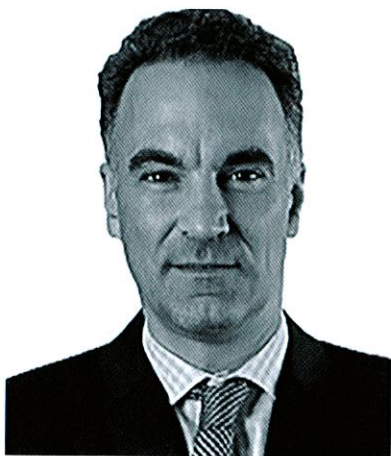


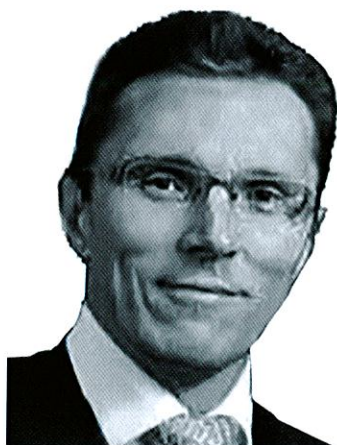
INVESTING IN AN INTEGRATED ASEAN

Australia's role in Asia



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In 2012, the Australian Government issued a comprehensive report seeking to define and guide Australia's role in 'The Asian Century', which tacitly acknowledged that Australia needed to engage more deeply with Asia to take full advantage of the immense growth opportunities.

Despite periods of engagement in the late 1970s and early 1990s, Australian investment flows have largely ignored Asia, as Australian business has looked instead to more culturally aligned markets, such as the UK, USA, Canada and New Zealand, for expansion. While Australian corporations have started to pursue more opportunities in Asia since the turn of the century, outside of Hong Kong and Singapore, the focus has gravitated towards China rather than Asia generally. Ironically, Australian corporations have appeared to have been among the least interested in the profound economic transformations occurring so close to home.

The Association of Southeast Asian Nations (ASEAN) was formed in 1967 by Indonesia, Malaysia, the Philippines, Singapore, and Thailand to promote political and economic cooperation and regional stability. According to the ASEAN Secretariat, at the end of 2012, total Australian foreign direct investment (FDI) into ASEAN totalled USD1.8 billion (representing a mere 1.6% of ASEAN total inbound foreign direct investment). As a result, outside of the mining sector and notable success stories, such as ANZ Bank, the influence of Australian business and financial institutions in ASEAN remains relatively low and nowhere near the level needed for Australia to become a long-term competitive force in the region.

In contrast, the US invested USD11.1 billion in ASEAN in 2012, more than its investment into China, India, South Korea, Hong Kong and Taiwan combined. According to Japan's Ministry of Economy, Trade and Industry, Japan invested USD20.8 billion in ASEAN in 2012, principally directed at long-term strategic infrastructure projects, manufacturing, banking and logistics. Chinese enterprises also continue to invest heavily in energy and power projects in the Lao PDR, Myanmar, Vietnam and Cambodia, as China seeks to secure its energy supply lines.

In the past, there appears to have been some reticence on the part of Australian business to invest in ASEAN due to perceptions of expropriation risk, low profitability, restrictions

on profit repatriation and deficiencies in the rule of law. The exponential increase in investment into ASEAN in recent years, as depicted in Figure 1, illustrates the risk for Australian business in not challenging these persistent views.

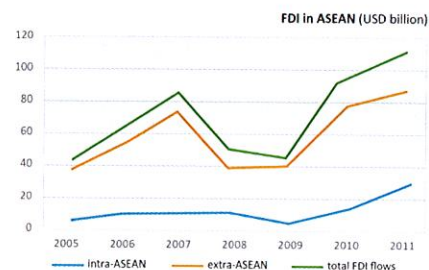


Figure 1: FDI Flow in ASEAN – Significant Growth Story

For many Australian corporations, concentrating investment activities in Australia will continue to be the most appropriate strategy. For many others, ASEAN is one destination that now warrants far greater attention.

ASEAN – The Third Pillar of Asia

ASEAN has one of the world's most dynamic economies. In a world beset by anaemic economic growth and growing debt levels, the ASEAN economies have averaged real annual GDP growth of approximately 6% over the past 15 years. If ASEAN were a single country, it would rank as the world's seventh largest economy – ahead of India – with a combined GDP of USD2.4 trillion in 2013, expected to rise to USD3 trillion in 2015. Collective government debt is less than 50% of GDP, which is considerably lower than any advanced Western economy.

Investing in ASEAN is increasingly seen as an attractive alternative or counterbalance to investing in other parts of Asia, particularly China, where labour and production costs are rising significantly and economic growth is slowing.

Demographics also play a key role in ASEAN's growth prospects. ASEAN countries have a combined population of around 630 million and a median age of only 28. This dynamic demographic not only drives an increasingly productive and affordable workforce but also creates increased domestic demand for goods and services as previously rural populations urbanise and become more prosperous. According to Nielsen, the region currently

SECTOR FDI ANALYSIS



CAMBODIA

ENERGY

- > Open market, high tariffs
- > No national grid
- > Oil & gas, hydro potential

FINANCIAL SERVICES

- > Banking/MFIs highly competitive
- > Insurance growth potential
- > Consolidation opportunities

MINING

- > Gold, bauxite & gem potential
- > Mid-range exploration activities
- > Developing sector

MANUFACTURING

- > Well developed
- > Garments, textile & footwear
- > Minimum wage issues

AGRICULTURE & FORESTRY

- > Rubber, cassava, timber & rice
- > Moratorium on new concessions
- > Attractive incentives

TOURISM

- > Rapid growth
- > Angkor Wat & coastal beaches
- > Border region casinos

REAL ESTATE

- > Phnom Penh & coast
- > Buoyant residential market
- > Commercial development

TELCO

- > Highly competitive
- > High penetration
- > Consolidation opportunities



LAO PDR

HYDROPOWER

- > Net exporter
- > Huge projects
- > Well-developed funding model

FINANCIAL SERVICES

- > Significant growth in financial leasing
- > ANZ a success story

MINING

- > Successful large mines
- > Moratorium on prospecting
- > Significant M&A activity

TRANSPORTATION

- > Railway is key to full development of mining sector
- > G2G discussions continue

AGRICULTURE & FORESTRY

- > Pulp trees, rubber, cassava, bananas & coffee
- > Low productivity

TOURISM

- > Huge growth sector
- > New regulations to be released

MANUFACTURING

- > Growing interest in SEZs on Thai and PRC borders
- > Incentives, cheap labour & energy

LEISURE

- > Casinos & multiplex development
- > Particular interest in border areas



MYANMAR

OIL & GAS

- > Natural gas exporter
- > Recent on/offshore tenders
- > Huge potential

SERVICES

- > Foreigners - no trading (restricted)
- > Underdeveloped
- > ASEAN liberalization

MINING

- > Gold, silver, copper & gems
- > JV required (large scale)
- > New law soon

MANUFACTURING

- > SEZs developing
- > Huge growth potential
- > Japan & Thailand FDI

AGRICULTURE, FORESTRY & FISHERY

- > Livestock, beans & pulses, rice, teak & fisheries
- > No foreign land ownership

TOURISM

- > Big 4 and coast
- > Developing rapidly
- > JV required in most cases

ENERGY & INFRASTRUCTURE

- > Inadequate infrastructure
- > Huge potential

TELCO

- > 2 licences granted (CAPEX)
- > New Telco Law (rules to come)
- > Network rollout underway



THAILAND

ENERGY

- > Complete national grid
- > Natural gas & hydro
- > Open market, high tariffs

FINANCIAL SERVICES

- > Banking/MFIs saturated
- > Insurance growth potential

MINING

- > World top 5 in tin & tungsten
- > Well-developed

MANUFACTURING

- > Textiles, electronics, light manufacturing
- > Large migrant worker population

AGRICULTURE & FORESTRY

- > Rice, rubber, cassava
- > Attractive incentives

TOURISM

- > World's #1 tourist destination 2013
- > Bangkok
- > Islands & beaches

REAL ESTATE

- > Bangkok & coasts
- > Buoyant residential
- > Commercial development

TELCO

- > Saturated
- > Consolidation
- > 3G/4G contract issues



VIETNAM

OIL & GAS

- > Well developed
- > Sovereignty issues
- > State involvement

ENERGY

- > Net importer (coal)
- > Low tariffs, reforming

MINING

- > Rich & diverse minerals
- > Largely undeveloped
- > Political

MANUFACTURING

- > Textiles, garments, electronics & food
- > Highest FDI (Japan)

AGRICULTURE & AQUACULTURE

- > Highly fragmented
- > Rich, coffee & fisheries

TELCO

- > Highly competitive
- > High penetration

FINANCIAL SERVICES

- > Large growth potential
- > Foreign investment caps
- > Cash-based economy

REAL ESTATE

- > Reducing inventory
- > Residential reform

Figure 2:



Figure 3: 7 Steps for a Successful ASEAN Investment.

has a middle class – defined as people with disposable income of USD16 to USD100 per day – of 190 million people. This is expected to more than double by 2020, creating demand for better infrastructure (fuelling investment in mining and construction), telecommunications, education, healthcare, financial services and quality agricultural produce. As ASEAN continues to develop, Australian companies are ideally placed to leverage that growth.

While opportunities will vary across the region, Figure 2 outlines potential sectors of interest in the high growth markets of Cambodia, the Lao PDR, Myanmar, Thailand and Vietnam, as well as some of the key issues currently affecting those sectors.

The Australia-ASEAN-New Zealand Free Trade Agreement (AANZFTA), which came into force in 2010, also offers increased opportunities for Australian business. In addition to guaranteed market access for Australian exporters into ASEAN and reduced tariff rates, the AANZFTA delivers greater certainty for Australian investors with access to international arbitration extended throughout the entire ASEAN region in the event of disputes.

ASEAN Economic Community (AEC) – A Developing Story

ASEAN integration continues apace, highlighted by the eagerly anticipated forging of the ASEAN Economic Community (AEC) at the end of 2015 and the conclusion of the regional comprehensive economic partnership (RCEP) negotiations in 2015, both of which are expected to reduce market barriers in ASEAN further.

The AEC envisions a single market and production base, characterised by the free flow of goods, services, skilled labour and investments and greater access to capital. Creating an integrated production base is

intended to increase ASEAN's competitive edge as a manufacturing hub.

FDI flow within ASEAN has increased dramatically as member states have worked towards closer integration, as illustrated by Figure 1. Many factors can explain the substantial increase in intra-ASEAN FDI, including new investments and the expansion of existing investments, strong M&A activity and an increase in infrastructure and energy investments. Other important contributors include legal and structural reforms and specific integration initiatives, such as the various intra-ASEAN agreements.

The intra-ASEAN agreement that has arguably done the most to improve trade among ASEAN investors is the ASEAN Trade in Goods Agreement (ATIGA). ATIGA aims to reduce customs duties throughout ASEAN to between 0% and 5% for the vast majority of goods by 2010 for Singapore, Indonesia, Thailand, Brunei, the Philippines and Malaysia and a more flexible schedule by 2018 for Cambodia, Laos, Myanmar and Vietnam.

In addition, the ASEAN Framework Agreement on Services (AFAS) provides the legal framework to enable ASEAN member states to lower restrictions on and enhance liberalisation of services within ASEAN. The AFAS framework was designed to require ASEAN member states to provide commitments or liberalise new sectors beyond that which had been provided for under the General Agreement on Trade in Services (GATS). In the context of the AEC, going forward, AFAS liberalisation commitments are intended to be based on the 'AEC Blueprint'.

In the mid and long term, the ASEAN Comprehensive Investment Agreement (ACIA) will, most probably, have the biggest impact on FDI and foreign investors. Indeed, the objectives and the scope of the ACIA, if fully

developed and implemented, would drive the ASEAN investment framework integration to a new level by liberalising and integrating further each ASEAN member state's investment framework (through the creation of one-stop investment centres, streamlined investment procedures and greater consultation with ASEAN business), as well as offering strong protection to foreign investors, both from within and outside ASEAN.

Navigating the ASEAN pathway

Based on our recent extensive experience in advising clients seeking access to ASEAN markets, we have noticed a distinct move towards an investment approach that is less country-specific and much more regionally focused. As a result, new entrants typically assess the regional ASEAN investment framework before deeper analysis of a particular country's legal and taxation framework, in line with the seven step framework in Figure 3.

Amid the optimism, key challenges still remain. In addition to time consuming legal and procedural requirements, cultural diversity and recent geopolitical tensions, the findings of the World Bank's Doing Business 2014 report suggests that challenges persist in accessing (among other things) appropriately skilled labour, essential infrastructure and efficient supply and distribution logistics.

Notwithstanding, ASEAN represents an excellent investment destination for Australian business. The advantages and attractions far outweigh the challenges and the pathway into ASEAN is becoming increasingly well-trodden by Australia's regional competitors. ^a

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