



Asia-Pacific Research and Training Network on Trade  
Working Paper Series, No 46, October 2007

## Investment Provisions in Regional Trading Arrangements in Asia: Relevance, Emerging Trends, and Policy Implications

By

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**UPDATE:** A revised and edited version of this paper has now been published as:

Kumar, N., 2007 "Investment provisions in regional trading arrangements in Asia: relevance, emerging trends, and policy implications", pp.1-23, Chapter I in ESCAP, *Towards coherent policy frameworks: understanding trade and investment linkages – A study by the Asia-Pacific Research and Training Network on Trade*, (United Nations, New York).

Available online at: <http://www.unescap.org/tid/publication/tipub2469.asp>

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## *Executive Summary*

Investment liberalization occupies an important place in the schemes of regional economic integration complementing trade liberalization to facilitate the process of restructuring of industry on more efficient lines. This restructuring enables fuller exploitation of the locational advantages or synergies between the member countries of the regional trading bloc besides facilitating businesses reaping the economies of scale and specialization. The Single Market Plan of the European Union has unleashed such a pattern of industrial restructuring not only European corporations but also the operations of foreign multinationals operating in the EU. Such restructuring also facilitates creation of supply capabilities in relatively poorer countries thus facilitating a convergence of levels of development.

In recent times, Asian countries have also started to attach a far greater importance to regional economic integration in their trade policy after decades of faithful adherence to multilateralism. A large number of free trade arrangements are taking shape in Asia at the sub-regional levels in Southeast Asia (ASEAN) and South Asia (SAARC) or between the sub-regional groupings and their dialogue partners and between the dialogue partners. There is also a discussion on building on these attempts and evolve broader grouping. Although many of Asian RTAs are early stages of their development, the trend is quite clear. Another noticeable trend is an increasing number of Asia-Pacific RTAs extend their scope to investments. Hence, there is recognition of the importance of investment liberalization for exploiting the full benefits of RTAs.

The investment provisions included in Asian RTAs have tended to follow progressive liberalization approach given the varying levels of development existing in the region. They also have included provisions on investment protection, promotion and facilitation, MFN and dispute settlement. Asia-Pacific RTAs are consistent with the provisions of multilateral disciplines on investment as enshrined in the WTO's TRIMs Agreement and have some times attempted to adopt a more ambitious approach to elimination of performance requirements.

ASEAN's attempt to progressively deepen regional economic integration through expedited schedules of implementation of AFTA, adoption of ASEAN Investment Area, ASEAN Industrial Cooperation (AICO) Schemes and Framework Agreement on Trade in Services indicate recognition of the potential of industrial restructuring by the grouping. ASEAN has also facilitated economic integration with other Asian countries by bring them together as dialogue partners. This process has led to a number of bilateral FTAs that together form an emerging virtual community. However, due to varying scope and coverage of trade and investment rules in these initiatives, they hardly provide a seamless market to the region's enterprises for facilitating efficiency-seeking industrial restructuring.

The approach of India towards regional economic integration in Asia, and the place of investment provisions in it, is also discussed in the paper. India has accorded due place to regionalism in its trade policy. Besides participating in sub-regional economic integration in South Asia, India has engaged ASEAN and other East Asian countries as a part of the Look East Policy since 1991 that have resulted a number of RTAs/FTAs involving ASEAN as a group and several ASEAN countries, China, Japan and South Korea. The recent

RTAs/FTAs being pursued by India with Asian countries include investment provisions and have led to significant industrial restructuring already.

It is imperative that these attempts to deepen regional integration are viewed as building blocs of a broader Asian Community. The launch of East Asia Summit (EAS) bringing together leaders of ASEAN and its six dialogue partners viz. Japan, China, Korea, India, Australia and New Zealand, provides an important forum for initiatives towards creating an East Asian economic space. By providing a framework for removing trade and investment barriers, a Comprehensive Economic Partnership of East Asia (CEPEA) has the potential of unleashing a process of efficiency-seeking restructuring across countries in Asia and facilitating exploitation of their locational advantages or synergies for mutual benefit.

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## *I. Introduction*

Regional economic integration has been a most striking trend of the 1990s led by Single European Market by European Union in 1992 and North American Free Trade Agreement (NAFTA) in 1994. These RTAs pursued a deeper type of integration covering preferential free trading arrangements complemented by investment liberalization across the region. The level of economic integration was progressively deepened and coverage of RTAs expanded over time. Thus EU progressively evolved into an economic union and then a monetary union with a single currency while expanding the membership to cover 27 countries and possibly more.

A major motivation for pursuing deeper regional economic integration has been to facilitate restructuring or rationalization of industry across the region on the most efficient basis so as to exploit the economies of scale and specialization and strengthen the competitiveness of their industries. These RTAs have over time become major factors in shaping global patterns of trade, foreign direct investments (FDI), production, and competitiveness. As they began to account for the bulk of global trade, other regions also started to evolve their own schemes of global economic integration.

Asian countries which had continued to follow multilateralism all along very faithfully, began to respond to the trend of regionalism towards the late-1990s. The East Asian Crisis of 1997 provided a much needed stimulus for regional economic integration in the region. The ASEAN countries expedited the programme of implementation of ASEAN Free Trade Area (AFTA) from 2008 to 2002 and moved on to further deepen the economic integration. Japan revised its trade policy in 1999 giving a due place to regional economic integration and concluded its first FTA with Singapore. Other Asian countries also followed the trend. In particular, ASEAN facilitated the trend of regional economic integration by bringing all major Asian countries viz. Japan, China, India, Republic of Korea, and Australia and New Zealand together as dialogue partners. This has led to ASEAN+1 FTAs evolving between ASEAN countries and the dialogue partners besides a number of FTAs between the dialogue partners themselves such as those under negotiation between India and Republic of Korea and India and Japan. South Asian Association for Regional Cooperation (SAARC) has also adopted a SAFTA in 2004 which is being implemented from 2006 over a ten year period. India has been a part of this emerging trend of RTAs and FTAs in Asia. Besides being a part of SAFTA, it is evolving bilateral FTAs with a number of Asian countries. It considers these sub-regional and bilateral initiatives as building blocs of a broader Asian economic integration and has a vision of an Asian Economic Community.

The East Asian cooperation led to the launch of several regional initiatives such as the Chiang-Mai Initiative which brought together ASEAN plus three countries viz. Japan, Republic of Korea and China. Another initiative of interest is the launch in December 2005 of the East Asia Summit (EAS) as an annual forum of dialogue on regional affairs bringing together leaders of ASEAN10, Japan, China, Republic of Korea, India and Australia and New Zealand. Bringing together leaders of 16 largest and most dynamic economies of Asia, EAS is likely to provide a forum to launch a broader Asian community. Asia has therefore finally woken up to the importance of regional economic integration for its development and to respond to the challenge thrown by the worldwide trends. The emerging Asian regionalism has to be accompanied by investment liberalization to enable region's businesses to rationalize their operations to exploit the locational advantages or synergies for mutual benefit.

Against that backdrop, this paper begins by summarize the conceptual rationale for investment liberalization to fully exploit the potential of regional trading arrangements. It goes on to examine the treatment of investment in emerging FTAs/RTAs in the Asia-Pacific region and the specific investment provisions and their consistency with the existing multilateral provisions on

investment viz. WTO's TRIMs Agreement. The provisions of ASEAN framework on investment area and industrial cooperation are summarized in Section 4. Section 5 briefly examines the trends in India's RTAs policy in Asia and the emerging patterns of efficiency-seeking industrial restructuring unleashed by it. Finally Section 6 concludes with a few remarks on the importance of a broader framework for regional economic integration.

## 1.1 Relevance of Investment Liberalization in Regional Trading Arrangements: Lesson from European Economic Integration

Foreign direct investment (FDI) has a close relationship with the process of regional economic integration. By extending the effective size of the market by linking the partner countries, RTAs strengthen the investment climate for investors from outside the region. The EU has increased its share in global FDI inflows following the formation of the Single market from nearly 30 per cent in 1980s to about 50 per cent in 1990s and has stayed there.<sup>1</sup> More recent studies show that Mexico has seen a sharp rise in FDI inflows since becoming a part of NAFTA from US\$ 12 billion per year on average during 1991-93 to US\$ 54 billion during 2000-02.<sup>2</sup> A number of quantitative studies conducted in inter-country contexts have also found strong association between membership in RTAs and FDI inflows.<sup>3</sup> However, market extending (or enlargement) effect is only one and a relatively minor effect of RTAs. It is argued here that a more important effect of RTAs is strengthening of overall competitiveness of the region forming it through extensive industrial restructuring or rationalization across the region. This process of efficiency-seeking industrial restructuring is accomplished by intra-regional FDI. It is not a coincidence that the new age RTAs or FTAs generally extend their scope beyond trade to include investment liberalization and facilitation.

The trend of 'new regionalism', as the phenomenon is described to distinguish it from the earlier wave of shallow regional economic cooperation, was clearly motivated by the desire to strengthen the competitiveness of their industries is evident from the case of the EU. The major motivation of formation of the Single Market was not promotion of intra-regional trade as is commonly understood. The intra-regional trade was already quite high in the EU before the Single Market Plan and MFN tariffs were quite low and were nearly zero for intra-EU trade. The deeper regional economic integration was undertaken to facilitate restructuring or rationalization of industry across the region on the most efficient basis so as to exploit the economies of scale and specialization. The Cecchini Report commissioned by the European Commission which provided the basis for the White Paper on the Single European Market had empirically established that the European economies were losing substantially in welfare terms by not cooperating between themselves. The projected gains from industrial restructuring to exploit economies of scale and increased competition within the EU were estimated to be of the order of 3.7 per cent of GDP.<sup>4</sup>

The efficiency-seeking industrial restructuring is facilitated by liberalization of trade and investment regimes as a part of regional trading arrangements that enables free movement of goods across borders facilitating internal restructuring by removing the need to maintain horizontal national operations for multinational enterprises (MNEs). Therefore, MNEs restructure their operations by assigning the responsibility for serving specific regional or even global markets in particular product lines to certain affiliates. This strategy is sometimes called product mandating and results from the efficiency seeking restructuring or specialization within the MNE. The EU integration as also facilitated industrial restructuring of European businesses by adopting a statute of a European Company (*Societas Europaea*, S.E.) and through another legal instrument called the

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<sup>1</sup> See Kumar 1994; UNCTAD 2006

<sup>2</sup> see Kose et al. 2004

<sup>3</sup> see e.g. Kumar 2000; Medvedev 2006, among others.

<sup>4</sup> See Cecchini (1988).

European Economic Cooperation Agreement (EECA). The latter is a form of cooperation between two or more firms which become a single body corporate with the aim of furthering the business activities of the participating firms.<sup>5</sup>

The formation of Single European Market has led to a substantial restructuring of industry to seek efficiency or competitiveness. The restructuring takes the form of specific subsidiaries receiving their parent's mandate for specific goods or services for the given markets. The product mandates are given for the entire regional market in the specific product lines. For instance, Unilever decided to make all its dishwasher powder meant for European market at its Lyons (France) plant and all its toilet soap for Europe at Port Sunlight (UK) in preference to smaller plants catering to each individual market in the entire range of products.<sup>6</sup>

The Single Market Plan of the European Union has also prompted extensive industrial restructuring of American and Japanese MNEs operating in the EU to restructure their operations on a pan-European basis. For instance, IBM has reorganized its operations in pan-European basis with IBM UK looking after PCs, IBM Germany, mainframe computers and manufacturing industry; IBM France, telecommunications, and IBM Italy, mid-range machines. Thus this type of restructuring enables the enterprise to exploit the economies of scale and specialization. The location for specific product mandates is chosen on the basis of the advantages a particular country has for the particular activity. These could include factor availability and their prices, agglomeration economies and other locational advantages.<sup>7</sup> Quantitative studies conducted in the inter-country contexts have also found strong evidence of the role of RTAs in shaping the patterns of export-oriented investments made by US and Japanese MNEs across countries to exploit the potential of efficiency-seeking industrial restructuring.<sup>8</sup>

The studies on the existing RTAs have shown that in the deeper type of integration, the biggest beneficiaries are relatively poorer or lesser developed economies because of migration of industry to them helping their economy converge with those of more developed ones. It is evident that poorest economies of EU, viz. Spain, Portugal, Greece and Ireland have rapidly converged with more developed economies of the region such as Germany, France or the UK. Although resource transfers have also played a role, investment restructuring (such as relocation of production to low wage locations within the EU) has played an important role bringing about this convergence. It is also clear that investment liberalization becomes a key to facilitate the process of industrial restructuring<sup>9</sup>. The barriers to investment flows may not allow the full benefits to be reaped from the regional trade liberalization.

## 1.2 Regional Trading Arrangements in Asia-Pacific and Treatment of Investment

As observed earlier, Asian countries have been rather late entrants in exploiting the potential of FTAs/RTAs. According to data compiled by the Asian Development Bank, Asian countries were involved in only 35 FTAs –bilateral as well as plurilateral- and with regional as well as outside the regional partners in 2000. However, there is an indication that once started, Asian countries are fast catching up in the trend of signing FTAs/RTAs. By the end of 2006, Asian countries were involved in as many as 191 FTAs/ RTAs between themselves or with the outside world. The bulk of these FTAs/RTAs are at different stages of evolution and many of them may take years to implement their provisions. But the trend is clear that Asia has woken up to the

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<sup>5</sup> See Kumar (1994) for more details.

<sup>6</sup> see Kumar, 1994, for illustrations.

<sup>7</sup> see Dunning, 1998 for a typology of restructuring; Kumar 1994, 2001; Cool and Walters 1992, for a detailed analysis and case studies.

<sup>8</sup> See Kumar 1998, 2002, for evidence.

<sup>9</sup> Also see UNCTAD (2006) for a discussion.

potential of bilateral and regional arrangements like other regions to supplement trade liberalization in the multilateral framework.

As the focus of this paper is on RTAs of Asia-Pacific countries, we leave out FTAs initiated by Asia-Pacific countries with countries outside the region e.g. Singapore-US, or Australia-US. The FTAs initiated by Asian countries within Asia whether bilateral or plurilateral- are summarized in Table 1. It is apparent that they have been involved in 84 FTAs with other regional partners. As many as 26 of these agreements have been notified to WTO and 58 were in different stages of their evolution. Patterns across sub-regions suggest that countries in Central and West Asia were integrating between themselves with 17 FTAs. The other sub-regions such as East Asia, Southeast Asia and South Asia were integrating across the sub-regions. It is clear from as many as 12 FTAs between East Asia and Southeast Asia and 10 between Southeast and South Asian countries. The East Asian and Southeast Asian countries are also having 12 FTAs with the Pacific nations. These three sub-regions of Asia viz. East, Southeast and South Asia and the Pacific seem to be integrating with each other which might eventually lead to formation of a broader community.

**Table 1: Free Trade Arrangements Involving Asian Countries within the Region, 2006**

| BILATERAL FTAs                     | WTO NOTIFIED |      | NOT WTO NOTIFIED     |      |        |      |                   |      |                               |      |          |      |                    |      | TOTAL                     |      |
|------------------------------------|--------------|------|----------------------|------|--------|------|-------------------|------|-------------------------------|------|----------|------|--------------------|------|---------------------------|------|
|                                    |              |      | Under Implementation |      | Signed |      | Under Negotiation |      | (FA) Signed/Under Negotiation |      | Proposed |      | Total Not Notified |      | Notified and Not Notified |      |
|                                    | 2000         | 2006 | 2000                 | 2006 | 2000   | 2006 | 2000              | 2006 | 2000                          | 2006 | 2000     | 2006 | 2000               | 2006 | 2000                      | 2006 |
| <b>Within sub-region</b>           |              |      |                      |      |        |      |                   |      |                               |      |          |      |                    |      |                           |      |
| Central and West Asia              | 2            | 9    | 0                    | 0    | 8      | 8    | 0                 | 0    | 0                             | 0    | 0        | 0    | 8                  | 8    | 10                        | 17   |
| East Asia                          | 0            | 1    | 0                    | 0    | 0      | 0    | 0                 | 1    | 0                             | 0    | 0        | 2    | 0                  | 3    | 0                         | 4    |
| South Asia                         | 0            | 1    | 0                    | 2    | 0      | 1    | 0                 | 1    | 0                             | 0    | 0        | 1    | 0                  | 5    | 0                         | 6    |
| Southeast Asia                     | 1            | 1    | 0                    | 0    | 0      | 0    | 0                 | 0    | 0                             | 0    | 0        | 0    | 0                  | 0    | 1                         | 1    |
| The Pacific                        | 2            | 2    | 0                    | 0    | 0      | 0    | 0                 | 0    | 0                             | 0    | 0        | 0    | 0                  | 0    | 2                         | 2    |
| <b>Across sub-region</b>           |              |      |                      |      |        |      |                   |      |                               |      |          |      |                    |      |                           |      |
| Central and West Asia + South Asia | 0            | 0    | 0                    | 0    | 0      | 0    | 0                 | 0    | 0                             | 0    | 0        | 2    | 0                  | 2    | 0                         | 2    |
| East Asia + South Asia             | 0            | 0    | 0                    | 0    | 0      | 1    | 0                 | 1    | 0                             | 0    | 0        | 2    | 0                  | 4    | 0                         | 4    |
| East Asia + Southeast Asia         | 0            | 3    | 0                    | 1    | 0      | 1    | 0                 | 5    | 0                             | 0    | 0        | 2    | 0                  | 9    | 0                         | 12   |
| East Asia + The Pacific            | 0            | 0    | 0                    | 0    | 0      | 0    | 0                 | 1    | 0                             | 2    | 1        | 3    | 1                  | 6    | 1                         | 6    |
| Southeast Asia + South Asia        | 0            | 0    | 0                    | 1    | 0      | 0    | 0                 | 2    | 0                             | 2    | 0        | 5    | 0                  | 10   | 0                         | 10   |
| Southeast Asia + The Pacific       | 0            | 4    | 0                    | 0    | 0      | 0    | 0                 | 2    | 0                             | 0    | 0        | 0    | 0                  | 2    | 0                         | 6    |
| The Pacific + South Asia           | 0            | 0    | 0                    | 0    | 0      | 0    | 0                 | 0    | 0                             | 0    | 0        | 1    | 0                  | 1    | 0                         | 1    |
| <b>Regional or Plurilateral</b>    |              |      |                      |      |        |      |                   |      |                               |      |          |      |                    |      |                           |      |
| Asian Bloc                         | 4            | 4    | 0                    | 2    | 0      | 0    | 0                 | 0    | 0                             | 1    | 0        | 1    | 0                  | 4    | 4                         | 8    |
| Asian Bloc + Asian Country         | 0            | 1    | 0                    | 0    | 0      | 1    | 0                 | 1    | 0                             | 2    | 0        | 0    | 0                  | 4    | 0                         | 5    |
| <b>TOTAL</b>                       | 9            | 26   | 0                    | 6    | 8      | 12   | 0                 | 14   | 0                             | 7    | 1        | 19   | 9                  | 58   | 18                        | 84   |

Notes: As of December 2006

Central and West Asia - Afghanistan; Armenia; Azerbaijan; Kazakhstan; Kyrgyz Republic; Pakistan; Tajikistan; Turkmenistan; Uzbekistan

East Asia - China, People's Republic of; Hong Kong, China; Japan; Republic of Korea, Republic of; Mongolia; Taipei, China

South Asia - Bangladesh; Bhutan; India; Maldives; Nepal; Sri Lanka

Southeast Asia - Brunei Darussalam; Cambodia; Indonesia; Lao PDR; Malaysia; Myanmar; Philippines; Singapore; Thailand; Viet Nam

The Pacific - Australia; Cook Islands; Fiji Islands; Kiribati; Marshall Islands; Micronesia, Federated States of; Nauru; New Zealand; Palau; Papua New Guinea; Samoa; Solomon Islands; Timor-Leste; Tonga; Tuvalu; Vanuatu

Asian Plurilateral - refers to groupings of more than two countries where all the members are Asian countries.

Source: Author based on data provided by ARIC/ADB, Tables 5 and 6, available at [www.aric.adb.org](http://www.aric.adb.org).

## *II. Treatment of Investment in Asia-Pacific RTAs*

As regionalism is a relatively recent trend in Asia, most of the FTAs are in early stages of their evolution. A number of them are still being considered by the countries concerned and others are in the process of negotiation or implementation. Table 2 lists 56 FTAs/RTAs initiated by Asian countries with Asian partners, for which some information is available. It also indicates whether the scope of FTA/RTA extends to cover investment and commercial presence as a mode of service delivery which is akin to FDI in services. It finds that only 26 of 56 RTAs listed do cover investment provisions. A closer examination will suggest some patterns. One is that more recent agreements are generally more likely to include investment than the older ones. This is because of the recognition of the importance of investment liberalization in overall scheme of economic integration and its role in facilitating efficiency-seeking industrial restructuring. Some of the older arrangements are being revised to extend their scope to cover investment. India-Sri Lanka FTA is one such agreement originally signed in 1998 and in force since 2000 which is being evolved into a Comprehensive Economic Partnership Agreement covering trade in goods, services and investments. The other noticeable pattern is that FTAs/RTAs involving capital exporting countries such as Japan, Australia, New Zealand, Singapore tend to include investment provisions.

## *III. Scope of Investment Provisions in Asia-Pacific RTAs*

To examine in greater detail the scope of investment provisions in Asian RTAs, we focused on 18 Agreements involving investment provisions of which texts are available. The texts of other 8 Agreements containing investment provisions are not yet available.

Generally the investment chapter of the agreements follows a structure beginning with definitions of investments, treatment of investors and investments from the partner country including liberalization of that, sometimes it defines the criteria of determining the origin of investors (like rules of origin in the case of trade in goods) and provisions for MFN. Some investment chapters also cover treatment of performance requirements (which are like non-tariff barriers in the case of trade in goods), such as local content requirements. Some times they specify the types of performance requirements prohibited with the framework of the agreement like TRIMs Agreement in WTO, others may just quote TRIMs provisions. An important part of investment chapters is devoted to investment protection and promotion and some times on cooperation and transparency etc. Investors from the partner countries are assured of a fair compensation in the event of any nationalization or expropriations. They also list the conditions that can be treated as expropriations. These provisions may seem innocuous but have become important in the light of NAFTA disputes on regulatory takings viz. where companies have filed suits against governments of partner countries on the policy changes affecting their profitability or prospects and seeking compensation as deemed expropriation. The investment chapter also covers provisions on settlement of investment disputes and whether investor from one party can resolve disputes against the host governments or disputes between governments. Finally, there are provisions for safeguards, exceptions, and review of the agreement.

**Table 2: Treatment of Investment in Select Asian RTAs**

| Short Title          | Agreement  | Status                       | Coverage of Investment and Mode 3 in Services |                     |
|----------------------|--|------------------------------|---|---------------------|
|                      |  |                              | Commercial Presence                           | Investment (Others) |
| AJCEP                | Framework Agreement for ASEAN – Japan Comprehensive Economic Partnership       | in force since 2004          | No  | Yes                 |
| ANZCERTA             | Australia-New Zealand Closer Economic Relations Trade Agreement                | in force since 1983          | Yes   | No                  |
| APTA                 | Asia-Pacific Trade Agreement (Bangkok Agreement)                               | in force since 1976          | No  | No                  |
| ASEAN-CER            | Framework Agreement for ASEAN-ANZCERTA Free Trade Agreement                    | under negotiation since 2004 | Yes   | Yes                 |
| ASEAN                | ASEAN Free Trade Area  | in force since 1993          | No  | Yes                 |
| ASEAN Services       | ASEAN Framework Agreement on Services  | in force since 1996          | Yes   | No                  |
| ASEAN-China FA       | ASEAN-China Framework Agreement on Comprehensive Economic Cooperation          | in force since 2003          | Yes   | Yes                 |
| ASEAN-India FA       | ASEAN-India Framework Agreement on Comprehensive Economic Cooperation          | in force since 2004          | Yes   | Yes                 |
| ASEAN-Korea FA       | ASEAN-Korea Framework Agreement on Comprehensive Economic Cooperation          | in force since 2006          | Yes   | Yes                 |
| Australia-China      | Australia – China Free Trade Agreement   | under negotiation since 2005 | No  | Yes                 |
| Australia – Japan    | Australia-Japan Trade and Economic Framework                                   | under negotiation since 2007 | No  | Yes                 |
| Australia-Malaysia   | Australia-Malaysia Free Trade Agreement  | under negotiation since 2005 | No  | Yes                 |
| Australia-Thailand   | Thailand-Australia Free Trade Agreement  | in force since 2005          | Yes   | Yes                 |
| Bhutan-India         | Bhutan-India Free Trade Agreement  | in force since 2006          | No  | No                  |
| BIMSTEC              | Bay of Bengal initiative for Multi-Sectoral Technical and Economic Cooperation | in force since 1997          | No  | Yes                 |
| China-Hong Kong, SAR | Mainland and Hong Kong Closer Economic Partnership Agreement                   | in force since 2004          | Yes   | No                  |
| China-Korea          | China-Korea Free Trade Agreement   | under negotiation since 2005 | No  | No                  |
| China – MACAO,       | Mainland and Macao-SAR Closer Economic Partnership Agreement                   | in force since 2004          | Yes   | No                  |
| China-Pakistan       | Free Trade Agreement between China and Pakistan                                | pending country ratification | No  | Yes                 |
| China – Thailand     | China-Thailand Free Trade Agreement  | in force since 2003          | No  | No                  |
| India-Afghanistan    | India-Afghanistan Preferential Trade Agreement                                 | in force since 2003          | No  | No                  |
| India-Bangladesh     | Trade Agreement between India and Bangladesh                                   | in force since 2006          | No  | No                  |
| India-Nepal          | Indo-Nepal Treaty of Trade   | in force since 1991          | No  | No                  |
| India-Singapore      | India-Singapore Comprehensive Economic Cooperation Agreement                   | in force since 2005          | Yes   | Yes                 |
| India-Sri Lanka      | Free Trade Agreement between the Republic of India and Sri Lanka               | in force since 2001          | No  | No                  |
| India-Thailand       | India-Thailand Framework Agreement for establishing a FTA                      | in force since 2004          | No  | Yes                 |
| Japan-Brunei         | Japan-Brunei Darussalam Economic Partnership Agreement                         | under negotiation            | No  | No                  |

|                       |  |                              |      |     |
|-----------------------|--|------------------------------|------|-----|
| Japan-India           | Japan-India Economic Partnership Agreement   | under negotiation since 2007 | Yes  | Yes |
| Japan-Indonesia       | Japan-Indonesia Economic Partnership Agreement                                       | under negotiation since 2005 | No   | No  |
| Japan-Korea           | Japan-Korea Free Trade Agreement   | under negotiation since 2004 | No   | No  |
| Japan-Malaysia        | Japan-Malaysia Economic Partnership Agreement  | in force since 2006          | Yes  | Yes |
| Japan-Philippines     | Japan-Philippines Economic Partnership Agreement                                     | pending country ratification | Yes  | Yes |
| Japan-Singapore       | Japan-Singapore New-Age Economic Partnership Agreement                               | in force since 2002          | Yes. | Yes |
| Japan-Thailand        | Japan -Thailand Economic Partnership Agreement                                       | pending country ratification | Yes  | Yes |
| Japan-Vietnam         | Agreement between Japan and Vietnam on Economic Partnership                          | under negotiation since 2006 | No   | No  |
| Kazakhstan-Uzbekistan | Free Trade Agreement between Kazakhstan and Uzbekistan                               | in force since 1997          | No   | No  |
| Korea-India           | Korea-India Comprehensive Economic Partnership Agreement                             | under negotiation since 2006 | Yes  | Yes |
| Korea-Singapore       | Free Trade Agreement between Republic of Republic of Korea and Republic of Singapore | in force since 2006          | No   | Yes |
| Lao, PDR – Thailand   | Lao PDR – Thailand Preferential Trading Arrangement                                  | in force since 1991          | No   | No  |
| Malaysia-Korea        | Malaysia-Korea Free Trade Agreement  | under negotiation since 2005 | No   | No  |
| Malaysia-New Zealand  | Malaysia-New Zealand Free Trade Agreement  | under negotiation since 2005 | No   | No  |
| Malaysia-Pakistan     | Agreement on the Early Harvest Programme for Malaysia-Pakistan FTA                   | in force since 2006          | No   | No  |
| MSG                   | Trade Agreement Among the Melanesian Spearhead Group Countries                       | in force since 1994          | No   | No  |
| New Zealand-China     | New Zealand-China Free Trade Agreement   | under negotiation since 2004 | No   | Yes |
| New Zealand-Hong Kong | Hong Kong-New Zealand Closer Economic Partnership                                    | Under negotiation since 2001 | No   | No  |
| New Zealand-Singapore | Agreement between New Zealand and Singapore on a Closer Economic Partnership         | in force since 2001          | Yes  | Yes |
| New Zealand-Thailand  | New Zealand – Thailand Closer Economic Partnership Agreement                         | in force since 2005          | No   | Yes |
| Pakistan-Sri Lanka    | Pakistan-Sri Lanka FTA   | in force since 2005          | No   | No  |
| PATCRA                | Agreement on Trade and Commercial Relations between Australia and Papua New Guinea   | in force since 1977          | No   | Yes |
| PICTA                 | Pacific Island Countries Trade Agreement   | in force since 2006          | No   | No  |
| PTA-D-8               | Preferential Tariff Agreement – Group of 8 Developing Countries                      | pending country ratification | No   | No  |
| SAFTA                 | South Asian Free Trade Area  | in force since 2006          | No   | No  |
| Singapore-Australia   | Singapore-Australia Free Trade Agreement   | in force since 2003          | Yes  | Yes |
| Singapore-Pakistan    | Singapore-Pakistan Free Trade Agreement  | under negotiation since 2005 | No   | No  |
| Singapore-Sri Lanka   | Singapore-Sri Lanka Comprehensive Economic Partnership Agreement                     | under negotiation since 2003 | No   | No  |
| SPARTECA              | South Pacific Regional Trade and Economic Cooperation Agreement                      | in force since 1981          | No   | No  |

*Source:* Author based on the database of Asian RTAs available at UN-ESCAP website.

The investment provisions included in recent FTAs/RTAs are generally more ambitious compared to bilateral investment protection and promotion agreements (BIPAs). The scope of BIPAs generally tended to include limited national treatment of investments (as opposed to investors) made in accordance to national laws and policies, investment protection and promotion and dispute settlements. Therefore, BIPAs did not generally cover investment liberalization which has been the main objective of the RTAs/FTAs.

The key investment provisions in the 18 agreements are summarized in Table 3. In what follows, we summarize the highlights of these agreements.

### 3.1 Definition of Investments:

Most of the FTAs/RTAs signed by Asia-Pacific countries have adopted a broad definition of investments covering transfer any assets or intellectual property. However, some of them such as ASEAN Investment Area and New Zealand-Thailand FTA have employed a narrow definition restricting the scope to only direct investments. ASEAN Investment Area and Japan-Malaysia FTA have specifically excluded portfolio investments from its scope thus effectively confining to direct investments. Most of the agreements also define criteria of determining the origin of an enterprise or investor and generally tend to adopt majority ownership in the country of origin as a basis of determining the nationality.

**Table 3: Key Investment Provisions in Select Asian RTAs**

| Agreement  | Definition of Investment | Pre-establishment National Treatment      | Post-establishment National Treatment | MFN      | Performance Requirements                         | Investment Protection, Promotion, Facilitation, | Dispute Settlement Provisions           |
|--|--------------------------|---|---------------------------------------|----------|--|---|---|
| ASEAN Investment Area (1998, amendments 2001, 2003)          | Direct investments       | -ive list                                 | -ive list                             | yes      | -  | Yes   | ASEAN DSM                               |
| ASEAN-China Framework  | To be defined            | Progressive (+list)                       | implicit                              | implicit | to be defined                                    | Yes   | to be defined                           |
| ASEAN-Australia-NZ CER Framework                             | To be defined            | progressive                               | implicit                              | implicit | to be defined                                    | Yes   | to be defined                           |
| ASEAN-India Framework  | To be defined            | progressive                               | Implicit                              | implicit | to be defined                                    | Yes   | to be defined                           |
| ASEAN-Republic of Korea Framework                            | To be defined            | Progressive (+list)                       | Implicit                              | implicit | to be defined                                    | Yes   | to be defined                           |
| ASEAN-Japan Framework  | To be defined            | To be defined                             | Implicit                              | implicit | to be defined                                    | Yes   | to be defined                           |
| China-Hong Kong SAR CER                                      | -                        | -   | -                                     | -        | -  | Yes   | -                                       |
| Japan-Singapore  | broad                    | -ive list                                 | -ive list                             | yes      | TRIMs-plus                                       | Yes   | Investor-State (I-S), State-State (S-S) |
| Japan-Malaysia   | broad                    | -ve list (excludes portfolio investments) | -ive list                             | yes      | TRIMs  | Yes   | I-S, S-S                                |
| Japan-Philippines  | broad                    | -ve list                                  | -ive list                             | Yes      | TRIMs-plus; (labour and environmental standards) | Yes   | to be negotiated                        |
| Republic of Korea-Singapore                                  | broad                    | -ive list                                 | -ive list                             | yes      | TRIMs-plus                                       | yes   | I-S, S-S                                |
| India-Singapore Comprehensive Economic Cooperation Agreement | broad                    | +ive list                                 | +ive list                             | yes      | TRIMs  | yes   | I-S, S-S                                |
| India-Thailand Framework for FTA                             | To be defined            | progressive                               | Implicit                              | implicit | to be defined                                    | yes   | to be defined                           |
| Australia-Singapore  | broad                    | -ive list                                 | -ive list                             | -        | -  | yes   | I-S, S-S                                |
| Australia-Thailand   |                          | +ive list                                 | -ive list                             | yes      | -  | yes   | I-S, S-S                                |
| New Zealand-Singapore  | broad                    | -ive list                                 | -ive list                             | yes      |  | yes   | I-S, S-S                                |
| New Zealand-Thailand   | Direct investments       | +ive list                                 | -ive list                             | yes      | -  | yes   | I-S, S-S                                |
| BIMSTEC Framework  | To be defined            | progressive                               | Implicit                              | implicit | to be defined                                    | yes   | to be defined                           |

Source: Author on the basis of original texts of FTAs.

### 3.2 Treatment of ‘Investors’ or Pre-establishment National Treatment

A key provision of the investment arrangements in FTAs relates to pre-establishment national treatment as it determines the level of investment liberalization. Most of the FTAs/RTAs involving Asia-Pacific countries provide pre-establishment national treatment on a positive list basis or they provide a progressive liberalization through putting sectors on an annex where foreign investors are treated on par with national or domestic investors. However, an increasing number of agreements have also incorporated pre-establishment national treatment based on a negative list basis. These typically include countries that have adopted open regimes for foreign capital already such as countries like Singapore. These agreements therefore provide a liberal treatment to foreign investors because unless specified in the annex; all investments from the partner country receive a treatment ‘not less favourable’ to that given to a national investor (however, more favourable treatment is not excluded).

### 3.3 Treatment of ‘Investments’ or Post-Establishment National Treatment

More countries tend to accord national treatment of investments that have been made. Hence, NT in post-establishment phase is generally built on the negative list basis or on the same basis as pre-establishment NT. Thailand’s FTAs with Australia and New Zealand are cases in point where the pre-establishment NT is based on a positive-list basis and post-establishment NT is on a negative list basis.

### 3.4 Performance Requirements and Consistency with TRIMs

Treatment of performance requirements is another aspect of liberalization of investment policy regimes. Here the benchmark or MFN treatment is provided by the WTO Agreement on Trade Related Investment Measures (TRIMs). TRIMs Agreement seeks to eliminate a few types of performance requirements such as local content regulations and requirements limiting imports to certain proportion of output. It leaves a number of other performance requirements and investment measures including export obligations that can be imposed by WTO members on enterprises and investors.<sup>10</sup> A number of FTAs/RTAs have tended to expand the list of investment measures included in TRIMs to cover others such as export obligations, requirement to transfer technology or perform R&D etc. By prohibiting such performance requirements for investments originating in FTA partner countries, these provisions seek to liberalize the conditions for investment. A number of Asian RTAs/FTAs have included TRIMs plus provisions on performance requirements. These include Japan-Singapore New Age Partnership Agreement which lists a number of investment measures that will not be imposed by the parties. Japan-Philippines Agreement also includes TRIMs-plus provisions. The Japan-Philippines Agreement is perhaps unique in Asia to include performance requirements based on labour and environmental standards also. These two Agreements tend to follow the treatment of performance requirements as incorporated by the FTAs signed by the US which is trying to evolve WTO plus provisions in investments and IPRs, among other spheres, through bilateral FTAs. Other FTAs/RTAs have provided for TRIMs type of treatment either explicitly (India-Singapore, Japan-Malaysia) or implicitly (by being silent and hence leaving the treatment to TRIMs).

### 3.5 MFN, Investment Protection, Promotion and Facilitation

MFN provisions are generally included in most RTAs/FTAs. Different RTAs/FTAs vary in terms of the extent of investment promotion and facilitation covered. Some of them, as China-Hong Kong CER focus on investment facilitation exclusively. Some of them go on

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<sup>10</sup> See Corea and Kumar (2003) for a detailed analysis of TRIMs Agreement and its provisions.

to specify facilitation activities such as cooperation between the investment promotion agencies, linking up of websites (as provided in the India-Singapore CECA) to promote investment flows. Provisions on investment protection are also generally found in almost all FTAs/RTAs providing a fair and equitable treatment in the event of an expropriation although there is a variation in terms of coverage of what constitutes an expropriation. A liberal definition of expropriation adopted by NAFTA covers the changes in business prospects resulting from any policies or regulations imposed by the host government. This liberal treatment has led to a large number of disputes in NAFTA brought by companies against governments. Asian RTAs have followed a more cautious approach in this respect although there is a variation across them.

### 3.6 Dispute Settlement Mechanism

Most of the FTAs/RTAs also provide guidelines for settlement of investment disputes. They provide limited form of investor to state dispute settlement through consultation and suggest other means of dispute settlement if the consultation does not work in some circumstances. Most of the FTAs/RTAs also refer to dispute settlement mechanism available within the framework of ICSID (International Convention of Settlement of Investment Dispute) managed by the World Bank and UNCITRAL (such as setting up of ad hoc tribunals). State-to- state dispute settlement is generally provided in most of the RTAs/FTAs.

## *IV. ASEAN FTAs and Investment Area for Facilitating Industrial Restructuring*

Among the Asian RTAs, ASEAN stands out as one having recognized the potential of regional trade and investment liberalization in fostering efficiency-seeking industrial restructuring and overall competitiveness of the grouping. ASEAN has closely followed the EU's example in regional trade liberalization through AFTA, liberalizing trade in services through ASEAN Framework Agreement for Trade in Services (AFAS) and facilitating the exploitation of the potential of industrial restructuring through additional policy measures viz. ASEAN Industrial Cooperation (AICO) scheme and ASEAN Investment Area (AIA). In what follows we take a brief look at the steps taken by ASEAN to exploit the potential of regional economic integration especially in industry.

### 4.1 ASEAN Free Trade Agreement (AFTA)

The decision taken during the Fourth ASEAN Summit in 1992 to establish the ASEAN Free Trade Area (AFTA) by the year 2008 is the most significant and ambitious step taken by ASEAN so far in terms of regional economic integration. The AFTA Treaty was signed in Singapore by the six original founding members, Indonesia, Malaysia, Philippines, Singapore, Thailand, and Brunei. In mid-1995, Vietnam gained admission as the seventh member of ASEAN. Laos and Myanmar followed suit two years later in 1997 with Cambodia joining in 1999. AFTA provides a framework and forum for ASEAN members-states for moving towards deeper economic integration between themselves. The main mechanism for the implementation of AFTA is the Common Effective Preferential Tariff (CEPT). The CEPT is an agreed effective tariff which is preferential to ASEAN member-states, and is to be applied to goods that have been identified for inclusion under the CEPT scheme originating from member-states. The original schedule required the CEPT tariffs to be reduced to between 0-5 percent within 15 years, i.e. by 2008, while non-tariff barriers were to be eliminated beginning 1 January 1993. In September 1994, ASEAN agreed to accelerate the establishment of AFTA by reducing the initial time frame from 15 to 10 years. Under the

1994 amended timetable, the full realisation of AFTA with tariffs falling between zero and 5 percent was expected by the year 2003 for the original ASEAN five: Indonesia, Malaysia, Thailand, Singapore and the Philippines as well as Brunei. The deadline for Vietnam was 2006 and for Myanmar and Laos, 2008. To facilitate recovery from the economic crisis of 1997, ASEAN members announced a further advancement of the AFTA schedule in December 1998 for the six original signatories by one year from 2003 to 2002. The six also agreed to achieve a minimum of 90 percent of their total tariff lines with tariffs between 0-5 percent by the year 2000. In theory, this would account for 90 percent of intra-ASEAN trade.<sup>11</sup>

Furthermore, ASEAN has complemented formation of AFTA with other initiatives to facilitate intra-regional trade and speed up the industrial restructuring with other initiatives. These include harmonization of customs procedures and standards. ASEAN initially targeted 2002 for the adoption of an ASEAN Harmonized Tariff Nomenclature and has brought forward the adoption of the WTO Valuation Agreement (WVA) to 2000. ASEAN is developing product-specific mutual recognition arrangements (MRAs) for cosmetics, pharmaceutical, electrical and telecommunication products, among other products. ASEAN harmonized national standards with international standards such as those of the International Standards Organisation (ISO), the International Electro-technical Commission (IEC) and the International Telecommunications Union (ITU) for 20 priority product groups that some of the most widely traded in the region such as radios, televisions, refrigerators, air conditioners and telephones.

## 4.2 ASEAN Framework Agreement on Trade in Services (AFAS)

In recognition of the growing importance of trade in services, ASEAN adopted AFAS on 15 December 1995 to substantially eliminate barriers to trade in services among ASEAN countries and in order to improve the efficiency and competitiveness of ASEAN services providers. AFAS provides the broad guidelines for ASEAN Member Countries to progressively improve market access (MA) and provide national treatment (NT) for ASEAN services providers following GATS-Plus commitments. To further expedite liberalization of trade in services, ASEAN amended AFAS in 2003 to enable for the application of “ASEAN Minus X” formula in the implementation of Member Countries’ services commitments. Under this formula, countries that are ready to liberalize a certain service sector may proceed do so without having to extend the concessions to non-participating countries. Under AFAS major progress has been achieved in liberalization of financial services and air transport services. Mutual Recognition Arrangements (MRAs) have also been concluded on engineering services and nursing services and negotiations are in progress for architecture, accountancy, surveying, medical practitioners, and tourism. ASEAN expects to have free flow of services across all sectors and modes across the region by 2015.<sup>12</sup>

## 4.3 ASEAN Industrial Cooperation (AICO)

To facilitate efficiency-seeking industrial restructuring and strengthen the competitiveness of ASEAN’s manufacturing industry, the ASEAN Industrial Cooperation (AICO) Agreement was signed in 1996. For companies in the AICO scheme, the ASEAN market was almost fully integrated even before the 2002 deadline for CEPT of 0-5%. In AICO, goods produced by and traded between companies operating in two or more ASEAN countries enjoyed full AFTA treatment immediately i.e. 0-5 per cent tariffs. Therefore, participating companies could benefit from economies of scale by restructuring across the region by taking advantage of preferential tariff rates. To maintain the relevance of the AICO scheme beyond 2002 when the CEPT rates reached 0-5% as per the AFTA, AICO scheme

<sup>11</sup> See <http://www.aseansec.org/> for more details.

<sup>12</sup> see for more details <http://www.aseansec.org/6626.htm>

was amended to provide for new preferential tariff rates to be given to new approved AICO projects: zero percent for Brunei Darussalam, Cambodia, Indonesia, Laos, Malaysia and Singapore; 0-1 percent for the Philippines; 0-3 percent for Thailand; and 0-5 percent for Myanmar and Viet Nam. The Philippines, Thailand and Myanmar will work towards reducing the preferential tariff rates to zero percent for AICO arrangements by 1 January 2005, while Viet Nam will do so by 1 January 2006. By early 2004, 118 applications for AICO arrangements had been approved, which were expected to generate an estimated value of about US\$ 1.2 billion worth of transactions per year.<sup>13</sup>

#### 4.4 ASEAN Investment Area (AIA)

The Framework Agreement on the AIA was signed in 1998 to allow free flow of direct investment, technology and skilled professionals between ASEAN countries to enable investors to harness synergies of Member Countries in order to maximize business and production efficiency by adopting regional business strategies and regional production networks. The AIA calls for opening up of all industries in the region to ASEAN investors and granting of national treatment (NT) to them (excepting those on temporary exclusion lists, TEL). The industries on the temporary exclusion lists were to be reviewed after 2 years and phased out by 2010 by ASEAN-6 countries and by 2015 by the CLMV countries. In 2001 the AIA Agreement was amended to cover manufacturing, agriculture, mining, forestry and fishery sectors, and services incidental to these sectors and provided a new expedited schedule for phasing out the TEL. The new schedules required TEL in manufacturing in the case of ASEAN-6 countries and Myanmar by 2003 and by 2010 for the other three countries. The 'ASEAN investor' for the purpose of according NT has been defined very liberally and qualifies a number of foreign joint ventures too. Recognizing the importance of investment in delivery of services, and to exploit business opportunities to globally competitive services industries, ASEAN in yet another amendment to AIA adopted in 2003 expanded the AIA to include services such as, education services, health care, telecommunication, tourism, banking and finance, insurance, trading, e-commerce, distribution and logistics, transportation and warehousing, professional service such as accounting, engineering and advertising, even on ASEAN-X principle as agreed in AFAS.

#### 4.5 Beyond AFTA and AIA

ASEAN has moved towards deepening regional economic integration by aiming to create an ASEAN Economic Community by 2020 as a part of ASEAN Vision 2020 adopted in Bali Summit in 2003. Subsequently the date of completion of the ASEAN Economic Community has been advanced to 2015. ASEAN has also facilitated the broader Asian economic integration by bringing together other major Asian countries viz. Japan, China, Republic of Korea, India and Australia and New Zealand as dialogue partners and starting FTA negotiations with them (the so called ASEAN+1) FTAs most of which have investment provisions, as observed in the previous section. This interaction as dialogue partnership has also facilitated FTAs between individual ASEAN countries and the dialogue partners (e.g. India-Singapore) and also between the dialogue partners themselves (e.g. India-Japan).<sup>14</sup> This interaction has led to multiple FTAs combining nearly all pairs of ASEAN and its dialogue partners representing an emerging virtual community. However, this virtual community is not real as it will not provide a seamless market to the businesses to restructure themselves to exploit the synergies fully due to varying scope, coverage and rules governing different agreements as observed above with respect to investment provisions. ASEAN need to drive this process to creation of a broader framework that can coalesce all these bilateral arrangements in a single framework. Such attempts have not succeeded so far in the

<sup>13</sup> see for more details <http://www.aseansec.org/6361.htm>

<sup>14</sup> see Kumar 2005 for a more detailed analysis.

framework of ASEAN+3 bringing together Japan, China, and Republic of Korea because of differences between major dialogue partners viz. Japan and China. In December 2005 in Kuala Lumpur a new forum of East Asia Summit was launched with leaders of ASEAN and six dialogue partners viz. Japan, China, Republic of Korea, India, Australia and New Zealand. At their second session in Cebu in January 2007, EAS leaders have launched a track-II study on the feasibility of a Comprehensive Economic Partnership of East Asia (CEPEA) covering the 16 countries. It is conceivable that CEPEA could provide a framework for a broader regional arrangement for liberalization of trade and investment regimes in Asia for facilitating the exploitation of efficiency seeking industrial restructuring in the continent. A number of studies have highlighted the relevance of a broader regional arrangement like CEPEA in bringing major welfare gains for the region and the rest of the world because of its trade creating potential.<sup>15</sup>

## V. *Investment in India's Regional Economic Integration Policy*

India has attached a high importance to regional economic integration in its trade policy all along. It has been a founding member of the Bangkok Agreement that happens to be one of the first preferential trade agreement having been signed in 1975 combining some of the Asian countries including China, Republic of Korea, Sri Lanka, Bangladesh and Lao PDR. India has also been an active member of the Asian Clearing Union since its inception in the mid-1970s. India has been participating in South Asian Association for Regional Cooperation formed in 1985. In recent years, especially over the past decade, India's efforts towards regional economic integration have acquired considerable momentum as summarized below.

### 5.1 India's RTAs in Asia-Pacific

Within the South Asia Sub-region, India has concluded two free trade agreements (FTAs)—the India-Sri Lanka Free Trade Agreement (signed in 1998 and effective from 2000) and the South Asian Free Trade Area (signed in 2004 and effective from 2006). Aside from these recent, and broader initiatives, India has had long-standing arrangements in the sub-continent, such as India's bilateral treaties of trade and transit and FTAs with Nepal and Bhutan and exchange of trade preferences with South Asian countries under four rounds of South Asian Preferential Trade Agreement (SAPTA) since 1995. A preferential trade agreement was also signed between India and Afghanistan in March 2003. The initial evidence on the India-Sri Lanka free trade agreement (ISLFTA), which was signed in 1998 and been in operation since 2000, appears positive with respect to increasing trade and investment flows and is now moving towards a further deepening within the framework of a comprehensive economic partnership, covering trade in goods, services, investment and economic cooperation.<sup>16</sup>

India's regional economic integration initiatives outside the South Asian sub-region have been driven by the 'Look East Policy' adopted by the country in 1991, to strengthen economic relationships with the East Asian countries. The policy was initially aimed primarily at improving political, strategic and economic relationships with ASEAN but has since been extended to reinforce economic relationships with China, Republic of Korea and Japan. As part of the Look East Policy, India became a Sectoral Dialogue Partner of ASEAN

<sup>15</sup> See Kumar (2005) and Brooks et al. (2005) for more details. Also see RIS (2006).

<sup>16</sup> See Kelegama and Mukherjee 2007, for an analysis of the impact of India-Sri Lanka FTA.

in 1992 and Full Dialogue Partner in 1996. In November 2002, the India-ASEAN partnership was upgraded to a Summit-level dialogue and has seen a substantial transformation of economic relations since then. The Framework Agreement on Comprehensive Economic Cooperation between India and ASEAN incorporating FTA was signed at the Bali Summit in 2003. At the Laos Summit in 2004, they signed a long-term Partnership for Peace, Progress and Shared Prosperity based on the work done by the think-tanks of ASEAN and India<sup>17</sup>. The India-ASEAN FTA currently under negotiation is expected to be implemented in a phased manner from 2007. The India-ASEAN FTA Framework Agreement is complemented by a Comprehensive Economic Cooperation Agreement (CECA) signed between India and Singapore in 2005, and the India-Thailand bilateral Free Trade Framework Agreement Early Harvest Scheme under which preferential concessions have been exchanged on a specified set of commodities applicable since September 2004. India is also a part of BIMSTEC (Bay of Bengal Initiative for Multisectoral Techno-Economic Cooperation) which combines seven South and Southeast Asian countries and which is also moving towards a FTA with a Framework Agreement signed in 2004. India also has a programme of sub-regional cooperation viz., Mekong-Ganga Cooperation (MGC), combining Cambodia, Laos, Myanmar, Vietnam, Thailand and India focusing on infrastructure development. All these FTAs or comprehensive arrangements being evolved by India with ASEAN countries involve investment liberalization, as summarized in the previous sections.

In the recent years India has strived to strengthen her economic linkages with the Northeast Asian countries viz., China, Japan, and Republic of Korea. Joint study groups were set up with each of these countries to examine the feasibility of free trade arrangements or comprehensive economic partnership arrangements. A comprehensive economic cooperation arrangement between India and Republic of Korea is currently in the process of negotiation and are likely to be completed in 2007. Negotiations of India-Japan comprehensive economic partnership arrangement have been launched in early 2007 and will be completed by 2008. Both these arrangements with Korea and Japan will have investment provisions. India and China are also examining the possibility of negotiating a preferential trading arrangement.

Currently, there are discussions with New Zealand and Australia to set up study processes for evaluating feasibility of bilateral arrangements.

As a result of conscious engagement by India of the East Asian countries (viz. ASEAN, China, Japan and Republic of Korea) as a part of the Look East Policy, they have emerged as the largest trade partners of the country ahead of the North America and Europe. The share of these countries in India's trade has gone up from 17 per cent to 28 per cent between 2000 to 2006 indicating a major shift in the geography of her economic engagement.<sup>18</sup>

India sees this growing engagement with East Asian countries as building blocs of a broader Asian grouping and has articulated a vision of an Asian Economic Community as an 'arc of advantage' peace and shared prosperity in Asia bringing together different sub-regions of Asia in a phased manner.<sup>19</sup> The formation of an Asian Economic Community could thus be viewed as the culmination of India's Look East policy. India participates in the East Asia Summits launched as a forum for dialogue on regional cooperation in Asia along with

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<sup>17</sup> See RIS (2004a).

<sup>18</sup> see Kumar (2007) for more details.

<sup>19</sup> See Prime Minister Dr Manmohan Singh's speech at the Third ASEAN-India Business Summit, 21 October 2004. Also see RIS (2003)

ASEAN member countries, Japan, China, Republic of Korea, Australia and New Zealand and supports the CEPEA study.

## 5.2 Emerging Patterns of Industrial Restructuring

India's emerging FTAs with Asian countries such as Sri Lanka, Thailand, Singapore, Republic of Korea have already led to a significant trend of industrial restructuring. A typical example is an investment made by an Indian tyres company, CEAT to set up a large export-oriented tyres plant in Sri Lanka to cater to its growing markets in Pakistan, Middle East and other countries taking advantage of abundant supply of natural rubber in the country. As a result of the growing trend of investments made by Indian companies to exploit the potential of the India-Sri Lanka FTA, India has emerged as the third largest source of FDI in Sri Lanka. UNCTAD's *World Investment Report 2003* has highlighted how Sri Lanka attracted Indian investments of US\$ 145 million in a very short period making India as the third largest source of investments for the island. Because of the investments in building supply capabilities in Sri Lanka facilitated by the India-Sri Lanka FTA, the trade deficit of Sri Lanka has come down to less than half. This success has prompted Sri Lanka to seek to expand the scope of the India-Sri Lanka FTA to cover investments and services in a comprehensive economic partnership agreement (CEPA).<sup>20</sup> Similarly the India-Nepal trade and transit treaty giving unilateral duty free access to Nepali products to Indian market has also led to some industrial restructuring. For instance, Colgate-Palmolive India Ltd. (a subsidiary of Colgate-Palmolive, Inc.) has set up a venture with authorized capital of Rs 540 million in Nepal for production of 12000 tonnes of toothpaste per annum and tooth powder to feed their markets for the product in North India. As a result tooth paste exports from Nepal to India have grown from US\$ 11 million in 1997-98 to about US\$ 61 million in 1998/9, making tooth paste one of the most important item of Nepal's exports to India.<sup>21</sup> Other companies likely Hindustan Lever have followed suit. Dabur India, a domestic Indian group has invested in a fruit processing plant to produce and package fruit juices for the Indian market. Dabur's principal focus is ayurvedic and herbal medicinal preparations. It has also started using its Nepal venture for these preparations. Dabur Nepal was apparently contributing as much as 15 per cent of Nepal's exports to India.<sup>22</sup> Presently all the fruit juices sold in North India are packaged at its Nepal plant. Kodak Nepal, a venture of Kodak India and Eastman Kodak, USA was planning to service the North Indian market from its Nepalese base.<sup>23</sup> Subsequently however, this process of industrial restructuring between India and Nepal was disrupted because of the political turmoil in the country. It is expected that with the peace returning to Nepal with the revival of the democratic process, the process will be restored again.

India-Singapore Comprehensive Economic Cooperation Agreement (CECA) was signed in 2005. So it may be too early to expect industrial restructuring to become a major trend. However, one can see a growing interaction and integration happening stimulated by the CECA. Following the signing of CECA, the financial institutions of the two countries have come interacting. Singapore investment company Temasek has become an important investor in India. Over 2000 Indian companies have reportedly set up bases in Singapore to expand into East Asian region. Some large IT companies like TCS and Satyam have made Singapore as their regional headquarter. However, the emerging pattern of industrial restructuring is best illustrated by the acquisition of NatSteel, Singapore by Tata Steel of India recently and the emerging pattern of supply chain integration. Apparently Tata Steel and NatSteel plants in different Southeast Asian countries would be covered by a scheme of regional production network which would involve pallets going from India to the NatSteel plants and special steels to come from NatSteel's Southeast Asia plants to India. This way the

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<sup>20</sup> see RIS 2004b.

<sup>21</sup> see FNCCI (2000)

<sup>22</sup> see Mukherjee, (1998)

<sup>23</sup> see *Financial Times*, (26 August 1999)

synergy or the locational advantages of India emanating from the iron ore deposits will be available to the NatSteel plants and their specialization for some special steels to Tata Steel, will be exploited for mutual advantage.<sup>24</sup>

## *VI. Concluding Remarks*

To sum up the foregoing discussion, it has been argued that investment liberalization occupies an important place in the schemes of regional economic integration complementing trade liberalization to facilitate the process of restructuring of industry on more efficient lines. This restructuring enables fuller exploitation of the locational advantages or synergies between the member countries of the regional trading bloc besides facilitating businesses reaping the economies of scale and specialization. The Single Market Plan of the European Union has unleashed such a pattern of industrial restructuring not only European corporations but also the operations of foreign multinationals operating in the EU. Such restructuring also facilitates creation of supply capabilities in relatively poorer countries thus facilitating a convergence of levels of development.

In recent times, Asian countries have also started to attach a far greater importance to regional economic integration in their trade policy after decades of faithful adherence to multilateralism. A large number of free trade arrangements are taking shape in Asia at the sub-regional levels in Southeast Asia (ASEAN) and South Asia (SAARC) or between the sub-regional groupings and their dialogue partners and between the dialogue partners. There is also a discussion on building on these attempts and evolve broader grouping. Although many of Asian RTAs are at early stages of their development, the trend is quite clear. Another noticeable trend is an increasing number of Asia-Pacific RTAs extend their scope to investments. Hence, there is a recognition of the importance of investment liberalization for exploiting the full benefits of RTAs.

The investment provisions included in Asian RTAs have tended to follow progressive liberalization approach given the varying levels of development existing in the region. They have also included provisions on investment protection, promotion and facilitation, MFN and dispute settlement. Asia-Pacific RTAs are consistent with the provisions of multilateral disciplines on investment as enshrined in the WTO's TRIMs Agreement and have some times attempted to adopt a more ambitious approach to elimination of performance requirements.

ASEAN's attempt to progressively deepen regional economic integration through expedited schedules of implementation of AFTA, adoption of ASEAN Investment Area, ASEAN Industrial Cooperation (AICO) Schemes and Framework Agreement on Trade in Services indicate recognition of the potential of industrial restructuring by the grouping.

ASEAN has also facilitated economic integration with other Asian countries by bring them together as dialogue partners. This process has led to a number of bilateral FTAs that together form an emerging virtual community. However, due to varying scope and coverage of trade and investment rules in these initiatives, they hardly provide a seamless market to region's enterprises for facilitating efficiency-seeking industrial restructuring. It is imperative that these attempts are viewed as building blocs of a broader Asian Community as has been envisioned by some Asian leaders which could become an arc of advantage, peace and shared prosperity in Asia.

The launch of East Asia Summit (EAS) bringing together leaders of ASEAN and its six dialogue partners viz. Japan, China, Korea, India, Australia and New Zealand, provides an

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<sup>24</sup> see Kumar 2007, for a more detailed treatment.

important forum for initiatives towards creating an East Asian economic space. The Second EAS has agreed to launch a feasibility study of a Comprehensive Economic Partnership of East Asia (CEPEA). By providing a framework for removing trade and investment barriers, CEPEA has the potential of unleashing a process of efficiency-seeking restructuring across countries in Asia and facilitating exploitation of their locational advantages or synergies for mutual benefit!

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