

FDI Conference
Session I – Overview of Key Issues to be Addressed
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Chanpen Puckahtikom

1. **Over the last decade, China and Southeast Asia have seen a remarkable increase in FDI.** Such capital has now become an important source of growth for these countries. Nonetheless, countries' experiences have varied, and there have been questions about the economic effects of FDI, the stability of FDI, and the right approach to FDI policies.

2. **These are the type of questions that we are seeking to explore in this conference and which I would like to preview briefly.** Three broad themes are being addressed: first, the main analytical issues and the trends of FDI flows; second, based on the experience of East Asia, the key factors driving FDI and the main policy issues that have arisen; and third, the policy priorities for Cambodia, Laos and Vietnam going forward.

3. **As background, we will start off in Session I with the main analytical issues.** In particular,
 - What factors determine the direction of FDI?
 - How does FDI affect investment and growth, and does FDI do more than simply result in a higher level of investment? What determines the pace of technology transfer and the spillover effects of FDI?
 - Is FDI truly distinct from portfolio capital flows in its economic impact?

4. **This will be followed by a review of how important FDI flows have been, relative to other sources of capital, with particular emphasis on Asia.** What have been the recent global and regional trends for such flows? FDI has been regarded as stable relative to other forms of private capital flows, but how stable have FDI flows actually been?

5. **Against this analytical and factual background, we will examine in Session II the experience of East Asia in attracting FDI.** The focus will be on assessing the relative importance of such factors as openness, investment climate, and FDI strategies. The main questions and policy issues that will be covered can be grouped under five main headings.

6. **First, what factors drive FDI?** Specifically,
 - From the perspective of Japan, an important source of FDI for the ASEAN 4 countries, what explains the rapid expansion of Japanese FDI to these countries in the 1990s before the Asian crisis, and the falloff thereafter? How important are such factors as low production cost, local market demand, the presence of AFTA, and the open trade and FDI regimes in these countries?
 - As a counterpoint, what is the lesson from the record of India where FDI has been relatively modest, in spite of its large domestic market and abundant labor? What importance should be attached to streamlining licensing and approval procedures, easing barriers to entry, and upgrading infrastructure?
 - What might help to maintain the momentum of FDI? From the experience of Indonesia, where FDI has fallen sharply in recent years, what is the role played by

an uneven application of the rule of law? And is there a good case for adopting a negative list for FDI, and keep FDI out of selected sectors?

7. **Questions under the second heading concern how can countries maximize the benefits of FDI?** Or to quote one of the case studies in this conference, how can FDI be brought in line with national interests? In a region with a high rate of domestic savings such as East Asia, the benefit of FDI might not primarily be quantitative, in the form of additional funding for investment. Rather, a more lasting benefit may be qualitative, through improving productivity. This can be achieved through upgrading technology and management skills, via direct transfer of technology to subsidiaries or joint ventures or through spillovers to domestic firms. Have countries fully tapped this qualitative potential of FDI? More specifically,

- From countries as diverse as China and Indonesia, how effective are the so-called 'performance requirements' or 'local ownership requirements'? For Indonesia, have such requirements in fact spawned the corruption that ultimately drove away FDI?
- At the same time, however, are export performance requirements different from other requirements in terms of economic effects?
- For China and Thailand, FDI has been an important source of growth and multinational corporations have helped to upgrade industrial structure and expand exports. But questions have also been raised about how to step up the transfer of advanced technology and enhance spillovers in these cases. For China, in particular, how important are issues of market access and the protection of intellectual property rights in attracting high value-added, technology-intensive

industries? And for Thailand, should active, and selective interventions be adopted to encourage innovative FDI programs aimed at promoting technological developments and spillovers?

8. The third group of questions concerns the main policy pitfalls.

- From the experience of China, can tax incentives grow too complex with the consequent risks for corruption and lost revenues? More broadly, can preferential treatment for FDI become excessive, and should domestic firms and foreign invested firms be put more on an equal footing?
 - At a more basic level, do tax incentives matter? Have they been effective and at what cost? If incentives are unavoidable, how can they be designed so as to minimize fiscal costs and distortions?
 - What are the risks of too much FDI going into speculative real estate developments or too much physical capital?
9. **Fourth, what are the limits of FDI policies?** Should countries try to influence the mix of FDI, for instance by seeking to draw in only export-oriented and smaller firms and keep out multinationals in order to limit the risks of monopoly? China has succeeded in attracting FDI into Special Economic Zones in the coastal and major urban areas but has been less successful in drawing FDI into rural areas. How effective have countries been in directing FDI into specific locations or socially preferred sectors?
10. **Fifth, if countries have to sequence their policies due to capacity constraints, what are the most important, early prerequisites?** From the experience of China, how important is it to ensure early on a transparent legal framework, and to create a

favorable investment climate, even if the legal and governance systems are not fully up to international standards?

11. Tomorrow morning, following an overview of FDI trends in Cambodia, Lao PDR, and Vietnam, policymakers of these countries will give an account of their experience with FDI, the achievements so far and the challenges ahead. In the case of Cambodia and Lao PDR, how can they meet the special challenges posed by their small local market size, by the shortage of skilled labor, and by the weakness of physical infrastructure and supporting institutions? Vietnam fares better on some of these dimensions, but it too faces the challenges of regaining the confidence of investors, building market-based institutions, and further easing market access. For Lao PDR, in spite of a liberal investment policy, some of the main issues for FDI relate to policy transparency and the stability of business environment. And for Cambodia, the land issue is critical but particularly intractable. In all, how can these countries press ahead with the right sequencing in tackling the various policy requirements? For instance, if stronger institutions and governance are a prerequisite for FDI, how can they make progress in these areas when their administrative capacity is relatively weak?

12. The conference will close with a panel discussion on lessons for successful FDI strategies. Drawing on the experiences of Asian countries, what are the key policy priorities looking forward?

13. This is a full program and we look forward to an active exchange of views, from different perspectives.