Emerging Markets Queries in Finance and Business

The foreign direct investments in South-East Asia during the last two decades

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Abstract

Foreign direct investments have played an important role in the economic development of ASEAN states, especially after the 1990’s. However, the two economic crises, from 1997 and 2007, have significantly influenced the investments’ inflows in South-East Asia, each country from the region experiencing a different evolution of the FDI. The purposes of the present paper are to analyse the trends of the ASEAN’s inward FDI between 1990 and present, by identifying the factors that have encouraged or discouraged these flows in the context of the two crises, and to estimate the possible future evolution of these investments. In order to achieve these purposes, we have analysed and interpreted information included in several statistical reports, data-bases and year-books. The conclusions underline that, despite the economic downturns, South-East Asia will continue to attract the investors due to its competitive advantages.

Keywords: South-East Asia; foreign direct investments; economic crisis; reforms;

1. Introduction

The foreign direct investments (FDI) have played an important role in the economic development of the South-East Asia over the last two decades, as a source of capital and technological know-how. These countries have benefited of the foreign direct investments made not only by their neighbors, such as Japan or the newly industrializing economies (like the Chinese Taipei), but they have also attracted investments from the rest of the OECD, notably the United States and Europe. With high economic development achievements during the

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period 1991-1997, the FDI inflows to South-East Asia (ASEAN) have reached about 8% of the global foreign direct investments, being placed among the world’s largest recipients of FDI in the 1990s.

However, the attention of the investors shifted away from South-East Asia after the 1997-1998 regional economic collapse. It was the moment when the international investment patterns have changed dramatically and the FDI flows started to move to developed countries. Therefore, we may notice that during the period 1998-2001, the FDI flows into ASEAN declined sharply, the percentage of the FDI inflows to this region from the global FDI has fallen significantly to 2.76% in 2001 (from 7.85% in 1996). Meanwhile, a significant deterioration of the economic growth could be seen in some ASEAN member countries, in the end of the XXth century. However, the revival of the economic growth after the crisis has not been waited for long, since the exit of the economic reform has boosted the FDI flows into ASEAN. The success of some South-Eastern Asian states in attracting investments during the nowadays global economic downturn demonstrates that the reforms implemented after the Asian crisis have made many ASEAN states much more resistant against the external shocks.

2. Aim, objectives and research methodology

The aim of the present paper is to analyse the evolution of the FDI in South-East Asia since 1990, taking into consideration the two economic downturns that have occurred since then: the 1997 and 2007 crisis.

Considering these aspects, the main objectives of the research are:

• To identify the trend of the FDI in ASEAN between 1990 and 1997;
• To analyse the foreign direct investments in the region after the 1997 crises started, by identifying the factors that have encouraged or discouraged the investors;
• To determine the evolution of these investments’ inflows in the context of the nowadays crisis.

In order to achieve the established objectives, we have collected, tabulated, analysed and interpreted the information included in several statistical reports, data-bases and year-books.

3. Results and discussions

3.1. Foreign direct investments in South-East Asia before 1997

Analyzing the statistical information regarding the evolution of FDI in ASEAN 4 (Malaysia, Indonesia, Thailand and Philippine), we could notice that the region has been a major recipient of foreign direct investments until 1997. However, the amount of the investments attracted by Philippines was smaller than of the other three states. This situation is understandable considering the fact that until the 1990s the country did not generally welcome the foreign investors.

South-East Asia’s success in attracting FDI was mainly as an export platform because, with the exception of Indonesia, the markets were too small to welcome much market-seeking investments, especially Singapore and Malaysia, and, at that time, the regional integration was not sufficient. Despite these drawbacks, the export platform strategy had a great success.

Foreign investors in ASEAN 4 were mainly attracted by those sectors that have registered the fastest export growth. Therefore, the ASEAN 4 members were able to shift quickly towards manufacturing-based countries in which the economic growth was driven by the fast expanding exports. As Thomsen, Otsuka and Lee (2011) have noticed, the region was gradually integrated into the world economy and became a global production platform, with the help of the increasing influx of foreign direct investments into the export-oriented industries. Actually, these large inflows of foreign investments started to become more visible since the end of the 1980s, when companies from Japan and the Newly Industrializing Economies (NIEs) became interested in settling the
production bases abroad, in order to escape from the appreciation of their currencies and from the loss of preferential access to many OECD markets (for the NIEs).

In the Table 1 could be noticed that the ASEAN 4 members have been considered together among the most important destinations for the FDI outside of the OECD area, between 1990 and 1997, being placed on the fifth position. However, they were still situated far behind China.

Table 1. Top 5 according to the total FDI inflows between 1990 and 1997 (in million USD)

<table>
<thead>
<tr>
<th>Country</th>
<th>Value of FDI inflows (million $)</th>
</tr>
</thead>
<tbody>
<tr>
<td>USA</td>
<td>414074</td>
</tr>
<tr>
<td>China</td>
<td>200578</td>
</tr>
<tr>
<td>UK</td>
<td>176889</td>
</tr>
<tr>
<td>France</td>
<td>149587</td>
</tr>
<tr>
<td>ASEAN 4 (Malaysia, Indonesia, Thailand, Philippine)</td>
<td>84417</td>
</tr>
</tbody>
</table>


However, despite the emergence of China after 1991, the ASEAN share of the total stock of FDI in developing countries (excluding tax havens in the Caribbean) has registered a positive trend during the end of the last century, increasing from about 8% in 1986 to more than 20% in 1996 (UNCTAD, 1998).

Until 1997, Singapore remained by far the largest recipient of FDI in the region. Up to the middle of the 1990s, Malaysia had almost 1/4 of the total inflows into ASEAN, while the shares of Indonesia, Thailand and the Philippines remained far below the percentage of Malaysia. According to UNCTAD (1998), in the first half of the 1990s, the net capital inflow relative to gross domestic capital formation represented more than 19% in Malaysia, 30% in Singapore, 10% in the Philippines and 4% in Thailand.

Over the time, the evolution of the foreign investments has been influenced not only by the external conditions but also by the internal environment of the ASEAN countries. The policies implemented in each ASEAN state have largely determined the distribution of these inflows within the region. For example, while Malaysia has shifted the export promotion within the ASEAN 4 into a constant ability to attract investments made by the export-oriented firms, Thailand has attracted both market-seeking and export oriented investors. Meanwhile, most of the Indonesia’s success could be related to the oil and gas sector.

3.2. FDI in South-East Asia between 1997 and 2007

The Asian financial crisis that has started in 1997 has generated a slowdown in the FDI inflows into the ASEAN countries. The worse affected by the crisis seemed to be Malaysia, if we compare the level of the FDI attracted by it immediately after 1997 to the level of the previous two decades and to other major FDI-receiving countries from the region. A possible explanation for this situation could be given by the fact that the Malaysian economy is caught into a “middle-income trap”: it is no longer able to compete with China or other countries that have a low-cost production and, moreover, it lacks the innovative ability and skills to specialize in the high-end tasks in the global production networks of the region (World Bank 2011).

Even if in Indonesia and Thailand the magnitude of the foreign direct investments’ recession was not comparable to that of Malaysia, these two countries were also negatively influenced by the economic and financial downturn. Actually, the decline in the FDI attracted by Malaysia, Thailand and Indonesia could be seen until the end of 2001.
An explanation for the foreign direct investments’ decreasing trend in ASEAN region at the end of the XXth century could be given by the fact that the volume of the FDI, as that of trade, increases together with the GDP and diminishes with the „resistance” posed by geographic and policy barriers. These barriers refer especially to the regulations and institutions, to the education level and to the innovation capability. To all these, another significant element could be added - the distance, which involves costs related to information, communication and corporate control (Eichengreen and Tong 2007).

According to Eichengreen and Tong (2007), another possible explanation for the reduction of the FDI inflows into the ASEAN countries after 1997 could be the fact that a large amount of FDI was attracted by China. However, this argument is largely debated, some other analysts considering that China has actually helped the ASEAN countries, by attracting the investors in the region (Cheong and Plummer, 2009). As Thomsen (2004) has noticed, “FDI is not a zero sum game, with one country gaining at the expense of all others. Investments in China can stimulate greater FDI throughout East Asia, acting like a regional magnet for investors much as Singapore has done within ASEAN” (Thomsen, 2004).

As resulting from the statistical reports, starting with 2003, the ASEAN states were prepared to attract the foreign capital. The FDI inflows to South-East Asia have significantly increased from 17.33 billion U.S. dollars in 2002 to 24.84 billion U.S. dollars in 2003. In 2007, the amount of the FDI has reached a peak of 73.97 billion U.S. dollars, meaning 3.52% of global FDI. With this statistics, the ASEAN countries’ share of the world GDP has regained its pre-crisis position, reaching 2.5% of global GDP.

However, after 2000, it was noticed that most of the investors in the ASEAN region have been attracted especially by Singapore and Thailand, Malaysia continuing to lose ground after the financial crisis from 1997. Indonesia, which has also faced a significant contraction of FDI inflows between 1998 and 2000, has regained the credibility in front of the investors after 2000.

This positive evolution of the investments’ flows was a result of the ASEAN’s reforms in FDI laws and regulations, as they opened further to foreign investments.

3.3. The foreign investments’ evolution in ASEAN after 2007

The global economic crisis from 2007-2008 have hit again the FDI flows into ASEAN, their value dropping sharply from almost 74 billion U.S. dollars in 2007 to 49.49 billion U.S. dollars in 2008 and to 39.62 billion U.S. dollars in 2009. Meanwhile, it can be noticed that, despite the fact that global FDI has fallen from 2100 billion U.S. dollars in 2007 to 1114 billion U.S. dollars in 2009, China and India have still remained very attractive for the foreign investors during this period.

As a result of the different degrees of the external economic dependency and market liberalization within the region, the ASEAN states were uneven influenced by the global crisis. The more an economy was connected to the external demand, the more significant was the loss in terms of the FDI inflows. Considering this aspect, it is easy to understand why the investments attracted by Singapore and Malaysia have sharply decreased. Meanwhile, the relatively large economies, more dependent on the internal demand, like Indonesia, Philippines and Vietnam were less adversely affected. However, no matter the magnitude of the impact, the recovery was very rapid: the severe drop in FDI inflows into ASEAN between 2008 and 2009 was compensated by the recovery that started in 2010, when the total inflows have returned to the level gained in 2007 - the historic peak for their inflows. South-East Asia has seen a big revival of the FDI inflows thanks to the flexible rules, sustained growth and greater political and economic stability. Inflows to the 10 ASEAN countries more than doubled in 2010, when they reached the value of 79 billion USD. This positive trend was led especially by the sharp increases in Indonesia, Singapore, Philippines, Malaysia and Thailand’s inflows (see Table 2).

The same evolution could also be seen in 2011, when the inflows received by South-East Asia were around 92 billion USD, meaning an almost 14% increase, compared to 2010. These good performances of the region were driven again by the sharp increases of the FDI inflows to Indonesia, Malaysia, Singapore and Thailand.
However, some low-income ASEAN states, like Cambodia, the Lao People’s Democratic Republic and Myanmar, had also success in attracting the foreign investments.

Table 2. Distribution of FDI flows among countries, by range*, in 2010

<table>
<thead>
<tr>
<th>Range</th>
<th>Inflows</th>
</tr>
</thead>
<tbody>
<tr>
<td>Above 50 billion UDS</td>
<td>China and Hong-Kong</td>
</tr>
<tr>
<td>10 to 49 billion UDS</td>
<td>Singapore, India, Indonesia</td>
</tr>
<tr>
<td>1 to 9,9 billion UDS</td>
<td>Malaysia, Vietnam, Korea, Thailand, Iran, Macao, Taiwan, Pakistan, Philippines, Mongolia</td>
</tr>
<tr>
<td>0,1 to 0,9 billion UDS</td>
<td>Bangladesh, Cambodia, Myanmar, Brunei, Sri Lanka, Timor-Leste, Maldives, Lao</td>
</tr>
<tr>
<td>Below 0,1 billion UDS</td>
<td>Afghanistan, Nepal, Bhutan</td>
</tr>
</tbody>
</table>

*The countries are listed according to the size of their FDI inflows


An annual survey conducted by UNCTAD in 2012 shows that Indonesia and Thailand started to become preferred by the transnational corporations as host economies, fact which proves that there are strong chances for further increases in FDI inflows to the two countries, in the next years. The statistics show that up to now, the amount invested by the multinational companies from OECD states in ASEAN countries - more than 320 billion USD, overpasses the sum received by China and India considered together. These data demonstrate that ASEAN has a growing role in the global production networks.

Moreover, the ASEAN states are continuing the economic reforms, which also include an improvement in their investment’s environment, being aware of the fact that the FDI could help them sustain the growth. ASEAN member states have already signed the ASEAN Comprehensive Investment Agreement in 2009 and are trying to establish the ASEAN Economic Community by 2015. The purpose of this Community will be to transform ASEAN into an integrated region with free movement of goods, services, investments, skilled labor and freer flows of capital (Hoang, 2012).

4. Conclusions

During time, the evolution of the foreign investments has been influenced not only by the external environment but also by the internal political conditions from each ASEAN country. The statistics show that the ASEAN 4 have been a major destination for the FDI until 1997. The investors from all over the world have considered the region a good location for their production, especially because it had an important role as an export platform.

However, the Asian crisis from 1997-1998 induced a slowdown in the FDI inflows into the ASEAN countries. Malaysia seemed to be the worst affected by the crisis but, looking at the numbers, it could be seen that Indonesia and Thailand have also experienced a decrease in the investments’ inflows. This negative trend of the FDI attracted by the three states did not last for long since the FDI inflows to South-East Asia regained a positive evolution after 2002. The peak of the FDI inflows was reached in 2007, when they totaled 3.52% of the global FDI amount. This ascending trend of the investments’ inflows could be partly explained by the reforms implemented in the ASEAN states, regarding the FDI laws and regulations, meant to open further the economies to the foreign investors.

The global financial and economic downturn from 2007-2008 have hit again the FDI inflows to ASEAN, their value dropping sharply. However, the magnitude of the crisis was not the same for all these countries. Yet,
for all of them, the recovery seemed to be very rapid, since the total inflows into this region have reached, in 2010, the maximum level obtained in 2007.

As shown in various studies conducted on the multinational companies, some of the South-East Asian states started to become preferred by these corporations as host economies, fact that allows us to assume that there are strong chances for further increases in FDI inflows to the region, in the next years. This trend is positively influenced by the economic reforms that the ASEAN states continue to implement, which are focused on improvements in their investments’ environment.

Considering these last aspects, it would be interesting to investigate, in a future research, if these assumptions will prove to be true and if ASEAN will compete with China and, maybe, with the states from the Central and Eastern Europe, for the first place in the top of the most attractive FDI destinations.

References


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