

Overview of the Determinants of Investment Flows for APEC Economies

Paul Kennelly
*Senior Policy Adviser to the APEC
Investment Experts Group Convenor*
Australian Treasury

Capacity Building to Enhance Investment Flows in APEC Economies

1-8 April 2008, Melbourne

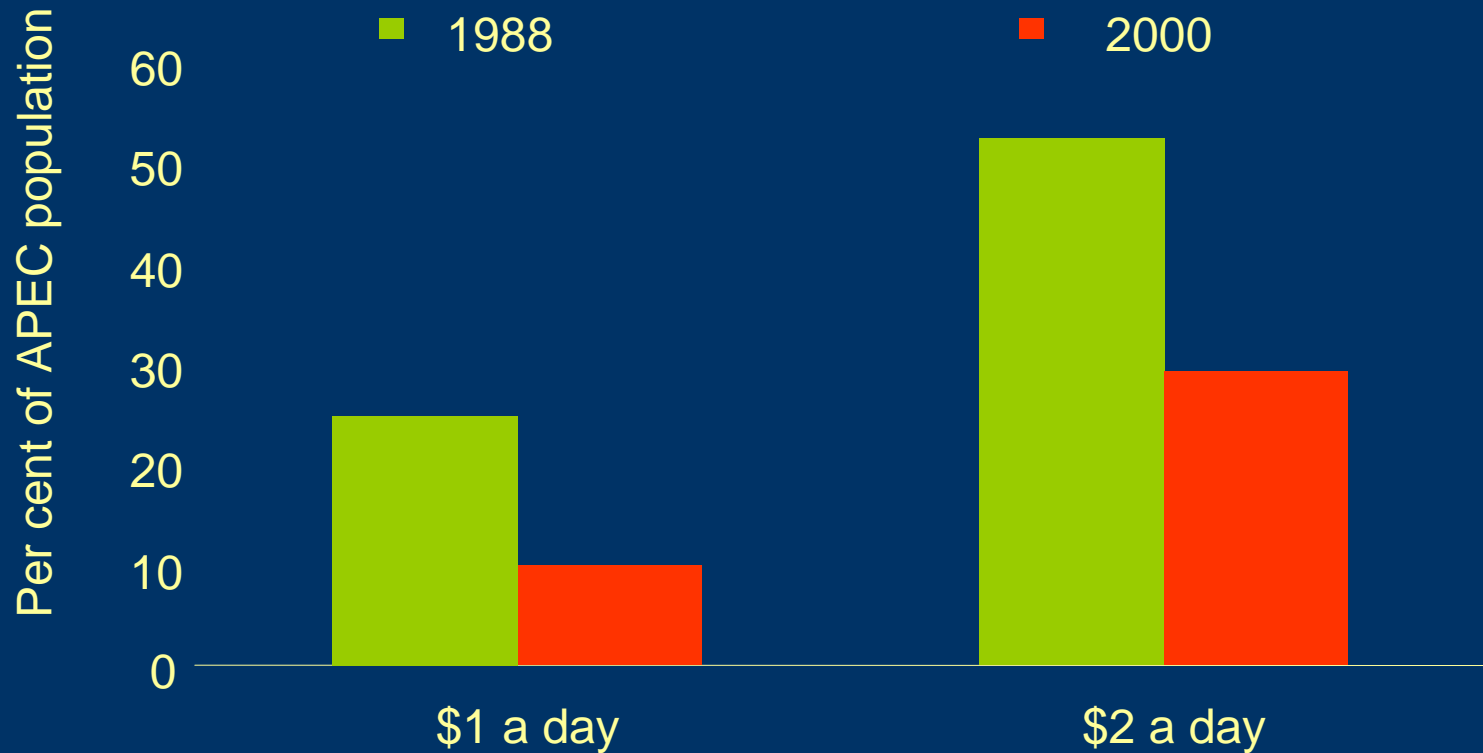
Presentation Structure

- Overview
- At Border Barriers to FDI Flows
- Behind-the-Border Barriers to Foreign and Domestic Investment

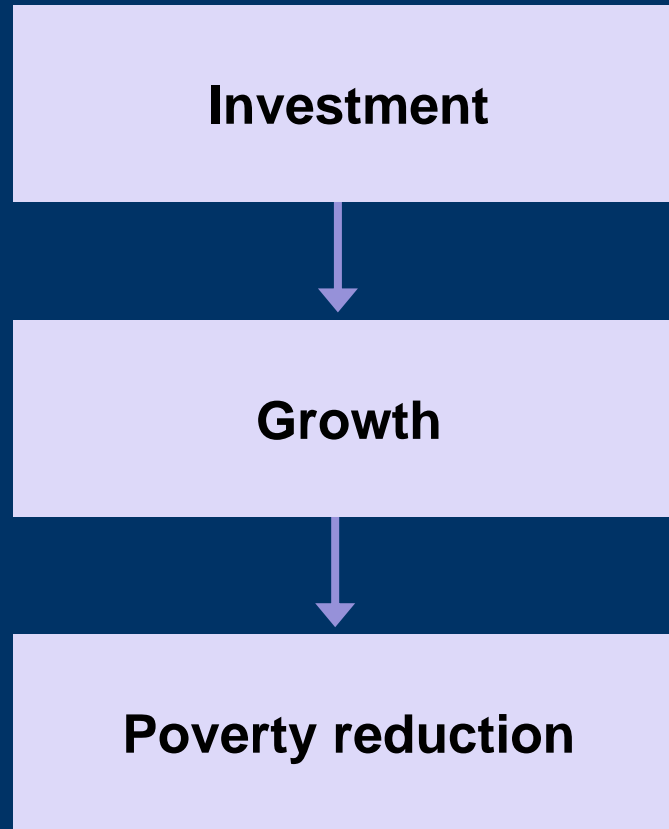
Overview

- 1) Falling poverty across APEC and drivers of poverty reduction and sustainable development
- 2) APEC work on investment to address these issues
 - Stage 1 Study: At Border Barriers
 - Stage 2 Study: Behind-the-Border Barriers
- 3) Summation of Key Issues
- 4) What to do?

1). Poverty rates have fallen across APEC



The key role of investment



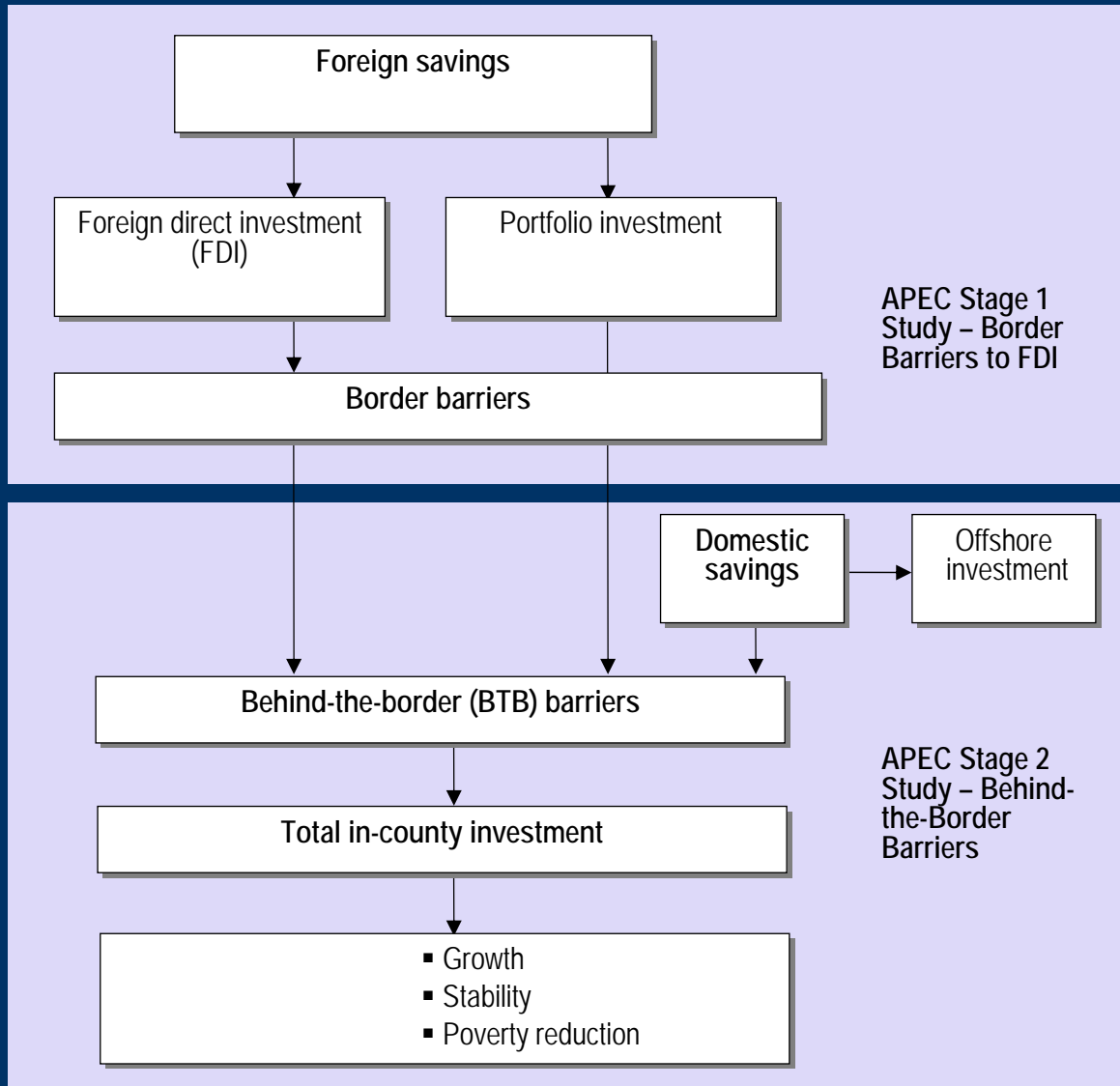
Drivers of poverty reduction and sustainable development

- Growth leads to poverty reduction
- Only two ways income per person can grow
 - Productivity (the amount of output per unit of input)
 - Investment (more capital per person)
- Foreign Direct Investment (FDI) offers both
- But there are significant barriers to FDI among low income APEC economies
 - Border barriers
 - Behind-the-border (BTB) barriers

Drivers of poverty reduction and sustainable development (continued)

- What boost to APEC growth would there be from removing those barriers?
- More quantification on barriers to investment at the border than BTB barriers

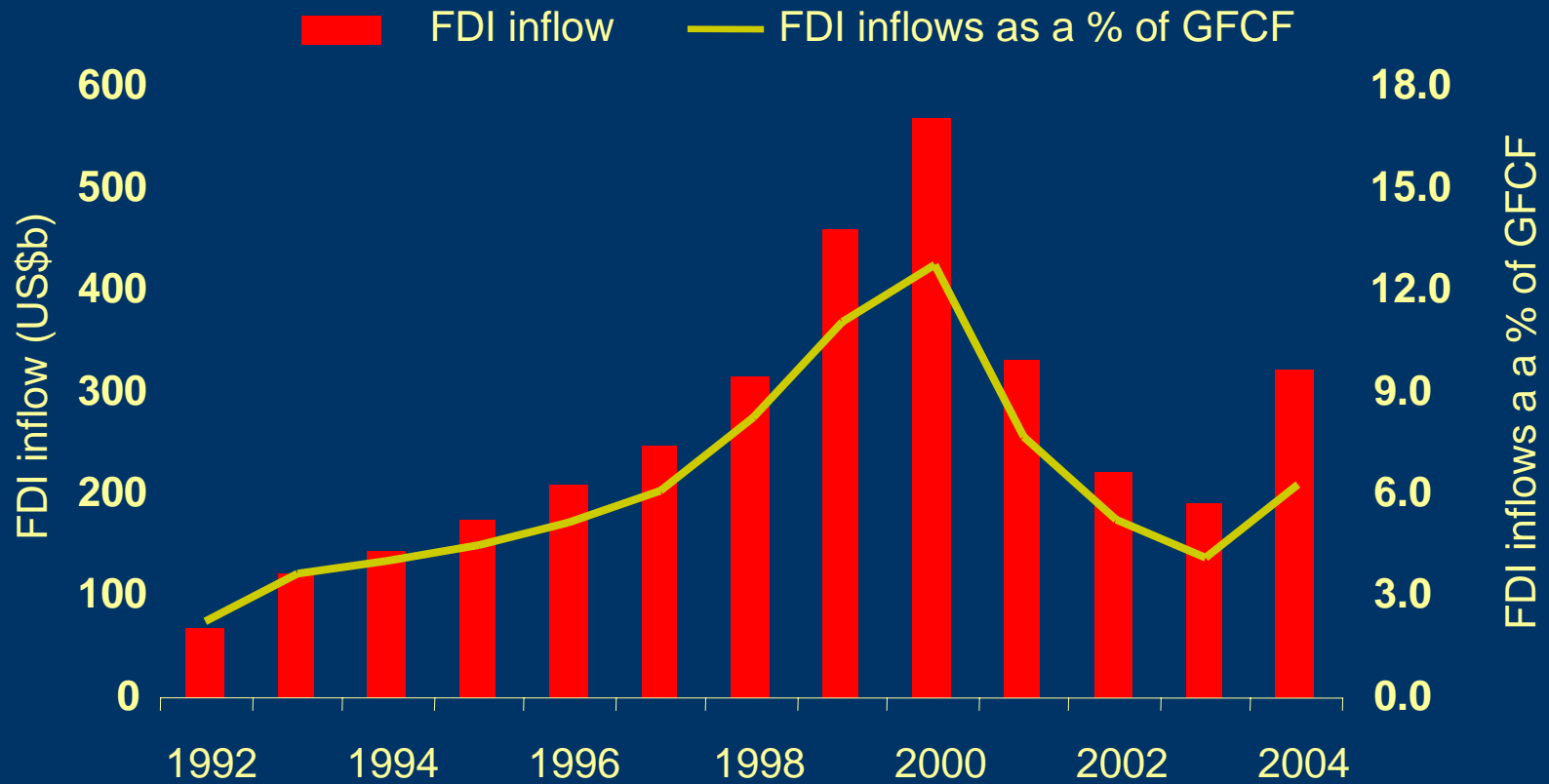
2). APEC work on investment to address these issues



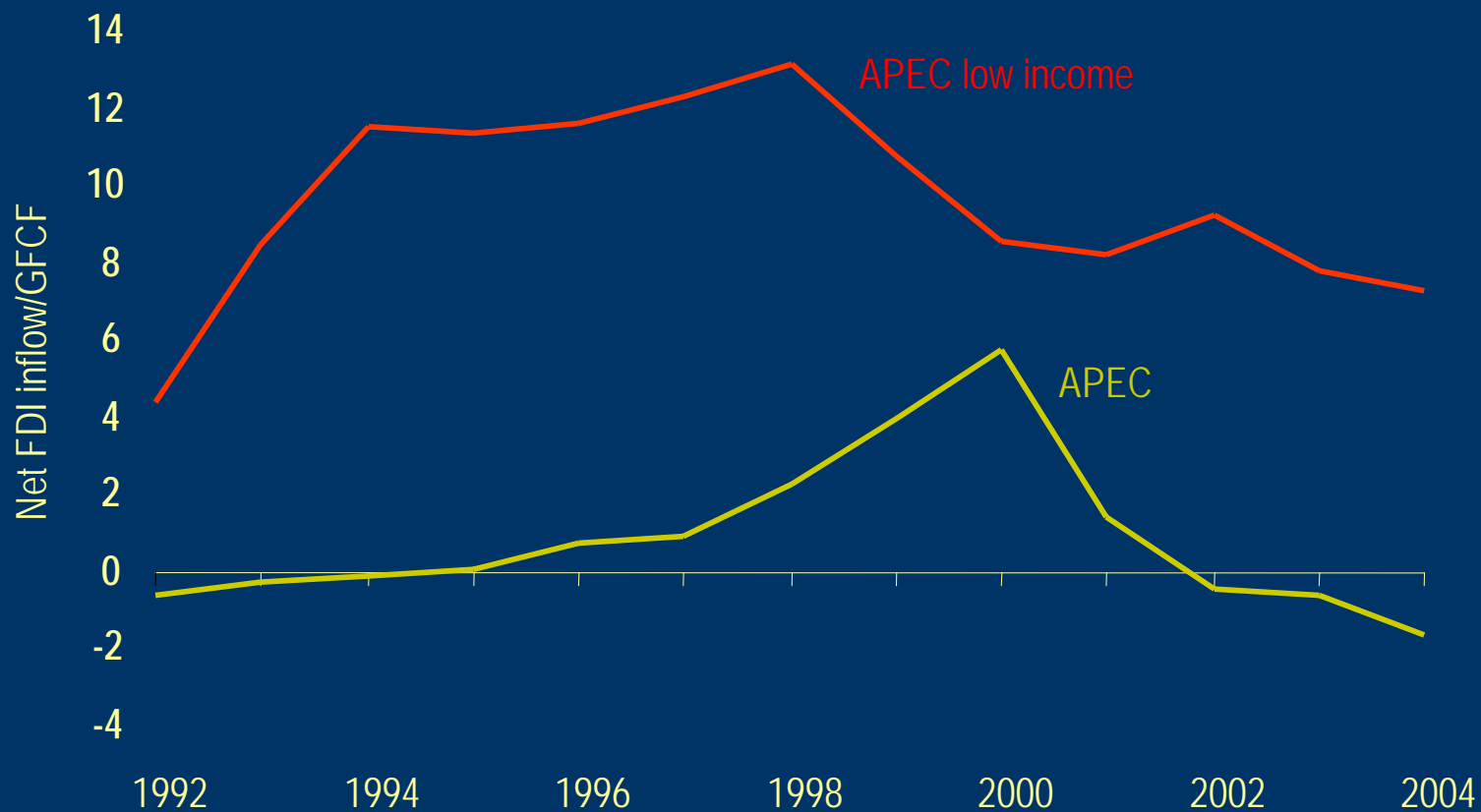
Stage 1 Study: At Border Barriers

- Brief look at FDI flows in APEC
- What is known about barriers from
 - OECD
 - UNCTAD
- What can be concluded about analyses of removal of barriers

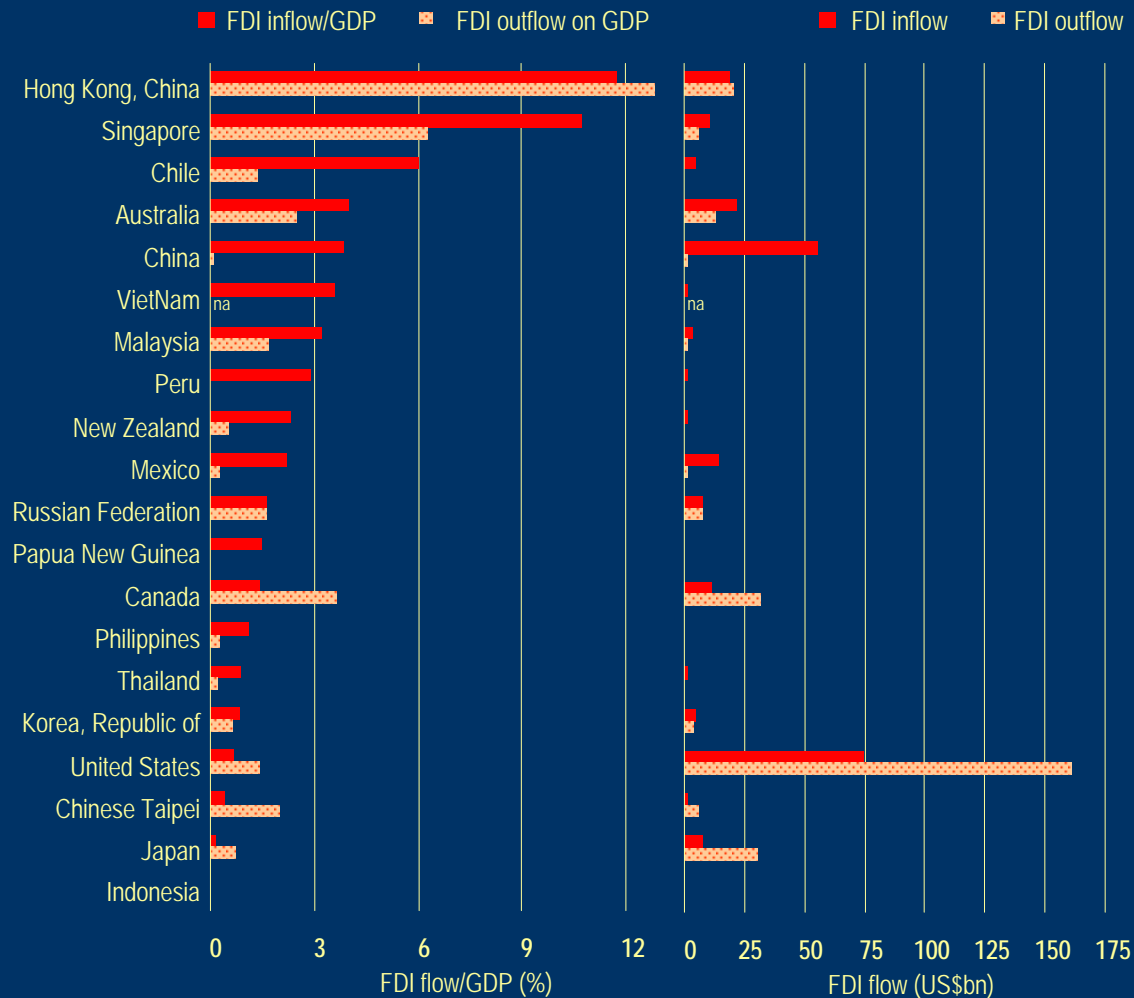
FDI inflows into APEC economies



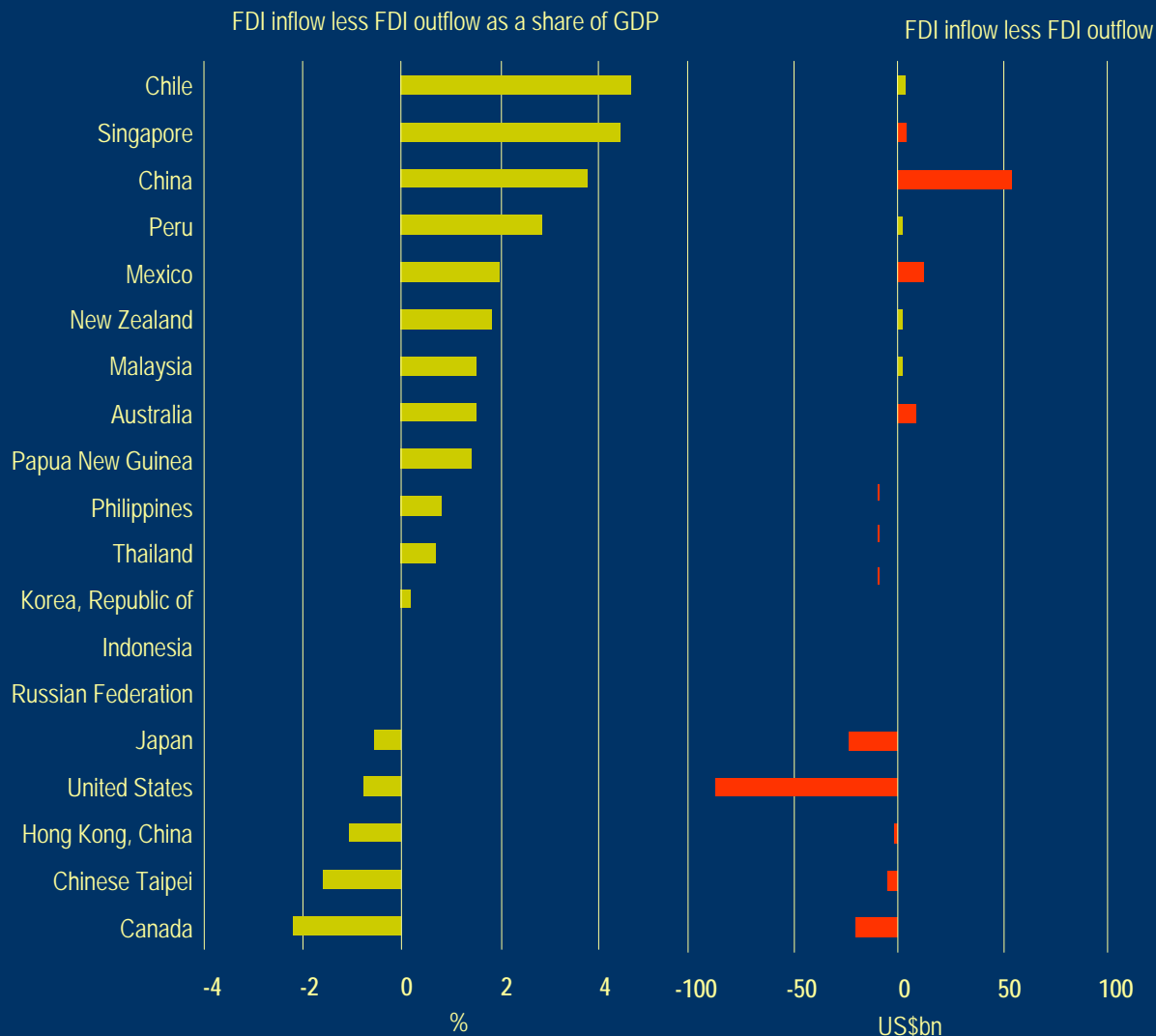
FDI inflows less FDI outflows for APEC economies



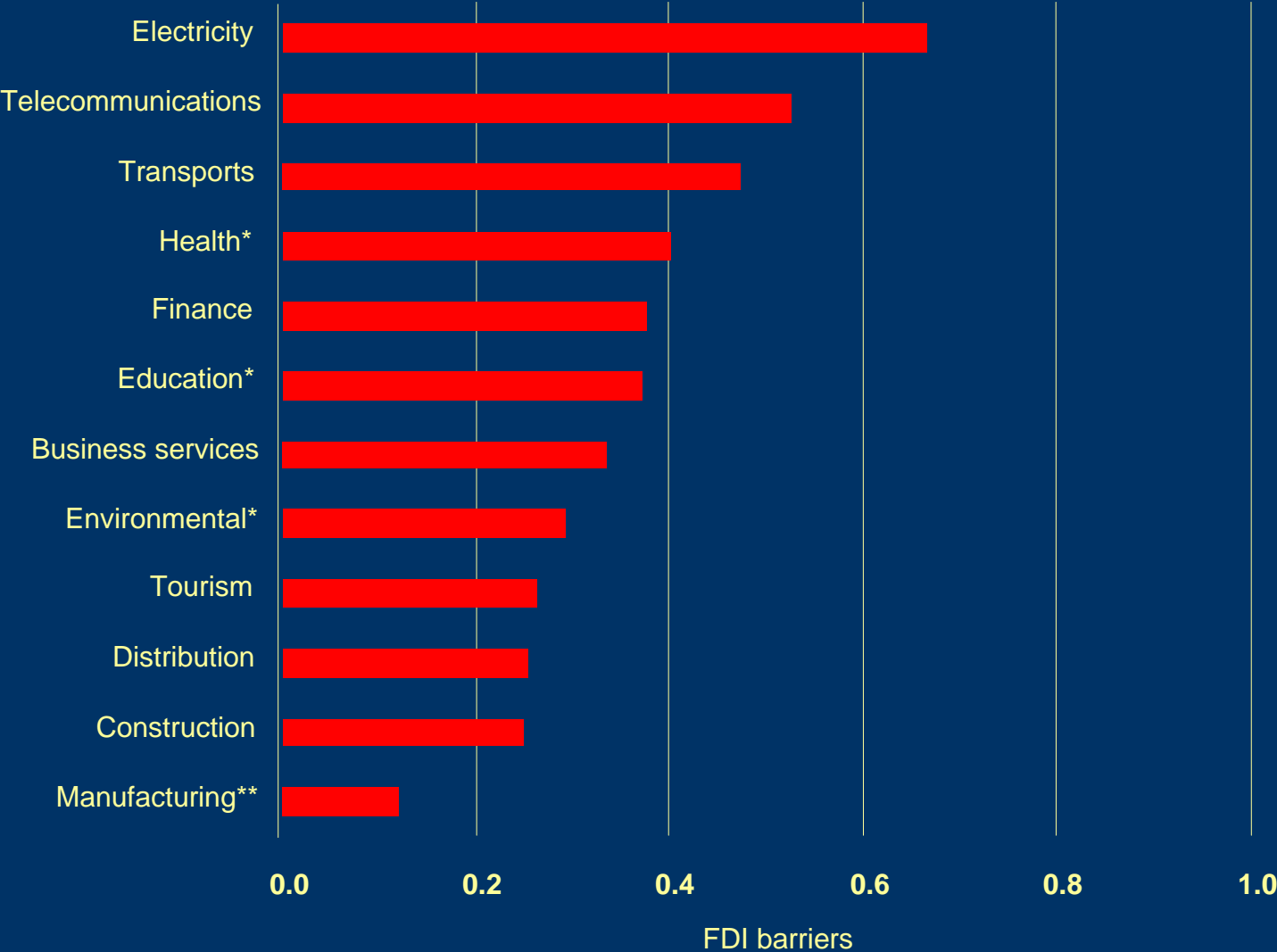
FDI inflows and outflows for APEC economies (average for 2002-04)



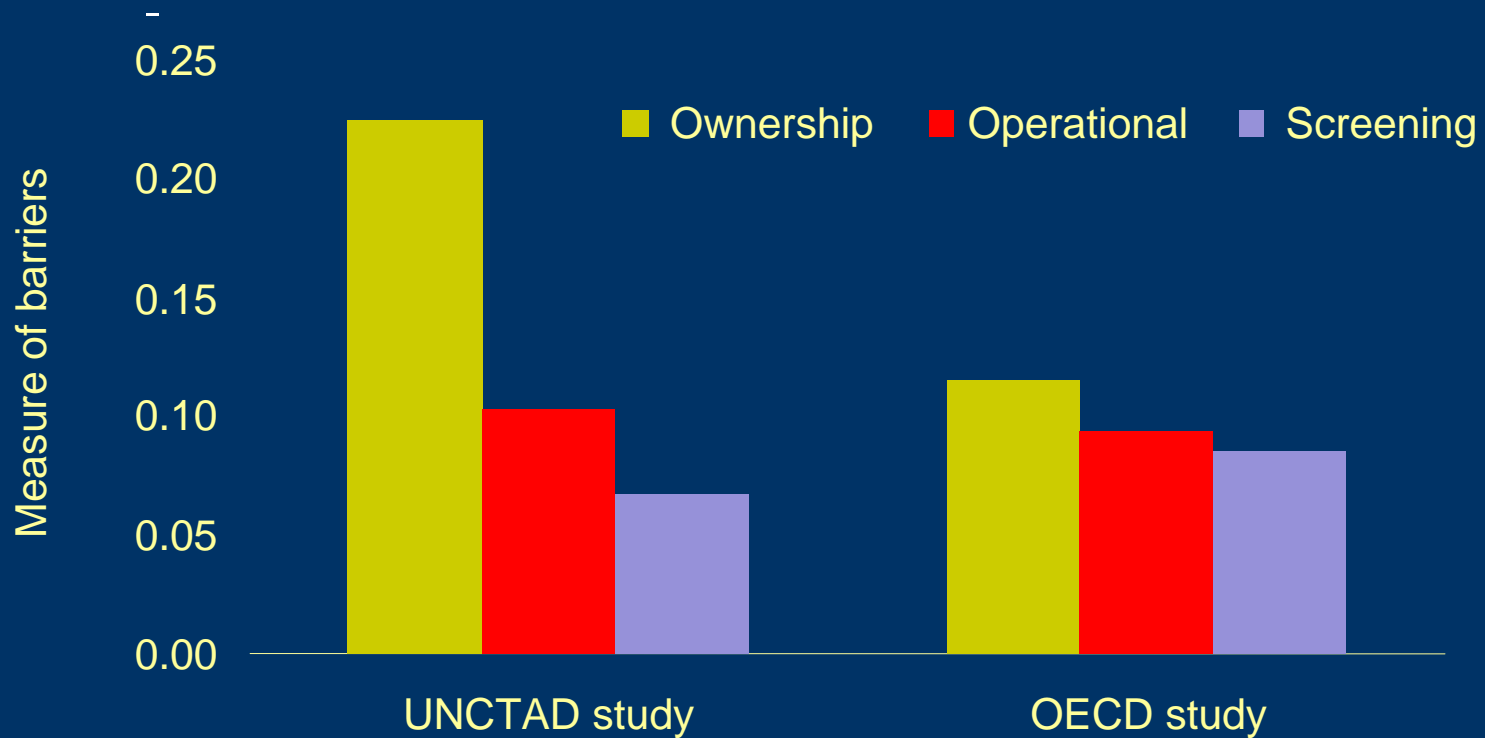
FDI inflow less FDI outflow for APEC economies (2002-04)



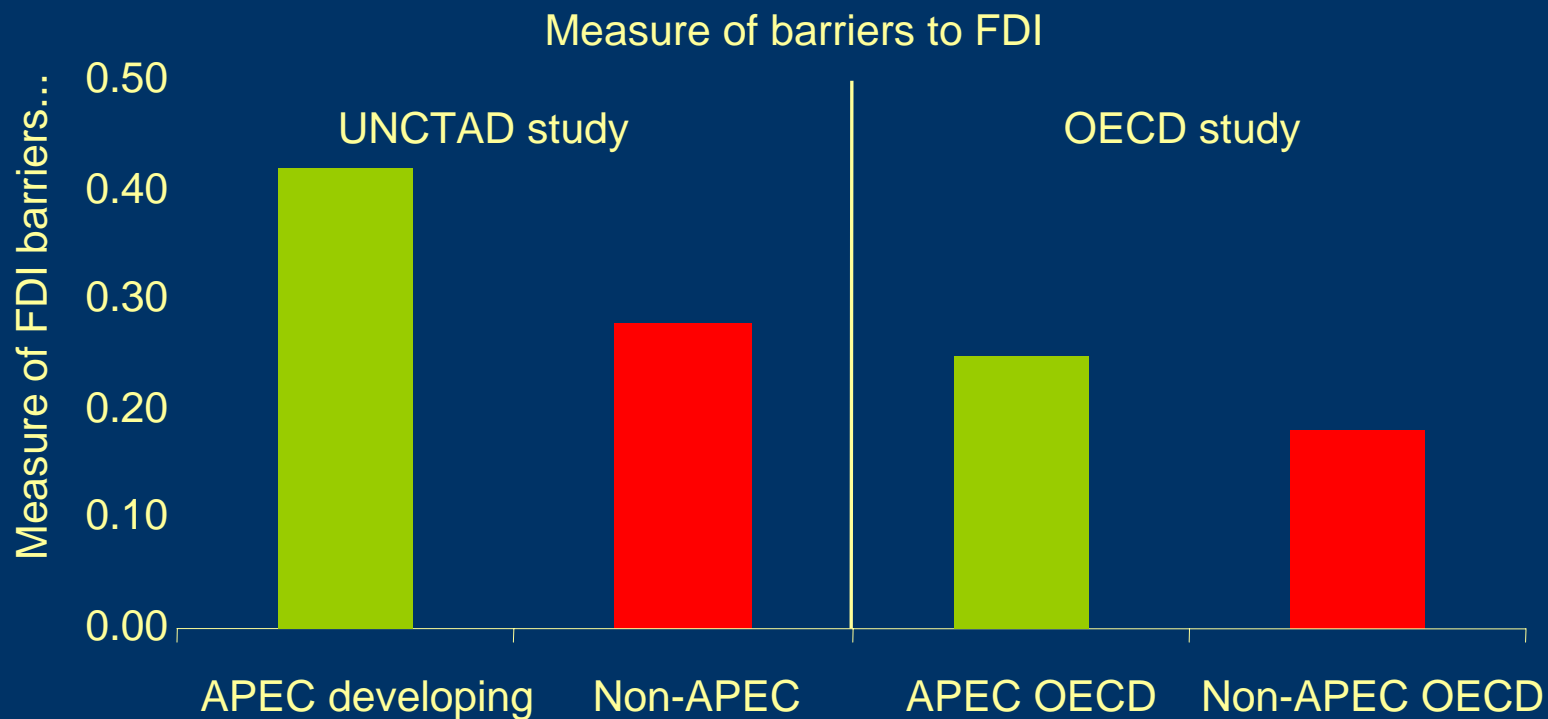
Barriers in the APEC region by sector



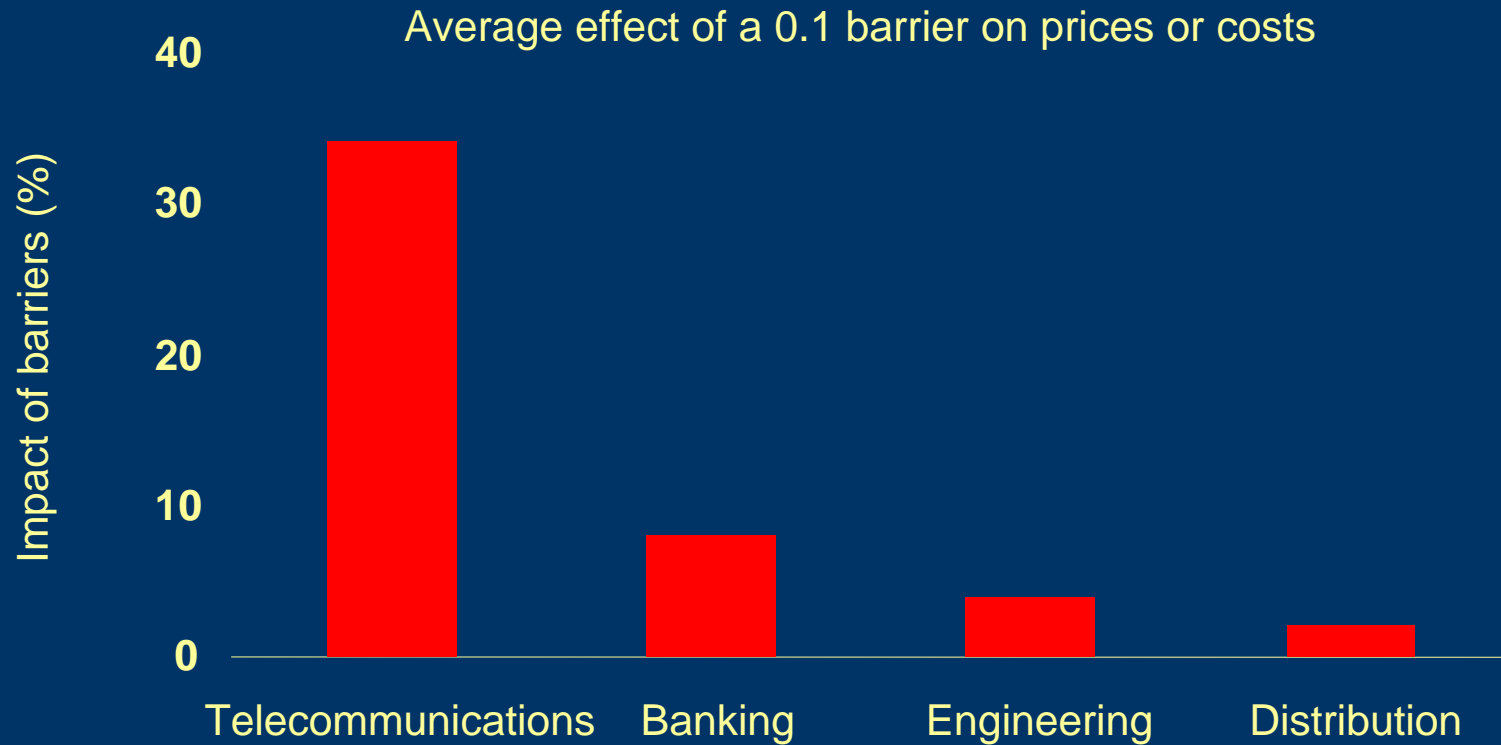
Types of FDI barriers in APEC economies



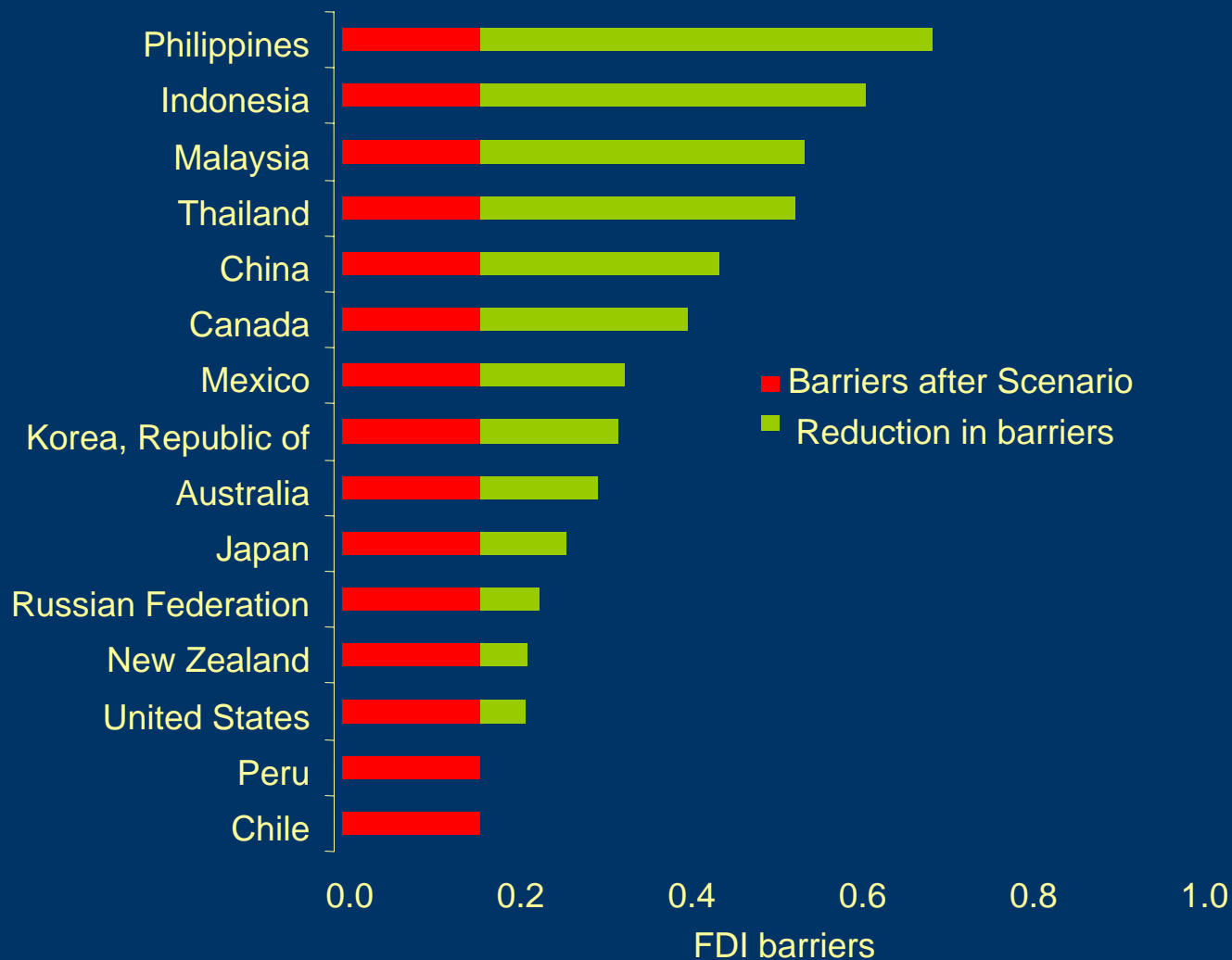
Barriers in APEC economies are higher than in other regions



Impacts of barrier on prices/costs in different industries



What's at stake: change in barriers under policy scenario



What could be the effect of lowering barriers to that of the most open APEC economies?

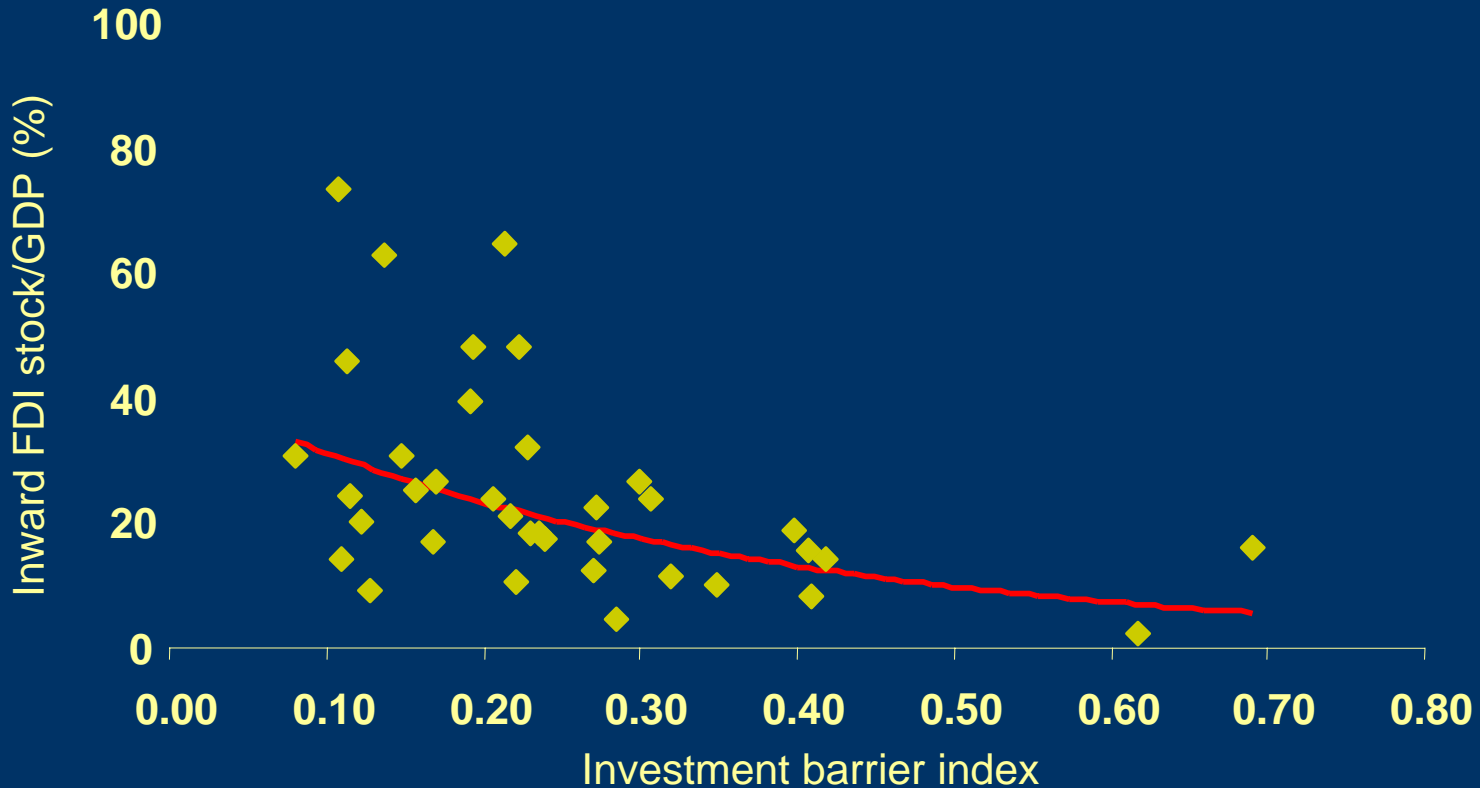
- Increase FDI across APEC by 26 per cent
- Could boost GDP by 2.6 per cent (at low end of range)
- Have biggest effect in low income economies (up to 86 per cent FDI increase)
- Reduce poverty (US\$1/day) by 20 per cent

But ...

- Estimates are partial, no flow-on effects
 - No economy-wide repercussions for interest rates or activity in rest of world
 - Do not have complete coverage of APEC economies
 - Relationship between increase in FDI and removal of barriers is imprecise

What do we know?

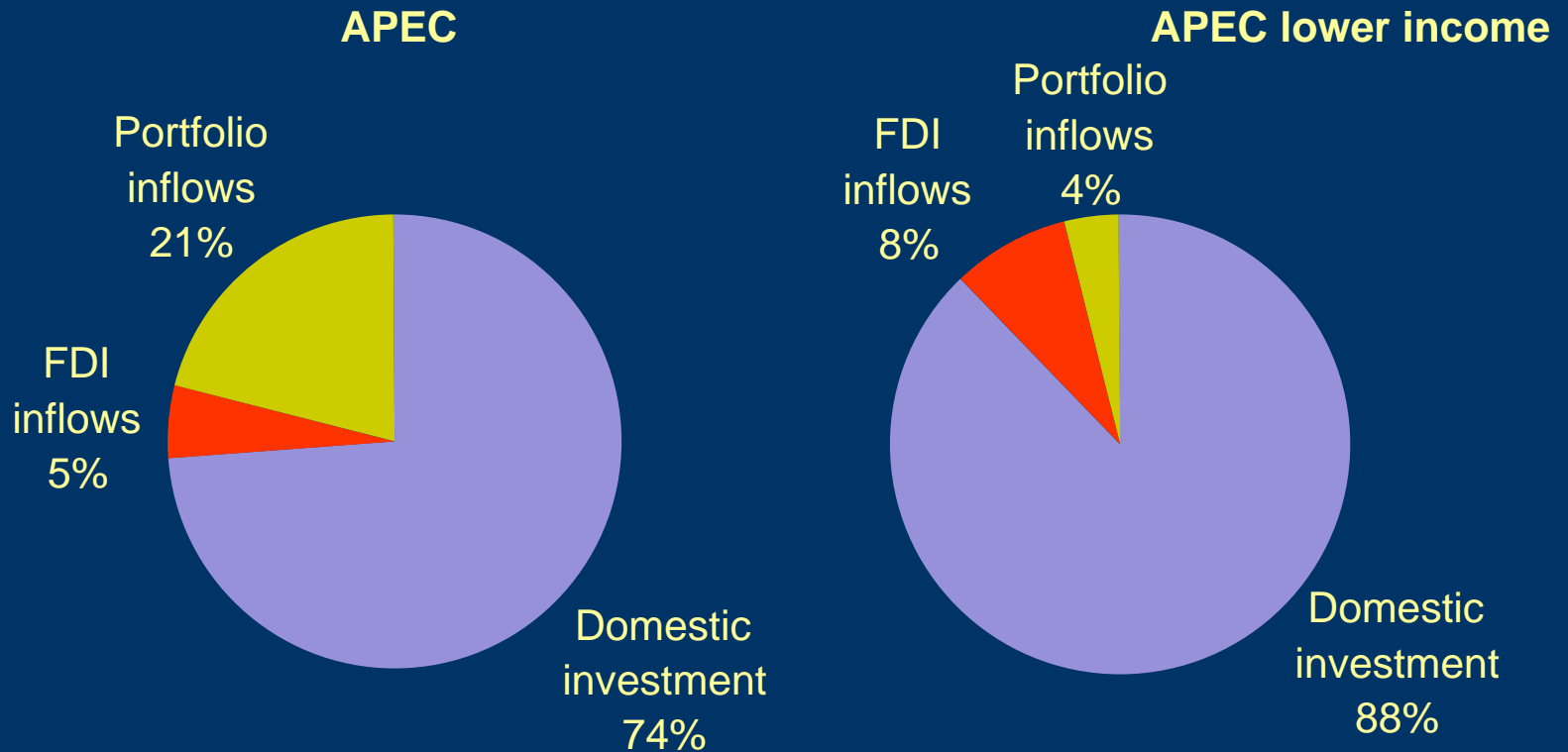
FDI falls as barriers increase - FDI and barriers in the service sectors of 37 countries



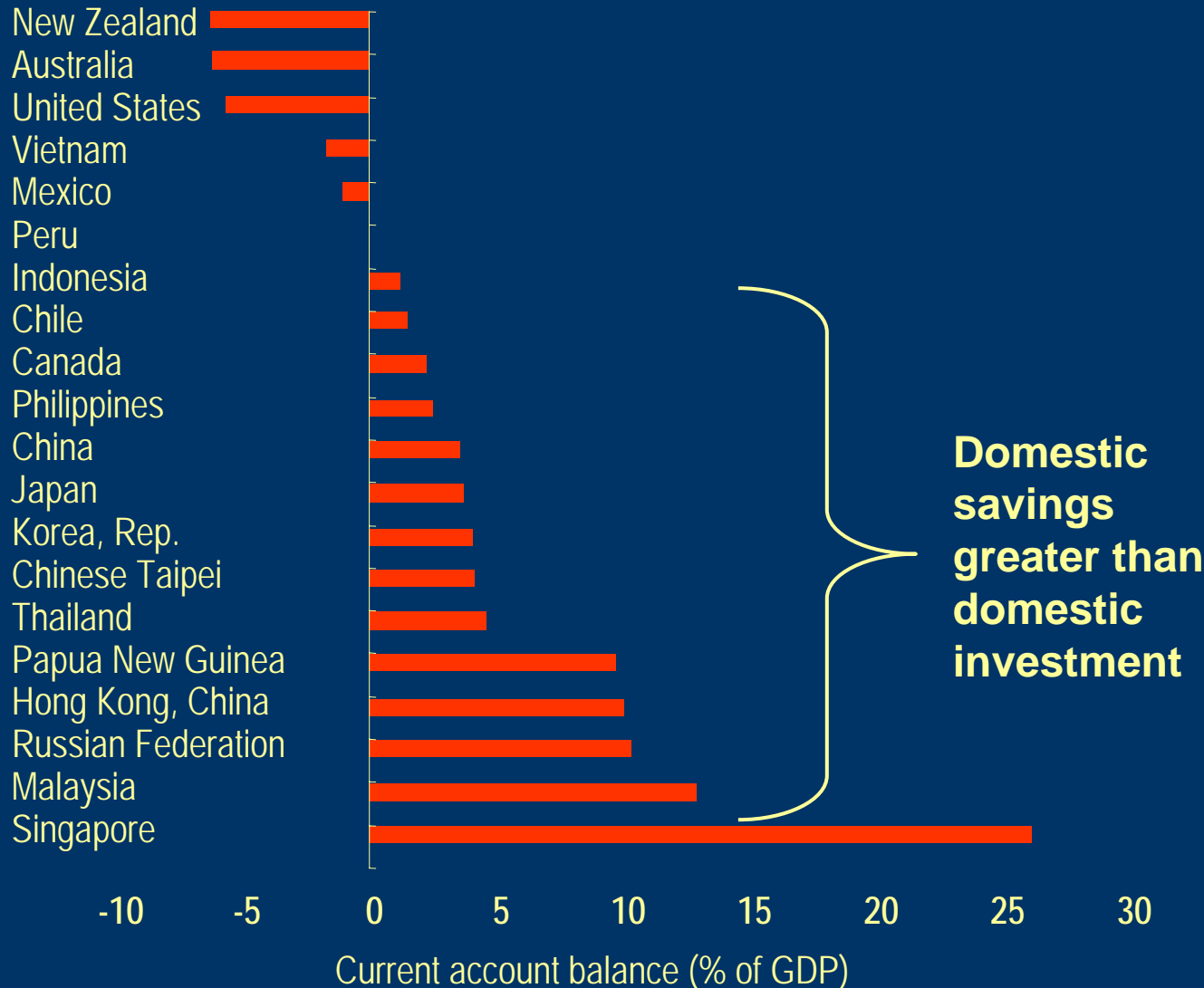
Stage 2 Study: Behind-the Border (BTB) Barriers

- The relative importance of foreign and domestic investment
- The significance of BTB barriers given disparities in FDI flows between economies with similar at border barriers?

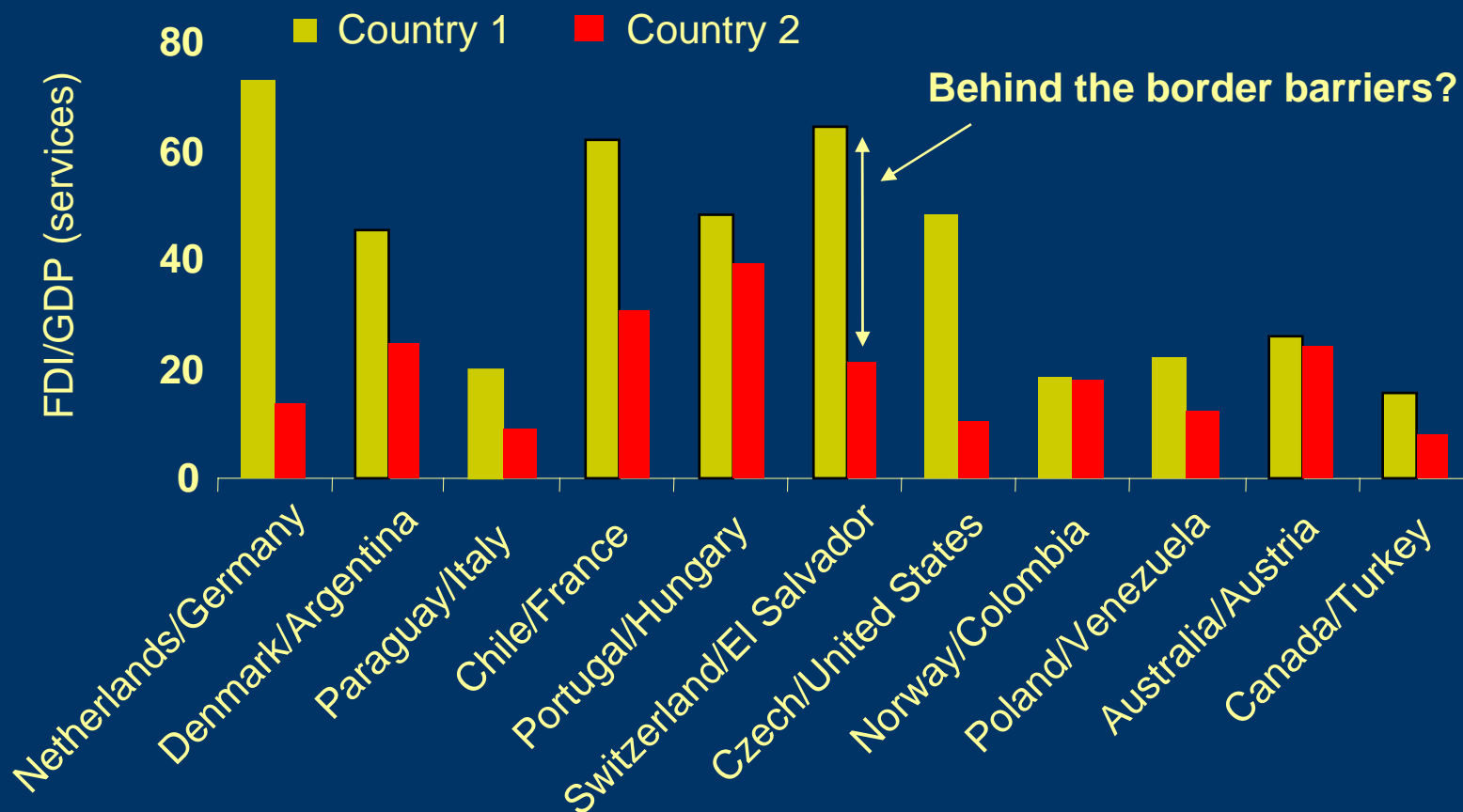
Composition of investment in APEC (average 2002 to 2004)



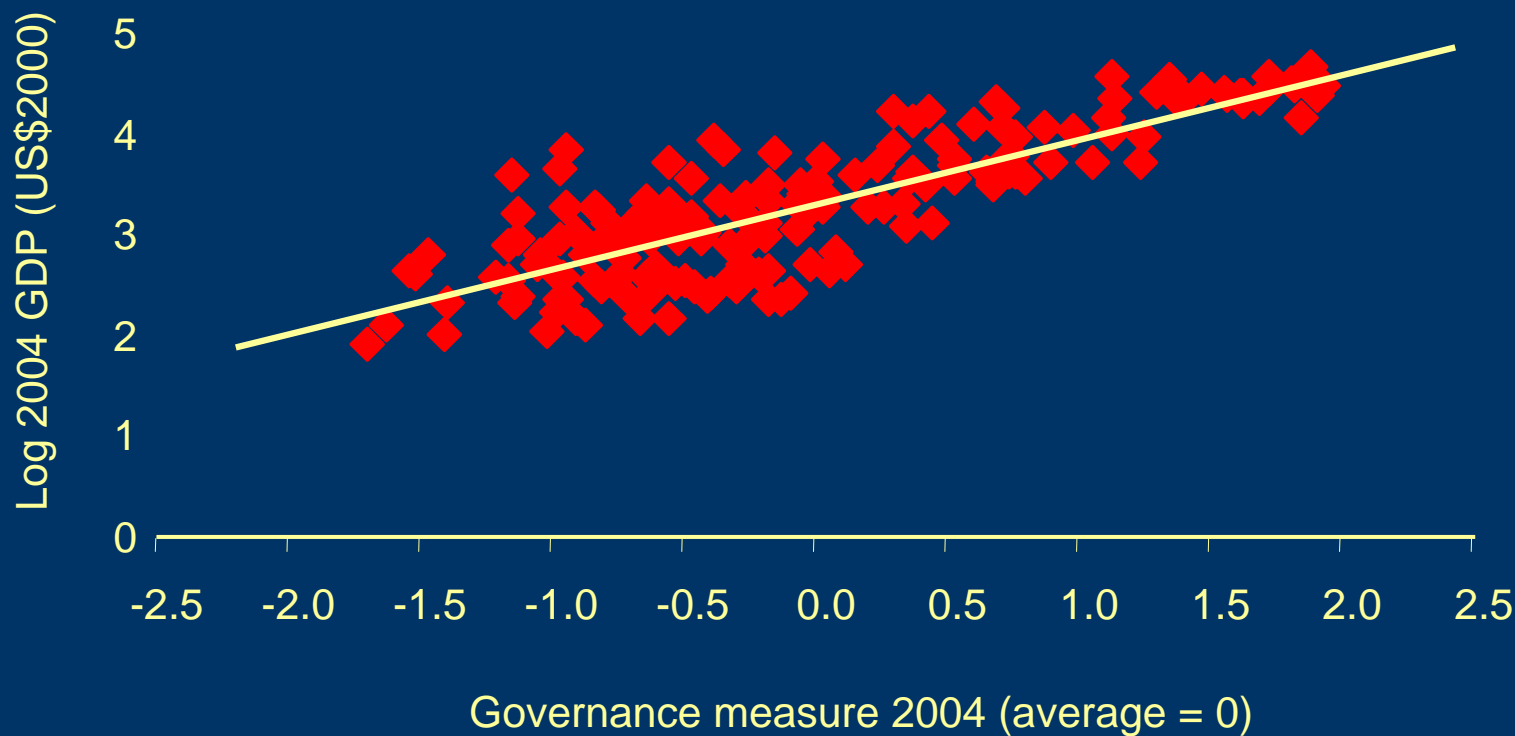
Low investment in some APEC economies is not due to low savings



Economies with similar barriers have different FDI – is this due to behind-the-border (BTB) barriers?



BTB barriers are important - income and measures of governance for 171 countries



APEC Stage 2 Study – its approach

- Outlines framework to conceptualise barriers
- Presents case studies to highlight successful examples of economic reform
 - 1. Greater Mekong Subregion Transport
 - 2. Thailand's Bankruptcy Law Reform
 - 3. China's accession to the WTO
 - 4. Vietnam's Enterprise Law Reform
 - 5. Australia's Competition Policy

Behind-the-border barriers

- Finance costs
- Inefficient taxes
- Regulatory burden
- Corruption
- Poor infrastructure
- Legal systems
- Property rights
- Contract enforcement
- Policy predictability and credibility
- Barriers to entry
- Competition law
- Functioning finance markets

Cost

Risk

Competition

Productivity

Growth

3) Summation of Key Issues for Stages 1 and 2 Studies

- There are some 30 per cent of people in APEC in poverty (US\$2 per day)
- Growth is the main driver for poverty reduction
- Investment is a precursor to growth
- Low investment in many poor economies is not due to low savings

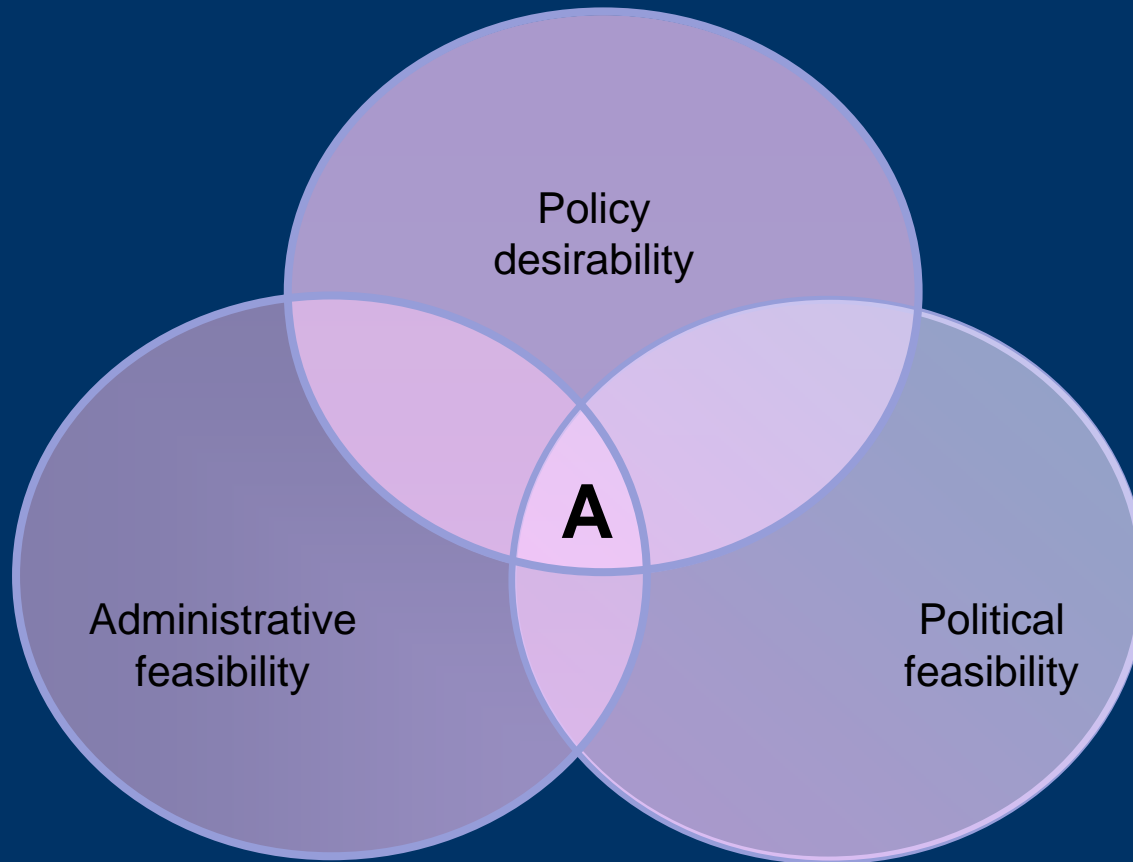
3) Summation (continued)

- There are large barriers to investment across APEC economies
 - Higher in poor countries
 - Border barriers to FDI well-known, higher in APEC
 - But BTB barriers more important and less well researched
- Both the quantity and quality of investment matters
- Better investment across APEC is needed
 - right amount, right type, right area, right time
 - all at least cost

4) What to do?

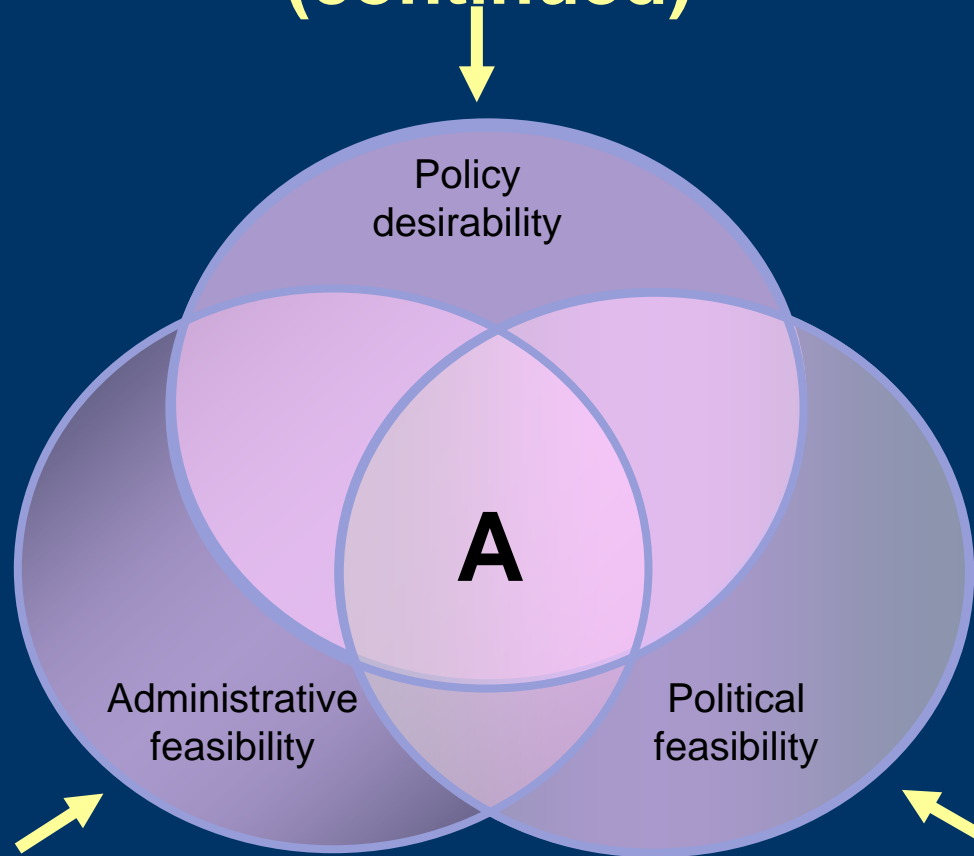
- Host of factors need to be right for better investment to lead to economic growth
- Factors are different for each economy
- Issues are *within* economies — the BTB issues
- Challenge is for each economy to harness their own institutional processes that best address their BTB barriers
- Lessons from others on *how* reforms undertaken may help

The challenge: increasing the 'sweet spot'



Source: *World Bank Development Report, 2005*

The challenge: increasing the 'sweet spot' (continued)



Source: *World Bank Development Report, 2005*

Next steps

- Good start to BTB barriers is World Bank's *Doing Business* report:
 - Covers nearly all APEC economies
 - Is amenable to quantification
 - Exists for several years
 - Consistent and comparable

Next steps (continued)

- An approach that allows some quantification if members choose is useful:
 - Encourages transparency
 - Knowing what is at stake helps motivate change
 - Helps set priorities
 - Builds knowledge base
 - All barriers either increase rents, costs or risk
- Case studies of where barriers have been removed and the experience can give valuable lessons

Thank you

Paul Kennelly
Foreign Investment and Trade Policy Division
Department of Treasury
Canberra , Australia
Paul.Kennelly@treasury.gov.au