financial crisis, Vietnamese government enterprises including the Vietnam Electricity Group, Vietnam Coal and Mineral Industries Group, Petrovietnam, Viet-Laos Power Joint-stock Company and Hoang-Anh Gia Lai developed energy, mineral and oil projects in Laos. Since the end of 2008, there have been 46 mineral projects worth nearly USD 120 million in Laos. The next largest recipients of Vietnam's OFDI are Cambodia and Russia. Vietnam's preferred sector has been capital intensive mining and quarrying, for energy security reasons, largely led by Petrovietnam, followed by manufacturing. Major Vietnamese investors abroad are all state-owned.

Figure B. 4.: Vietnam FDI Outflows by Country and Sector

(Registered capital basis; cumulative 1989-2009)



Source: General Statistics Office.

[16] Hiratsuka (2006)

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Annex II. FDI data quality and availability in ASEAN economies

To gauge the consistency, comparability and reliability of FDI data for Southeast Asian economies, the data collected from each national authority (central bank/ statistical office) and from international organizations (OECD, IMF, and UNCTAD) are compared. Variations in data availability and quality indicate that a clearer picture might be obtained if more complete and internationally-standard FDI statistics could be provided by governments.

The limited availability of sectoral FDI data makes a regional FDI comparison difficult. Especially, the compilation of FDI in services needs further improvement. In the case of Malaysia, sector-wise FDI inflows on a balance of payments basis are not available on the government website. Even for the registration and approval related data, disclosing data in terms of time series would be useful. In addition, Malaysia might like to consider including reinvested earnings when compiling its FDI data. In the case of Thailand, while the banking sector is known to benefit largely from FDI, FDI data on a balance of payments basis are compiled only for the non-banking sector. In the case of Vietnam, FDI data on disbursement are not fully disclosed by country and economic sector over time. Thus, this paper has relied on FDI approvals to observe the trend in both Vietnam and Malaysia. In the case of Singapore, its statistical office does not disclose FDI flow data but only reports the country's investment position, i.e. FDI stock.

Second, the inconsistency between FDI data from national governments and from international organizations leads to a question concerning the accuracy of data. In the case of Vietnam, for example, a continuous gap was observed between the FDI disbursement data from the country's Ministry of Planning and Investment (MPI) and FDI data from UNCTAD and ASEAN. This is because the MPI defines FDI as total investment in FIEs and therefore includes shares of capital from both domestic and foreign investors. Compiling good quality FDI data is crucial for ASEAN for two main reasons. Firstly, FDI plays a more important role in bringing in capital and technology for economic growth to the region than is the case in many other developing countries. It is therefore crucial that FDI data be accurate to support decisions by policy makers in the region. Secondly, ASEAN is expected to establish an AIA (ASEAN Investment Area) where accuracy and consistency of FDI data is vital to evaluate its effectiveness.

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Due to the limited capacity and resources of the statistical authorities, challenges persist. A joint project between the OECD and ASEAN could be organised to share the experience of OECD member countries with FDI data compilation on the basis of international standards, including the OECD Benchmark Definition of Foreign Direct Investment (2008 version) and to enhance further the quality and conformity with such standards of ASEAN FDI statistics to build a more accurate FDI data set for policy making.

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