CHAPTER 3

FOREIGN DIRECT INVESTMENT MAKES A MODEST COME-BACK

A. OVERVIEW OF RECENT TRENDS IN FOREIGN DIRECT INVESTMENT

1. Global trends

Global foreign direct investment (FDI) inflows, at $1.76 trillion in 2015, reached their highest level since the financial crisis of 2008-2009. This amounted to a 38% increase compared with 2014. However, this rise in FDI was mainly attributed to a surge in cross-border mergers and acquisitions (M&A) that were, to a large extent, used for corporate reconfiguration including tax inversions.[1] After discounting for these flows, the increase in 2015 was about 15% (UNCTAD, 2016). The rise in FDI inflows was more prominent in developed economies, which received $962 billion in 2015, i.e. 84% more than in 2014. This is in contrast to the past three years, when developed economies experienced declining FDI inflows and a smaller share in global FDI flows. On the other hand, developing economies received $800 billion in 2015, a mere 5.9% increase, due to the continued decline in commodity prices, especially of crude oil, metals and minerals, which made investment in the primary sector less attractive (UNCTAD, 2016).

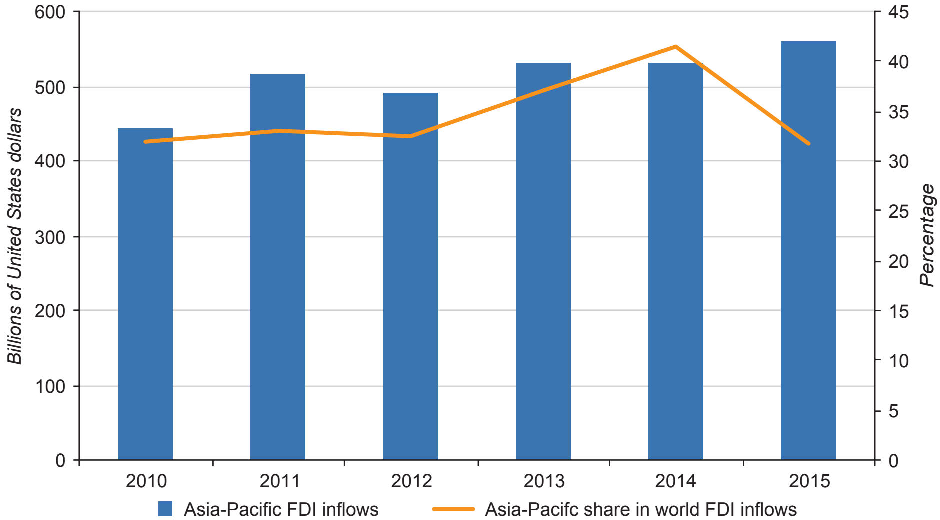
"The Asia-Pacific region recorded only a 5.6% increase in FDI inflow in 2015, resulting in a 10 percentage point fall in the region's share of global FDI inflows from its 2014 share of 42%."

2. Regional trends

The Asia-Pacific region continued to receive a significant amount of FDI inflows, totalling $559 billion in 2015, an increase of 5.6% over 2014 level. However, this increase paled in comparison to jump of global FDI inflows. Therefore, the region's share in global FDI inflows declined from 42% in 2014 to 32% in 2015 (figure 3.1).

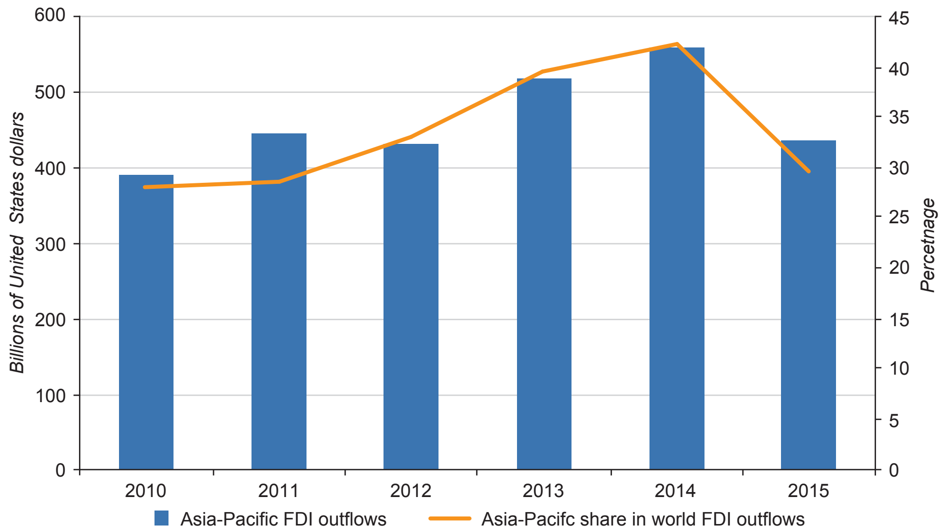
The economies of the Asia-Pacific region have also contributed less to FDI outflows. The region invested $435 billion in 2015, a 22% decrease compared with the previous year (figure 3.2). The low level of investment to and from the region once again reflects the fragile global economy, volatility of global financial markets, and weak aggregate demand at the global and regional levels. In addition, the decrease in FDI outflows registered in 2015 may be attributable to a return to the "historical" average level of outflows – i.e. in 2013 and 2014 there was an unprecedented high

Figure 3.1 **FDI inflows to the Asia-Pacific region and their share in global FDI inflows, 2010-2015**



Sources: ESCAP calculation based on UNCTAD (2016).

Figure 3.2 **FDI outflows from the Asia-Pacific region and their share in global FDI outflows, 2010-2015**



Sources: ESCAP calculation based on UNCTAD (2016).

increase in FDI outflows from the region, specifically from India and Hong Kong, China, which did not reoccur in 2015. The outflows in 2015 were thus close to the region's average recorded since the recovery after the financial crisis, ignoring the 2013 and 2014 outliers.

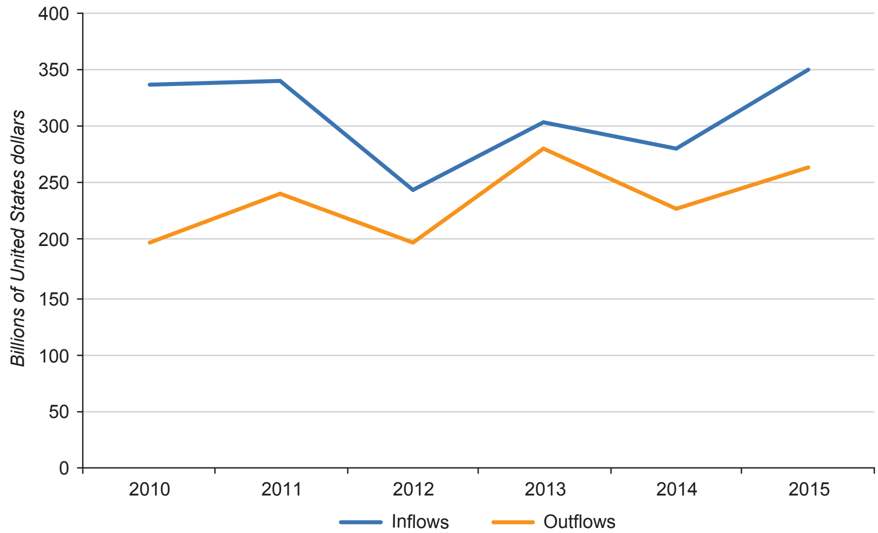
Greenfield FDI inflows to the Asia-Pacific region increased by 26% in 2015, which was a significantly higher growth when compared with that of global inflows, which increased by only 6%. The region received $352 billion in total greenfield FDI, which accounted for 40% of the global total. Greenfield FDI outflows from the Asia-Pacific region in 2015 also increased by 15% to $263 billion. Announced greenfield FDI data (figure 3.3) are considered as demonstrating the contribution of FDI to local economic growth, measured by capital expenditures using firm-level data (Investment Consulting Associates, 2016).

B. ASIA-PACIFIC SUBREGIONAL TRENDS

1. FDI inflows

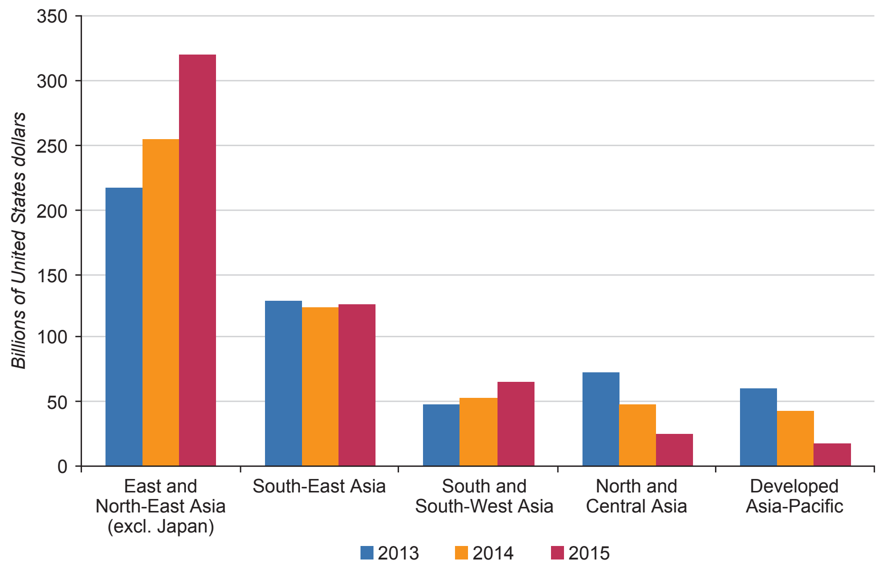
Within the Asia-Pacific region, FDI inflows during 2013-2015 varied among the subregions and individual economies (figure 3.4).

Figure 3.3 Greenfield FDI flows in the Asia-Pacific region, 2010-2015



Sources: ESCAP calculation based on fDi Intelligence data, 2016.

Figure 3.4 FDI inflows to Asia-Pacific developing subregions and developed economies, 2013-2015



Sources: ESCAP calculation based on UNCTAD (2016).

Note: Due to the small share of outflows from the Pacific small island developing States, that subregion is not included in this figure.

(a) Developing East and North-East Asia

Developing East and North-East Asia showed a significant increase in the level of FDI inflows compared with 2014. A 53% increase in FDI inflows to Hong Kong, China was the primary reason. This increase was partly due to corporate reconfigurations. These reconfigurations could involve a large movement in the balance of payments but little change in actual operations. For example, in the restructuring of the conglomerate Cheung Kong Holdings and Hutchison Whampoa they became incorporated in the Cayman Islands, which led to a significant increase in FDI inflows into Hong Kong, China (UNCTAD, 2016).

In China, which accounts for more than 40% of the subregion, FDI inflows increased modestly in 2015 by 6% to $136 billion. The slowdown in FDI inflows is in line with that of China's economic growth. However, this moderate economic growth, which President Xi Jinping has called the "new normal", is perceived as being inevitable and in the long term more sustainable; similarly, the slowdown in FDI is considered to be inevitable to some extent (World Bank, 2015).

China is losing its significant edge in manufacturing in general and in labour-intensive production in particular, due to rising wages. The country is going through structural adjustments aimed at shifting from an export-led investment-driven growth model to a consumption-driven one, in order to expand the services sector in the economy (Drysdale, 2015a). As China is strategically moving away from manufacturing and labour-intensive production, these industries could experience decreased levels of FDI inflows. The intensity and direction of reforms could have an impact on the level and nature of FDI inflows in the coming years.

(b) South-East Asia

With almost no change in total FDI inflows to South-East Asia, Indonesia experienced a steep decline of 29% in FDI inflows in 2015 compared with 2014, while accounting for more than 10% of the FDI inflows of the subregion. One factor is that the Government of Indonesia implemented a ban on unprocessed exports of raw minerals, introduced by the Mineral and Cola Mining Law (2009) that came into force in 2014. Subsequently, in the first quarter of 2014, FDI fell significantly; however, a series of regulations relaxing the laws followed, which went some way to recovering FDI flows (Parisotto, Santibáñez and Heal, 2016).

FDI inflows to Thailand in 2015, in contrast, tripled compared with 2014, although the amount was still much lower than that recorded in 2012 and 2013. However, other small and low-income economies, including the Lao People's Democratic Republic, Myanmar and Viet Nam, all continued to perform well, with low labour and other production costs, and their Governments' push to liberalize and promote FDI. In 2015, FDI inflows to Myanmar almost doubled, while FDI inflows to the Lao People's Democratic Republic and Viet Nam were also significantly higher by 69% and 28%, respectively, compared with 2014.

(c) South and South-West Asia

The South and South-West Asia subregion received an increased level of FDI inflows, which mostly went to India, the biggest economy in the subregion. India received $44 billion in 2015, which was a 28% increase over 2014. India is certainly improving the environment for investment and regulatory settings. Under the Government's economy strategy, including "Make in India", India is pursuing a strategy of liberalizing investment restrictions further. Also, the Reserve Bank of India (RBI) has successfully kept inflation under 6%, lower than the historical average, which further contributed to investors' confidence in the country (*Economist,* 2016).

The increase in greenfield FDI inflows to India in 2015 was even more striking: they more than doubled in 2015, received the biggest flows after the financial crisis, and surpassed the inflows to China for the first time (Panda, 2016). However, there is still potential for India to perform even better.[2] In particular, improvement of the private investment environment, especially that of infrastructure, would position India for playing a much larger role in global and regional value chain production networks. In addition, there is scope to adopt more flexible labour laws and improve coordination between the central and state Governments and their investment promotion agencies (Drysdale, 2015b). Thanks to rising FDI in labour-intensive manufacturing, inflows to Bangladesh also jumped by 44% to $2.2 billion in 2015, a historically high level.

(d) North and Central Asia

In contrast, FDI inflows to North and Central Asia continued to contract due to low commodity prices (especially in the case of crude oil), weak domestic markets, and the direct and indirect impacts of geopolitical tensions affecting mainly the Russian Federation. The Russian Federation and Kazakhstan, the two major economies in the subregion, received severely reduced investment inflows in 2015. The economic crisis and regulatory changes in the Russian Federation also reduced the scale and scope of round-tripping FDI, depressing FDI inflow figures.

(e) Pacific developing economies

The Pacific developing economies received $2.3 billion FDI inflows collectively in 2015, an increase of 16%. However, FDI inflows to the subregion are very volatile, possibly due to the structural characteristics that continue to limit FDI options, such as the lack of adequate transport, communications and energy infrastructures, low productivity capacities and the concentration on a narrow set of commodities/sectors (ESCAP, 2015). Several economies are aiming to achieve, or have pursued, economic diversification that could attract sustainable FDI flows. However, progress in these efforts is uneven and would be long-term processes that need to be incorporated in the economic policies of these economies (Asian Development Bank, 2016; Dornan and Cain, 2015; and Fingar, 2016).

(f) Developed Asia-Pacific economies

The developed Asia-Pacific economies also experienced a sharp decline in FDI inflows in 2015. FDI inflows to Japan fell to a net divestment as European TNCs withdrew investments (UNCTAD, 2016). This could be due to the high costs of doing business and pursuing M&As in Japan, as pointed out in a recent survey (Urata, 2015). Australia and New Zealand also continued to experience decreased FDI inflows, as in the case in the past few years, with continued depressed commodity prices.

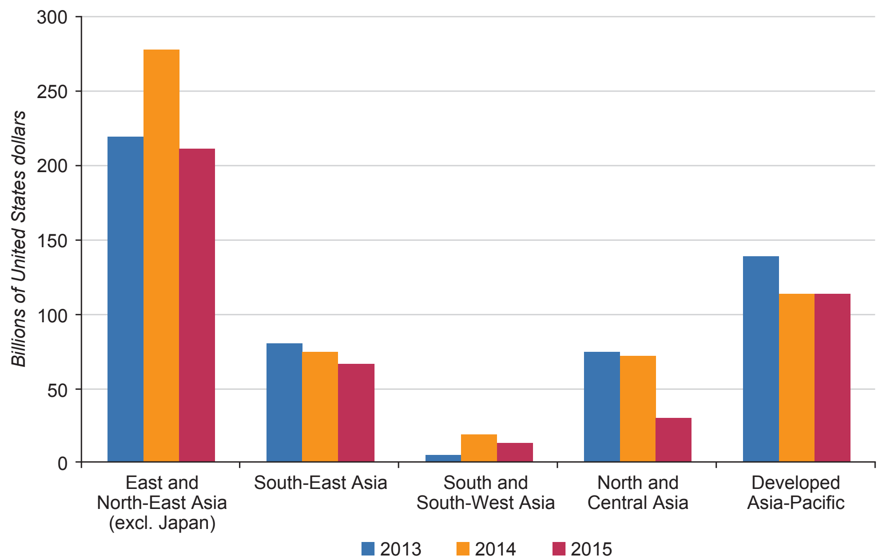
2. FDI outflows

Most FDI outflows from the Asia-Pacific region are from East and North-East Asia. That subregion accounts for 78% of total FDI outflows from the region as a whole, but almost exclusively from China, followed by Hong Kong, China, and Japan (figure 3.5). Also, these outflows are increasingly invested intraregionally (see section C for more details). It should also be noted that the subregion captures most of intraregional trade flows, on both the import and export sides (see chapter 1 for more details).

China has continued to expand its outward FDI, on the one hand, to secure mineral and petroleum resources, and on the other hand for efficiency seeking due to rising labour costs at home. Since the Government initiated its "going out" strategy in 1999, China has focused its FDI in areas that contribute directly to China's development, such as natural resources, lower production costs and, most recently, strengthening its technological base as the country is facing over-capacity in the labour-intensive manufacturing sector. It is aiming to move towards attracting FDI in technologically advanced sectors (Sauvant and Nolan, 2015). China remains the third-largest outward investing country worldwide and has emerged as a leading investor in developing economies, particularly in Africa and increasingly in countries that are part of the Belt and Road Initiative (UNCTAD, 2016). After a surge of outward FDI in 2014, investment from Hong Kong, China has more than halved as it has been affected by divestment due to strategic corporate restructuring (UNCTAD, 2016).

With regained confidence and traditionally facing limited prospects in the home market, Japan continued to seek growth opportunities abroad. Japan recovered

Figure 3.5 **FDI outflows from Asia-Pacific developing subregions and developed economies, 2013-2015**



Sources: ESCAP calculation based on UNCTAD (2016).

Note: Due to the small share of outflows from the Pacific small island developing States, that subregion is not included in this figure.

its FDI outflows to the levels existing prior to the financial crisis in 2008-2009, recording $129 billion in FDI outflows in 2015, which was a 13% increase over 2014.

C. INTRAREGIONAL FOREIGN DIRECT INVESTMENT FLOWS

> *"The share of intraregional greenfield FDI inflows in total greenfield FDI inflows to the Asia-Pacific region has continuously increased during the past few years, accounting for 52% in 2015."*

As the economic relevance and dynamism of the Asia-Pacific region increases, intraregional greenfield FDI flows are replacing those from the traditional big investors such as the United States and countries in Europe (ESCAP, 2013). After the financial crisis in 2009-2009, in particular, the share of intraregional greenfield FDI inflows in total greenfield FDI inflows to the Asia-Pacific region has continuously increased, accounting for 52% in 2015 (figure 3.6).

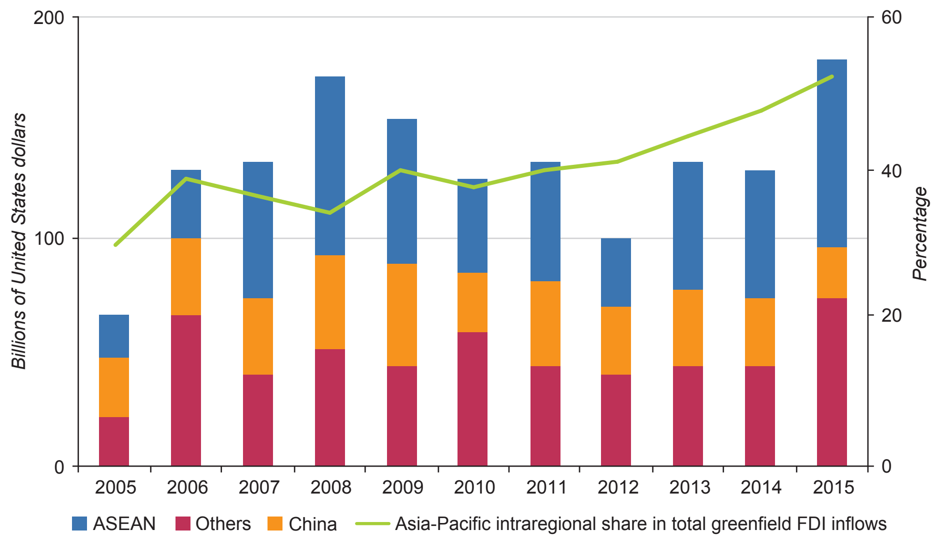
Increasing intraregional FDI flows can be, at least partially, attributed to continuous efforts for regional and subregional integration within the Asia-Pacific region.

The Association of Southeast Nations (ASEAN), which includes all economies in South-East Asia except Timor-Leste, has become a popular destination for intraregional FDI, thanks to its continuous collaborative efforts on subregional integration with outward-oriented focus approach, and further developments on investment environment. In 2015, $83 billion was received from countries in the Asia-Pacific region, which amounted to 46% of total intraregional inflows.

As production costs are rising in labour-intensive industries in China, the smaller and less developed countries in ASEAN are benefiting from a shift of FDI to these industries despite their overall poor investment climate. Specifically, development challenges in CLMV countries (Cambodia, Lao People's Democratic Republic, Myanmar and Viet Nam) were noted and efforts are ongoing through the Initiative for ASEAN Integration and other aid programmes (OECD, 2016). Possibly because of these factors, CLMV countries have received steady and increasing FDI inflows since 2011. The total FDI inflows have reached $18 billion in 2015, an increase of 70% compared with 2011. In this regard, it appears that ASEAN is attracting a significant portion of FDI inflows from its neighbours, mainly China, Japan and Republic of Korea, and some other countries in the region, which together accounted for 72% of total greenfield FDI inflows to ASEAN during 2013-2015 (figure 3.7).

> *"Intraregional greenfield FDI flows are gradually replacing those from the traditional big investors in Europe."*

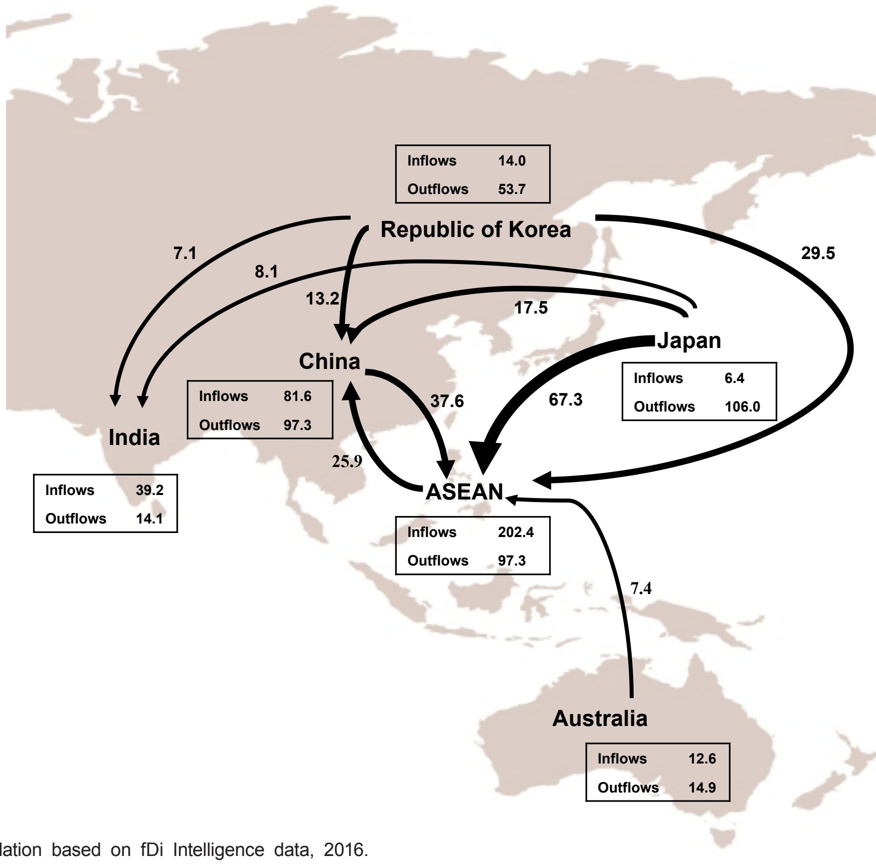
Figure 3.6 **Asia-Pacific intraregional greenfield FDI inflows and their share in total greenfield FDI inflows, and major destinations, 2005-2015**



Sources: ESCAP calculation based on fDi Intelligence data, 2016.

Note: "intraregional" in the context of the above figure implies flows in a country or a subregion from the rest of Asia and the Pacific.

Figure 3.7 **Intraregional greenfield FDI flows between selected economies, and total intraregional inflows and outflows to and from those economies, 2013-2015**



Sources: ESCAP calculation based on fDi Intelligence data, 2016.

Note: In order to even out the volatile annual FDI flows, the total invested FDI flow during 2013-2015 is used instead of annual flows.

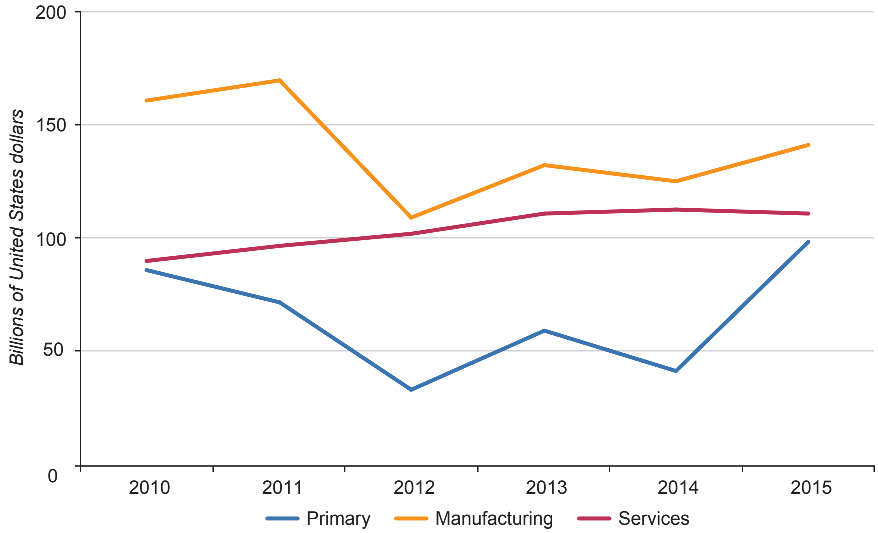
It should also be noted that major investors are highly concentrated in one or two key industries and sometimes also in certain economies. For example, Chinese companies dominate the FDI in manufacturing (48% of total manufacturing FDI), and are the largest investors in the Lao People's Democratic Republic at 62% of FDI flows, mainly focused on infrastructure. For Viet Nam, 67% of FDI flows in 2015 were in manufacturing and were led by investors from the Republic of Korea (ASEAN Secretariat and UNCTAD, 2016).

> *"While FDI inflows to China are slowing down, more FDI is directed towards economies in ASEAN instead."*

D. SECTORAL FOREIGN DIRECT INVESTMENT FLOWS

The Asia and Pacific region continued to receive significant FDI in both the manufacturing and the services sectors. However, in 2015, greenfield FDI inflows to the primary sector increased noticeably. The coal, oil and natural gas industries received $67 billion in 2015, 2.6 times more than in the previous year; the metals sector received $28 billion in 2015, more than double than the previous year (figure 3.8). Taking a closer look reveals that the following industries received a significant portion of greenfield FDI flows in 2015: fossil fuel electric power, petroleum refineries; iron and steel mills, and ferroalloy, and natural, liquefied and compressed gas. The increase of greenfield FDI in the primary sector differs from the decreased level of overall FDI flows to developing economies. However, it is in line with the significant increase in overall greenfield FDI flows to the region. Also, the fact that companies are still investing in the primary sector in the region despite the low commodity prices could be an indication of a potential rebound in FDI as macroeconomic and financial conditions improve in the Asia region (UNCTAD, 2016). Also, it is worth noting that greenfield FDI inflows are on an announcement basis only; thus, there could be time delays between the announcement and actual transactions.

Figure 3.8 **Greenfield FDI inflows to the Asia-Pacific region by sector, 2010-2015**



Sources: ESCAP calculation based on fDi Intelligence data, 2016.

During 2013-2015, the industries listed in table 3.1 received the biggest FDI inflows. Among them, real estate and alternative/renewable energy received almost double the amount compared with 2010-2012.

Many economies in the region are paying more attention to attracting FDI in technologically more advanced industries in order to move away for reliance on labour-intensive manufacturing as they believe that such FDI would bring desired spillover effects to the economy alongside capital inflows and contribute to sustainable development (box 3.1).

In addition to FDI inflows to technologically more advanced industries, investment in infrastructure serves important roles as catalyzers. Not only the physical infrastructure such as railroads, ports, and highways, but also soft infrastructure such as financial services and information and communications technology would be critical for attracting further FDI investment in host countries (ASEAN Secretariat, 2015b). FDI inflows in these sectors are also encouraged by regional integration efforts such as recently announced the Belt and Road Initiative and Asian Infrastructure Investment Bank (AIIB), and existing initiatives such as the Eurasian Development Bank (EDB), with its focus on regional integration and economies ties. Therefore, countries have paid special attention to promote and/or control investment in infrastructure industries, through investment policies and other means.

Table 3.1 **Greenfield FDI inflows to top 10 industries, 2013-2015**

(Millions of United States dollars)

Top 10 industries (ranking in 2010-2012)	Total greenfield FDI inflows, 2013-2015
Coal, oil and natural gas (1)	125 701
Real estate (6)	100 896
Metals (3)	63 522
Financial services (2)	54 264
Alternative/renewable energy (new)	52 814
Automotive OEM (5)	46 886
Transportation (7)	43 129
Communications (10)	41 952
Chemicals (4)	39 010
Food and tobacco (9)	36 658

Source: ESCAP calculation based on fDi Intelligence data, 2016.

Box 3.1 **Attracting FDI for sustainable development**

Increasingly, economies are putting much effort into attracting the FDI that would enable sustainable growth. Originally, it was believed that FDI inflows would automatically result in growth and, hence, many economies pursued outward-oriented growth strategies that not only focused on increasing international trade but also encouraging high levels of FDI. However, empirical evidence has revealed that these FDI inflows by themselves do not automatically translate into growth, and particularly what is considered to be sustainable growth. The following prerequisites as well as required host country characteristics are necessary for attracting FDI for sustainable development.

First, absorptive capacities are needed to ensure positive spillovers, which arise when resources, notably knowledge, are spread and transferred (Meyer, 2004). These positive spillovers lead to productivity growth via enhanced knowledge and skills (Görg and Greenaway 2004). Absorptive capacities and host country characteristics matter in making a difference in the extent or speed with which spillovers occur. Some of well-discussed absorptive capacities include research and development (R&D) capacities, human resources, technological capacity and infrastructure (Guimón 2013; and Görg and Greenaway 2004). These positive spillover effects, in turn, enhance the attractiveness of host countries for FDI and, therefore, contribute to retained and continuous inflows of FDI with long-lasting positive effects.

Second, national FDI policies and regulations should seek to balance investors' rights with the public interest in order to ensure that FDI will bring growth in the three pillars of sustainable development (i.e. economic, social and environmental). With the 2030 Agenda for Sustainable Development and the 2015 Addis Ababa Action Agenda on Financing for Development reaffirming the importance of sustainable development, more attention is given to this area. For example, FDI in extractive industries can certainly generate government revenue, foreign exchange earnings and employment; however, they also can aggravate or cause serious environmental, health and social problems, including conflict and war (Liebenthal, Michelitsch and Tarazona, 2003). FDI in high-tech industries can potentially bring technology transfer and technological spillovers. However, it can also lead to pollution, such as e-waste or other negative externalities.

It is therefore important that Governments ensure that efforts are put in place to enhance absorptive capacities as well as ensure that encouraging FDI should not deter domestic policies and regulation in the public interest. Governments, therefore, should balance the economic, social and environmental dimensions of FDI and demand corporate responsibility from investors, in accordance with internationally accepted principles and standards.

E. NATIONAL INVESTMENT POLICIES

National investment policies continue to be geared towards investment liberalization and promotion. According to UNCTAD (2016), 46 countries and economies adopted 96 policy measures affecting foreign investment in 2015. Of these measures, 71 were related to liberalization, promotion and facilitation of investment, while 13 introduced new restrictions or regulations on investment.

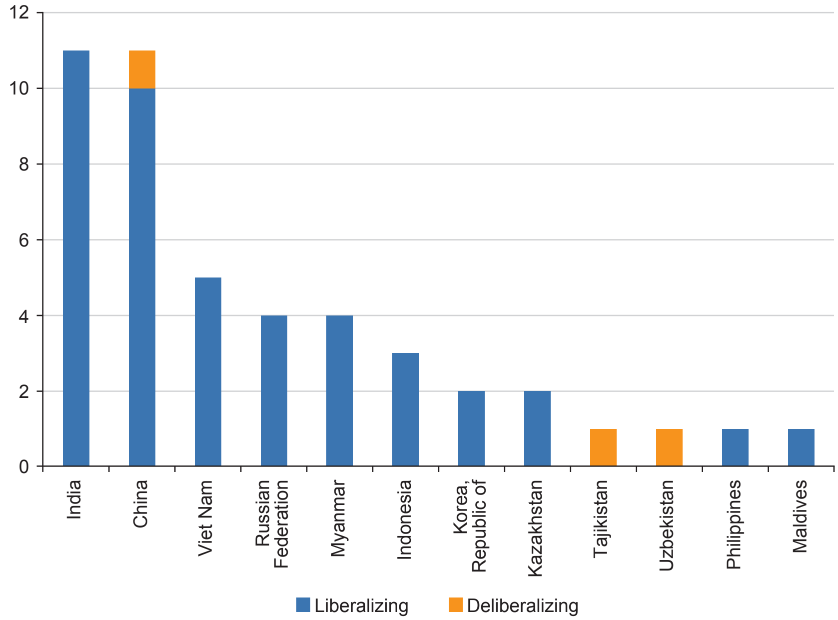
> *"Asia-Pacific countries lead with investment liberalization and promotion policies accounting for almost half of such measures adopted in 2015."*

Asian and Pacific countries are in the lead with investment liberalization and promotion policies. According to the same report (UNCTAD, 2016) the region adopted 46 investment policies affecting foreign investment, accounting for almost half of the global total (figure 3.9). Of these measures, 43 were related to liberalization, promotion and facilitation of investment, while only 3 introduced new restrictions or regulations on investment. These investment policy changes removed restrictions on foreign investment, strengthened investment promotion and facilitation, and further ensured the rights of investors. Two areas of investment policy changes earn special attention, i.e. liberalization of industry sectors and special economic zones (SEZs).

1. Liberalization of industry sectors

For many years, emerging Asian economies have been pursuing economic development by emphasizing their openness and integration into the global economy. In particular, two of the largest emerging economies in Asia, China and India, were the most active in opening up various industries to foreign investors in 2015.

Figure 3.9 **Investment policy changes in Asia-Pacific countries, 2015**



Sources: ESCAP calculation based on the UNCTAD Investment Policy Monitor Database, 2016.

For many years, emerging Asian economies have been pursuing economic development by emphasizing their openness and integration into the global economy. In particular, two of the largest emerging economies in Asia, China and India, were the most active in opening up various industries to foreign investors in 2015.

In China, with the announcement of the draft Foreign Investment Law (FIL) from the Ministry of Commerce (MOFCOM), a comprehensive reform of the legal system for foreign investment in China is anticipated. The FIL is intended to move the focus from supervision of the organizational structures and business activities of foreign companies investing in China to post-investment supervision, which mainly concerns reporting obligations and national security (Yang and Huang, 2016). This is contrary to the current pre-establishment system, which regulates foreign investment with a positive list approach, approving investment on a case-by-case basis. While seeking public opinion and in anticipation of enacting the FIL, China is piloting the foreign investment negative list in the Shanghai, Tianjin, Guandong and Fujian Free Trade Zones (FTZs). As indicated in a recent government statement, China intends to open more sectors to foreign investors, such as education, finance, culture and manufacturing (Bloomberg News, 2016).

Despite a clearly intended move towards liberalization in general, China is also protecting core industries in terms of national security. MOFCOM and the National Development and Reform Commission (NDRC) jointly released an updated version of the Guiding Catalogue on Foreign Investment in Industry in March 2015, which lifts restrictions on foreign investment in several areas, but remains largely unaltered in industries that have traditionally faced heavy restrictions, such as banking, telecommunications and cultural industries (United States Department of State, 2016a). A recent National Security Law, enacted in July 2015, has also raised concerns that the Law may be used to restrict foreign investment in some sensitive sectors (Wong, 2015).[3]

India has also taken up major reforms since 2014, including various liberalization measures such as:

(a) Permitting FDI up to 100 per cent ownership under the automatic route (instead of government approval route) in the manufacturing of medical devices, telecommunications, railway infrastructure and non-banking finance companies;
(b) Increasing the FDI cap from 26% to 49% for foreign ownership in the insurance and defence sectors;
(c) Relaxing sourcing norms for single-brand retail trading for high-tech segments;
(d) Increasing the thresholds of inward FDI projects that require prior approval from INR 20 billion to INR 50 billion[4] (UNCTAD, 2016; ENS Economic Bureau, 2016; and D.H. Law Associates, 2015).

India also introduced a comprehensive FDI liberalization strategy and relaxed FDI rules in 15 major sectors, including agriculture, civil aviation, construction, defence, manufacturing and mining (UNCTAD, 2016). India is also continuing its liberalization measures in other sectors such as, for example, e-commerce, which is expected to further encourage FDI inflows to India (box 3.2).

Box 3.2 **India: liberalizing e-commerce**

Among the sectors recently opened up to FDI in India is e-commerce. The Government of India announced that FDI of up to 100% would be permitted in the marketplace-based model of electronic commerce (e-commerce), in Press Note No. 3 released on 29 March 2016 (Cave, 2016). However, the liberalization comes with restrictions; according to the notification, e-commerce companies would not be allowed to influence prices of the goods sold on their website, and not more than 25% of goods sold can come from a single merchant (Reuters, 2016).

E-commerce, referring to the trading or facilitation of trading in goods and services using computer networks, poses a huge opportunity to trigger growth, especially for developing countries. E-commerce has become essential for many industries that have globally dispersed value chains. The existence of sophisticated platforms for e-commerce could significantly enhance the attractiveness of economies as investment destinations and trade partners. Together with many other countries – including China, which allows full foreign ownership of e-commerce business[a] – India has followed suit. While India has taken steps in the right direction, greater clarification of the restrictions is needed. In addition, India needs to develop the supporting infrastructure for e-commerce, including basic Internet connectivity, trade facilitation, streamlining non-tariff measures, and to improve the regulatory regime for services (Johns, 2016).

[a] The Ministry of Industry and Information Technology of China issued Announcement No. 196 (2015) on 19 June 2015, allowing full foreign ownership of e-commerce business. On 20 June 2015, the State Council released policy guidelines for supporting cross-border e-commerce.

In 2015, there were also some noteworthy measures from smaller Asia-Pacific economies. For example, Viet Nam implemented a number of reforms of its investment policy, including: (a) implementation of a “negative list” approach; (b) allowing foreign investors in its airport and aviation industry; and (c) lifting a 49% cap on foreign ownership in some industries (Peel and Linh, 2015; United States Department of State, 2016b). The Philippines issued a revised negative list, removing foreign ownership restrictions in a number of sectors. In Myanmar, the Parliament approved amendments to the Foreign Investment Law and the Myanmar Citizens Investment Law in December 2015, aimed at paving the way for speedier investment approvals (Economist Intelligence Unit, 2016).

2. Special economic zones

Special economic zones (SEZs) have become popular, especially in developing economies, as modalities to attract FDI. There are more than 4,500 SEZs of various types worldwide (*Economist*, 2015). SEZs refer to “geographically limited and specially administered areas within a country that are established to attract local and foreign direct investment, trade, employment and industrial development” (UNCTAD, 2015). They typically provide certain advantages such as preferential tax or duty treatment or exemptions from restrictions on the repatriation of profits, direct subsidies and enhanced physical infrastructure as well as expedited permitting and related services. The popularity of SEZs is based on anticipated benefits such as increased FDI inflows and employment, despite mixed experiences and persisting concerns about social and environmental effects. However, SEZs can provide a platform for developing the infrastructure and regulatory environment in a geographically limited area without the need to reform relevant laws of a country/economy (UNCTAD, 2015).

In Myanmar, the country’s first SEZ in Thilawa became fully operational in September 2015, aimed at attracting foreign investors with hard and soft infrastructure, and providing easier establishment procedures and other concessions. In late-2015, the Government approved the development of another SEZ in Kyaukphyu, including an industrial park and a deep-sea port. However, the Dawei SEZ has experienced many obstacles, such as private sector partners’ exhausted funding and withdrawal from the project, which have delayed the project. With renewed support from the Governments of Thailand and Japan, and other private sector partners, construction is still ongoing but it will be many years before the Dawei SEZ will be fully operational. The Russian Federation is committed to opening a Free Port in Vladivostok, a customs-free zone with special tax incentives for companies operating within it. In Kazakhstan, the Government approved the Law on the Astana International Financial Centre (AIFC), a financial-oriented SEZ that streamlines employment procedures for foreign employees and offers tax exemptions such as exemption from corporate income tax as well as property and land taxes for AIFC members until 1 January 2066.

The nature of industries operating in SEZs has also evolved, moving away from being exclusively locations for business processes using low-skilled labour to locations for a variety of more complex business processes requiring more highly-skilled labour, including labour associated with finance and logistics centres. For example, in 2013, in China the Shanghai Free Trade Zone opened for business, with a focus on attracting the insurance industry (UNCTAD, 2015). In 2015, three new FTZs were opened in Tianjin, Fujian and Guangdong, providing national treatment in the pre-establishment phase, and adopting the negative list for approving investments.

F. INTERNATIONAL INVESTMENT AGREEMENTS

> *"The Asia-Pacific region has assumed a central role in the global IIA universe."*

For decades international investment agreements (IIAs) have been used to underpin the active FDI agenda in the Asia-Pacific region. This has contributed to the region's status as a major player in FDI. Although IIAs have traditionally been in the form of bilateral investment treaties (BITs), they are increasingly including other forms of agreements with investment provisions such as free trade agreements (FTAs), regional trade and investment agreements (RTIAs) and economic partnership agreements (EPAs).

Economies in Asia and the Pacific have increasingly assumed a crucial role in shaping the global IIA universe. According to the UNCTAD Investment Policy Monitor Database, in 2015 the Asia-Pacific region witnessed the signing of 14 IIAs and 13 IIAs entering into force, out of 29 IIAs being signed and 19 IIAs entered into force globally. It shows the degree that the Asia-Pacific region was very actively participating in IIAs.

Importantly, there is a movement towards the formation of so-called "mega-regional" agreements, such as the Trans-Pacific Partnership (TPP) signed on 4 February 2016. Furthermore, in South-East Asia the ASEAN Economic Community (AEC) entered into force on 31 December 2015. While commentators have remarked that this does not have a big legal significance, it marks an important milestone on the road to regional economic integration among ASEAN economies (ASEAN Secretariat, 2015a). Leading up to 2015, progress was achieved in, among others, eliminating tariffs, liberalizing and facilitating investment, and facilitating mobility of skilled labour (ASEAN Secretariat, 2016). In particular, the ASEAN Comprehensive Investment Agreement (ACIA) provides for profoundly progressive liberalization of national investment regimes in ASEAN member States.

In North and Central Asia, the Eurasian Economic Union (EAEU) entered into force on 1 January 2015, replacing the Eurasian Economic Community (EAEC) and integrating five Commonwealth of Independent States (CIS) economies – i.e. Armenia and all former EAEC members except Tajikistan – into a single market with free movement of goods, services, capital and labour, thus further enhancing regional integration in that subregion (Llosa, Ratna and Mikic, 2016).

In addition to these regional agreements, a number of bilateral IIAs have been signed and entered into force. Viet Nam is especially notable, as it has concluded agreements with a large number of countries through its FTAs with the European Union, the EAEU and the Republic of Korea as well as signing the TPP. The Republic of Korea was party to three other major FTAs that entered into force in 2015, i.e. with China, New Zealand and Canada, all of which included investment chapters.

The fact that the Asia-Pacific region has assumed a central role in the global IIA universe is a reflection of the shift in the paradigm of IIAs, moving to a more balanced investment regime that serves the interests of foreign investors and host countries. This is partly in reaction to rising disputes between investors and host countries, as IIAs used to focus on provisions for investment protection and promotion, with little or no regard for preserving the regulatory space of host countries (Berger, 2015). This has become a major concern for host countries, which rely heavily on FDI in sensitive sectors such as the extractive industry, which often faces environmental and community problems when foreign investors' interests precede the rights of local workers and communities.

Another reason behind the shift is the increasing number of developing and emerging economies that have become major destinations as well as sources of FDI. These emerging economies have pushed for a more balanced approach as they accelerate their investment abroad. For example, while China initially took the restrictive approach in its BITs, it has progressively broadened its consent to arbitration for disputes with foreign investors and increased the level of substantive protections afforded to investors; this approach has been taken in order to receive equal and reciprocal protection for its own investments abroad, as China's outward FDI has continued to increase in recent years (Sauvant and Nolan, 2015). At the same time, China has firmly restricted FDI in industries that they deem to be important for national security, as mentioned above. China and many other developing countries have become important investors, which gives them greater bargaining power when IIAs are being negotiated.

G. CONCLUSION

The Asia-Pacific region has continued to be a significant actor in the global FDI scene. The region in total received FDI inflows of $559 billion in 2015, accounting for 32% of total global inflows. However, the region experienced only a small increase in FDI inflows compared with the previous year, and accounted for a smaller share of the global FDI inflows. While this is partly due to the global economic uncertainties and volatilities affecting global FDI, it is specifically due to a sharp decline in FDI to North and Central Asia, due to low commodity prices, weakening domestic markets, regulatory changes, and the direct and indirect impacts of geopolitical tensions.

However, it is worth noting that greenfield FDI inflows to the region increased by 26% in 2015 compared with the previous year, which was significantly higher than the increase in global greenfield inflows. The region experienced a reduced level of outflows, at $435 billion in 2015. Again, economic conditions prompted the decrease, which is not very high compared with the average outward FDI flow in recent years given the unprecedented high increase in FDI outflows in 2014.

Amid varied FDI flows in different subregions and economies, there are a number of areas that stand out. First, intraregional FDI flows are continuing to be significant. The share of intraregional greenfield FDI inflows in total greenfield FDI inflows to the Asia-Pacific region has continuously increased during the past few years, accounting for 52% in 2015.

Second, while FDI inflows to China are slowing down as the country is losing its competitive advantage in traditional industries due to rising production costs, more FDI is flowing to economies in ASEAN instead. Small and low-income economies, such as the Lao People's Democratic Republic, Myanmar and Viet Nam, have continued to perform well. These countries have low labour costs and Governments that are actively pursuing liberalization and promotion of FDI. This is also reflected in intraregional FDI flows. In particular, ASEAN has become a popular destination for intraregional FDI, receiving $83 billion in 2015 from countries in the Asia-Pacific region, and accounting for 46% of total intraregional inflows.

Third, another country that has attracted higher FDI inflows is India, as the country is improving its regulatory environment for investment. The Government's economic strategy appears to be paying off well as inflation has been brought under control, and the country has become the top Asia-Pacific destination for FDI greenfield flows. With further improvements in the private investment environment, especially infrastructure, the country would enhance its attractiveness to foreign investors even more.

Many Asia-Pacific countries have actively pursued investment liberalization and promotion policies that have contributed to the success of the region, to become both an investment destination and a source. The majority (43 out of 46) foreign investment-related policies that were adopted in 2015 in the region comprised policies related to liberalization, promotion and facilitation of investment. In particular, two of the largest emerging economies in Asia, China and India, were the most active in opening up various industries to foreign investors. Other small economies were also pursuing further liberalization, such as Myanmar, the Philippines and Viet Nam.

One particular channel of liberalization has come in the form of SEZs. Some success cases of SEZs in the region have prompted many countries to follow suit; even though there have been mixed experiences and persisting concerns over the social and environmental effects of SEZs, they are still perceived as a useful means of attracting foreign investment and a testing ground for infrastructure development and regulatory reform. With the shifting nature of industries operating in SEZs, they could become more relevant as modalities for encouraging FDI for sustainable development.

Another channel of investment liberalization has come in the form of international investment agreements. The Asian and Pacific economies have assumed an increasingly crucial role in shaping the global IIA universe. It is noteworthy that many Asia-Pacific economies were, and still are active members of some mega-regional agreements, such as TPP, RCEP, and EAEU. The end of 2015 saw the entry into force of the AEC, which incorporates the ASEAN Comprehensive Investment Agreement that is a far-reaching subregional agreement that sets a standard for enhanced investment cooperation and integration among member States.

Endnotes

[1] Tax inversion, or corporate inversion, is the practice of relocating a corporation's legal domicile to a lower-tax nation, or tax haven, usually while retaining its material operations in its higher-tax country of origin.

[2] The World Bank's Doing Business Index, the World Economic Forum's Global Competitiveness Index and the Milken Institute's Global Opportunity Index point out that India still ranks lower than China. (Sauvant and Allman, 2016).

[3] Also referred to in www.amcham-shanghai.org/ftpuploadfiles/insight/ Security%20Reviews%20and%20Neg%20List.pdf.

[4] The Government of India, through the Ministry of Commerce and Industry recently issued its consolidated Foreign Direct Investment Policy Circular of 2015 that updates the FDI regulations.

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