

Growth and the Investment Climate: Progress and Challenges for Asian Economies

Lauren Phillips¹

Summary

Introduction

Sustaining high rates of growth will be one of the main challenges facing Asian governments over the coming years. High investment levels, by both domestic and foreign firms, have contributed to the high growth rates achieved to date. This paper examines the broad set of political, economic, legal and physical conditions – together comprising the investment climate – which are influencing investment decisions in the Asian region.

Main findings

The various components which form the investment climate fall into two main categories: governance and infrastructure. Governance refers to factors such as corruption, legal systems, regulations and competition policy. Infrastructure includes both hard infrastructure (roads, ports, airports, bridges and irrigation systems) and soft infrastructure (telephony and other technologies).

The investment climate varies considerably between Asian countries as well as within countries, between cities, regions and industries. In general, East Asia has implemented more measures considered in line with best practice than South Asia.

Infrastructure constraints – and in particular electricity – are perceived as serious impediments to doing business in Asia. This problem is particularly pronounced in South Asia: in Bangladesh and India, for example, it takes around 80 days to get an electrical connection. A major constraint to public-private partnerships in Asian infrastructure and other investments are perceptions of political, policy and macroeconomic risk.

Regulatory burdens tend to fall disproportionately on micro, small and medium sized enterprises, reducing incentives to invest. Large domestic firms, which are usually in competition with multinational companies, are most affected by issues such as the state of ports and airstrips as well as by tariffs and customs regulations. The investment climate is also central to determining the levels of foreign direct investment (FDI) in Asian economies.

Key research findings

- As agriculture has more impact than any other sector on poverty reduction in Asia, reform efforts focused on the legal, land and regulatory constraints faced by agricultural and rural enterprises will need to be prioritised.
- Reform efforts should also be focused on encouraging investment in infrastructure and reducing regulations which increase the time cost of doing business.
- The international community can encourage investment in infrastructure in Asia through mechanisms designed to enhance reputation and reduce risk (e.g. challenge funds).
- Reform policies formulated in collaboration with interested stakeholders, such as businesses and local and regional governments, have more chance of success.

¹ Lauren Phillips is a Research Fellow at the Overseas Development Institute, London.

- Asian governments will benefit from engaging with other countries in the region, as well as with international institutions, to share insights and experiences on the costs and benefits of different reform strategies.