6. Towards a Strong Services Sector and An Open Investment Environment in ASEAN

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Towards An Open Services and Open Investment Environment in ASEAN

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Abstract

The investment and services sectors in the Association of Southeast Asian Nations (ASEAN) towards 2040 will see major differences compared with the trade in services and investment in the region in 2018. The services sector will see a major transformation towards meeting new trends and the use of digital technology as the mode of delivery. Changes in the services sector, coupled with the economic dynamics in ASEAN, will also change the investment approach in the region. The economic development of newer ASEAN Member States (AMS) and increased intra-ASEAN investments may cause changes in investment policies. The policies of AMS may also move away from focusing on natural resources-based investment towards efficiency seeking and strategic assets investments. To move up the global value chain and the income level, ASEAN must increase the contribution of the services sector to the economy of AMS, including services contributing towards manufacturing.

Key Words: **Investment, Services, Megatrends, Global Value Chain, Linkages, Liberalisation**

1. Introduction

The Association of Southeast Asian Nations (ASEAN) Member States (AMS) have always been important destinations for foreign direct investment (FDI) in Asia and the Pacific. Despite economic difficulties in many parts of the world, such as the financial crisis in Europe and the United States (US), ASEAN continues to receive FDI and to invest in other countries in the form of outward FDI. The success of ASEAN in attracting FDI makes it the envy of other regions (Organisation for Economic Co-operation and Development (OECD), 2018). Reasons for the continued interest of investors include the availability of resources for export-oriented efficiency-seeking investment; export-oriented manufacturing-based investments; and market-seeking investments, as ASEAN has a large population of about 625 million people with about 100 million middle class (OECD, 2014).[1]

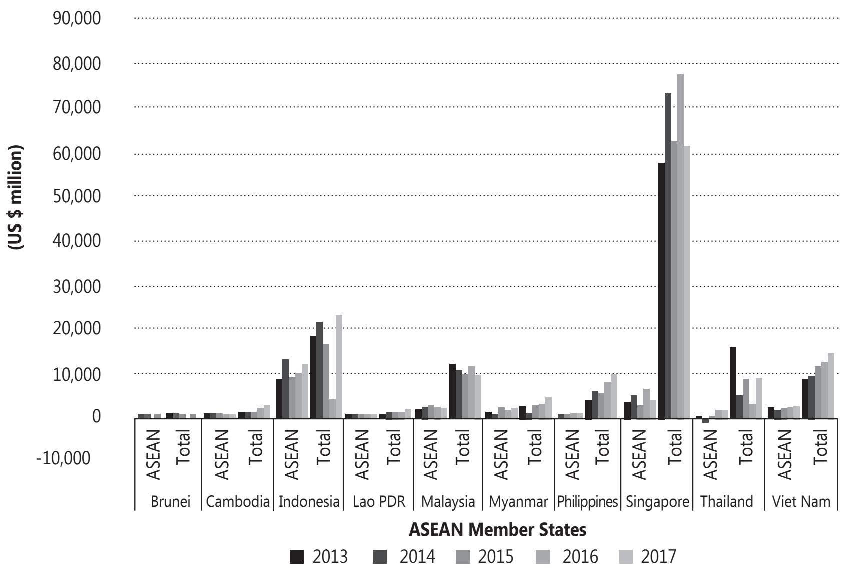
In turning ASEAN into a single production base, connected to the world through Global ASEAN under the ASEAN Vision 2025 Forging Ahead Together (ASEAN, 2015), ASEAN has to focus on quality and sustainable FDI. In addition, to move up the global value chain (GVC) and the income level, ASEAN must increase the contribution of the services sector to the economy of AMS, including services contributing towards manufacturing. This chapter addresses measures that AMS may undertake to achieve the objective of attracting more FDI and increasing the contribution of the services sector to the economy of ASEAN. It discusses the current FDI and services contribution to AMS, and the challenges faced to attract more FDI in the main and service sectors. The chapter will refer to the main ASEAN documents in investment and services: the ASEAN Comprehensive Investment Agreement (ACIA) and the ASEAN Framework Agreement on Services (AFAS). The AMS are currently negotiating the ASEAN Trade in Services Agreement (ATISA) as an improvement to the AFAS. The chapter will then address the megatrends which may affect the service sectors leading up to 2040. In conclusion, it proposes several policy measures for ASEAN to consider undertaking towards 2040.

[1] For an analysis of the ASEAN Comprehensive Investment Agreement (ACIA) and its role in ASEAN investments, see Chaisse and Jusoh (2016).

2. Existing FDI and Services Sectors in ASEAN

FDI is important to AMS as it brings the advantages of advanced technology, management practices, and assured markets. FDI also contributes to gross domestic product (GDP) growth, foreign exchange earnings, employment creation, and increases in incomes, especially of skilled and semi-skilled workers in these industries. In analysing investments, one should refer to both investments in the main sectors (e.g. manufacturing and mining) and the services sector (e.g. financial services, professional services, and accounting).

Figure 1: FDI Inflow into ASEAN, 2013–2017 (in US$ million)



FDI = foreign direct investment, ASEAN = Association of Southeast Asian Nations, Lao PDR = Lao People's Democratic Republic.

Source: ASEANstats, Flows of Inward Foreign Direct Investment (FDI), https://data.aseanstats.org/fdi-by-hosts-and-sources (accessed 15 December 2018).

Total FDI inflow to ASEAN grew from $121.75 billion in 2013 to $137 billion in 2017 (Figure 1). More than half of the FDI inflow goes to Singapore, mainly to financial services, high technology services, and manufacturing. At the end of 2017, FDI inflow to Viet Nam surpassed that of the more traditional FDI destinations in ASEAN such as Indonesia, Malaysia, and Thailand. At the same time, intra-ASEAN investment has increased from 15% in 2013 to 21% in 2016 and 19.3% in 2017. This shows that a significant amount of FDI inflow to ASEAN still comes from non-ASEAN investors, whereas the intra-ASEAN investments could also be contributed by third-country investors who qualify as ASEAN investors as defined under the ACIA. Intra-ASEAN investments are mainly in natural resources, manufacturing, wholesale and retail, financial and insurance activities, and estates. Most of the non-ASEAN investments flow into manufacturing and financial services, followed by investments in natural resources, wholesale and retail, and real estate activities (ASEAN, 2017a; Masudi, 2016).

The proportion of FDI inflows to GDP in AMS from 2013 to 2017 is shown in Table 1.

Table 1: Proportion of FDI Inflows to GDP in the AMS, 2013–2017

Country	2013	2014	2015	2016	2017
Brunei Darussalam	4.29	3.32	1.32	(1.32)	
Indonesia	2.55	2.82	2.30	0.49	2.17
Cambodia	12.29	10.30	9.42	11.43	
Lao PDR	3.57	6.88	9.88	6.31	
Myanmar	3.74	3.32	6.84	5.18	6.76
Malaysia	3.49	3.14	3.33	4.54	3.02
Philippines	1.37	2.02	1.93	2.72	3.20
Singapore	21.18	22.32	23.21	23.97	19.65
Thailand	3.79	1.22	2.22	0.74	2.00
Viet Nam	5.20	4.94	6.11	6.14	6.30
World	2.56	2.20	3.12	3.12	2.44
East Asia and Pacific	2.77	2.80	2.80	2.37	2.21
European Union	3.37	2.11	3.84	5.23	3.68
High-income	2.47	2.10	3.50	3.62	2.73
Low-income	4.52	3.64	3.87	4.03	
OECD members	2.28	1.74	3.08	3.30	2.36
Upper middle-income	2.92	2.44	2.39	2.22	1.86
ASEAN	6.15	6.03	6.66	6.02	4.31

( ) = negative, AMS = ASEAN Member States, ASEAN = Association of Southeast Asian Nations, FDI = foreign direct investment, GDP = gross domestic product, Lao PDR = Lao People's Democratic Republic, OECD = Organisation for Economic Co-operation and Development.

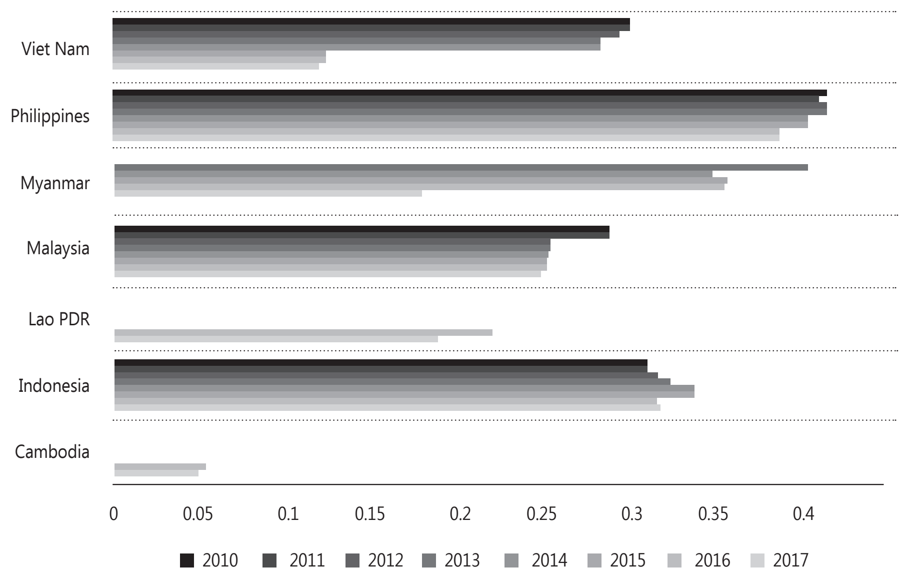
Source: World Bank (2018), *World Development Indicators: Growth of Output*, http://wdi.worldbank.org/table/4.1 (accessed 15 December 2018).

Table 1 shows that FDI makes a significant contribution to Singapore's GDP, with an FDI to GDP ratio of 19%–23% compared with the ASEAN average of 4%–7%. Singapore's double-digit ratio raises the ASEAN average above the 2%–3.6% of high-income countries. Since 2016, Viet Nam's FDI to GDP ratio has also grown above the ASEAN ratio. Table 1 also shows that most of the newer AMS–Cambodia, the Lao People's Democratic Republic (Lao PDR), and Myanmar–have a high FDI to GDP, whereas the ASEAN 5 (which excludes Singapore) have an average FDI to GDP ratio lower than the ASEAN average. Hence, it is important to note that Singapore and the newer AMS would need continuous FDI to support their economic growth.

Other AMS are less reliant on FDI for their economic growth, which is contributed by domestic direct investment (DDI) or government spending. However, these countries need to sustain the DDI to contribute towards continuous economic growth. With the help of increased FDI and linkages with DDI, their economic output may also increase. Building linkages between FDI and DDI will assist countries to accelerate productivity gains through access to foreign technology and frontier knowledge that, if successfully absorbed by local firms, can improve their productivity directly. FDI can also increase competition amongst firms in the local market by leading to a reallocation of resources away from less productive to more productive firms, thereby increasing aggregate productivity in the long run (World Bank, 2018). Those countries with higher reliance on FDI will need to counter any potential shock from external disruptions by increasing contributions from DDI.

To enhance ASEAN's competitiveness as a single investment destination, AMS will need to address national measures that restrict FDI. This is very important for AMS which have both low FDI and DDI.

Figure 2: ASEAN FDI Restrictiveness Index, 2010–2017



Country	Cambodia	Indonesia	Lao PDR	Malaysia	Myanmar	Philippines	Viet Nam
2010	0.000	0.312	0.000	0.290	0.000	0.417	0.302
2011	0.000	0.312	0.000	0.290	0.000	0.412	0.302
2012	0.000	0.318	0.000	0.255	0.000	0.417	0.296
2013	0.000	0.325	0.000	0.255	0.406	0.417	0.285
2014	0.000	0.339	0.000	0.254	0.350	0.406	0.285
2015	0.000	0.339	0.000	0.253	0.359	0.406	0.124
2016	0.54	0.317	0.221	0.253	0.357	0.390	0.124
2017	0.05	0.32	0.19	0.25	0.18	0.39	0.12

ASEAN = Association of Southeast Asian Nations, FDI = foreign direct investment,
Lao PDR = Lao People's Democratic Republic.

Source: Organisation for Economic Cooperation and Development (OECD) (2018) *OECD.Stat, OECD FDI Regulatory Restrictiveness Index*, https://stats.oecd.org/Index.aspx?datasetcode=FDIINDEX# (accessed 15 December 2018).

FDI restrictions in ASEAN are generally higher than the OCED and non-OECD country average (Figure 2). FDI restrictions in several AMS remain above the non-OECD average: Indonesia (0.32), Malaysia (0.25), and the Philippines (0.39). Viet Nam has reduced its FDI restrictions, where the index dropped from the ratio of 0.302 in 2010 to 0.12 in 2017, which is below the non-OECD average of 0.126, and further liberalisation could be one of the factors that contribute to increased FDI inflow to the country. Myanmar has also undertaken policy reform by introducing the Myanmar Investment Law, 2016, and has reduced the number of sectors in the restricted sectors list.[2]

Any discussion on investment must also relate to trade since trade and investment rely on each other, especially in the age of the GVC where a final product is made from various components made in different locations. There is evidence of positive self-reinforcing relationships between bilateral trade and FDI flows, with trade inducing FDI as well as FDI inducing trade in ASEAN (Chaisrisawatsuk and Chaisrisawatsuk, 2007). It is estimated that 66% of ASEAN exports are accounted for by participation in GVCs, making the region the second largest regional grouping worldwide in terms of GVC presence, behind only the European Union (EU), which has a 70% share (Pricewaterhouse Coopers, 2018).

Countries that export the most also have the highest FDI flows (Sjöholm, 2013). This is clearly shown in Table 2, where Singapore, which receives the largest amount of FDI, also trades the most with international trade forming 310%–365% of its GDP. The same is true for Viet Nam, which received the second largest amount of FDI in ASEAN in 2017, at 200%. Indonesia has a smaller trade to GDP ratio, at 39% at the end of 2017, since most of the FDI in Indonesia is natural resource-seeking and market-seeking investment, rather than efficiency-seeking investments as in the case of Malaysia, Singapore, or Viet Nam.

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[2] For discussion on Myanmar investment policy reform, see Jusoh (2018); and for Myanmar and the Lao PDR, see Jusoh (forthcoming).

The traditional notion of investment and trade, relating to the main sectors or tangible products, is slowly being eroded by the increase in cross-border trade in services, making investment in services ever more important. It can be implied that strong growth in trade in goods and services is one of the factors for the continued attractiveness of AMS as investment destinations. By 2016, the services sector had accounted for 53.1% of ASEAN's GDP (ASEAN, 2017b). In terms of contributions to national GDP, it is estimated that services contributed the following percentages to each AMS at the end of 2017: 42.3% in Brunei Darussalam, 41.9% in Cambodia, 45.9% in Indonesia, 45.9% in the Lao PDR, 54.7% in Malaysia, 39.39% in Myanmar, 59.8% in the Philippines, 75.2% in Singapore, 55.6% in Thailand, and 41.3% in Viet Nam (Central Intelligence Agency, 2017).

The services sector is also the most significant recipient of FDI flows to the region. FDI in services increased from about 60% of total FDI inflow to ASEAN in 2001 to 80% in 2016. Almost half of the FDI to the services sectors generally goes to finance and insurance; about 20% to the wholesale and retail trade and repair services of motor vehicles; 10%–14% to real estate; and 3%–6% to transportation and storage (ASEAN, 2017b). The main investors in services in ASEAN are from Japan, the EU, and the US, followed by the intra-ASEAN investors.

In terms of trade, ASEAN's exports reached $326.8 billion in 2016 or almost 2.5 times the level just a decade earlier, while its imports reached $316.5 billion in 2016 or almost doubled within the same period. Singapore has the largest ratio of total services trade to GDP, at 103% in 2017, followed by Thailand at 26% and Malaysia at 25% (Table 2).

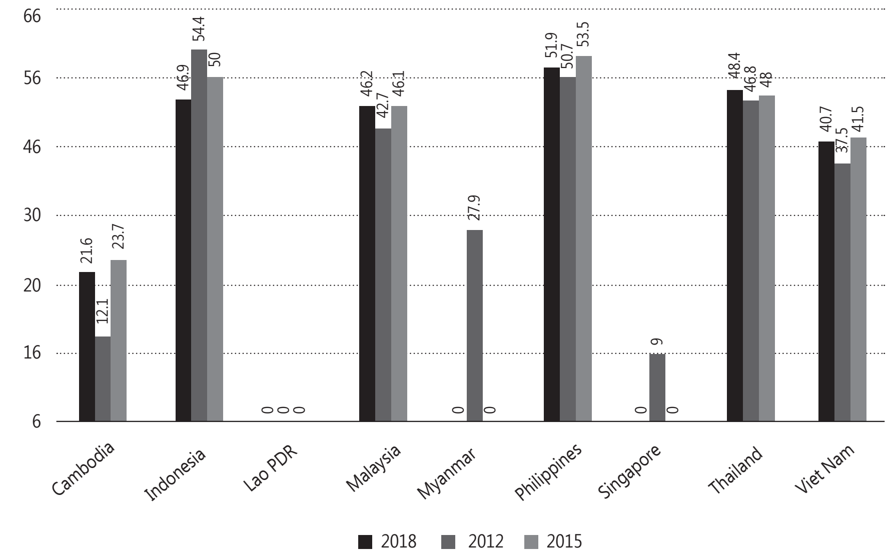
Table 2: Total Trade and Total Trade in Services as a Share of GDP, 2013–2017

	2013		2014		2015		2016		2017	
	Total Trade	Services	Total Trade	Services	Total Trade	Services	Total Trade	Services	Total Trade	Services
Brunei Darussalam	110.94	18.52	99.37	16.05	84.90	17.80	87.32	19.07	85.18	
Indonesia	48.64	6.35	48.08	6.41	41.94	6.17	37.44	5.76	39.54	5.63
Cambodia	130.05	34.52	129.61	34.09	127.86	32.56	126.95	30.43	124.89	
Lao PDR	98.18	11.01	99.06	9.51	85.80	10.33	75.09	9.17	75.83	
Myanmar	38.58	8.19	42.26	8.14	47.36	10.35	39.06	9.98		10.15
Malaysia	142.72	26.99	138.31	25.85	133.55	25.34	128.64	25.54	135.92	25.26
Philippines	60.25	14.59	61.47	16.31	62.69	17.99	64.90	18.16	70.66	19.68
Singapore	365.69	96.64	359.25	104.12	329.05	105.91	310.26	103.44	322.43	103.57
Thailand	133.41	25.26	131.80	24.74	125.90	25.98	121.66	26.99		26.69
Viet Nam	165.09	14.33	169.53	13.68	178.77	13.82	184.69	14.57	200.31	13.44
World	60.13	12.24	59.84	12.75	57.81	12.79	56.21	12.73		12.78
High-income	62.66	10.16	62.77	10.85	61.00	10.59	59.45	10.39		10.11
ASEAN average	129.35	14.32	127.88	15.02	121.78	15.00	117.60	14.94	105.47	15.22

ASEAN = Association of Southeast Asian Nations, GDP = gross domestic product, Lao PDR = Lao People's Democratic Republic.

Source: World Bank (2003), World Development Indicators, 2003. Washington, DC: World Bank. http://www.worldbank.org/data/wdi2003/index.htm (accessed 27 August 2003).

Figure 3: ASEAN Services Trade Restrictiveness Index, 2008–2015



Lao PDR = Lao People's Democratic Republic.

Source: World Bank (2018), Services Trade Restrictiveness Index, https://tcdata360.worldbank.org/indicators/trade.stri.stri (accessed 15 December 2018).

Access to the ASEAN services market is also subject to national restrictions and policies. The World Bank Services Trade Restrictiveness Index (STRI, Figure 3) shows that AMS (i.e. Indonesia, Malaysia, the Philippines, Thailand, and Viet Nam) tend to impose a higher degree of restrictions on services trade, which is above the global mean of 32.7248 (François and Manchin, 2016). With a reduction in the STRI, some AMS such as Malaysia and Thailand could increase investment in services and enhance trade in services' contribution to GDP.

3. The ASEAN Investment and Services Framework

Under the ASEAN Economic Community Blueprint 2025: Forging Ahead Together (ASEAN, 2015), ASEAN leaders envisioned that by 2025, ASEAN was set to achieve a highly integrated and cohesive regional economy which supports sustained high economic growth by increasing trade, investment, and job creation; improving regional capacity to respond to global challenges and megatrends; deeper integration in trade in services; and more seamless movement of investment, skilled labour, business persons, and capital.

The blueprint also envisions a competitive, innovative, and dynamic community which fosters robust productivity growth, including through the creation and practical application of knowledge, supportive policies towards innovation, a science-based approach to green technology and development, and by embracing the evolving digital technology; promotion of good governance, transparency, and responsive regulations; effective dispute resolution; and a view towards enhanced participation in GVCs.

In the quest for a freer and more open investment regime based on international best practice, the ASEAN Economic Ministers (AEM) signed the ACIA, which consolidated two existing agreements – the ASEAN Investment Guarantee Agreement (IGA) and the ASEAN Investment Area (AIA) Agreement – on 26 February 2009. It encompassed four pillars: liberalisation, facilitation, protection, and promotion, containing new features to promote and encourage FDI inflows to ASEAN. The ACIA covers 10 sectors, as shown in Table 3 and the AMS agreed to liberalise other areas subject to agreement by all member states. In terms of liberalisation, the ACIA enshrines provisions which accommodate the expansion of the scope of this agreement to cover other sectors in the future.

Table 3: Liberalised Sectors in ACIA

Sectors	Examples/Illustrations/Opportunities for Foreign Investors
Manufacturing	Manufacture of food products and beverages Manufacture of textiles
Agriculture	Growing of crops, market gardening, and horticulture Farming of animals)
Fishery	Fishing, operation of fish hatcheries, and fish farms
Forestry	Forestry
Mining and quarrying	Extraction of crude petroleum and natural gas Mining of coal and lignite and extraction of peat
Services incidental to manufacturing	Manufacture of basic metals on a fee or contract basis Manufacture of office, accounting, and computing machinery, on a fee or contract basis
Services incidental to agriculture	Services providing agricultural machinery with drivers and crew Harvesting and related services Services of farm labour contractors; animal board, care, and breeding services Services to promote propagation, growth, and output of animals
Services incidental to fishery	2Services related to fishery and operational services of fish hatcheries or fish farms
Services incidental to forestry	Timber evaluation, fire-fighting, forest management including forest damage assessment services Logging-related services
Services incidental to mining and quarrying	Drilling services Repair and dismantling services Oil and gas well casings cementing services

ACIA = ASEAN Comprehensive Investment Agreement, ASEAN = Association of Southeast Asian Nations.

Source: Authors; International Standard Industrial Classification (ISIC) Revision 3 and the United Nations Provisional Central Product Certification (pCPC) 1991.

The ACIA covers both FDI and portfolio investment, while the AIA covers FDI only. Benefits of the ACIA are extended to ASEAN investors as well as foreign-owned ASEAN-based investors.

In ensuring substantial elimination of restrictions to trade in services amongst AMS to improve the efficiency and competitiveness of ASEAN services suppliers, the AEM signed the AFAS on 15 December 1995 during the 5th ASEAN Summit in Bangkok, Thailand. The AFAS provides broad guidelines for progressive improvement of market access amongst AMS and ensures equal national treatment for services suppliers in ASEAN. Its rules are consistent with international rules for trade in services provided by the General Agreement on Trade in Services (GATS) of the World Trade Organization (WTO). Liberalisation of services trade under the AFAS is directed towards achieving commitments beyond member states' commitments under GATS, known as the GATS-Plus principle.

The AFAS was implemented through several rounds of negotiations, which resulted in commitment packages from each AMS in each agreed economic sector/subsector and mode of supply. The AEM has signed 10 packages of commitments under the AFAS since 1 January 1996. Each package provides details of the commitments of the respective AMS in various services sectors and subsectors. Under the AFAS, the ASEAN Finance Ministers Meeting (AFMM) signed six additional packages of commitments on financial services and air transport.

Both the ACIA and AFAS adopt the principle of 'progressive liberalisation', which follows the mechanism in use within the WTO, especially in relation to the liberalisation of the services sector under the GATS Article XIX. ASEAN also adopts this approach in the AFAS. Article XIX of the GATS calls for achieving progressively higher liberalisation, promoting the interests of all participants on a mutually advantageous basis, and securing an overall balance of rights and obligations. The mandate further states that negotiations will take due regard of national policy objectives and the level of development of individual members, both overall and in individual sectors. It also states that individual developing countries will have appropriate flexibility to open fewer sectors, liberalise fewer types of market transactions, and progressively extend market access in line with their development situation and flexibility of attaching market access conditions to foreign service suppliers. The principle also includes the concept that once liberalisation of sectors occurs, the government should not backtrack or reintroduce restrictions that have been removed.

To enhance ASEAN's trade and production networks, as well as to establish a more unified market for its firms and consumers, there is a need to broaden and deepen services integration within ASEAN and ASEAN's integration into global supply chains in services, and to enhance AMS' competitiveness in services. AMS agreed to pursue the maximisation of the potential contribution of the services sector to economic development and growth, and continued to broaden the coverage and reduce the limitations on market access and national treatment across the services sectors, with the negotiations of the ATISA as the legal instrument for further integration of the services sectors in the region.

The ATISA sets out to review existing flexibilities, limitations, thresholds, and carveouts; enhance mechanisms to attract FDI to the services sectors to support GVC activities; have further liberalisation; establish possible discipline on domestic regulations to ensure the competitiveness of the services sector, taking into consideration other non-economic, development, or regulatory objectives; consider the development of sectoral annexes; and enhance technical cooperation in the services sector for human resources development, joint promotion activities to attract FDI to the services sector, and the exchange of best practices.

4. Challenges Faced by ASEAN on Investment and Services

The ASEAN Economic Community still faces challenges in moving towards a single investment destination and developing a region-wide services sector (OECD, 2014). First, a development gap remains between the ASEAN 6 and the newer member states. In addition, as discussed earlier, a large gap persists between the FDI received by Singapore and the FDI of the rest of ASEAN.

Second, 'behind-the-border' legacy issues related to domestic regulations before the formation of ASEAN and the ASEAN Economic Community impose obstacles to full liberalisation in ASEAN. This is illustrated in the STRI index and FDI restrictiveness indexes (Figures 2 and 3), which show that the degree and type of liberalisation vary from one member state to another.

Third, investors in ASEAN are concerned with political risks relating to transparency and investment facilitation. They have highlighted the inconsistent investment regulations and treatment in AMS in many surveys and publications such as World Bank (2018), A.T. Kearney (2013), and The Economist (2013); and at the ACIA Forum in Kuala Lumpur in March 2013. The Economist (2013) survey shows that investors are concerned about the uncertain legal environment, especially the protection of domestic markets in certain AMS. The respondents are concerned that governments may reverse policies on legal issues and important legislation with little warning, and court decisions can be highly arbitrary.

The Economist (2013) survey found that the largest impediments to business in Asia-10 countries are laws governing the establishment of a commercial presence and those restricting the movement of both skilled and unskilled labour. Most AMS impose foreign equity limits on certain sectors or activities. The use of a foreign equity limit varies significantly from country to country. In some countries, legal and administrative instruments require that foreign investors obtain government approval for almost all investments, even in non-sensitive sectors. The survey was also of the view that some countries are more open and less protected than others.

5. ASEAN Investment and Services Sectors in the Face of Global Megatrends

5.1 'Servicification' of the Economy

Moving towards 2040, AMS could face challenges from global megatrends, including the 'servicification' of the economy. Servicification of the economy is evident throughout the world, but especially in developed countries. Services trade is critical to keep manufacturing sectors competitive. Moreover, there is a rise in service value chains wherein input and output along the value chains are primarily services. Developed countries are very competitive in services exports, especially English-speaking countries such as the US and the United Kingdom (Table 4). Asian countries in general have a huge services deficit from developed countries. At the same time, whilst the US goods trade deficit is huge, its service surplus is also massive (Pakravan, 2018).

Table 4: Services Trade Balance, 2016 ($ billion)

Item	Export	Import	Balance
G7	2,011	1,658	353
United States	759	510	249
United Kingdom	348	211	137
China	208	442	(233)
Japan	176	186	(10)
India	162	96	66
Indonesia	23	30	(7)

( ) = negative.

Source: Organisation for Economic Co-operation and Development (2018), *Trade in Services*, https://data.oecd.org/trade/trade-in-services.htm (accessed 15 December 2018).

It is widely believed that the US has a huge trade deficit with Asia, especially China, which results in the frustration of many US administrations, particularly the Trump administration. However, if we look at trade in services between the US and China, the US has a huge surplus that is increasing rapidly (Reynolds, 2016). Many ASEAN countries such as Indonesia will face a similar situation to that of China sooner or later. Once services trade becomes as large as goods trade, most Asian countries may have an overall trade deficit. Hence, it is perhaps necessary for ASEAN to identify the services sectors that can earn surplus. Tourism and back office operations are typical examples, but other service sectors may also have development potential.

5.2 Digitalisation of the Economy

The second megatrend is the digitalisation of the economy, or the internet of things (IoT), which is inevitable for both developed and developing nations. Examples of well-known companies that take advantage of digitalisation are Uber, Facebook, Airbnb, and Alibaba. It is important to note that the majority of IoT companies originated in the United States, although Alibaba is from China.

Information and communication technology (ICT) is transforming society significantly. With it, the world has seen the rise of the internet and digital economy, smart manufacturing, artificial intelligence (AI), 3D printing, blockchain, and IoT. This new wave of technologies is creating opportunities but also testing governments' ability to harness their benefits and provide prudent oversight. If harnessed correctly, these technological developments could be a key driver of economic growth (WTO, 2018) and development, deeper economic integration, and more inclusive outcomes.

E-Commerce has huge potential to change economic integration inside and beyond ASEAN. E-Commerce transactions are mostly domestic (OECD, 2016). However, the share of international e-commerce transactions is rapidly increasing in many developed countries, especially for members of the EU and the North American Free Trade Agreement (OECD, 2016). This implies two possible scenarios. First, there is a large opportunity to increase intra-ASEAN (or Asian) e-commerce. Second, there is a risk that future transaction of e-commerce in ASEAN (or Asia) could be dominated by international e-commerce providers in Europe and North America (and Japan and the Republic of Korea (henceforth, Korea)) (UNCTAD, 2017).

The largest challenge to promote e-commerce in ASEAN/Asia is the huge gap in readiness, as illustrated by the United Nations Conference on Trade and Development (UNCTAD) E-Commerce Index (Table 5). The index has four sub-components: internet use, payment, secure server, and delivery, which give us reasonable policy implications related to services and investment reform. Good internet infrastructure (both broadband and mobile) is necessary. The role of foreign investment and foreign service providers may be critical in this regard. A strong financial sector which provides people with e-payment facilities is important. Logistics services are also critical because products purchased online may be delivered from warehouses abroad.

Table 5: UNCTAD E-Commerce Index

Country	
Rep. of Korea	95.5
Japan	93.6
New Zealand	93.0
Australia	92.0
Singapore	90.0
Malaysia	77.0
Thailand	68.0
China	60.0
Viet Nam	50.0
India	44.0
Lao PDR	41.0
Philippines	40.0
Indonesia	36.0
Cambodia	29.0
Myanmar	23.0

Lao PDR = Lao People's Democratic Republic, UNCTAD = United Nations Conference on Trade and Development.

Source: UNCTAD (2017), *UNCTAD B2C E-commerce Index*, https://unctad.org/en/PublicationsLibrary/tn_unctad_ict4d09_en.pdf (accessed 15 December 2018).

An appropriate legal and institutional environment needs to be in place covering concerns such as (i) e-transactions, including rules related to electronic signatures and authentication; (ii) consumer protection; (iii) data protection and privacy; and (iv) cybercrime (Asian Development Bank (ADB), 2017). Those are the items covered by e-commerce chapters in free trade agreements (FTAs) signed by Asian countries, including ASEAN members. It is important to note that the e-commerce chapter in some FTAs emphasises the necessity of capacity building support for institutional development (e.g. see the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) Chapter 14.15).

5.3 Demographic and Ageing Society

Higher life expectancy, falling birth rates, and migration are expected to have a significant impact on demographics. Higher life expectancy and falling birth rates will lead to societies with ageing populations which in turn will impact consumer spending and strain existing social welfare systems as well as pose the challenge of how to integrate youth populations into saturated labour markets (Pricewaterhouse Coopers, 2018). Migration ('replacement migration') would have delayed the inevitable but it has its own challenges such as wage differentials; difference in fertility, resulting in demographic shifts; possible welfare dependence; and managing heterogeneity.

The International Labour Organization estimates that ASEAN will record the second largest growth in labour force worldwide from 2018 to 2030 (behind only India) as another 59 million people are projected to enter its workforce by 2030. ASEAN will continue to represent the third largest labour force worldwide, behind only China and India, accounting for 10% of the global labour force by 2030. In fact, ASEAN's labour force will be more than twice the size of the next ranked market, the US, with 175 million in its labour force by then. However, ASEAN also faces the risk of underutilising this demographic opportunity if it fails to generate quality employment at the required scale while training this growing workforce in the skills needed to shift to higher value-added jobs in time to boost productivity levels (PriceWaterhouse Coopers, 2018).

As for the demand-side factors impacting economic growth, the region is poised to witness the expansion of ASEAN's middle-income segment (defined as $10–$100 in daily expenditure). This group is projected to represent two-thirds of the overall population by 2030, compared with only 29% in 2010. This emerging middle class, which is associated with a higher willingness to pay for quality, convenience, and choice, will drive the demand for more discretionary and aspirational product categories in the coming years. However, to target these growth opportunities, companies will need to align business strategies with shifts in consumption patterns being witnessed in the region. Online retail will increasingly challenge the traditional brick-and-mortar model, with consumers demanding more personalised products and services, through an integrated omni-channel experience (Kelleher, 2018).

One of the most serious social problems that developed countries face is ageing. The impact of this problem on developed countries which accept migration may be manageable (e.g. Australia–Table 6), but for those that do not accept migration, the entire economy could become unsustainable. An obvious example of this type of country is Japan, but countries like China may also have serious ageing problems. In this context, it is important to note that some countries will continue to have a large youth population even in 2050 (Table 6). In ASEAN, the ageing population in Cambodia, Indonesia, the Lao PDR, Myanmar, and the Philippines is likely to be less than 20% even in 2050.

Table 6: Ageing Population Ratio

Country	2016	2050
Japan	33.4	42.5
Korea	19.3	41.5
Singapore	18.7	40.4
Thailand	16.4	37.1
China	15.7	36.5
Brunei Darussalam	8.1	30.9
New Zealand	20.8	29.4
Australia	20.7	28.3
Viet Nam	10.7	27.9
Malaysia	9.5	23.6
Indonesia	8.5	19.2
India	9.1	19.4
Myanmar	9.2	18.8
Cambodia	6.9	17.6
Lao PDR	6.1	14.7
Philippines	7.4	14.0

Lao PDR = Lao People's Democratic Republic.

Source: United Nations, Economic and Social Commission for Asia and the Pacific (UNESCAP) (2016), *Population data sheet.* https://www.unescap.org/resources/2016-escap-population-data-sheet (accessed 15 December 2018).

If some ageing societies do not accept migration (say Japan), other forms of adjustment become necessary, often in the form of services trade. This is natural, because services that were supposed to be supplied domestically by migrants should then be supplied internationally.
Thus, the magnitude of the ageing problem can be mitigated by further integrating services and investment in ASEAN and Asia. There is significant potential to increase international services in 'silver industries', which deal with ageing persons.

Many aged persons are expected to live in a nursing or retirement home where they can receive various services from caregivers. To fill the demand for trained caregivers, some standardisation of the caregiver 'profession' may be necessary amongst Asian countries, perhaps through a form of mutual recognition agreement (MRA). It may be wise for both importing and exporting countries of caregivers to agree on the basic competencies of caregivers (see the discussion below on MRAs). Further, companies running nursing homes may want to establish nursing homes in nearby conducive environments such as Indonesia, Thailand, or the Philippines. This would lead to liberalisation of Mode 3 (commercial presence) for social services and medical tourism.

With the potential demand for professional/trained caregivers, nursing homes in Indonesia, the Philippines, or Thailand could provide the necessary work experience before supplying such services in requesting countries such as Japan. AMS such as Indonesia, the Philippines, and Thailand could develop medical tourism for aged persons. Developed ASEAN markets such as Brunei Darussalam and Singapore, which have more advanced institutions and infrastructure as well as ageing populations, will need to focus on increasing technology adoption to counter declining productivity growth (Pricewaterhouse Coopers, 2018).

5.4 International Movement of Students and Professionals

The international mobility of people is expected to continue to be enhanced, partly because of the declining trend in air travel costs. It is critically important to carefully consider the prospect of international movement of students and professionals, which are intrinsically linked since students who obtain engineering degrees become professional engineers.

Mutual recognition of professional qualifications is critical to enhance the international mobility of professionals. While ASEAN has some MRAs, it is desirable to have more MRAs within ASEAN and between ASEAN and non-ASEAN countries (Hamanaka and Jusoh, 2018). If Japanese or Korean engineers can practise in developing ASEAN countries (e.g. the Lao PDR) under MRA schemes, that would help enhance the capacity of Laotian engineers if the MRA were designed properly (such as joint practice requirements). Laotian engineers would also have an opportunity to go to Japan or Korea to enhance their skills under MRAs.

Students in developing countries often have to move to developed countries for a good university or post-graduate education. This is not necessarily a bad phenomenon but it has two risks. First, students who study abroad may not return to their home country and decide to stay abroad. Second, the flow of people is one-sided: from developing to developed countries (Bista, 2018). So, the question is how to avoid the brain drain and achieve more mutual exchange of talent.

AMS could enhance efforts to attract offshore or satellite campuses of foreign universities, including those of other ASEAN/Asian countries (e.g. offshore campuses of Chinese universities). Offshore campuses of developed country universities are likely to facilitate the inflow of foreign professors, which could contribute to an improvement in the quality of domestic professors. ASEAN countries' exportation of offshore campuses to fellow ASEAN members and other Asian countries (say Japan) could also prove useful such as a Philippine university's offshore campus in Korea.

Further, intra-regional student exchanges should be increased. This could lead to some harmonisation of curricula, and even MRAs. Suppose a university in Korea opens an offshore campus in the Philippines and Filipino students study engineering there. If he/she obtains an engineering qualification in the Philippines/Korea, it would be advantageous if he/she could also practise in Korea/the Philippines. This becomes possible with an MRA. Higher international mobility of university students would considerably transform the international service flow for the movement of natural persons.

5.5 Improved Infrastructure

The most important consideration is that ASEAN requires improved infrastructure to spearhead economic growth through increased trade, investment, competitiveness, and connectivity in the region and with the rest of the world. ADB estimates that the total infrastructure investment needs in ASEAN from 2016 to 2030 will be $2.8 trillion (baseline estimate) to $3.1 trillion (climate-adjusted estimate) (ADB, 2017).

These infrastructure needs are important to support the increasing amount of ASEAN trade, with total merchandise trade increased from $4 trillion in 2010 to $5 trillion 2017 (ASEAN, 2018). The total merchandise trade is projected to increase as ASEAN grows from the seventh to the fourth largest economy in the world by 2050, with annual GDP growth of 5.25% from 2016 to 2020 (Tan, 2017).

5.6 Sustainable Resources and Climate Change

Rising greenhouse gas emissions are causing climate change and driving a complex mix of unpredictable changes. We have seen the devastating effects of climate change in the rise in unpredictable weather patterns and natural disasters (Riebeek, 2005). These can impact our economies through increased global temperatures, increased intensity of storms, and wetter monsoon seasons (consequently, increased instances of flooding). There is a need to address this issue as it not only results in disruptions in food supply and economic activities, but the destruction it brings about will tax the economy in the form of costs associated with recovery.

The combined pressures from population growth, economic growth, and climate change will increase the stress on essential natural resources, i.e.

water, food, arable land, and energy. Demand for food, water, and energy is projected to grow by about 35, 40, and 50% over this period until 2030, resulting in food and water shortages. Governments will need to inculcate sustainable resource management and identify alternative sources of power.

While abundant across Southeast Asia, natural resources are depleting rapidly as they are used for industry and to meet the consumption needs of growing populations. Depletion reduces national wealth; and most natural resources, when transformed into energy, unavoidably aggravate pollution. Accordingly, their mobilisation and sale must be carefully weighed against economic and social costs. Market prices do not always reflect social costs. Similarly, corporate balance sheets rarely account for environmental effects.

5.7 Economic Power Shift

Emerging economies like China, India, and Brazil are projected to dominate the world's top 10 economies in 2050. Other potential economies identified are Viet Nam, the Philippines, and Nigeria. The US and the EU stand to lose ground to China and India. This means that these emerging economies will exert more influence on the direction of the global economy. The rise of China and India in the global economy increasingly challenges ASEAN to enhance its competitiveness. Over the coming decades, competitive pressures will not only come from within Asia, but also more distant economies such as the Russian Federation, Brazil, South Africa, and Turkey (ADB Institute, 2016).

With the economic power shift, AMS will have to identify optimal trade and investment partners. In the long run, as globalisation increases the importance of multipolar development, the region should be able to leverage its diversity. Through investment in research and development (R&D) and innovation, competitiveness can be built in agriculture, manufacturing, and services from high-yielding crops to industrial clusters, tourism, telecommunications, and finance, to name a few strategic sectors.

6. Conclusion and The Way Forward Towards 2040

The above discussion shows that investments in manufacturing and services are important for ASEAN to remain competitive into the future, and for integration into the GVC and the global economy. As ASEAN is moving towards becoming an economic powerhouse, it is important to focus on increasing investment in services.

At the same time, the dynamics of the investment landscape in and around ASEAN may change in the future. Intra-ASEAN investment could increase, with Malaysia, Singapore, Thailand, and Viet Nam as potential FDI exporters. Similarly, the dynamic of FDI inflows to ASEAN may also change, with Viet Nam potentially attracting more FDI than traditional destinations such as Indonesia, Malaysia, and Thailand. Myanmar is also striving towards being a new focus of FDI in the region.

The dynamics in the investment sector may also change by 2040.
The changes may be forced on the AMS by the new megatrends discussed above. Many AMS will become ageing societies which require recalibration of services and products produced in those countries. Technological changes may also affect consumer behaviour related to the services and products they will purchase and how the products and services are delivered. These technologies may be either homegrown or from abroad, mainly China and India. Further, the sources of FDI may also change, as China and India are expected to become more economically dominant. Hence, the way FDI is secured and sectors are promoted needs to be changed. The disruptions expected in the future may not just come from technologies but also from political economic changes as well as changes taking place within ASEAN.

Moving towards 2040, ASEAN may have to rethink the way to handle investments, domestic and foreign, in the main and services sectors. ASEAN should look at recalibrating the economic and investment focus or promoted sectors, which will have to be based on the niche of each AMS, considering the megatrends and domestic considerations discussed above. Recalibration may take place in several forms, such as

(i) changing the list of promoted sectors, which is normally in the form of a positive list; and (ii) reducing services and FDI restrictions through the liberalisation of ownership and control of certain sectors, which is normally conducted through the national negative list, which may differ from the negative list in the annexes to the FTAs.

Based on the above, moving forward to 2040, the paper makes several recommendations.

First, ASEAN should work towards reducing restrictions for investment in the services and main sectors. Reduced restrictions may be achieved through a short national consolidated negative list, which covers the whole country and not just the non-conforming measures normally found in the FTAs. Negative lists should be short and cover high-risk sectors related to national security; plant, animal, and human health; the environment; and sustainability. AMS should conduct proper cost and benefit analysis in setting up the negative list. The preparation of the negative list will involve all levels of government (central and sub-central levels), with one coordinating central agency in charge. AMS should have a much more open investment regime because FDI is critical for technology upgrade and innovation. Hence, AMS may consider raising the allowable foreign equity share to at least 70%, and expand areas with allowable 100% foreign equity participation.

Second, liberalisation does not just include the opening up of sectors but also the loosening of admission rules. AMS may consider minimising other restrictions on foreign investors. This means reducing the need to screen investors and their investments at the pre-establishment phase of an investment, providing investment facilitation, and reducing the unnecessary regulatory burden. AMS may also increase national treatment provisions in the pre-establishment phase of an investment to promote bilateral FDI (Berger et al., 2013). Market access liberalisation, along with the provisions on non-discrimination (Büthe and Milner, 2008 and 2014) and the treatment of investors in an international investment agreement, is important to attract investors to any destination (Kenyon and Margalit, 2014). Again, investment entry liberalisation will have to involve all levels of government.

Third, ASEAN should focus on selecting niche investment sectors for both promotion and liberalisation. Increased linkages are needed between foreign and domestic investors. Accelerating technological diffusion and absorption in key areas with large spillover to the rest of the economy should be one goal. Exploiting synergies with science, R&D, and innovation could make ASEAN a leader in emerging market niches. These sectors should further integrate AMS within the regional and global value chains.

Fourth, ASEAN needs to re-strategise FDI and domestic investment promotions. Based on the megatrends, China and India together with Japan and Korea will be the new powers in the east, leaving behind the EU and the US. Thus, more products and services will be traded between ASEAN and these countries, leaving room for investments to take place in ASEAN.

Fifth, to facilitate investment and growth in the services sector, ASEAN should encourage investments that develop seamless connectivity in the region. The ability to travel, transit, and trade across borders is a priority for ASEAN countries as they build a truly borderless economic community. Improved connectivity, such as through aviation, will allow AMS to exploit their strategic location next to China and India. Domestic connectivity is also important in providing public services (electricity, water, sanitation, and telecommunications) where they are most needed and in linking peripheries to urban centres, allowing remote areas to unlock their development potential. Enhanced connectivity is crucial for improving competitiveness in all aspects of economic activity, including participation in production networks and supply chains.
Sixth, ASEAN should develop an integrated investor after-care and retention mechanism. This consists of a system to track investors, including investment implementation and grievances. An investor grievance mechanism will assist AMS to deal with issues raised by investors before they escalate to disputes.

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