

ASEAN Investment Report 2016

Foreign Direct Investment and MSME Linkages



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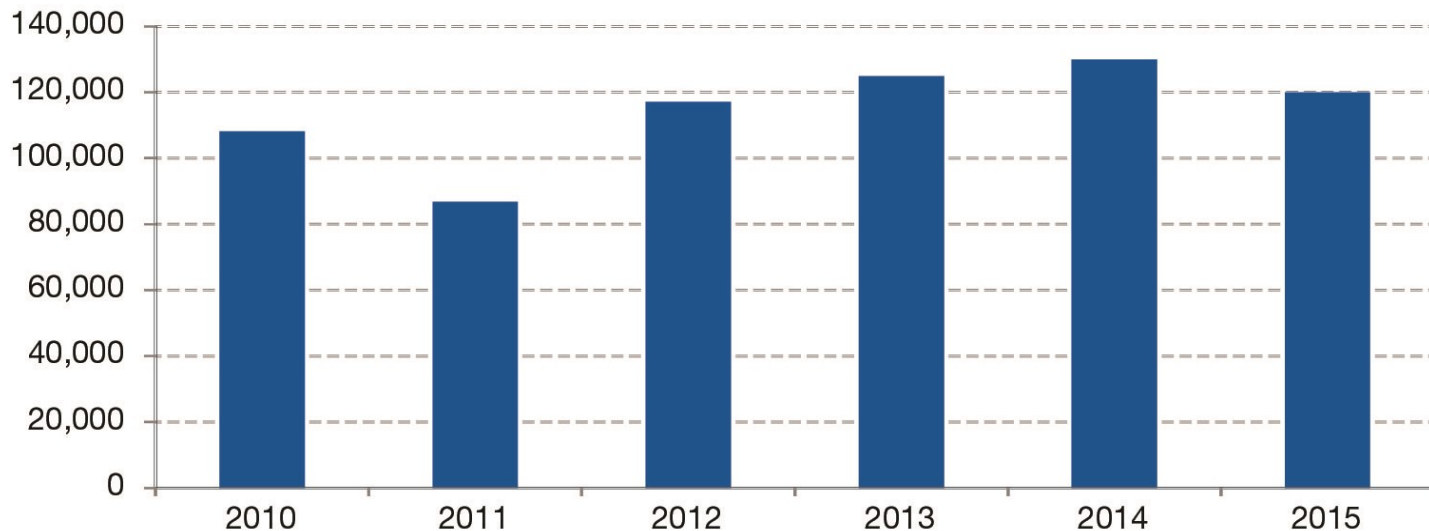


INVESTMENT TRENDS

FDI and MNE Development in ASEAN

- After 3 consecutive years of rapid increase, FDI inflows declined by 8% (from \$130 billion in 2014 to \$120 billion in 2015)

FDI flows in ASEAN, 2010–2015 (Millions of dollars)



Source: ASEAN Secretariat, ASEAN FDI database.

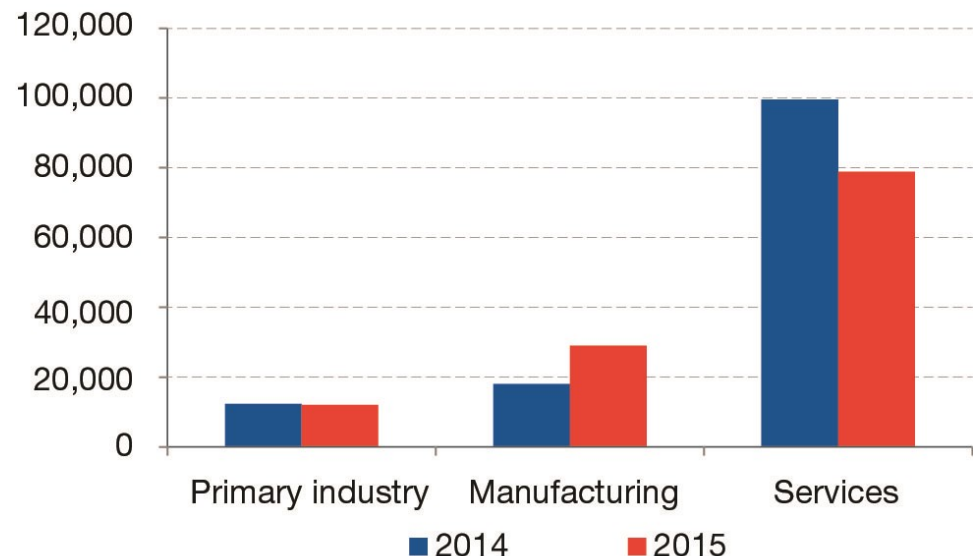
- *But ASEAN remains a significant recipient of FDI flows in 2015 (16% of global FDI flows to developing economies)*

FDI and MNE Development in ASEAN cont.

- The contours of the decline in FDI inflows were reflected in:
 - FDI in Services (primarily Finance)
 - Intracompany Loans
 - Cross-border M&As
 - (Note: Global increase in FDI was mainly because of corporate reconfiguration)
- Nevertheless there were bright spots:

FDI in manufacturing
rose by 61% from \$18
billion to \$29 billion,
And...

FDI in manufacturing rose to \$29 billion

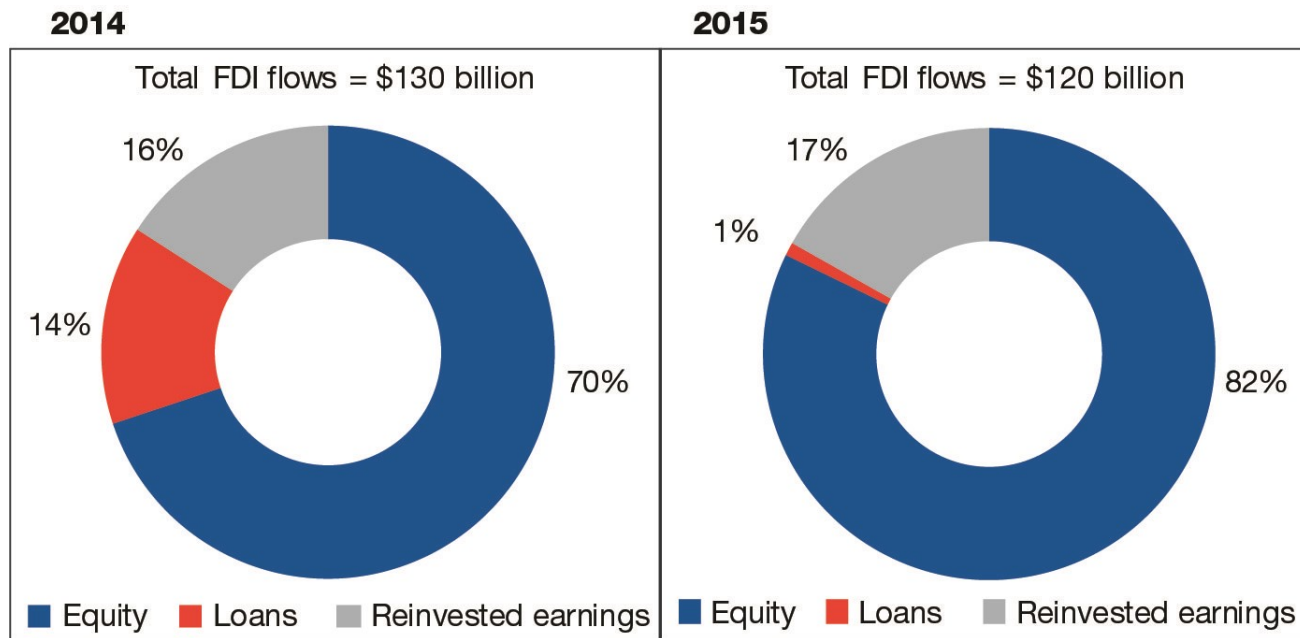


Source: ASEAN Secretariat, ASEAN FDI database.

The Equity Capital Component of FDI was at an all time high..

- At \$96 billion or 82% of all inward FDI in the region

FDI flows in ASEAN, by types of financing sources, 2014 and 2015



Source: ASEAN Secretariat, ASEAN FDI database.

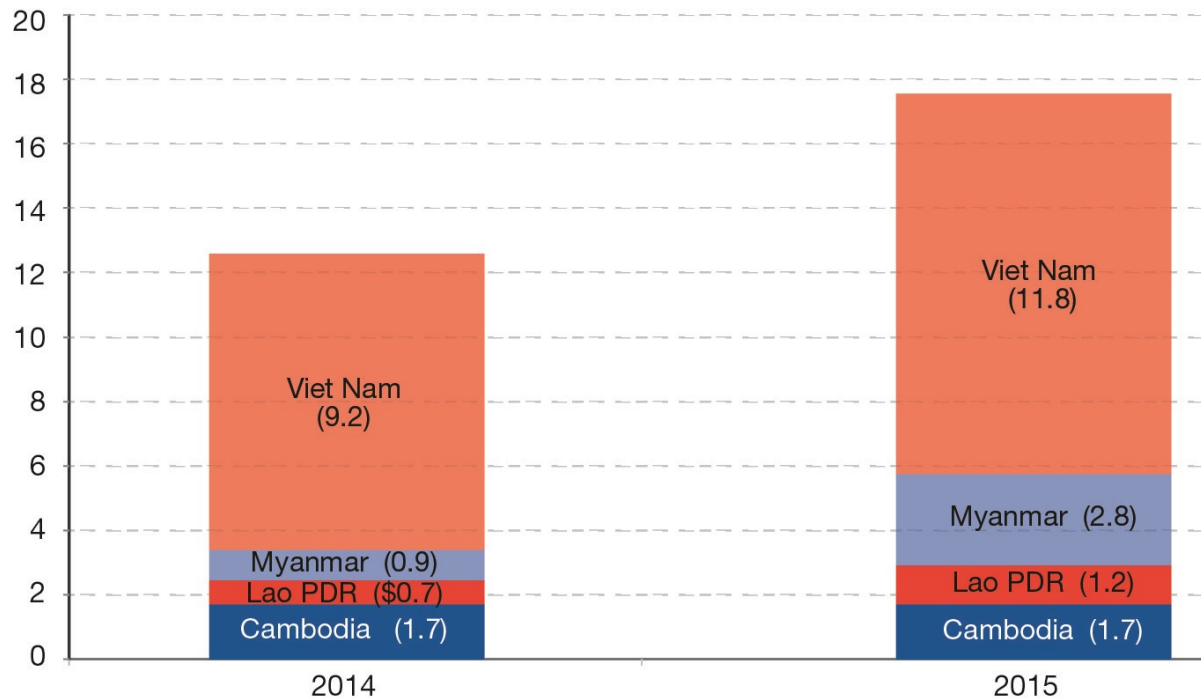
Other Investment developments...

- Intra-ASEAN investment rose marginally to \$22.1 billion
 - In 2015 the intra-regional share of total FDI was 18.5% as compared to 17% the previous year
- MNEs continue to expand their operations in the region
 - As well as across ASEAN, with regionally integrated operations and investments in multiple countries
- FDI from prospective RCEP partners economies rose by 11% to \$40 billion
 - 30% of FDI flows in 2014-2015

Greater attention by investors to CLMV countries...

- Leads to a 38% rise in FDI flows to \$17 billion in 2015
 - 14% of total FDI flows to the region

FDI to CLMV countries, 2015 (Billions of dollars)



Source: ASEAN Secretariat, ASEAN FDI database.

FDI developments in CLMV countries

Cambodia:

- *FDI in finance leads; investment in manufacturing declines*

Lao PDR:

- *Investment in infrastructure continues to dominate, especially in power projects*

Myanmar:

- *Increasing investor interests across all sectors*

Viet Nam:

- *Strong manufacturing investments push up FDI inflows to a new level*

Asian investors continue to dominate the FDI landscape in CLMV countries (ASEAN, China, Republic of Korea and Japan)

Risks and Challenges to the Region

There are risks and challenges to the region, which could impact on corporate activities, investment plans and future FDI flows

- The fragility of the global economy, including macro-economic shocks, remains a concern
- Global FDI flows in 2016 are expected to decline
- Geopolitical tensions in the region increase uncertainty
- Weak economic growth prospects for some major FDI source countries

Modest prospects overall

- The fundamentals of the ASEAN economy remain strong
- AEC-2015 has increased investors' confidence
- ASEAN's regional integration endeavours have strengthened FDI determinants
- Continued efforts by ASEAN members to improve their respective national investment policy environments
- MNEs continue to announce expansion plans, and new investment projects

Against the backdrop of emerging risks and challenges, and cognizant of ASEAN's strengths, FDI flows to the region are likely to remain modest to flat in 2016...

...and still at a high level

CASE STUDIES

KOREAN AND UNITED STATES FDI

AND MNES IN ASEAN

ASEAN is a major destination for Korean FDI

- 16% of Korea's global FDI flows go to ASEAN
- Over 40% of Korean FDI flows to Asia in 2010-2015 went to ASEAN
- Over \$40 billion of Korean outward FDI stock is in ASEAN
- Some 3,770 Korean subsidiaries operate in the region - and the number is growing
- Manufacturing is the primary industry receiving attention by large Korean MNEs and SMEs, followed by services and the primary sector in that order
- There are growing linkages between Korean MNEs and MSMEs in ASEAN

The United States is a major source of FDI in ASEAN

- The largest share of US FDI stock in Asia is in ASEAN (30% of the total)
- US FDI stock in ASEAN rose sharply in the period from 2000 to 2014, from \$50 billion to \$226 billion
 - 20% of FDI stock in ASEAN)
- Over the period 2010-2015, the US was the 4th largest investor in ASEAN (after intra-ASEAN, EU and Japan)
- Over 1,500 US parent companies operate in the region - many with operations in a number of ASEAN countries
- US MNEs continue to expand their regional footprint. Many have substantive sourcing and contract manufacturing activities in ASEAN (including with ASEAN MSMEs)

INTERNATIONALIZATION **by ASEAN MSMEs**

The Significance of ASEAN MSMEs

Micro-, small- and medium-sized enterprises (MSMEs) are important economic actors in ASEAN countries.

They account for the following shares in Member States:

- 88-99% of establishments
- 51-97% of employment
- 23-58% of contribution to GDP
- 10-30% of total exports

ASEAN MSMEs internationalize for various reasons...

...for instance:

- To grow and expand to new markets
- To increase their competitiveness
- To access assets and resources (including skilled labour, raw materials and strategic assets)
- In essence, in most cases to follow a natural development path for their business

...and in principle *their drivers and motivations are similar to those for large firms, namely:*

ASEAN MSMEs are involved in various modes of internationalization

Including:

- Exports (serving overseas markets through international trade)
- Franchising (as franchisees and franchisors)
- Licensing
- Contractors and sub-contractors (e.g. contract manufacturing, contract services, contract farming)
- Foreign direct investment

Contractual or non-equity modes (NEMs)

The report provides detailed case studies, and illustrates many MSME players in each internationalization mode

Factors affecting MSME internationalization

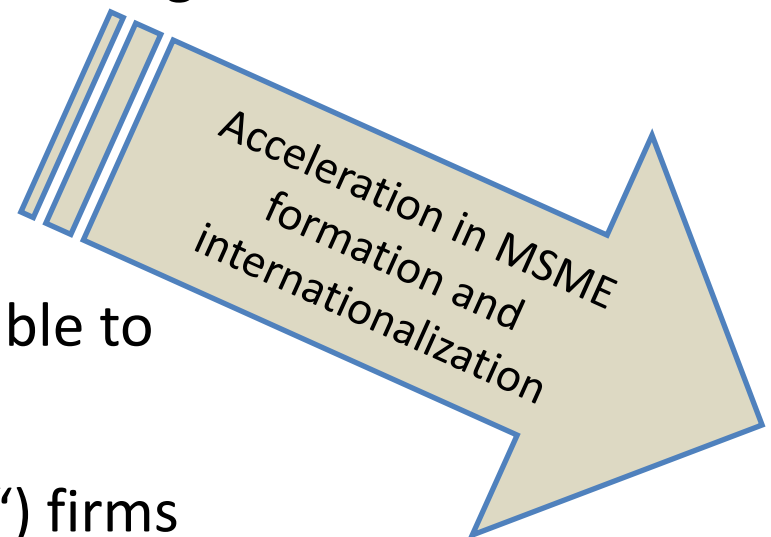
- Factors internal to the firm and founders (vision, leadership, capacity etc.)
- Opportunities come knocking (including MNEs)
- Influence of technology, e-commerce platforms and business models which facilitate internationalization
- The home country and industry ecosystem
- Government policy and support
- Access to finance
- Others

Some MSMEs internationalize faster than others, others are happy (or able) to remain domestic

Types of ASEAN MSMEs international investors

- Firms going through a «traditional» development path:
 - from small to large...
 - spilling into the international arena through..
 - Exports
 - direct investment
- MSMEs internationalizing through linkages with MNEs (contractual modes)
- MSMEs established by women entrepreneurs
- Technology-platform start-ups, able to internationalize rapidly
- "Born global" (or "born regional") firms

These types are not mutually exclusive



ASEAN MSME and MNE International Linkages

1. Supply of inputs to MNEs under contract (e.g. through contract manufacturing)
2. Production network players
 - As “1” above, but more fully integrated as suppliers into MNE production networks, including their regional value chains
3. “Foreign direct investment NEMs”
 - Involves MSME establishing an overseas affiliate in order to better act as a supplier to a MNE’s production network
4. International franchisee to foreign brands (can be in more than one ASEAN countries; another type of FDI NEM)

MNE-SME linkages are common in many industries, including: automotives, electronics, apparel, fast food services, software and ICT, oil and gas services, engineering services, infrastructure

Challenges and considerations to internationalization

- **Should MSMEs internationalize?**
 - *Internationalization provides a way to address/grow MSME and home country competitiveness...*
 - *and home governments can play a critical role*
- **Challenges:**
 - Absence of an international mindset by owners and managers
 - Including concerns about the risks inherent in internationalization
 - Constraints in capability
 - Insufficient experience, lack of technology or skills, inability to meet foreign standards
 - Financial constraints, unwillingness of banks and others to offer loans
 - Lack of knowledge of foreign markets (dearth of information)
 - Government policies (including creating an enabling environment/ecosystem)

Policy options to facilitate MSMEs internationalization

In attracting FDI and further improving the policy framework to facilitate MSME internationalization, ASEAN can consider pursuing policy options (adapted as appropriate) as indicated or illustrated in:

- The UNCTAD Investment Policy Framework for Sustainable Development (IPFSD)
- World Investment Report 2011: Non-Equity Modes of International Production and Development
- World Investment Report 2013: Global Value Chains: Investment and Trade for Development
- And a large number of case studies on best practices, including in AIR 2016 and previous reports by the ASEAN Secretariat and UNCTAD

Some selected potential policy options

- Build domestic capacities to participate in GVCs and RVCs:
 - Policies that support enterprise development
 - Strengthen skills of workforce
- Build domestic capacities for MSMEs involved in NEMs using:
 - Entrepreneurship policy
 - Education policy linked with entrepreneurship development
 - Improve access to finance
- Enhance investment policy framework using measures and action menu suggested in IPFSD



THANK YOU



The report is available at:

<http://investasean.asean.org/index.php/page/view/news-and-events/view/669/newsid/103/asean-investment-report-2016.html>

Or:

http://unctad.org/en/PublicationsLibrary/unctad_asean_air2016d1.pdf

