

# Towards an investment agenda for APEC

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The Asia-Pacific Economic Cooperation forum has only recently included investment liberalization on its agenda. A review of actions since the Bogor declaration of 1994 reveals that critical components of an investment liberalizing strategy are already being assembled within APEC. For example, an investment experts group has been meeting regularly, and it has undertaken work on impediments to investment and on non-binding investment liberalizing procedures. Investment is also now a required component of each country's annual individual action plan. It would be useful to formalize this process and then move towards adoption of the rules-based investment provisions of NAFTA, especially the national treatment principle. Then the process developing within Asia-Pacific Economic Cooperation to liberalize investment as well as trade by 2020 would help to speed up the economic integration of APEC.

## Introduction

The ninth meeting of the Asia-Pacific Economic Cooperation (APEC) forum took place in Vancouver, Canada, in November 1997. APEC has evolved into a quasi-institution with an important trade and investment agenda since its founding meeting in Canberra, Australia, in 1989. That meeting represented a triumph for Australian foreign policy since the membership of APEC is unique in involving the People's Republic of China, Taiwan Province of China and Hong Kong Special Administrative Region of China (hereinafter Hong Kong, China); two of the world's economic super-powers (the United States and Japan); and all the other important economies

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bordering the Pacific Ocean.<sup>1</sup> APEC has also evolved in political importance, as (starting in 1993 at the Seattle meeting) there have been five annual meetings of heads of government, in addition to the ongoing meetings of trade and finance ministers. The government leaders also met in 1994 in Bogor (Jakarta), Indonesia; in 1995 in Osaka, Japan; and in 1996 in Subic Bay (Manila), Philippines. Thus, the Vancouver, Canada, meeting in 1997 was the fifth APEC summit meeting of government leaders and the ninth APEC ministerial meeting.

With the participation of government leaders, APEC has been transformed from a largely technical and low-key talk-shop to a quasi-institution in which the 18 member economies are becoming increasingly committed to economic cooperation and free trade. While not a formal international institution like the World Trade Organization (WTO), APEC has an emerging consultative process that helps to overcome the disadvantage of its very small secretariat and lack of well-developed procedural rules. Such economic substance as exists is being added through the recent development of an ongoing trade and investment agenda carried out by committees reporting to leaders subject to peer group pressure. In particular, there is a growing process of trade-liberalizing measures. This process reflects the consultative style of Asian trade and business negotiations, rather than a Western-type rules-based style. APEC, in short, is an evolving Western-style international institution with an Asian shape.

## **APEC and trade liberalization**

The main signpost of progress in trade liberalization can be traced back to the 1994 declaration in Bogor, Indonesia, whereby the member economies undertook to meet the goals of free and open trade and investment in the region. While investment is mentioned in the declaration, most of the subsequent action has been focused on trade liberalization. More specifically, members agreed to eliminate tariffs in developed countries by 2010 and in all developing countries by 2020. While these two categories were not defined, the declaration set all 18 members on the same path towards trade liberalization. In the 1995 meetings at Osaka, all members agreed to an "action

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<sup>1</sup> The 18 members of APEC are: Australia, Brunei Darussalam, Canada, Chile, the People's Republic of China, Hong Kong, China, Indonesia, Japan, the Republic of Korea, Malaysia, Mexico, New Zealand, Papua New Guinea, the Republic of the Philippines, Singapore, Taiwan Province of China, Thailand and the United States of America.

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agenda" in which their internal trade barriers would be identified and a voluntary commitment would be made to reduce them.

There are two key principles behind the common framework of the Osaka action plan of each economy. First, it is comprehensive, as all members in APEC agree to eliminate tariffs and foster investment across all sectors. Secondly, it is flexible, to reflect the economic reality of different stages of development and divergent conditions. However, this flexibility is confined to timing (i.e., 2010 or 2020 to eliminate trade barriers) rather than to systemic sector exclusions; the only sector with special treatment is agriculture.

To implement these free trade measures, the APEC members have agreed to trade liberalization measures that are parallel to the main principle of the GATT/WTO. In particular, they have agreed to most-favoured-nation treatment (non-discrimination) and transparency. The tariff reductions organized through APEC will be fully consistent with membership of most of these 18 countries in the WTO (although neither the People's Republic of China nor Taiwan Province of China is a member of the WTO). In this sense, APEC is a forum of "open regionalism", as trade-reduction benefits help members, and no new external tariffs are introduced against non-members.

At the 1996 meeting in the Philippines, each of the members filed Individual Action Plans (IAPs). The individual IAPs are now on record as a collective initiative called the Manila Action Plan for APEC (MAPA), and there is a commitment to implement the MAPA beginning in 1997. The MAPA is a process leading towards the comprehensive trade and investment liberalization of 2010 or 2020 agreed to in the Bogor declaration of 1994. APEC members have agreed to build on MAPA, to deepen the IAPs and to improve the comparability and comprehensiveness of the IAPs (APEC Leaders' Declaration, 1996). In Vancouver, the IAPs were to be further reviewed and amended to take account of private sector views. This was being facilitated by the formal acceptance (at the Philippines summit of 1996) of advice from the APEC Business Advisory Council (ABAC). The agenda of the ABAC is to make recommendations to the leaders of APEC concerning the movement of business people; the enhancement of FDI; alignment of professional standards; advice on infrastructure planning; policies for small and medium-size enterprises; and greater business participation in economic and technical cooperation.

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In the IAP, each member filed a formula revealing its own barriers to trade across 13 areas, including tariffs, non-tariff barriers, obstacles to trade in services and intellectual property. The identification of such trade (and investment) barriers provides a necessary benchmark against which future measures to liberalize trade and investment can be negotiated. The filing of IAPs is similar to the GATT/WTO process of individual country trade-policy review mechanisms, which have also been useful in benchmarking trade barriers and providing an agenda for future reductions in such barriers. Further progress on reducing trade barriers within APEC is highly likely, but the untold story is how investment barriers are to be liberalized.

## **APEC and foreign investment**

The only formal APEC statement dealing with the liberalization of foreign direct investment (FDI) is the Bogor declaration of 1994 on free and open trade and investment (UNCTAD (1996)). This was a path-breaking statement of non-binding investment principles, but was of little immediate value since the process for achieving FDI liberalization was not spelt out. The lack of a deeper agenda on FDI for APEC is, of course, a major weakness since over half the world's trade is conducted by large transnational corporations (TNCs) as a result of the FDI in which they engage (UNCTAD (1997)). A trade agreement without agreement on investment is like Hamlet without the Prince of Denmark. Indeed, some APEC members, especially Malaysia, have been opposed to the inclusion of investment rules in APEC. The majority of APEC members are recipients of strong inward FDI flows and they do not yet see the need to stabilize the climate for investment, whereas the wealthier countries have TNCs which need secure access for FDI. It is inevitable that these initial tensions over rules for investment will be replaced by a greater sensitivity to the leading role of TNCs in Asian development, and this will lead to pressure for an investment code. The remainder of this article will explore ways in which FDI measures are being gradually incorporated into APEC.

The lack of a clear process for the liberalization of investment in APEC does not mean that investment-related issues are not being dealt with. For example, each of the 18 IAPs reveals the current level of FDI, the nature of regulations affecting FDI and any proposals for the restructuring of those regulations. Therefore, there is some prospect that some of the APEC members can use these investment measures as benchmarks (in a manner similar

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to that in which trade barriers are used) and negotiate to reduce them in the future "rounds" of APEC (or the WTO). Indeed, coupling the investment-related measures with the trade-related measures in the future development of the IAP implementation process would be a great step forward.

In addition, there is an APEC investment experts group. It had two meetings in 1996 (in Singapore and Tokyo) and had three meetings arranged for 1997 in Victoria (British Columbia), Quebec and Hong Kong, China, before the November summit of APEC leaders in Vancouver. The investment experts group has considered and published work on impediments to investment and on investment liberalization, including the NAFTA experience. It is the group to be responsible for looking at the investment component of each of the 18 IAPs, as these were to be filed at the 1997 Vancouver meeting and subsequent annual APEC leaders' summits. The APEC members have endorsed a set of non-binding investment principles UNCTAD (1996)), rather than a set of NAFTA-type rules for investment. These are significant actions, but their effect cannot yet be gauged, and at this time it is unclear whether the investment-liberalization objectives for 2020 can be achieved.

There is another committee which is ongoing and does work on FDI at the technical level. It is a working group on trade and investment data. This group, headed by the Australian statistical agency, is trying to improve data on stocks of FDI, a notoriously unreliable area of statistics for most APEC members, which report flows of FDI and usually do not include retained earnings. This group's report in Vancouver could help to clarify the legal framework for FDI in members and suggest principles for the harmonization of regulations.

Another process mechanism for broadening APEC to consider FDI more seriously is the mandate given by APEC leaders to the business sector via ABAC. This group in turn, has also been advised by the Pacific Basin Economic Council (PBEC), a group which includes academic, as well as business leaders. In article 22 of the Subic Bay, Philippines, Leaders' Declaration of November 1996, the ABAC is required to: "enhance investment flows, strengthen investment protection in terms of transparency, predictability, arbitration and enforcement of contract . . ." This amounts to an agenda for a formal set of investment rules, which will be a departure from the non-binding nature of current APEC investment practice.

There are three key principles of any such investment code. In order of importance, a set of rules for FDI needs to:

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- Provide transparency (i.e., openness in the administration of regulations);
  - Ensure predictability in FDI treatment (in practice, this requires the provision of “national treatment” and “right of establishment” provisions, which are discussed below in more detail); and
  - Provide arbitration and enforcement of contracts, i.e., through appropriate dispute-settlement mechanisms, which are now available to investors in NAFTA (Rugman, 1994) and would be included in any set of multilateral rules for the management and organization of FDI that might emerge from either the OECD or WTO (Rugman, 1997).

In summary, the emerging process-driven nature of APEC already provides useful avenues for the “deepening” of trade diplomacy towards liberalization of FDI. Following the Bogor statement about FDI in APEC, the leaders’ repeated commitment to liberalization of trade and investment has put in place very useful committees and other mechanisms which already place FDI on the APEC agenda. As the APEC leaders consider FDI at future meetings, we can now consider the potential shape of a deeper agreement on FDI. This could usefully build upon the investment provisions of NAFTA, which will now be briefly outlined and related to APEC.

## **APEC and NAFTA’s investment provisions**

The investment provisions of NAFTA are the best codification to date of disciplines and procedures concerning international capital movements. No other multi- or bilateral investment agreement goes as far as NAFTA in terms of the scope of coverage, the depth of coverage or the enforcement of FDI rules. However, NAFTA also contains numerous provisions and exclusions which either place significant administrative pressures on investment patterns (for example, tight rules of origin in the automobile industry) or constitute outright discrimination (for example, specific sectoral exemptions by all three parties). (For a discussion of these issues, see Rugman (1994), Gestrin and Rugman (1994) and Rugman and Gestrin (1996).) A critical question is whether a new set of FDI rules in APEC could build on the investment provisions of NAFTA. More specifically, is it possible to generalize from the NAFTA experience in order to gain insight into international rule-making for investment? The NAFTA experience could contribute in three ways to an emergent set of investment rules in APEC.

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The first contribution relates to the nature of the investment environment for which the NAFTA rules were designed. The North American economy experienced rapid trade- and investment-led economic integration and policy convergence during the 1980s. The NAFTA investment rules therefore sought to address the requirements of a highly integrated regional production system by means not only of strong investment rules but also of an integrative approach to rule-making that reflects the interrelatedness of investment, trade, competition policy, intellectual property protection and services. Therefore, to the extent that NAFTA addresses itself to the kinds of "regional" investment relationships and production structures that are likely to become increasingly common in the global economy, it provides practical experience in investment rule-making not only in North America but also in other parts of the world, including the Asia-Pacific region.

The second contribution relates to weaknesses in the NAFTA investment provisions that reflect parochial national and regional protectionist interests. The issue is how to establish a mechanism that serves the dual purpose of locking in the signatories so that additional discriminatory measures may not be adopted and of establishing a process whereby existing discriminatory measures can be gradually rolled back. NAFTA's use of the "negative list" concept (explicit identification of all existing measures and practices of the signatories that run counter to one or more provisions in the agreement) well serves the objective of "lock-in" and could also function as the basis for further liberalization. This occurs if the transparency generated by the lists motivates a bargaining dynamic whereby parties begin to trade off derogations. Furthermore, the negative lists facilitate accession of countries whose investment regimes are below NAFTA standards, because they serve to establish transparency and precise liberalization commitments in the form of "phase-outs". This process could become acceptable to APEC members, despite their differences in economic background.

The third contribution which NAFTA makes to an understanding of the need for FDI rules in APEC relates to "procedural" weaknesses in the agreement that relate to investment. These include attempts by the Government of the United States to enhance national competitiveness through policies (in particular, subsidy programmes) that discriminate against foreign investors and investments, and through the tight rules of origin, which have the effect of reducing competition in certain industries, such as automobiles and textiles/apparel. Although these measures are not as economically significant as the mainly sectoral derogations contained in the negative lists, they identify issues that are likely to bear upon future multilateral negotia-

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tions over investment rules. In this connection, it is necessary to flag another procedural weakness, namely that the investor-state dispute-settlement mechanisms have not been used in the first two years of NAFTA, although the very existence of such an arbitral mechanism may itself encourage FDI (Kirton and Soloway, 1996).

## **APEC and the Multilateral Agreement on Investment**

Another forum of relevance to the development of an action plan in APEC for investment relates to work well under way to establish generalized rules for FDI. This is being done in Paris at the OECD, where new rules are currently being negotiated that are meant to govern the foreign investment undertaken by TNCs in the framework of a Multilateral Agreement on Investment (MAI).<sup>2</sup> The ways in which NAFTA's investment provisions are relevant for an MAI<sup>3</sup> and the role of an investment accord for APEC have been explored elsewhere. In May 1995, a two-year period of negotiations on an MAI began at the OECD, which is not inconsistent with its transfer to the WTO after the work has been completed.<sup>4</sup>

The MAI could potentially include many provisions, such as the right of establishment; national treatment; legal rights to machinery for dispute settlement in specific cases of expropriation and/or unilateral changes in the rules; transparency, notifications, binding obligations and general dispute-resolution procedures; and agreements on transfer pricing, taxation and competition policy. A broad-ranging MAI will make domestic markets internationally contestable, to the benefit of all consumers and global producers. A narrower MAI will still be better than the alternative of an increasing array of discriminatory regional and bilateral trade and investment treaties. The private sector in APEC has a strong interest in the success of the MAI, and it should be supporting the transfer of the MAI from the OECD to the WTO. The MAI is likely to provide a useful basis for the seven OECD members of APEC (Australia, Canada, Japan, the Republic of Korea, Mexico, New Zealand and the United States) to link their rules-based

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<sup>2</sup> The rationale for an MAI can be traced to comparatively recent literature (see Bergsten and Graham, 1992; Sauvé, 1994; Brewer, 1995; Lawrence, 1995; Graham, 1996; Brewer and Young, 1995a, b; Rugman, 1997).

<sup>3</sup> On that relevance, see Gestrin and Rugman, 1994, 1996; Graham and Wilkie, 1994; Brewer and Young, 1995c; Rugman and Gestrin, 1996; and Strategico, 1991. On APEC, see Gusinger, 1993; Graham, 1995; and Green and Brewer, 1995.

<sup>4</sup> For a review of the status of negotiations, see Engering, 1997.

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experience with the non-binding APEC investment provisions apparently favoured by some of the eleven non-OECD members of APEC.

## Conclusions

The APEC already has in place a set of procedures which could promote liberalization of investment. Investment is on the regular agenda for APEC because it is a line item in each member's annual individual action plan report and also because of the ground-breaking work of the investment experts group in advocating a set of non-binding investment principles, endorsed by Ministers in 1994. While the Osaka action agenda did not endorse a rules-based approach to investment liberalization, it is inevitable that APEC members will need to consider a deeper form of FDI integration and a rules-based system well before 2020.

The role of FDI and TNCs as engines for APEC economic integration is likely to continue to increase; thus, the more attention APEC can pay to establishing well-known procedures for open FDI, the better. In the future, APEC should consider much more seriously the NAFTA experience with respect to investment. NAFTA demonstrates the need for an integrated approach to international investment issues, in the form of strong rules for FDI. The investment provisions of NAFTA could provide a guide for similar provisions in the MAI and at APEC. ■

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