

Global Value Chains (GVCs) Investment Climate Improvement Report

Table of Contents

1. Background
2. APEC past initiatives related to investment
 - (1) Non-Binding Investment Principles (NBIP)
 - (2) Investment Facilitation Action Plan (IFAP)
 - (3) APEC investment strategy
3. Study results summary
 - (1) Roles and characteristics of GVCs in East Asia and Southeast Asia
 - (2) Cooperation between investing companies and local communities
 - (3) Identifying critical factors for private companies/sectors making investment
 - (4) Roles of public sector including foreign investment promotion activities
4. Conclusions
5. Appendix 1: Preliminary Study
 - (1) Economies where global value chain is under development
 - (2) Some of the features related to GVCs in each economy
 - (3) Five key factors for investment decisions
 - (4) Case study of the five critical factors
 - (5) Interviews with private sectors about their investment decision-making process
6. Appendix 2: Past Public-Private Dialogues
 - (1) Malaysia
 - (2) Lima
 - (3) Tokyo

1. Background

In the modern globalized world, economies and companies compete and cooperate against and with each other to grow and provide livelihoods for society. Economies can either utilize globalization and value chains to enhance the rate and level of economic development or ignore current economic trends demanding productivity, efficiency, and ingenuity. Each economy possesses competitive advantages and restrictive factors such as human and financial capital for the development of its economic. In this regard, no economy is truly self-sufficient and most economies have specialized in and engaged Global Value Chains (GVCs) to some level.

GVCs dominate modern day international trade. As GVCs characterize the range of value-adding activities of bringing goods or services through various production phases and final delivery to customers, companies must consider where to better integrate into GVCs, taking into considerations many factors such as infrastructure, institutions, human capital, trade policy, research and development (R&D) and technology, and countless other competitiveness factors.

Geographies with better infrastructure, transportation and telecommunications tend to attract more business activities and global investments, as they enhances overall efficiency for both firms and society to the areas that receive the investment.

Services are also the key to hold GVCs together, playing a critical role in supporting business operations and connectivity abroad. Although a service may not be a core business activity for a production company, the services often drive overall company competitiveness, either conducted in-house or outsourced.

Moreover, Foreign Direct Investment (FDI) is a driver of GVCs and openness to foreign investment enhances global connectivity, provides employment opportunities, increases exports and diversity of local products, brings in different technologies and ways of doing business, and can have a number of other positive spillovers. GVC economists purport that openness to FDI and participation of Multi-National Corporations (MNCs) in developing economies raise the productivity levels of domestic firms. Aside for putting additional pressure on local firms to improve to compete, MNCs deploy skills and technology trainings to raise human capital, bring in advanced capital to generate efficiencies, and connect to their wider global networks to access quality/cheaper intermediate goods and increase exports. GVC economists purport that openness to FDI and participation of MNCs in developing economies raise the productivity levels of domestic firms. Aside for putting additional pressure on local firms to improve to compete, MNCs deploy skills and technology trainings to raise human capital, bring in advanced capital to generate efficiencies, and connect to their wider global networks to access quality/cheaper intermediate goods and increase exports. For instance, MNCs deploy skills and technology trainings to raise human capital, bring in advanced capital to generate efficiencies, and connect to their wider global networks to access quality/cheaper intermediate goods and increase exports. Local companies of the recipient economies start to cooperate with the MNCs and thus improve and innovate on their own. In addition, benefits of GVC connectivity and openness to FDI are expected to trickle down to the population over time to improve basic human capital levels to achieve greater employment opportunities.

In 2014, Asia-Pacific Economic Cooperation (APEC) leaders endorsed the 'APEC Strategic Blueprint for Promoting GVCs Development and Cooperation' (hereinafter referred as 'GVCs Strategic Blueprint') and decided to realize efficient and workable GVCs within and between each of APEC economies. GVCs, as a dominant feature of the global economy, would offer new prospects for growth, competitiveness and job creation for APEC economies at all levels of development. Meanwhile, given the diverse needs and situations of APEC economies participating in global trade networks today, APEC Leaders recognized that an overall policy direction guiding improved cooperation and a more focused GVC evolution is essential to facilitating sustainable, inclusive and balanced growth in the Asia-Pacific region. In this context, APEC Leaders set up principles and 10 work streams for future GVCs undertakings.

So far, APEC members have been intensifying their work in an effective and cooperative manner with remarkable progress as follows.

- i. Addressing trade and investment issues that impact GVCs. (led by the United States)
- ii. APEC GVCs and TiVA(Trade in Value Added) Measurement (co-led by China and the United States)
- iii. Realize the critical role of trade in services within GVCs (led by Australia)
- iv. Enable developing economies to better participate in GVCs (co-led by Indonesia and China)
- v. Assist SMEs to benefit from GVCs (led by Korea)
- vi. Improve the investment climate for GVCs development (led by Japan)
- vii. Adopt effective trade facilitation measures (led by Singapore)
- viii. Enhance resiliency of GVCs (led by Japan)
- ix. Encourage public-private partnerships for GVCs (Encouraged to be undertaken in other work streams)
- x. Strengthen collaboration with other stakeholders on GVCs (led by China)

Japan has become a lead economy for the work-stream sixth; 'Improving the Investment Climate for Global Value Chains Development'. In the GVCs Strategic Blueprint, it is stipulated that 'APEC will help economies 1) implement sound investment strategies which deal with investment applications expeditiously, fairly, and equitably; and 2) facilitate investment through creating and maintaining transparent and sound administration procedures that apply for the lifetime of the investment', taking into account for the existing document related to investment such as the APEC Non-Binding Investment Principles, the APEC Investment Strategy and the APEC Investment Facilitation Action Plan (IFAP).

As the embodiment and implementation for the work-streams, Japan along with co-sponsor economies held related Public Private Dialogues (PPDs) twice in 2016: one was held in Kuala Lumpur in April (supported by Australia) and the other was held in Lima.

The main objective of PPD in Kuala Lumpur was not only to conduct a theoretical overview of GVCs but also to introduce investment promotion measures taken by authorities in South-East Asia. The other PPD in Lima mainly focused on the integration of regional value chains especially that of Asia and Latin America with the Caribbean considering that APEC consists of the trans-Pacific area.

Based on the result of these two PPDs, and the analytical and literature review, the PPD in Tokyo mainly focused on the following matters:

- i. To identify critical factors for private companies/sector to decide investment behaviors in the third economies/area
- ii. To demonstrate how these behaviors contribute to the development of GVCs
- iii. To share good practices and examples of how to match the authorities intention to boost and develop domestic economy with that of the companies' intention

2. APEC past initiatives related to investment

APEC has done various works in investment and GVCs field, among which the main ones are as follows:

(1) Non-Binding Investment Principles(NBIP)

APEC adopted the 'Non-Binding Investment Principles'(NBIP) in Jakarta 1994 and updated it in 2011, emphasizing APEC's underlying approach of open regionalism as well as the importance of promoting domestic environments that are conducive to attract foreign investment, it describes a series of principles and measures that member economies will take. Also, it recognizes that foreign investment contributes to the economic development, the stimulation of growth, the creation of jobs and the flow of technology in Asia-Pacific region, and thus aims to increase investment, including investment in small and medium enterprises, and to develop supporting industries.¹

The principles of NBIP (2011 updated version) that are recognized the critical factor for investment decision making are as follows;

- Transparency
- Consistency of Interpretation and Implementation
- Non-discrimination and National Treatment
- Regulatory Protections
- Investment Incentives
- Performance Requirements
- Expropriation and Compensation
- Transfers and Convertibility
- Settlement of Disputes
- Protection and Enforcement of Rights
- Entry and Sojourn of Personnel
- Avoidance of Double Taxation

¹ APEC Non-Binding Investment Principles
(<http://www.apec.org/Press/News-Releases/2010/~//media/965E37FDA6D848B4A0350D68D2A4BE1C.aspx>)

- Investor Behavior
- Removal of Barriers to Capital Exports

(2) Investment Facilitation Action Plan (IFAP)

Promoting further investment and facilitating cross-border investment flows, APEC leaders agreed in 2007 at Sydney APEC to the development of an 'Investment Facilitation Action Plan' (IFAP). It is critical that governments have investment procedures in place that do not necessarily increase cost or risks of doing business, or constrain business competition. Investment facilitation is governmental action aiming to maximize the effectiveness and efficiency of its administration through all stage of the investment cycle. Transparency, simplicity and predictability are most important principles. Effective investment facilitation can make a significant contribution to the sort of broader investment climate reform efforts widely practiced by APEC member economies.

The main aims of the IFAP are to (i) strengthen regional economic integration, (ii) strengthen the competitiveness and sustainability of economic growth of APEC's member economies, (iii) expand prosperity and employment opportunities in the APEC region, (iv) make further progress toward achievement of the Bogor Goals². And there have been progresses on IFAP Implementation so far. For example, specific actions on e-transparency includes: Viet Nam's online website called "National Business Registration Portal" allows organizations and individuals alike to transact online, including processes as business registration and corresponding issuance of business registration certificates, and makes related information readily available and accessible. Also, the Philippines, with its BOI-One Window Network (BOI-OWN), provides one-stop and one-window service for investment application and registration. Specific actions on reducing investor risk were also implemented, such as: Australia has maintained a mechanism to provide timely and relevant advice of changes in procedures, applicable standards, technical regulations and conformance requirements. Also, Brunei has established timely, secure and effective systems of ownership registration and / or property use rights for land and other forms of property. (Thang, 2017)

(3) APEC investment strategy

The 'APEC Strategy for Investment' set up in 2010 Yokohama APEC aims to promote increased investment flows throughout the APEC region. The Strategy is implemented under the pillars of (i) Advanced Principles and Practices (ii) Facilitation and (iii) Promotion. The activities under this Strategy include analytical studies on investment practices, Investment Facilitation Action Plan (IFAP) follow-up, public-private dialogues on investment, capacity building and information sharing, as well as cooperation with other international organizations.³

² Investment Expert's Group
(<http://www.apec.org/Groups/Committee-on-Trade-and-Investment/Investment-Experts-Group>)

³ Investment Experts' Group
(<http://www.apec.org/Groups/Committee-on-Trade-and-Investment/Investment-Experts-Group>)

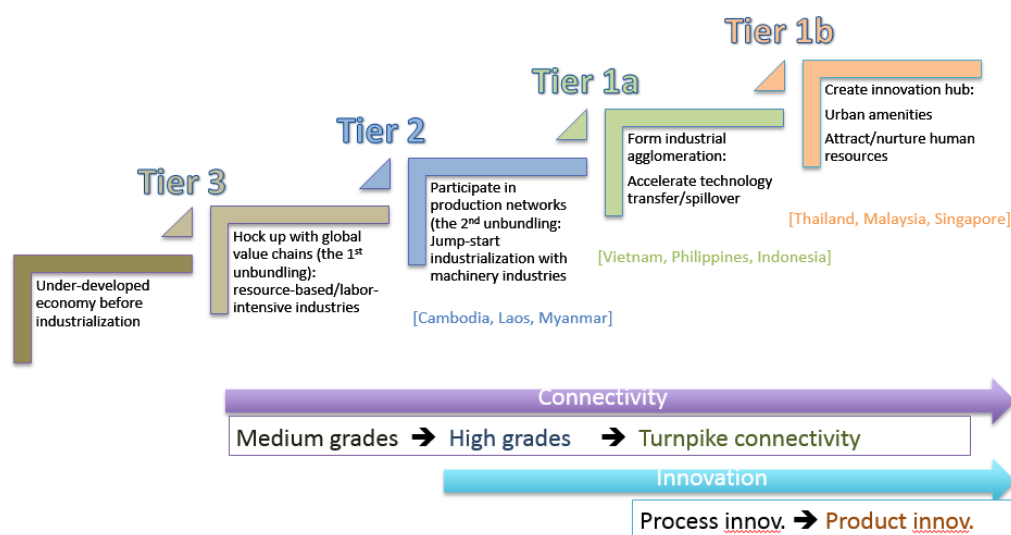
3. Study results summary

A preliminary study including interviews with private sectors, and the three PPD dialogues in Kuala Lumpur, Lima and Tokyo were conducted. Through these works, it is reconfirmed that it is essential to attract foreign investment, in order for developing economies and companies in developing economies to be incorporated into GVCs. The critical factors for private enterprises to make an investment decision as well as the environment that contributes to promoting FDI were identified. Main points are as follows:

(1) Roles and characteristics of GVCs in East Asia and Southeast Asia

GVCs are essential for development strategies in East Asia and Southeast Asia, especially in ASEAN. ASEAN economies proactively take advantage of GVCs, particularly in the manufacturing sector. It is proven by quantitative data that the economic growth driven by manufacturing sector contributes to increasing the employment and eliminating the poverty in developing economies. New business models are also disseminated from machinery to other industries such as services.

GVCs has its various stages; from primitive stage where there are only international division of labor, one where production networks are formed among certain areas, to those in which agglomeration economies are formed through an inflow of human resources from rural to urban areas as well as through innovations. Expanding employment opportunities, upgrading the income level among local communities and improving city infrastructures, the development of GVCs has positive effects on poverty reduction.



Source: ERIA (2015).

(2) Cooperation between investing companies and local communities

Following examples shows how private company, local community and the government in East Asia and Southeast Asia cooperate each other to promote GVCs.

A) The very first public-private partnership project (PPP) between Japan and Viet Nam

"Lakufen International Port Construction Project" is a PPP project between Japan and Viet Nam. Construction of new port facilities started to compensate for the tightening operation of the two major ports, Hai Phong Port and Cai Lan Port, which support Viet Nam's cargo logistics. It is the first PPP project of Japan and Viet Nam, building an international deep-sea port on the Kut Hi island, located in the eastern part of Hai Phong city, as well as improving the surrounding infrastructure. It is considered that the improved infrastructure of ocean freight contributes greatly to future economic development in Viet Nam.⁴

B) Establishment of a technical school by a Japanese private company

Toyota is committed to contributing to the Indian economy through job creation as well as to the Indian automobile industry development. In 2007, "Toyota Industrial Technology School" was established for junior high school graduates who have financial difficulty to acquire the expertise of manufacturing. It is a boarding school and has three years term. In addition to industrial subjects, students can also learn painting, welding, automobile assembly and mechatronics, and join technical internship at TKM. Registration fee and tuition fee are fully covered by TKM. Toyota expects the graduates to become core management in TKM production operations in the future.⁵

C) Provision of educational opportunities by a Japanese private company

Nikon Group established "Nikon Shanti Scholarship System" in 2007 in Thailand, where the company has had a solid business relationship with for many years. For example, a production base of their video related goods is located in Thailand. The scholarship is operated in collaboration with NGOs. A total of 1,542 junior high/ high school and college students with financial difficulty has been offered scholarship over the past 9 years. Is it considered that this charitable activity contributes to the brand awareness and penetration into the local area.⁶

D) Dialogue between authorities and local stakeholders

Malaysia has been building on its existing competitive position as an outsourcing destination for transnational corporations (TNCs) in the electronics, automotive, machinery manufacturing, and oil & gas industries, since 2004. The economy also decided, via dialogue with private sectors, to leverage on its existing strengths to become a key player in the aerospace, medical, defense and photovoltaic industries. These industries are their special focus from 2016 to 2020 to build the strong domestic business ecosystem and reduce the dependence on foreign labor. Malaysia especially recognizes some issues to be addressed, such as inadequate R&D and design investment, lack of mid-level technical expertise, fragmented

⁴ Penta Ocean Construction Co., Ltd., press release (2013)

⁵ Toyota Motor Corporation, Global news room (2010)

⁶ Nikon (Thailand) Co., Ltd., CSR activities (2015)

industry and lack of high-end component manufacturing companies. (Othman, 2017)

E) Investment promotion measures taken by local authorities

Viet Nam is seeking for FDI increase: it has improved the FDI legislations over the years as illustrated in the table below, and currently multinational companies have various investment options, from green field investment to joint ventures with local private companies. The economy has constantly introduced favorable economic treatments to FDI, such as incentives on corporate income tax, import duties exemption and land rental fee exemption. However, it also recognizes that it is of crucial importance to make the legislation operate smoothly in practice and provide foreign companies with more equal treatments, eliminating corruption and unfair competitions. In addition, Viet Nam has been focusing on the following six industries to strength their capability as industry policy: Machineries and metal, Electronics and telecommunication, Textile and foot-wares, Agro-processing, Chemicals, and Renewable and new energies. (Thang, 2017)

	1986-1990	1992	1996	2000	2005	2014
Legal changes	- Law on Foreign Direct Investment (LOFDI)	Amendment of LOFDI	Amendment of LOFDI	Amendment of LOFDI	Unified Law on Investment for domestic & foreign	New Law on Investment
Licensing	-Licensing Authority: State Committee on Cooperation & Investment - Appraisal time: 3 months		- Simplified licensing; Piloting on decentralization - Appraisal time: 2 months	-Introduction of simplified investment registration procedure - Appraisal time: 45 days	- Full decentralization (except BOT, Oil & Gas, Banking, Insurance) - Appraisal time: 15 days and 45 days	- Further decentralization at local level - More projects under the simplified 15 day licensing process
Forms of Investment	- FDI allowed in forms of BCC, joint venture (with state-owned entities) & 100% owned - More incentives given to joint ventures	- Loosen regulations on joint venture (private sector allowed in JVs) - Equal treatments among joint venture and 100% owned - Introduction of BOT form	- Loosen regulations on JV (100 % owned allowed in JVs) - Encourage FDI under BOT form in infrastructure	-Loosen regulations on 100% owned form (allowed in all except 8 sectors e.g toursim, oil mineral, transport) - Introduction of M&A of FDI projects	- FDI allowed in form of jointstock company - Legalization of M&A and shareholding forms	-Detail instruction on M&A fo -Investors are allowed to invest in any business lines that are not prohibited by law (6 prohibited business lines)

(Thang, 2017)

(3) Identifying critical factors for private companies/sectors making investment

As will be detailed in the preliminary study section, the followings are the key factors for private enterprises to make an overseas investment decision

- i. Market (e.g. size, growth potential)
- ii. Value chain infrastructure (e.g. logistics infrastructure such as roads and harbors,

communication infrastructure)

- iii. Institution/ regulation (e.g. taxation and incentive scheme)
- iv. Personnel (e.g. personnel expenses, recruitment)
- v. Country risk (e.g. economy, compliance, geopolitics, natural disasters).

In case of Japanese private enterprises, Hitachi Transportation, first of all, it is critical to collect initial investment in a relatively short period of time. The company has three criteria for its overseas investment evaluation, which are securing and maximizing operating margin, FCF (free cash flow) and NPV (Net present value). Secondly, collaboration with their clients' manufacturers and distributors seems to be a key when conducting overseas investment, since it is hard to acquire customer right after entering the market, when they don't have any experience in local business operations. And for getting local expertise, local partners need to be obtained. Successful collaboration with local partners will bring a good understanding of local regulations and business practices, which will accelerate the market penetration in host economy. It is also essential to consider how to take majority in host economy market, and in order to make that happen, how to strategically approach to the government of recipient country.

In summary, as mentioned in the above case study of Hitachi Transportation, the three overseas investment criteria, which are operating margin, FCF and NPV, needs to be satisfied for private enterprises to invest overseas. Therefore, in addition to the size and growth potential of "(i) market" being a key factor, collaboration with existing clients as well as relationship with local government are also critical factors to promote overseas expansion. Moreover, local (ii) value chain infrastructure needs to be well in place to the extent that MNEs can stably operate their business in the first beginning of their business. The existence and the development of value chain infrastructure such as roads and harbors are, needless to say, the basis for the smooth business operation especially in the developing economies. Furthermore, it was suggested that the existence of local partner is another important key factor for private enterprises, as it is critical to understand the recipient country's local "(iii) institution/regulation". Thus, partnership type of foreign investment, such as joint venture, should be allowed and promoted, for attracting more FDI and forming GVCs.

There are a few more points to consider, which are related to training and compliance. Training local managers to provide local workers with a comfortable work environment is a key as it is sometimes difficult for Japanese administrators to well manage local workers. Education and Training of local workers can also avoid quality issues when the products manufactured in the local factory are exported back into home economy. For providing the education and training, differences in culture and language among the workers need to be taken into considerations. Forming the common ground on compliance makes a business stable; for example, compliance risk associated with local employees, such as theft of delivery goods and cargo by drivers, needs to be considered. The

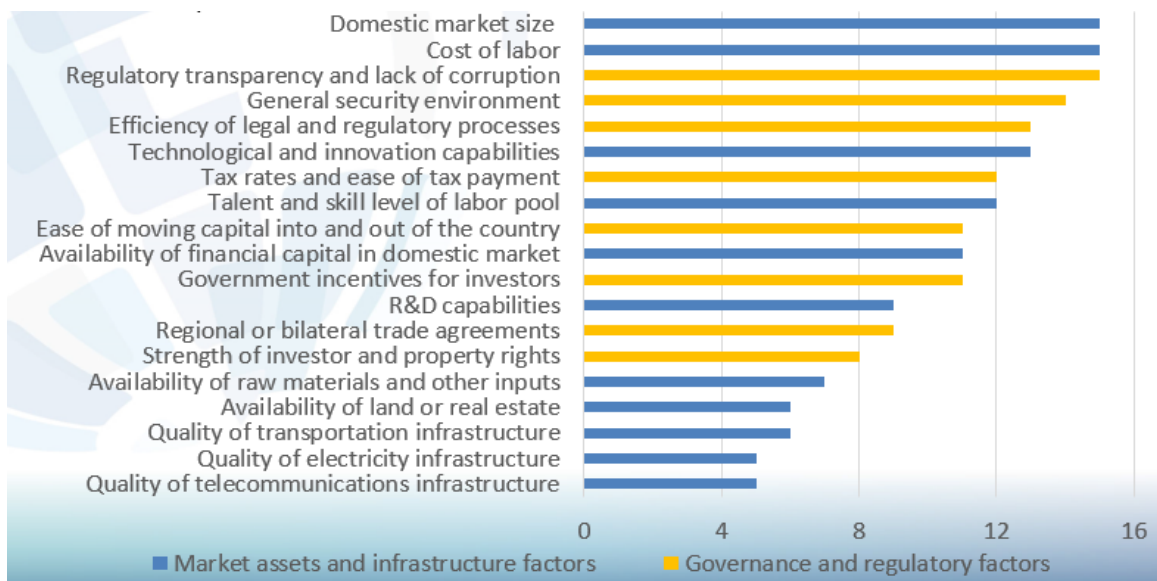
above-mentioned company Nisshin Transportation adopted a certain criteria for hiring employees, which is to hire people who owns house and thus the identity can be traceable. Thus, not only a personnel expenses aspect of (iv) human resources but also (iv) human resources in the context of education as well as (v) country risk such as compliance risk are critical factors to be taken into consideration.

【Reference 1】 Welcoming environment for foreign companies

There are some examples that Japanese companies were fully welcomed by host economy; KDDI, Japanese telecommunication carriers contributed to improving communication infrastructure as well as lowering service pricing by increased competitions. In addition, it seems that host economy appreciates foreign companies for creating employment, providing know-how of operational excellence and technology.

(Natori and Takahashi, 2017)

【Reference 2】 Factors that affect investors’ FDI decisions, 2016. (A.T. Kearney FDI Confidence Index)



(Bayhaqi, 2017)

【Reference 3】 Positive FDI determinants and obstacles in case of Viet Nam

Viet Nam identifies what factors constitute positively and negatively to foreign organizations making investment decisions in their own economy, as follows.

Positive Determinants:

- i. Cheap Labor Cost
- ii. Political Stability
- iii. Market size and Market growth

- iv. Living environments
- v. Strong commitment from central and local governments
- vi. International integration.
- vii. China+1 and Thailand+1

Obstacles:

- i. Increasing labor cost and transaction costs
- ii. Lack of skilled labor
- iii. Complicated administrative procedures
- iv. Underdeveloped infrastructure
- v. Incomplete legislation system (transparent, enforcement)
- vi. Poor suppliers and supporting industry
- vii. Transparency and Corruption
- viii. Poor performance of SMEs and reluctant SOE reform

(Thang, 2017)

(4) Roles of public sector including foreign investment promotion authorities

Attracting foreign investment is indispensable for GVCs to incorporate developing economies' businesses and economies. The volume of the absolute amount of FDI in recent years is increasing, and economic relations and trade relations within the APEC region are deepening.

Public sector support can take the form of creating industrial parks, reliable infrastructure, and vocational training with curricula designed by companies who wish to employ the graduates. Public programs for supplier identification, vendor development, and certification can be conducted in a transparent, competitive fashion, again with selection criteria laid out by firms who will provide purchase contracts to those that qualify.

The lessons for economies seeking to increase FDI are clear. Host authorities have to move beyond improving doing-business indicators to public sector interventions. These public sector interventions that include efficient pro-active investment promotion efforts, backed by infrastructure improvements and public-private partnerships for vocational training. The goal is to attract middle-skill and higher-skill foreign companies to set up affiliates that link the host to the global supply chains of the parents. Host authorities can then turn their attention to vendor-development programs that create backward linkages deep into the local economy. Comparative evidence from around the globe demonstrates that this is an effective route to increasing economic growth and expanding economic welfare for economies that are successful in the endeavor

To maximize benefits from participating in GVCs, most economies will need investments in human

capital, and both hard and soft infrastructure. While there is a great lack in physical infrastructure in many developing economies, the political economy of infrastructure provision points to a bias towards creation of green infrastructure with little emphasis on maintenance, which at the end of the day could be more cost effective or even offer more substantial relief in bottlenecks. Infrastructure that is not only geared towards trade but also towards enabling seamless movement within borders is critical for maximizing spillovers and domestic linkages in GVCs. This is for example, an especially difficult challenge for archipelagic economies like Indonesia and the Philippines. (Source: Australia PPD)

4. Conclusion

- Investment in physical and information technology infrastructure is essential for the development of GVCs, as better infrastructure attracts more private companies investing and doing business activities, in addition to several economic incentives such as taxation relief and subsidization.
- Private enterprises consider maximizing operating margin, free cash flow and NPV (Net Present Value), when making overseas investment. Furthermore, building good relationship with local government is considered as a key to take majority of recipient economy's market. And so do dialogues with local investors and employees.
- Considering that the number of employees in Japan's manufacturing industry has been relatively stable, development of GVCs could not deprive the employment in investing economy's domestic manufacturers.
- Investment promotion authorities serve as an integrated counselling service for public and private sectors. They coordinate the intention of private enterprises, the relevant authorities and ministries to increase FDI inflow and thus promote domestic economies' growth.
- Successful partnership among different economies contributes to the development of GVCs and improves business environment, by attracting high skilled workers and giving incentives to private sector to conduct R&D.
- The benefits of recipient economies for accepting foreign capital entities/companies can be lowered service prices due to increased business competitions, increased number of local employment, advanced operational excellence and transferred technologies.
- Open, transparent and predictable business environment of recipient economy contributes to developing GVCs by attracting foreign direct environment.
- APEC has worked on many initiatives to promote FDI for the formulation Non-Binding Investment Principles (NBIP), Investment Facilitation Action Plan (IFAP) and Bogor Goals etc.,, in order to expand ASEAN regional direct investment. It would be difficult to measure how much those efforts contribute to an increase in FDI and thus it is necessary to look at the quality of overall regulation. ASEAN should also address instable regulatory issues: in some economies, regulations such as foreign capital ratio and labor permission frequently change, which cause difficulty for private enterprises to make or sustain their investment in the economies.

- GVCs contributes to improving the productivity of host economies, and as a ripple effect, various technologies for increasing productivity spread downstream or upstream. In addition, GVCs causes competition within a limited area, resulting in improved efficiency and productivity over the long term.
- GVCs affect not only specific countries and regions but also many parts of the world through supporting industries. With East Asia as a leading model, it is necessary to further share best practices in APEC.
- IEG will continue discussing unsolved investment-related issues going forward, e.g. about institutional aspects of investment.

5. Appendix 1: Preliminary Study

(1) Economies that have increased FDI inflow

Japan External Trade Organization (JETRO) conducted a questionnaire survey of Japanese companies in 2015 about their current and future destinations of overseas expansion. It shows that the three Asian economies, Thailand, Viet Nam and the Philippines, are especially recognized as attractive among Southeast Asian developing countries, for the possible destination of foreign direct investment.

- Questionnaire survey on overseas business development of Japanese company in 2015⁷
 - i. List of locations that Japanese Companies have overseas operation bases⁸:
1st place: China, 2nd place: Thailand, 3rd place: USA, 4th: Chinese Taipei, 5th: Viet Nam
 - ii. Japanese companies' future direction of overseas expansion⁹:
1st place: USA, 2nd place: Viet Nam, 3rd: Mexico, 4th: Philippines, 5th: Australia

In addition, "Ranking of FDI investment destination in developing economies in Asia" also indicated the three economies as follows:

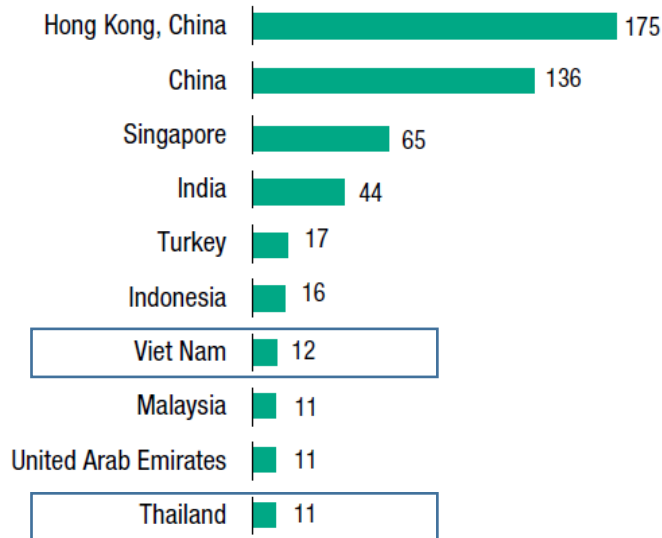
- FDI investment target ranking in Asian developing economies¹⁰
 - i. Top ten economies of FDI investment destination in Asian developing economies in 2015

⁷ JETRO "Questionnaire survey on overseas business development of Japanese company 2015"

⁸ Overseas office locations of 1,469 Japanese companies with overseas bases. Multiple bases in the same country are counted as one base for this particular questionnaire purpose.

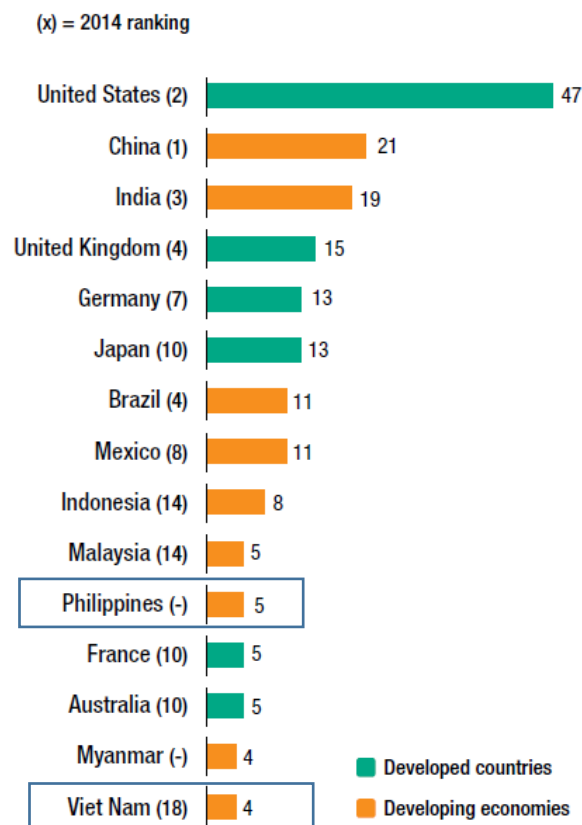
⁹ Overseas destinations of 895 Japanese companies with an intention to expand their overseas business operations in the future (about three year period).

¹⁰ UNCTAD 「World investment report 2016」



Source: ©UNCTAD, FDI/MNE database (www.unctad.org/fdistatistics).

Developing Asia: FDI inflows, top 10 host economies, 2015 (Billions of dollars)
 Future top investment destination economy prediction from 2016 to 2018



Source: ©UNCTAD business survey.

Note: Percentage of respondents selecting a country (each executive was asked to select the three most promising prospective host countries).

MNEs' top prospective host economies for 2016–2018 (Per cent of executives responding)

Therefore, this report especially focuses on those three economies (Thailand, Viet Nam and the Philippines), in order to capture the current situations of the global value chain in East Asia as below.

(2) Some of the features related to GVCs in each economy¹¹

i. Thailand

Thailand has developed a large aggregation of Automobile industry, due to its attractiveness in terms of taxation, industrial infrastructure and the wide base of subcontracting companies. Meanwhile, the diversification trend of supply chain bases have also been observed among the companies that had already advanced to Thailand, establishing factories in neighboring economies, in order to reduce production costs and utilize the AEC (elimination of intra-regional tariffs). In particular, due to the economic growth of the Mekong region, there has been a trend for Thailand's labor-intensive industries, e.g. parts suppliers, to shift a part of the production base to the region. Such a business model launched by Thai government is called "Thailand Plus One". The attractions of Thailand Plus One economies, which are Cambodia, Laos and Myanmar, are (1) inexpensive labor costs, (2) accelerated development of industrial infrastructure, (3) land routes to Thailand (Three Economic Corridors), etc.

ii. Viet Nam

Viet Nam has the third largest population in ASEAN, 8,971 thousand people, following Indonesia and the Philippines. As the capital city Ha Noi has 6,930,000 people and Ho Chi Minh has 7.81 million, the population is concentrated in the two big cities. Regarding international logistics with neighborhood economies, the movement of goods between Viet Nam and other Greater Mekong Subregion 31 economies is mainly operated by maritime transportation, but with ADB's support, road networks connecting GMS economies is under construction. Among them, the 1st East-West Corridor, 2nd East-West Corridor, which is also called Southern Economic Corridor, a Chuetsu Logistics seem very attractive for Japanese companies that entered Viet Nam.

iii. The Philippines

The population exceeded 100 million in 2014 and has the second largest population of ASEAN economies after Indonesia. The population of Manila metropolitan area is estimated 32 million people. The average age of the citizens is 24 years, and it is one of the characteristics of this economy that there are many young people. English is often used in business as the economy has the third largest English speaker population in the world. In recent years, the economy has become popular as business process outsourcing (BPO), especially for call center base for European and American companies and in 2012 ranked the world's No. 1 call center base. Also, the economy has a large number of migrant workers overseas, and the amount of transactions

¹¹ Mitsubishi UFJ Group (MUFG) "Trend of Japanese Companies in ASEAN" (2016)

¹¹ Tohatsu Quarterly Magazine "Business Risks" (2015)

they remittance to the Philippines extends to nearly 10% of GDP.

(3) Case study of private companies making investment decisions

Looking at examples where private enterprises decided to expand/invest overseas, factors that seem to have a significant influence on the decision-making process were identified as follows:

[Case 1] Example of “value chain infrastructure” being a key factor

According to the questionnaire comparing business environment of Thailand, India, Indonesia, China and Viet Nam, the five economies of which are especially popular among Japanese companies, Thailand ranked top in terms of infrastructure. It is concluded that the well-developed infrastructure makes it easier for private companies to enter into Thailand: there are highways developed nationwide, seven international airports, the Bangkok Skytrain (BTS), the Bangkok Metro (MRT), which is a subway, and six deep sea ports such as Laem Chabang Port in place. Electricity supply to the industrial estate is also stable. Also, the economy has been actively promoting the development of international transportation infrastructure network, with main focus on the three economic corridors as well as a new railroad crossing from Laos to Bangkok. 【Thailand】¹²

[Case 2] Example of “institution/regulation” being a key factor

In January 2015, the Board of Investment of Thailand (BOI) introduced New Investment Promotion Scheme, and the system changed from traditional zone system to industry-based benefits system, in which some specific industries recognized as high value added or innovative get more economic benefits such as corporate tax exemption and machine import tax exemption¹³. Following this, Thailand Toyota Motors, President Keiichi Tanada, strategically chose Thailand as a production base for HV (Hybrid Vehicle), out of many other potential locations in Southeast Asia, and expressed an intention to develop advanced technology there in the future. 【Thailand】¹⁴

[Case 3] Example of “market” and “institution/ regulation” being a key factor

In Viet Nam, there was deregulation of Foreign Investment, enforced in January 2009. Following this, it became possible also for multinational wholesale and trading companies, not only manufacturing companies, to enter into the market with 100% foreign capital. In response to this, Aeon opened its first

¹² Mitsubishi UFJ Research and Consulting “Current situation of Thai economy and future prospect” (2016)

¹² Tohatsu Quarterly Magazine “Business Risks” (2015)

¹³ The traditional investment incentive system was a system covering most industrial sectors by adopting a zone system that divides Thailand into three zones and gives more benefits to areas far from Bangkok. However the new investment incentive system abolishes the zone system and adopts “industry-based benefits”, in which some specific industries recognized as high value added or innovative get more economic benefits.

¹⁴ JIJI News Bulletin Asia “Thailand to become “eco car” production base. Top Japanese companies talks with prime minister Prayud” (2016)

¹⁴ BTMU Global Business Insight –Asia & Oceania- (2015)

store, a large one with 130 tenants, in 2014, at the Cledon City district, a region under rapid development. The company plans to actively open new stores in the Asian region, to take advantage of the rapidly growing middle income group with economic growth and sets the goal to increase overseas sales to the same scale as in Japan by 2020. 【Viet Nam】¹⁵

[Case 4] Example of “institution/ regulation” and “human resources” being a key factor

Government Investment Promotion Organization, The Philippine Economic Zone Office (PEZA, enforced in 1995), actively attempts to attract foreign investors and generates the employment, giving the multinational companies registered to the institution with incentives such as reducing corporate income taxes. Also PEZA issue special visa and simplifies import and export procedures to promote more investment from overseas. Epson, a Japanese electronics company, for example, produces most of its own consumer products in the Philippines, because it finds the PEZA's incentive schemes useful, such as their prompt approval and corporate/ VAT tax exemption. Another reason is that young talent is plenty available and that the rate of wage increase is relatively moderate. 【The Philippines】¹⁶

[Case 5] Example of “country risk” being a key factor

According to Manila Times, in the Philippines, there is a decelerating trend in FDI inflows. The Bureau of Statistics indicates that the total amount of FDI applications to seven investment institutions in the July-September period of 2016 was 26.7 billion peso, a decrease of 45% from the same period last year. It is reported that the main reasons are the following two political factors: 1) US economic policy change by the leadership transition, 2) potential risk in the Philippines associated with President remarks and security policy. 【The Philippines】¹⁷

In short, the above-mentioned cases one to five are summarized as below, in connection to the five factors.

¹⁵ Yomiuri Shimbun “Domestic demand type of business” going to Asian market with Japanese domestic market shrink (2012)

¹⁶ The Sanyo Shimbun “Philippine Economy Leaps Forward: OIBA Inspectorate Group Reports Special Zones” (2016)

¹⁷ Sankei Digital “Direct investment into the Philippines halved last July to September, with the new US economic policy” (2017)

	①Market	②Valuechain Infra	③Institution/ Regulation	④Human Resources	⑤Country Risk
Case1		○			
Case2			○		
Case3	○		○		
Case4			○	○	
Case5					○

(4) Five key factors for investment decision

After collecting and analyzing 25 reports and 35 case examples, including the above-mentioned five cases, where private enterprises advanced into emerging economies, the followings were identified as crucial factors in overseas investment decision making of the private sectors¹⁸:

- (i) Market (e.g. size, growth potential)
- (ii) Value chain infrastructure (e.g. logistics infrastructure such as roads and harbors, communication infrastructure)
- (iii) Institution/regulation (e.g. taxation and incentive scheme)
- (iv) Personnel (e.g. personnel expenses, recruitment),
- (v) Country risk (e.g. economy, compliance, geopolitics, natural disasters).

(5) Interviews with private sectors about their investment decision-making process

Interviews with private companies were conducted, focusing on Japanese global logistics service companies. Logistics service enterprises are often positioned as important partner in manufacturing and distribution businesses when expanding overseas, mainly into emerging economies, and thus play a core role in the global value chain construction. Therefore, it is considered that logistics service companies has comprehensive understanding of, not only the expansion strategy of manufacturing and distribution businesses, but also the environment and issues of host economies such as value chain infrastructure, institution/law regulation, human resources, economy risk, etc., when forming the global value chain.

A) Interview 1: Hitachi Transport System Co., Ltd.

An important factor that promotes overseas expansion and investment is collaboration with manufacturing industry and distribution retailing industry, etc. The detail of the interviews

¹⁸ Japan External Trade Organization(JETRO), "World Trade Investment Report" (2016)

¹⁸ Mitsubishi UFJ Group (MUFG) "Trend of Japanese Companies in ASEAN" (2016)

¹⁸ Japan Bank for International Cooperation (JBIC) "Investment Environment Reports - Thailand" (2012), "Investment Environment Reports - Viet Nam" (2014), "Investment Environment Reports – The Philippines" (2013)

¹⁸ Tohatsu Quarterly Magazine "Business Risks" (2015)

is as follows regarding the companies to make the decision of investment.

- i. Together with partners and clients
 - Usually the company goes into a new market in accordance with existing partners' strategy, rather than investing first alone
 - It is an important key factor whether suppliers including small- and medium-sized enterprises follow manufacturing industry and invest overseas together
- ii. Institutional benefits
 - From the viewpoint of manufacturing industry, there are cases in which preferential treatment system such as PEZA in the Philippines, triggers them to advance into a new economy.
- iii. Overseas Investment Criteria
 - The decision-making criteria of the company for overseas expansion and investment are similar to the approach of starting a new business, which is mainly business growth potential and ROI.

B) Interview 2: Nisshin Transport Co., Ltd.

Together with private enterprises in the apparel industry, Nisshin Transport has actively expanded into overseas. Based on the experience, the key points of overseas expansion are summarized into the following three:

- i. Presence of local partners

Established a joint venture with a local company who has a strong relation with the support of authority.. Ownership ratio: Nisshin: 55%, Royal Nay Nan Taw Business Group: 40%, AIS Inc.: 5%. Collaboration with local partners is indispensable to understand local regulations and business practices.
- ii. Education of local workers

As it is difficult for Japanese administrators to well manage local workers, training local managers to provide local workers with a comfortable work environment is a key. Compliance risk associated with local employees, such as theft of delivery goods and cargo by drivers, also needs to be considered. Adopting some legit criteria for hiring employees is crucial to avoid those risks, e.g. people who owns house and thus the identity can be traceable. Education and Training and of local workers is another key to ensure the quality required by end customers, because quality problems often occurs at the beginning of market entry.
- iii. Together with partners and clients

Going into a new market together with existing or prospect customers/ partners is a key, as it is hard to acquire customers/ partners right after entering the market without any local business operation experiences.

C) Interview 3: Sankyu Ink.

Overseas expansion are often proposed by customers mainly in the manufacturing industry. The company usually judges whether to go overseas after reviewing ROI of the business. As such, supporting overseas expansion of manufacturing companies, there has been some trends observed as follows:

i. The trend of private enterprises going to Myanmar market

Most recently, there has been many requests on entering Myanmar and other emerging economies, mainly by trading company customers.

ii. The needs of manufacturing industry

"Finance service × Logistics service", in which logistics companies purchase inventory and supply goods "just in time", are in demand, when supplying products to the manufacturing industry.

iii. Value chain infrastructure

When examining overseas expansion into emerging economies, the status of communication infrastructure development is an important key factor in addition to traditional infrastructure such as roads, ports and airports.

6. Appendix 2: Past Public-Private Dialogues

(1) Malaysia

- As GVCs now account for a significant share of world trade in clothing and textiles, food products, chemicals, machinery and equipment, the opportunities have been presented to add value in different stages of production in different locations enlarges the set of possible contributions to economic growth and development. To better take advantage of such opportunities in Southeast Asia, a Public-Private Dialogue on Improving the Investment Climate for Global Value Chain Development was convened in Kuala Lumpur, Malaysia, on 28-29 April 2016.
- Overview of the role of foreign investment and desirable investment climate for establishing of GVCs. Four recommendations for improving GVC's investment climate: Heavy-handed industrial policies, such as local content, joint venture, or export requirements, have been found to generally be ineffective or counterproductive. A lighter policy framework offering national treatment for investors will do more to nurture value chain development. Recommendations for improving the investment climate for GVCs can be grouped under four I's of infrastructure, institutions, incentives, and implementation.

A) Infrastructure

Reliable and efficient transportation and communication services are particularly important for connecting and coordinating the different links in global value chains. Reasonably priced and dependable power supplies are essential for producing most goods competitively. Water and

sanitation may also be important. All of these services require hard (physical) infrastructure, without which attracting and retaining investment will be difficult.

Soft (institutional) infrastructure should be developed as a complement to physical infrastructure, and increasingly so after physical infrastructure services become readily available. Information plays a central role in soft infrastructure, and certainty of the information helps to reduce risks.

Transport, storage, port facilities, ICT (for information and coordination), and support sectors (electricity, finance, etc.) infrastructure are needed for efficient value chain development. Urban infrastructure to facilitate economic activity and supply health, water, power, education, and housing is becoming increasingly necessary as the region urbanizes and seeks to retain investment and develop the benefits of agglomeration. The key actors that can ensure the availability of these infrastructures are the government – which can directly provide and manage infrastructure or set the environment and regulations for participation of the private sector for their provision and management – and the private sector, through private public partnerships.

B) Institutions

Institutions or “rules of the game” and related organizational structures are an essential part of the economic and investment climate. Institutional structures include: (a) Regulations and support for fulfilling regulatory requirements such as customs procedures; (b) International agreements; (c) Competition forms and policies; and (d) Cooperation (including international cooperation in the case of GVCs). The quality of institutions is paramount. Regulations should be clear, consistent, and implemented and enforced in order to reduce regulatory uncertainty.

Trade facilitation most often aims at improving border clearance procedures. At the same time, predictable legal rights and procedures, enforceable and equitable competition policy, and a sound regulatory framework are equally important. Long term, local currency bond markets that can support investment in general, and infrastructure investment in particular, should be developed.

C) Incentives

Incentives may be general and economy-wide or strategic and specific for firms participating in GVC development. Consideration may be given to incentives for investment, for employment objectives, to promote linkages, or to support risk taking or risk mitigation. Planning incentive structures should consider the likely impacts on investment retention and externalities, as well as attraction.

D) Implementation

Announcements of policy changes to improve the investment climate are common. However,

greater efforts are needed in is following through with policy implementation for investment climate improvement. This may involve capacity building activities (particularly for SMEs or government officials involved in managing GVC development). It also involves ensuring that infrastructure construction is followed by essential maintenance (politicians are often happy to announce the former but not to ensure financing for the latter).

(Source: Australia PPD¹⁹)

(2) Lima

- The purpose of this PPD was to delve into the dynamics of both Asian and Latin American value chains, the status quo of value chain development between the two regions, and what can be done to enhance the trade and investment relationship between the two regions. The PPD represents the interest in strengthening GVC connectivity between the two regions for mutually beneficial growth and development.
- Overview of GVCs in Asia and Latin America and the possibility of establish GVCs among regions will be discussed.

Elements to be improved and their potential for establishing GVCs in Asia and Latin America: The hope is that Latin American companies and economies can learn from Asia's experience building GVCs over the past thirty years as well as connecting to Asian companies and investments to fuel Latin industrialization. Moreover, the PPD highlighted some of the attractive opportunities in Latin America and strategies that could be applied to increasingly engage the region with incredible potential. Although there are no firm conclusions on how to better connect the two regions as there is no "silver bullet" to improve GVC incorporation, the PPD was successful in furthering the PPD between Latina and Asian stakeholders for future progress. The recommendations in the following section which include both high level and specific recommendations are based off of the extensive literature review conducted for this study, interviews with a diversity of professionals from six APEC economies, as well as the inputs from expert stakeholders from the PPD.

The points to be improved are summarized for each item to establish GVCs in Asia and Latin America as follows:

A) Infrastructure improvements

High-quality infrastructures is even more important when trying to do business between Asia and Latin America. The sheer distance across the Pacific or overland already incurs expensive logistics costs and challenges connecting with counterparts in differing time zones. Time constraints and additional and unforeseen costs will discourage increasing and sustainable trade and investment. As such, each economy, both in Asia and Latin America, should look to improve the supply of all types of infrastructure to efficiently engage GVCs.

¹⁹ <http://mams.rmit.edu.au/klnk5ekl756a1.pdf>

B) Trade cost reductions and trade facilitation

Asian and Latin America economies looking to better integrate into GVCs should pursue open trade regimes that allow for the efficient and manageable flow of goods, especially those commodities and intermediate goods that are utilized for adding value and support comparative advantage industries.

C) Transparent and consistent rules and regulations

Transparent rules and regulations inform businesses on what they need to be aware of and comply with when operating in an economy. This is incredibly important for FDI as foreign investors are not necessarily fully informed on the business regulatory environment, legal systems, and cultural sensitivities of diverse economies.

D) Continuous upgrading of education opportunities

Educational initiatives, especially those geared towards developing a work-ready population, support business growth and a company's ability to engage GVCs. Evidence supports that economies with superior educational attainment have higher per capita GDPs, standards of living, and GVC integration. This is evidenced in both Asian and Latin American economies where there are also numerous programs aimed at developing talent for a specific industry has led to successful growth.

E) Access to finance

Access to finance, whether it be through trade finance, project financing, SME finance, etc. is incredibly important to support local business development, upgrading, and international connectivity. As such, public sectors should cooperate with both public and private banking institutions to supply the capital necessary to grow industry while also putting the systems in place to regulate, enforce, and control excess borrowing.

F) Openness to FDI

Aside for being open to FDI, economies should actively pursue FDI into priority industries that demand additional capital and/or expertise. FDI also enhances direct linkages to other economies. As foreign companies and workers enter new markets, they get to know the investment economy, positive and negative qualities, and an appreciation for local culture. This provides an additional opportunity for local companies to link with the FDI business and potentially instigate exports or obtain higher quality/competitive pricing of products through the new connection.

(Source: LAC PPD²⁰)

²⁰ <https://aimp2.apec.org/sites/PDB/Lists/Proposals/DispForm.aspx?ID=1662>

(3) Tokyo

■ The PPD in Tokyo mainly focus on the following matters:

- To identify critical factors for private companies/sectors to decide investment behaviors in the third countries/area
- To demonstrate how these behaviors contribute to the development of GVCs
- To share the good practices and examples how to match the authorities intention to boost and develop domestic economy and that of the companies' intention

A) Current Situation of Global Value Chains in East Asia

There are various stages in GVCs; for example in ASEAN and China it is not just a production network, but it is in the stage of agglomeration economies. With respect to TPP, it contributes to the development of GVCs from the perspective of improving the business environment in a broader sense that attracts talents and gives incentives to conduct R&D. Services are particularly important for the development of GVCs, and government procurement and e-commerce are also important fields of investment. Despite Japanese companies advancing international division of labor through construction of GVCs, the number of employees in Japanese manufacturing industry has been relatively stable. Good division of labor has been carried out. There is a background that protectionist sentiment is relatively few in Japan. (Kimura, 2017) There are cases where Japanese companies that have advanced to Australia have deployed to the ASEAN market using Australia's FTAs signed with ASEAN economies. (Ogge-Cowan, 2017)

GVCs have various stages, from a stage where there are only international division of labor, one where production networks are formed, to those in which accumulated economies are formed through an inflow of human resources from rural to urban areas as well as through innovations. The development of GVCs has positive effects on not only city development itself but also poverty reduction. Despite Japanese companies advancing international division of labor through construction of GVCs, the number of employees in Japanese manufacturing industry is relatively stable. Good division of labor is being carried out. There is a background that protectionist sentiment is relatively few in Japan. (Kimura, 2017)

B) Identifying critical factors for private companies/sectors making investment

Logistics companies provide Japanese-style services; just in time, freezing/refrigerating technology, etc., even locally, as customers, especially Japanese companies, expand overseas and develop businesses. From the viewpoints of sales margin, prospect for profitability and expansion of present value etc., each investment is judged respectively.

The demand of private sector for the host government is to admit a share of over 50% held by foreign capital, and to relax and abolish restrictions on various regulations. For logistics enterprises, it would be particularly road infrastructure development, unified operation of HS

codes, elimination of baggage transshipment at country borders and countermeasures for traffic jam.

As for incentives to encourage recipient economy to expand the market in the service field, Japanese companies will be evaluated from partner economies such as expanding employment, providing Japanese service (operational excellence), introducing new technologies. (Natori and Takahashi, 2017)

C) Investment Climate which contributes to promote foreign direct investment

In comparison between APEC Non-binding Investment Principles (NBIP) and the investment principles of G20 and other investment agreements, issues included in NBIP such as transparency and consistency are generally taken up by the G20 investment principle as well. There was also a movement to conclude a binding multilateral investment agreement in OECD in the past as a circumstance surrounding the investment treaty, but due to negotiations having been abandoned and abandoned, now the bilateral investment agreement is mainstream. There, capital exporting countries such as Japan and the United States tend to protect investors, while capital importing countries, mainly developing countries, tend to protect state authorities. In such a situation, APEC's content of NBIP sees with concern whether investor protection is unbiased in such circumstances.

As a way of utilizing the characteristics of APEC, there seems to be a way to freely debate using APEC's unconstrained nature. While Bogor's goal represents freedom of trade and investment, it is not easy to measure the impact of investment and that the overall quality of regulation is examined.

The APEC Investment Experts' Meeting (IEG) is a framework in which the stakeholders of investment agencies of each economy are present. Although business personnel are not present, it is still beneficial to take up the issue in the same framework. (Bayhaqi, 2017)

D) Attracting foreign direct investment which contributes to the development of GVCs

About 10 years ago, the authority to approve investment was transferred from the central government to the local government/ province. As a result, competition between the provinces has become fierce in attracting investment, and each has developed its own measures. The central government has not focused on any sectors to give special incentive for. (Thang, 2017)