Obstacles to FDI in the APEC Economies: Problems in Investment Liberalization and Facilitation Measures

Submitted by: Waseda University
Survey on Investment Liberalization and Facilitation

“Obstacles to FDI in the APEC Economies: Problems in Investment Liberalization and Facilitation Measures”

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1. Introduction

Recent developments in foreign direct investment (FDI) and FDI environment

- FDI has become active in the world and particularly in APEC economies
- FDI liberalization has proceeded
- However, there still remain impediments to FDI in the areas of FDI liberalization and facilitation
- Important to recognize the problems to be solved/improved, in order to promote FDI, because FDI inflows would promote economic growth by expanding fixed investment, generating employment, increasing trade, transferring technology and management know-how, and etc
1. Introduction (continued)

Purpose of the study

- To identify the specific problems for investment liberalization and facilitation
- To propose policies and policy guidelines to improve investment climate for the APEC economies
- To develop technical cooperation programs under the APEC framework
1. Introduction (continued)

Approach

- Identify the problems in FDI liberalization and facilitation by using the results of the survey on multinational corporations
- Compare our results with the results of the studies conducted by the international organizations and think tanks
1. Introduction (continued)

Data

- JMC (Japan Machinery Center for Trade and Investment) Survey
  - JBCTIF (the Japan Business Council for Trade and Investment Facilitation)
- Period: July to September 2005
- Respondents: Members of 50+ (out of 150+) Industry Associations
- Japan (USA): Supplemented by the information obtained from different sources including the investment reports prepared by the EU, the US (Japan), and others
1. Introduction (continued)

Definitions

- **Investment liberalization**
  - Eliminating/reducing restrictions on FDI and related activities
  - Measures: discriminatory to foreign investment
  - Mainly in chapters on investment in FTAs, investment treaties, and chapters in investment laws

- **Investment facilitation**
  - Enhancing transparency and promoting simplification, harmonization of investment related rules, and capacity-building in institutions concerning investment
  - Measures: non-discriminatory to foreign and domestic investment
  - Mainly NOT in chapters on investment in FTAs, investment treaties, and chapters in investment laws
1. Introduction (continued)

Content of the presentation

1. Introduction
2. Analysis of investment climate
3. Discussion from the legal perspective
4. Findings from our study
5. Policy suggestions
6. Questions for panel discussion in Session 2
2. Analysis of investment climate

• 10 major categories to classify the types of FDI impediments (Tab. 3.1)
• The number of incidents for each impediment reported by respondents to the JMC Survey (Tab. 3.2)
• Some caveats in the interpretation of the data
  • # of incidents, not the degree of seriousness of impediments
  • Possibility of multiple categories => most relevant one is recorded
  • # of incidents tend to be correlated with the number of FDI cases
  • Manufacturing sector-bias
2. Analysis of investment climate (continued)

10 major categories of FDI impediments

- **Investment liberalization**
  
  i. Restrictions on foreign entry
  
  ii. Performance requirements
  
  iii. Restrictions on overseas remittances and controls on foreign currency transactions
  
  iv. Restrictions on the movement of people and employment requirements
2. Analysis of investment climate (continued)

10 major categories of FDI impediments

- Investment facilitation
  - v. Lack of transparency in policies and regulations concerning investment (institutional problems)
  - vi. Complicated and/or delayed procedures with respect to investment-related regulations (implementation problems)
  - vii. Insufficient protection of intellectual property rights
  - viii. Labor regulations and related practices excessively favorable to workers
  - ix. Underdeveloped infrastructure, shortages of human resources, and insufficient investment incentives
  - x. Restricted competition and price controls
<table>
<thead>
<tr>
<th>Table 3.2 Investment climate in the APEC economies: the number of incidents by category and economy</th>
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<td>i) Restrictions on foreign entry</td>
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<td>ii) Performance requirements</td>
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<td>iii) Restrictions on overseas remittances and controls on foreign currency transactions</td>
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<td>iv) Restrictions on the movement of people and employment requirements</td>
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<td>v) Lack of transparency in policies and regulations concerning investment (institutional problems) Complicated and/or delayed procedures with respect to investment-related regulations (implementation</td>
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<td>vii) Insufficient protection of intellectual property rights</td>
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<td>viii) Labor regulations and related practices excessively favorable to workers Underdeveloped infrastructure, shortages of human resources, and insufficient investment incentives</td>
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<td>ix) Restricted competition and price controls</td>
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<tr>
<td>Total</td>
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<td>Share by economy (%)</td>
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</table>

Data source: Authors’ calculation, based on JMC survey.
Note: The number of incidents for Japan and USA (government level) are calculated, based on various reports at the government level. See the text for details of these sources.

2007.5.29
Major findings

1. Serious impediments concerning FDI facilitation

2. Necessity of further FDI liberalization, particularly for low income economies
Major findings (continued)

3. Among 10 categories of impediments, priority areas for improvement:

vi) Lack of transparency in policies and regulations concerning investment (institutional problems)

v) Complicated and/or delayed procedures with respect to investment-related regulations (implementation problems)

ix) Underdeveloped infrastructure, shortages of human resources, and insufficient investment incentives

i) Restrictions on foreign entry

viii) Labor regulations and related practices excessively favorable to workers
Major findings (1): importance of FDI facilitation

Data source: Table 3.2.

Figure 3.1 Decomposition of issues into 10 categories

- i) Restrictions on foreign entry (8%)
- ii) Performance requirements (4%)
- iii) Restrictions on overseas remittance and controls on foreign currency transactions (4%)
- iv) Restrictions on the movement of people and employment requirements (6%)
- v) Institutional problems (25%)
- vi) Implementation problems (26%)
- vii) Insufficient protection of IPRs (6%)
- viii) Labor regulations (7%)
- ix) Underdeveloped infrastructure, shortages of human resources, etc (12%)
- x) Restricted competition and price controls (2%)

Restrictions on foreign entry are the major concern, followed by institutional problems and insufficient protection of IPRs.
2. Analysis of investment climate (continued)

Major findings: different impediments between high and low income economies

- FDI liberalization: Impediments are more serious in low income economies
- FDI facilitation:
  Low income economies: 1. vii) implementation problem, 2. vi) institutional problem, 3. ix) underdeveloped infrastructure
  High income economies: 1. v) institutional problem, 2. vi) implementation problem, 3. viii) labor regulations
Major findings (2): differences bet. two income groups

Figure 3.2 Decomposition of the problems and low and high income economies
(a) Decomposition of the problems into 10 categories: low/high income economies
(b) Decomposition of the problems into low/high income economies: 10 categories

Data source: authors' calculation, based on Table 3.2.
Note: low/high income economies are 11/10 APEC economies with GDP per capita of less than US$10,000 in 2005 (see Table 3.3 for GDP per capita).
Specific problems in

Category vi) Complicated and/or delayed procedures with respect to investment-related regulations (implementation problems) (26%)

- Complexity, delay, difficulty, and inefficiency of various administrative procedures
  
  e.g. customs clearance, visa application and its renewal, import tariff reimbursement/exemption, value-added tax exemption (including non-implementation), taxation, and withdrawal of business

- Arbitrary/inconsistent interpretation in implementing regulations
  
  e.g. safety certification system, customs clearance, and tax collection

- Corruptions
Specific problems in

- Category v) Lack of transparency concerning policies and regulations on investment (institutional problems) (25%)
  
  - Underdevelopment, lack of transparency, ambiguity, sudden changes, frequent changes, and uncertainty of various legal regulations and institutions

  e.g. taxation-related (including double taxation due to lack of investment treaty), safety and environmental standards and conformity-related, and transfer pricing-related
Specific problems in

◆ Category ix) Underdeveloped infrastructure, shortages of human resources, and insufficient investment incentives (12%)

e.g. difficulty in hiring and securing human resources (management staff and engineers), high turnover ratios, underdevelopment of industrial infrastructure (electric power, paved road, ports, and industry waste disposal), rapid increase in utility rates, insufficient investment incentives, underdeveloped financial market

◆ Category i) Restrictions on foreign entry (8%)

e.g. prohibition and restrictions on foreign entry, restrictions on foreign ownership ratios, joint venture requirements, restrictions on foreign ownership of land
2. Analysis of investment climate (continued)

Specific problems in

◆ **Category viii)** Labor regulations and related practices excessively favorable to workers (7%)

  e.g. difficulty of firing workers and wage-related issues (a rapid rise in wage levels, a dramatic increase in minimum wage levels), and labor regulations and related practices excessively favorable to workers

◆ **Category iv)** Restrictions on the movement of people and employment requirement (6%)

  e.g. nationality requirement of directors, restrictions on hiring foreigners including requirements of hiring (specific types of) local people, and difficulty and tightened issuance conditions in obtaining and/or renewing visa
Specific problems in

◆ Category vii) insufficient protection of IPRs (6%)
  e.g. widespread counterfeit goods and pirated copy, no
  ratification of IPRs treaty, and infringement of
  trademarks rights and patents

◆ Category ii) performance requirements (4%)
  e.g. local contents requirements, export requirements
  linked with investment incentives, and performance
  requirements according to the degree of investment,
  export, and production
2. Analysis of investment climate (continued)

Specific problems in

◆ Category iii) restrictions on overseas remittances and controls on foreign currency transactions (4%)

e.g. restrictions on remittance abroad, difficulty in getting an access to local currency financing, and restrictions on the use of foreign currencies

◆ Category x) restricted competition and price controls (2%)

e.g. insufficient enforcement, extraterritorial application, and non-disclosed cases of anti-trust laws and oligopolistic market structure
Comparison with other studies

- JMC2000
  - Assessment of FDI liberalization only
  - High # of incidents: performance requirement, restriction on foreign entry, work permit
- Ease of doing business
- Global competitiveness index
- IMD world competitiveness index
- Study by Australia (degree of FDI barriers)
2. Analysis of investment climate (continued)

Comparison with other studies (continued)

=> Major findings from other studies

1. Reducing complexity and time required for institutional procedures, flexibility of labor market, improving taxation regulations, and developing infrastructure are particularly important

2. Substantial improvement of business environment is required for low income economies

3. Consistent with our analysis: high correlation in country ranking (excl. IMD WCI) (Tab.3.4)
Table 3.4 Rank correlation matrix for 5 surveys

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<th>GCI</th>
<th>IMD</th>
<th>JMC2000</th>
<th>JMC2005</th>
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<td>JMC2005</td>
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</table>

Note: "***", "**", and "*" express statistical significance at 1%, 5%, and 10% level, respectively. Spearman method is used for 17 countries in all cases above. JMC2005 is our analysis.

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<th>JMC2005</th>
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<td>Study by Australia</td>
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<td>0.473 *</td>
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<td>0.692 ***</td>
<td>0.631 **</td>
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Note: See notes above. Spearman method is used for 14 countries. The ranking in study by Australia is for the degree of FDI barriers.
See also Table A.2.1 for components of each of 10 factors and their evaluation.

2007.5.29
See also Table A.2.2 for more detailed components and disadvantages of each economy.
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<th>Canada</th>
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</table>

Data source: IMD2006.

Note: Average ranking is calculated for a comparison among components.
<table>
<thead>
<tr>
<th>Focused on foreign investment</th>
<th>Inventory approach</th>
<th>Quantitative approach</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Survey on investment liberalization and facilitation (by Japan)</td>
<td>Survey on enhancing investment liberalization and facilitation in economic development in Asia-Pacific region (by Australia)</td>
</tr>
<tr>
<td>Focused on domestic investment</td>
<td>Surveys for private sector development (e.g. Canada, NZ, and World Bank)</td>
<td></td>
</tr>
</tbody>
</table>
3. Discussions from the legal perspective

For FDI liberalization

- Simple solution: eliminate or phase out restrictions through revision of the relevant laws

- Related normative principles
  - Ensure MFN and national treatment in FDI establishment and operation
  - Abolish WTO TRIMs-inconsistent performance requirements (local content requirements, trade balancing requirements, foreign exchange restrictions, and domestic sales requirements)
  - Ensure investors free and prompt transfers of investment-related funds in freely convertible currencies at market exchange rate
  - Review restrictions and controls on the temporary entry and sojourn of key foreign technical and managerial personnel
3. Discussions from the legal perspective (continued)

For FDI facilitation

- Not simple solution; build up practical APEC-wide schemes for technical cooperation and information exchange
  - Institution- and capacity-building in the public sector
  - Policy dialogue and regulatory harmonization within the region

- Attempts to be made
  - Continue and further elaborate the existing APEC endeavors
  - Close coordination with the OECD Policy Framework for Investment
  - Accelerate the conclusion of bilateral or regional agreements (RTAs/FTAs and BITs)
## Discussion from the legal perspectives (continued)

<table>
<thead>
<tr>
<th>10 major categories for FDI liberalization and facilitation</th>
<th>Corresponding chapters on investment in FTAs and investment treaties</th>
</tr>
</thead>
<tbody>
<tr>
<td>i. Restrictions on foreign entry</td>
<td>investment, trade in services</td>
</tr>
<tr>
<td>ii. Performance requirements</td>
<td>investment</td>
</tr>
<tr>
<td>iii. Restrictions on overseas remittances and controls on foreign currency transactions</td>
<td>investment, trade in services, finance</td>
</tr>
<tr>
<td>iv. Restrictions on the movement of people and employment requirements</td>
<td>investment, movement of business persons</td>
</tr>
<tr>
<td>v. Lack of transparency in policies and regulations concerning investment (institutional problems)</td>
<td>general provisions, trade in goods, trade facilitation, taxation, standards and conformity assessment procedures, environment</td>
</tr>
<tr>
<td>vi. Complicated and/or delayed procedures with respect to investment-related regulations (implementation problems)</td>
<td>general provisions, trade in goods</td>
</tr>
<tr>
<td>vii. Insufficient protection of intellectual property rights</td>
<td>intellectual property</td>
</tr>
<tr>
<td>viii. Labor regulations and related practices excessively favorable to workers</td>
<td>improvement of business environment</td>
</tr>
<tr>
<td>ix. Underdeveloped infrastructure, shortages of human resources, and insufficient investment incentives</td>
<td>investment, co-operation</td>
</tr>
<tr>
<td>x. Restricted competition and price controls</td>
<td>competition policy, anti-trust agreement</td>
</tr>
</tbody>
</table>
4. Findings from our study

1. Importance of FDI facilitation
2. Necessity of further FDI liberalization, particularly for low income economies, besides FDI facilitation
3. Among 10 categories, areas to be improved with the highest priority:
   vi) Lack of transparency in policies and regulations concerning investment (institutional problems)
   v) Complicated and/or delayed procedures with respect to investment-related regulations (implementation problems)
   ix) Underdeveloped infrastructure, shortages of human resources, and insufficient investment incentives
   i) Restrictions on foreign entry
   viii) Labor regulations and related practices excessively favorable to workers
5. Policy suggestions

- Conduct a periodic (annual) APEC survey to collect information on FDI impediments from FDI firms, possibly by building on JMC Survey, in order to assess FDI environment of APEC economies.
- Make concerted efforts to deal with high priority issues in FDI liberalization and facilitation within the APEC framework.
- Use various frameworks including BITs, FTA/RTA to deal with the FDI impediments.
- Capacity building is particularly important to deal with FDI facilitation.
- Cooperation between public and private sectors is essential in identifying the FDI impediments and removing them.
Reactions to our findings
- 10 major categories and the highest priority areas
- Their relationship with APEC’s recent focus on the behind-the-border issues

How can we deliver our message on the FDI impediments to the APEC Leaders, so that the impediments will be adequately dealt with?
How can we use the results from various surveys including those conducted by the JMC, the World Bank, Australia, the IMD, GCI and others, in order to improve FDI environment?

Examples:
- Monitoring on improvement of investment liberalization and facilitation by APEC/ABAC
e.g. conduct survey every year
- Provide opportunities to learn best practices of improved business environment and share them among the members
- Capacity building focused on high priority areas
e.g. establish transparent regimes concerning investment, implement them effectively, and involve private sector