

Asian Investment in New Zealand

New Zealand Inwards Foreign Direct Investment from Asian Nations

Report to the

Asia New Zealand Foundation

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Preface

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Executive Summary

Over the last 20 years, the amount of Asian outwards foreign direct investment (OFDI) has increased significantly. Asian OFDI stock grew from US\$70 billion and 9% of the world total in 1985, to US\$1,785 billion and 14.3% of the world total in 2006.

Two of the key factors promoting this growth in Asian OFDI have been the wealth created by domestic companies as these economies have developed, and the liberalisation of market and capital controls. As Asian markets are liberalised further, and Asian firms become wealthier, it is likely Asian OFDI will continue to grow.

Data suggest that a considerable portion of Asian OFDI stock is held in other Asian countries. Since the early 1990s there has been a strong and positive correlation between Asian OFDI and Asian inward foreign direct investment (IFDI). At the level of the firm there are a number of Asian companies which have set up production networks throughout Asia, or have invested in other Asian countries to gain access to markets.

Of the additional US\$1,715 billion FDI originating in Asia over the last 20 years, about US\$28 billion, slightly more than 1.5%, has been invested in New Zealand. If Australian data is excluded from the analysis, less than US\$0.5 billion Asian OFDI stock is held in New Zealand. Although the wealthier Asian nations, particularly Japan, Singapore and Hong Kong, were responsible for a reasonable portion of New Zealand IFDI in the early 1990s, the absolute value of New Zealand IFDI from these countries has changed little since then. Similarly, little of the growing OFDI from Taiwan, South Korea, China, Malaysia, India, Indonesia and other Asian nations, over the last five years, has been destined for New Zealand.

Generally, OFDI is motivated by a desire to gain access to a market, or to obtain control over resources. The small number of consumers in New Zealand offers little market opportunity for investing Asian firms. On the other hand, Asian firms have invested in New Zealand to gain control of resources, particularly in forestry and food processing. Another sector in New Zealand which has attracted Asian OFDI is tourism. These areas may attract additional FDI from Asia as Asian economies continue to grow and consumer tastes change.

To encourage Asian FDI to New Zealand care needs to be taken of our reputation as a destination for IFDI. Government intervention in blocking FDI sends the wrong signal to potential investors. Increasing awareness of the possibilities available to Asian investors may help to attract IFDI. Focusing on strengthening the links between Asia and New Zealand in trade and migration will also undoubtedly be of benefit.

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1. Introduction

Inwards and outwards foreign direct investment (FDI) has played an important role in New Zealand's economic development. Foreign companies investing in New Zealand have provided jobs and infrastructure, and have introduced new and beneficial technologies and business practices. By investing offshore, New Zealand firms have improved their efficiency and competitiveness, and have gained access to larger markets.

FDI has also been an important factor in the development of Asian economies. Many Asian nations, more commonly associated with inwards foreign direct investment (IFDI), are also undertaking considerable outwards foreign direct investment (OFDI). The flow of Asian OFDI grew steadily through the 1980s and 1990s, and has increased rapidly since 2003. However, very little Asian OFDI stock is in New Zealand. Excluding IFDI from Australia, in 2007 less than 5% of New Zealand IFDI stock was from Asia.

The paper considers New Zealand IFDI from Asian nations. The first section outlines the scope of the paper: purpose, coverage and data sources used. The next section examines the data on Asian OFDI. Section 3 considers New Zealand IFDI from Asian countries, and section 4 discusses the determinants of FDI. Section 5 looks at government involvement in FDI, and section 6 summarises the key findings of the paper.

For the purpose of this paper, Asia includes Australia, Brunei, Cambodia, China, Hong Kong, India, Indonesia, Japan, Korea, Laos, Malaysia, Myanmar, Pakistan, the Philippines, Singapore, Taiwan, Thailand and Vietnam. In the section on New Zealand IFDI, Australian OFDI is considered separately from OFDI from other Asian countries, due to the relatively large share of Australian FDI in New Zealand. The following analysis excludes independent investment in real estate, which is often for non-business purposes.

The data used in this report has been sourced for the most part from the United Nations Conference on Trade and Development (UNCTAD) and Statistics New Zealand. While these are both reliable sources of data, there are a number of factors which can lead to FDI data being under-stated or over-stated. These factors are discussed further in Appendix A.

2. Asian OFDI

From the mid 1980s the stock of world FDI steadily increased, reaching US\$12,474 billion in 2006, almost 16 times greater than 1985 values (total OFDI). Developed economies have been responsible, as both sources and destinations, for the vast majority of the world's FDI. However, from the mid-1980s Asia started first receiving, and then providing, a growing portion of world FDI.

Asian OFDI stock grew from US\$70 billion, 9% of the world total, in 1985, to peak at US\$739 billion, 19.8% of the world total in 1997. In 2003 a downward trend in Asian FDI flows reversed, and by 2006 Asian OFDI stock had reached US\$1,785 billion, 14.3% of the world total. See Figure 1 and Figure 2, page 6.

Figure 1, page 6 displays aggregate Asian outwards and IFDI flow and stock.

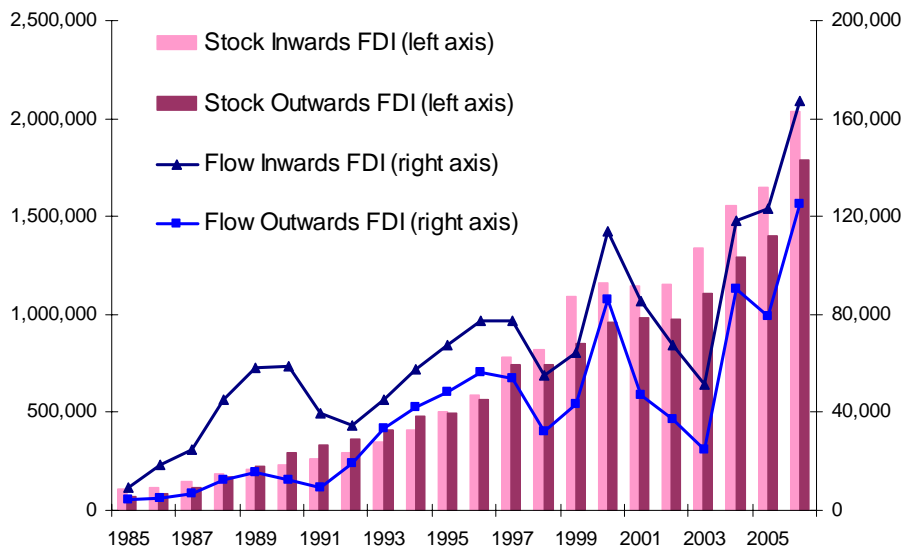
From 1985 to the early 1990s there was noticeable variance between inwards and outwards Asia FDI flows, relative to the following periods. The much smaller Asian inflow than outflow in the 1980s suggests that a reasonable portion of Asian IFDI came from outside the Asian region. The strong correlation between inwards and outwards flows from the 1990s is probably due to a growing share of Asian IFDI originating elsewhere in Asia. However, channelled and re-cycled FDI, as when capital passes through one Asian country before being invested in another Asian country, double-counts some of this FDI, strengthening the observed correlation.

Apparent in Figure 1 there is a period of very little change in outwards or IFDI stock, and a decrease in FDI flows. This corresponds to the years immediately after the Asian financial crisis in the 1990s. Anecdotal evidence suggests that over this period there may have been a shift in investment, with some Asian companies moving investments to non-Asian countries, and US and European based firms taking advantage of weak currencies and cheap assets to invest in Asia.¹ However, there is no indication in the data that this was the case for New Zealand. OFDI from most Asian nations to New Zealand decreased in the years immediately after the Asian financial crisis.

¹ Urata, S 2002. Japanese Foreign Direct Investment in East Asia with Particular Focus on ASEAN4

Figure 1 Asian aggregate inwards and outwards FDI stock and flow

Value of Asian aggregate inwards and outwards FDI stock US\$ million

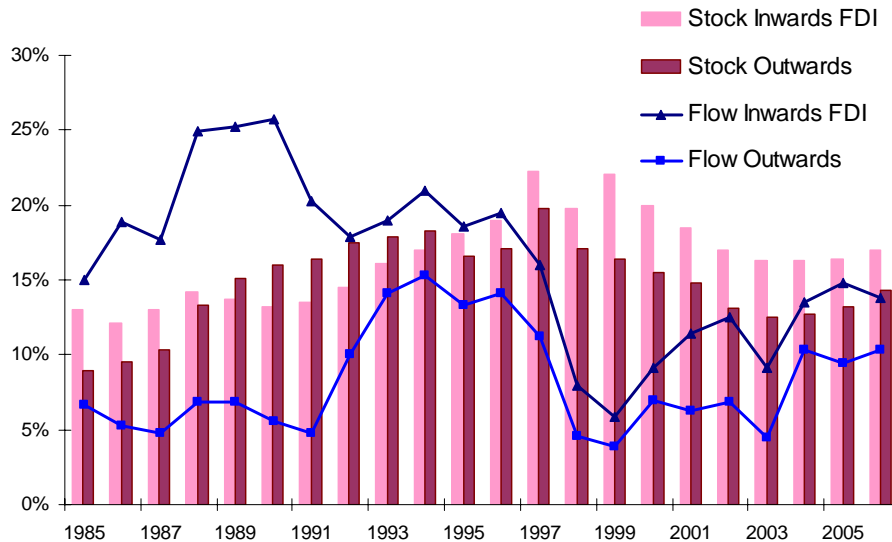


Source: UNCTAD FDI database, NZIER calculations

Note : Asia includes Australia, Brunei, Cambodia, China, Hong Kong, India, Indonesia, Japan, Korea, Laos, Malaysia, Myanmar, Pakistan, the Philippines, Singapore, Taiwan, Thailand and Vietnam

Figure 2 Asian aggregate inwards and outwards FDI stock and flow as share of world total

Value of Asian aggregate inwards and outwards FDI stock as share of world total



Source: UNCTAD FDI database, NZIER calculations

Note: Asia includes Australia, Brunei, Cambodia, China, Hong Kong, India, Indonesia, Japan, Korea, Laos, Malaysia, Myanmar, Pakistan, the Philippines, Singapore, Taiwan, Thailand and Vietnam

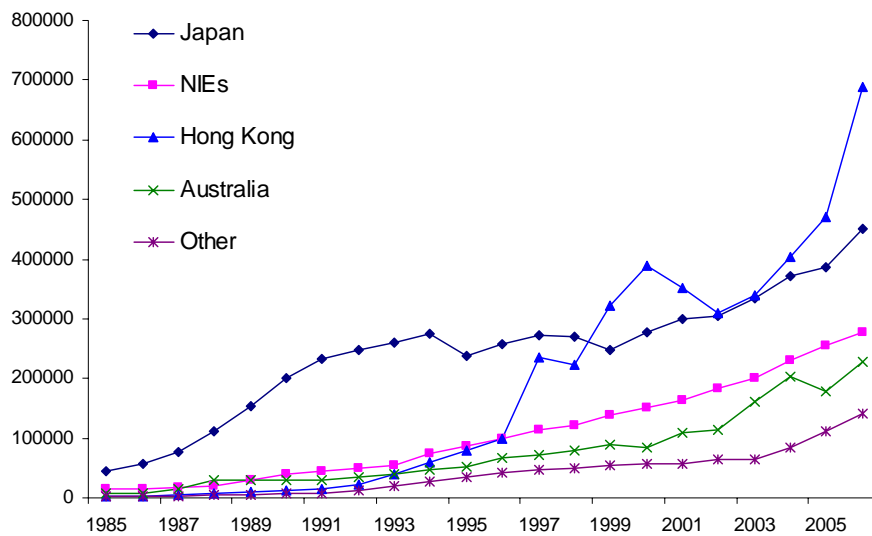
2.1 Japan and the Newly Industrialised Economies

The increase in Asian aggregate OFDI from the mid 1980s, up until the mid 1990s, was largely due to the influence of Japan's OFDI on the Asian total. Japan was the first of the Asian economies to undertake significant outwards FDI. In 1985 Japan held US\$44 billion in outward FDI, 64% of the Asian total. Although Japanese OFDI growth was patchy through the 1990s, by 2006 the value of Japan's OFDI had increased to US\$450 billion. Interestingly, even though the absolute value of Japan's OFDI was 10 times greater in 2006 than it was in 1985, Japan's share of Asia total OFDI decreased from 64% to 25%, over this 20 year period.

Growth of OFDI from the newly industrialised economies (NIEs) of Asia, lagged Japan's by a few years. In 1985 Singapore, South Korea and Taiwan collectively had US\$15 billion in OFDI stock.² By 2006, the combined OFDI of Singapore, South Korea and Taiwan had increased 18 fold to US\$278 billion. Over the same period of time, from 1985 to 2006, the value of Hong Kong's OFDI increased 294 times, primarily due to the influence of FDI to China.

Figure 3 Asian OFDI stock by source country or group of Asian countries

Value of OFDI stock by source country or group of countries, US\$ million



Source: UNCTAD FDI database

By 1999, Hong Kong appears to have taken over as the Asian nation with the largest stock of OFDI, (see Figure 3). However, these data should be interpreted with caution. From the mid 1990s a considerable amount of China's IFDI was channelled through Hong Kong. Capital originating from a number of countries was sent to Hong Kong, and then onwards to China as FDI. The simultaneous

² Hong Kong is considered separately from the other NIEs (Singapore, South Korea and Taiwan) due to the significant influence of capital flows to and from China on Hong Kong's recorded FDI.

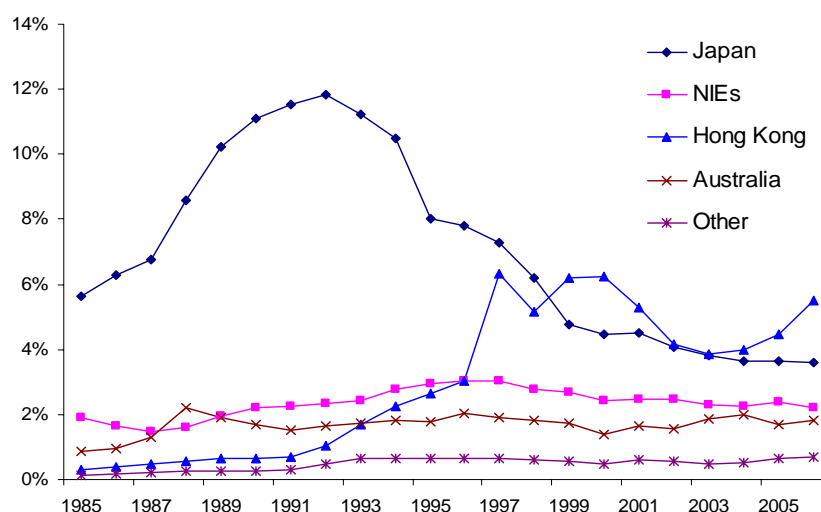
increase in both inwards and outwards Hong Kong FDI supports this claim. In the 10 years to 2006, inwards and outwards Hong Kong FDI increased by US\$689 billion and US\$589 billion respectively.

Figure 4 displays the same OFDI stock data as above in Figure 3, relative to world OFDI stock. This clearly shows the dominance of Japan among Asian countries, as a source of outwards FDI in the late 1980s and 1990s. The NIEs were also important source countries for FDI.

Two of the key factors promoting Japan and NIE OFDI during this period were the wealth which had been created by domestic companies as these economies developed, and the liberalisation of capital controls.

Figure 4 Asian FDI stock by source country, or group

OFDI stock by source country or group of countries, share of world total



Source: UNCTAD FDI database, NZIER calculations

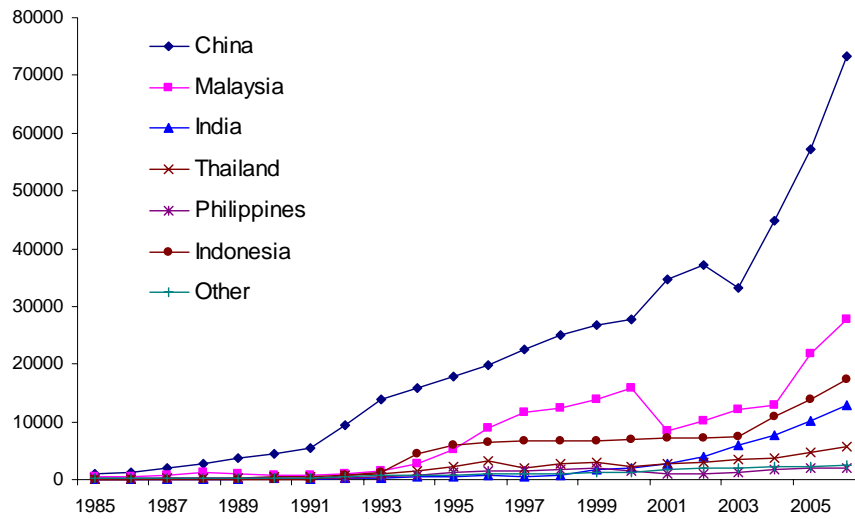
2.2 Other Asian economies

Figure 5 displays FDI data separately for the group of countries displayed collectively as “other” countries in Figure 3 and Figure 4. Although the value of OFDI stock held by these countries is small relative to that held by the countries shown individually in Figure 3 and Figure 4, it is worth noting that in a number of these “other” countries, OFDI has recently increased substantially. The key feature apparent in these data is the rapid growth in FDI from China since 2003. China’s outwards flow of FDI in 2006 was 17 times greater than in 2000, and the country’s stock of OFDI more than doubled between 2000 and 2006.

Part of the reason for the observed growth of China OFDI in absolute terms is simply that China is a large country. When measured per capita, OFDI from Thailand is 1.4 times larger than OFDI from China, and OFDI from Malaysia is 20 times larger than OFDI from China.

Figure 5 Asian OFDI stock, 'other' countries

Value of OFDI stock by source country US\$ million



Source: UNCTAD FDI database

Along with the increasing wealth of Chinese companies, government policies encouraged Chinese OFDI. In 2000, China launched a 'go global' strategy to promote OFDI. The government relaxed controls on the movement of capital and simplified administration procedures. This appears to have encouraged some OFDI from private enterprises. However, the main benefactors, and contributors to China OFDI have been State-Owned-Enterprises (SOEs). The ten largest Chinese enterprises in 2006, as measured by OFDI, were all SOEs.³

Figure 5 shows that the OFDI stock from each of Malaysia, Indonesia and India have all steadily increased from the early 2000s. Like the countries discussed already, this growth in OFDI coincided with increasing levels of wealth of domestically based firms, and relaxation of capital controls.

The data very clearly show significant increases in OFDI from many Asian nations over the last 20 years. Between 1985 and 2006, Asian aggregate OFDI increased 29 fold, by US\$2,928 billion. However, from 1993 (when Statistics New Zealand data are available) to 2006 the value of non-Australian New Zealand IFDI changed little.

³ OECD Investment News 2008 <http://www.oecd.org/dataoecd/28/10/40283257.pdf>

3. New Zealand Inwards FDI

Although OFDI from Asia has grown significantly over the last 15 years, New Zealand IFDI from non-Australian Asian nations appears to have changed little. The growing significance of Asia as a source of New Zealand IFDI since the 1990s is almost solely due to the influence of capital flows from Australia. The small amount of non-Australian Asian FDI outflow to come into New Zealand has primarily come from the more developed economies of Asia, particularly Japan, Singapore and Hong Kong.

From 1984, New Zealand FDI was encouraged with a range of policies, including deregulation of the financial sector, abolishment of exchange controls, and removal of barriers to entry in banking and stock-broking.⁴ In the early 1990s there were large inflows of FDI to New Zealand, as State-Owned-Enterprises were privatised, and foreign companies took advantage of the new laws governing investment. Between 1985 and 1996, New Zealand inward stock of FDI increased 17 times to US\$35 billion, before decreasing to US\$21 billion in 2001.

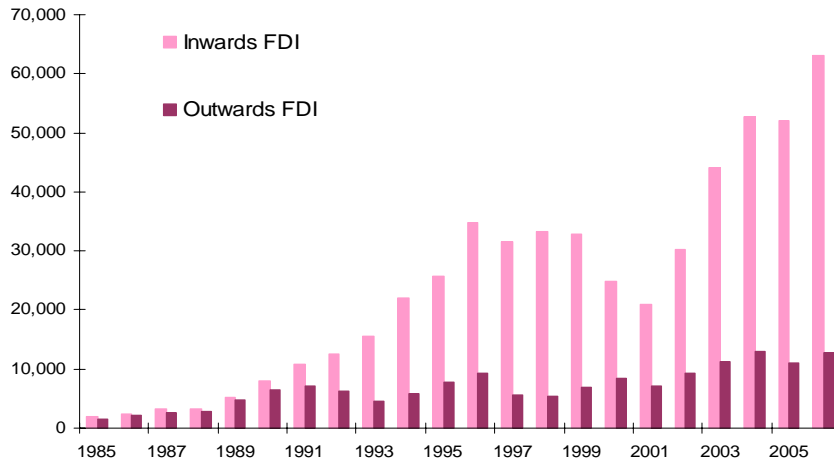
New Zealand inwards and outwards FDI stock are shown in Figure 6. Compared with the equivalent Asian aggregate data in Figure 1, there is a large difference in the value of New Zealand outwards compared to inwards FDI. In 2006, New Zealand's inwards stock was 5 times the value of OFDI stock.

The amount of domestic capital available in New Zealand is limited due to the small size of the economy, hence the country is relatively reliant on foreign sources of capital. Domestic capital alone, has not been enough to fund some of the country's larger investments. Our inwards FDI stock as a portion of GDP is similar to other small OECD economies. OFDI is also restricted by the small New Zealand market and the limited number of large New Zealand Trans-National Corporations (TNCs).

⁴ OECD 2001 Reviews on Foreign Direct Investment: New Zealand

Figure 6 New Zealand FDI stock

Value of New Zealand inwards and outwards FDI stock in NZ\$ million

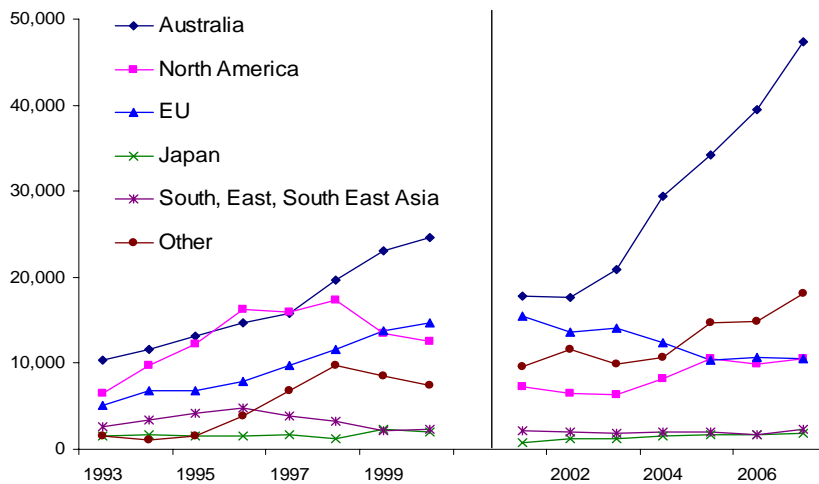


Source: UNCTAD FDI database

Figure 7 displays New Zealand IFDI stock by Asian country source. The split in the chart indicates the change in how Statistics New Zealand recorded FDI. Up until March 2000, investment resulting in foreign ownership of 25% or more of an asset, was recorded as FDI. From 2001 investment consisting of 10% or more ownership, was recorded as FDI. As such, although a good indication of the changing New Zealand IFDI sources, and their significance, the series are not directly comparable.

Figure 7 New Zealand inwards FDI stock by source

Value of New Zealand IFDI stock in NZ\$ million by source country



Source: Statistics New Zealand

It is clear from the chart that IFDI from Australia has been growing in significance, particularly since 2003. In 2007, over 50% of the IFDI stock in New Zealand originated from Australia. FDI from other Asian nations was comparably

insignificant. Japan and all other Asian nations respectively accounted for 2% and 2.6% of New Zealand IFDI stock.

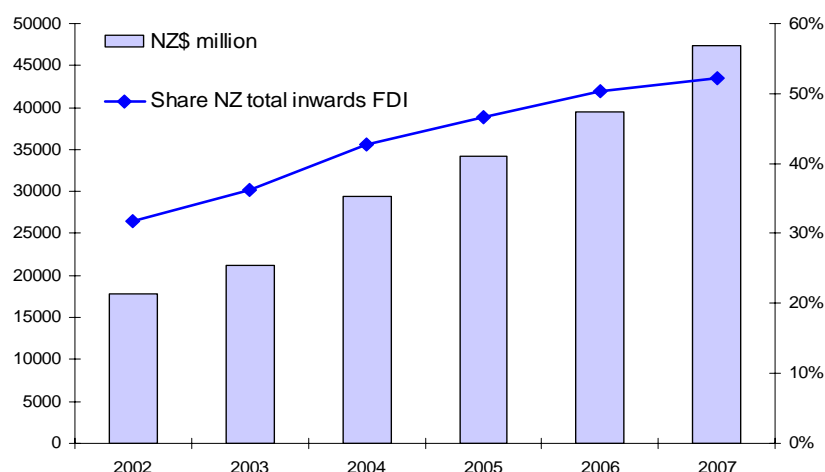
3.1 Australia

Since the liberalisation of New Zealand markets in the mid 1980s, Australia has been the single most important source of New Zealand IFDI. Of the 30 largest affiliates of foreign TNCs in New Zealand in 1999, 14 had head offices in Australia.⁵ These firms are spread throughout the New Zealand economy in industrial, tertiary and primary sectors.

In theory, one of the most important features for the relatively large amount of Australian New Zealand FDI is the proximity of the two countries. Generally, firms invest in neighbouring countries when they first undertake FDI. This is true of firms right across Asia. Also encouraging Australian firms to invest in New Zealand are the similar cultures and business climates.

Figure 8 New Zealand Inwards FDI stock from Australia

New Zealand IFDI stock from Australia, value in NZ\$ million and share of New Zealand total



Source: Statistics New Zealand, NZIER calculations

Another factor encouraging FDI flows between New Zealand and Australia from the early 1980s was the Closer Economic Relations Trade Agreement (CER) entered into by the two countries. The CER Trade Agreement came into force on 1 January 1983, to encourage the flow of merchandise, services, labour and also investment between the two countries. As part of the CER, the investment regimes of both countries have been adapted so that most investment proposals do not need approval from their respective investment authorities. Over the last ten years neither country has rejected an investment proposal from the other country.⁶

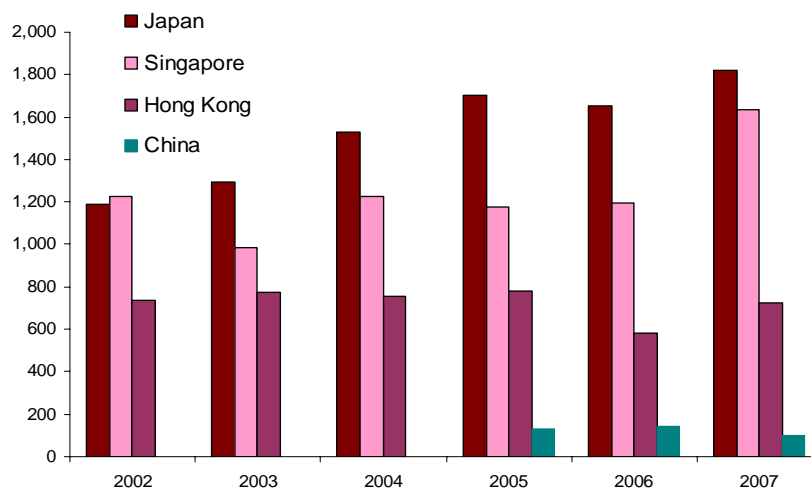
⁵ UNCTAD country profile: New Zealand 2005

⁶ The New Zealand Ministry of Foreign Affairs. The Australia New Zealand Closer Economic Relations (CER) Trade Agreement

3.2 Other Asia

Figure 9 New Zealand inwards FDI stock by source: non-Australia Asia

New Zealand IFDI from selected Asian countries, value in NZ\$ million



Source: Statistics New Zealand, NZIER calculations

3.2.1 Japan

In 2007, of the non-Australian Asian nations Japan held the largest stock of New Zealand IFDI. In 1999, Japan was the home economy of four of the 30 largest affiliates of TNCs in New Zealand.⁷ Since 2001, the flow of FDI from Japan to New Zealand has been positive each year and, in 2007, Japanese companies held NZ\$1.8 billion New Zealand IFDI stock.

Japanese OFDI to New Zealand has been mainly into the tertiary sector. Of the five largest New Zealand affiliates of Japanese TNCs in 1999, three were classified as Tertiary, Automotive Trade and Repair, and one was classified as Tertiary, Other Business Activities. The fifth operated in the Finance and Insurance sector. Also worth noting is the investment by Japanese firm Sumitomo Chemical Company in New Zealand Aluminium Smelters in 1994.

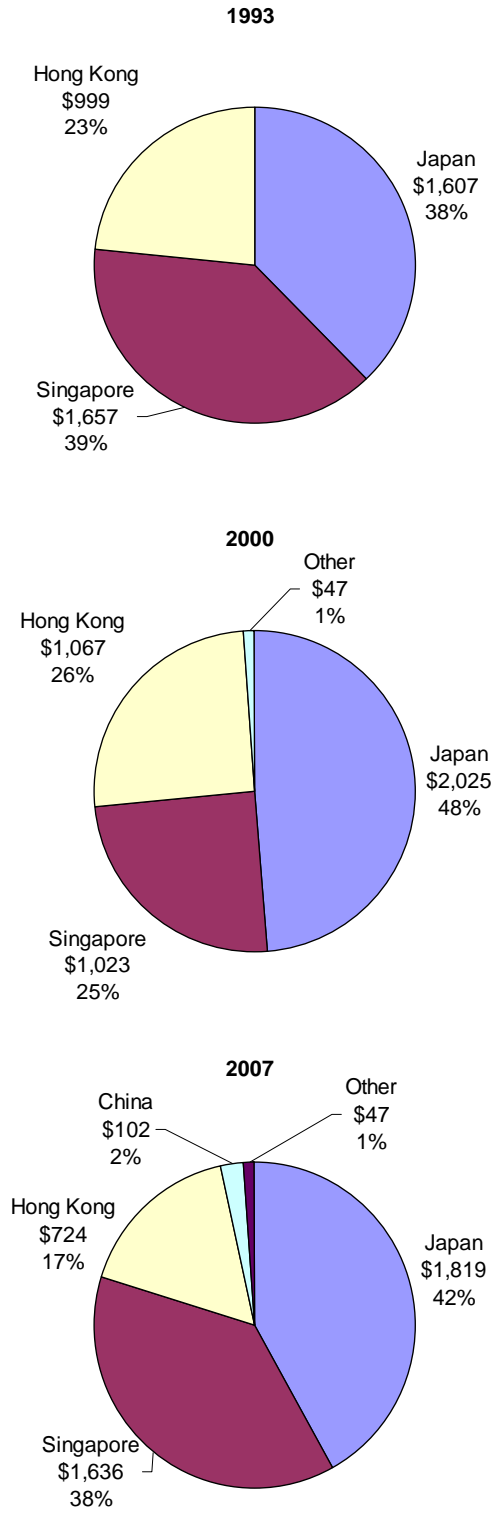
3.2.2 Singapore, Taiwan and South Korea

In the early and mid 1990s, Singapore held more New Zealand IFDI stock than any other non-Australian Asian economy, including Japan. This had changed by 2000, see Figure 10, page 14. In 2007, Singapore was the source country of NZ\$1,177 million New Zealand IFDI, the second largest amount of non-Australian Asian New Zealand IFDI, as can be seen in Figure 9, page 13.

⁷ UNCTAD country profile: New Zealand 2005

Figure 10 Non-Australian Asian New Zealand inwards FDI stock 1993, 2000 and 2007

New Zealand IFDI from non-Australian Asian countries, NZ\$ million and by share of New Zealand non-Australian Asian total



Source: Statistics New Zealand, NZIER calculations

It is possible that other Asian New Zealand FDI is included as Singapore New Zealand FDI. A number of TNCs from around Asia have installed head offices in Singapore, to take advantage of lower tax rates and other country specific benefits. Many Indian companies especially have head offices in Singapore. FDI flow from a company based in Singapore will be recorded as Singapore FDI, regardless of where that company originated.

Statistics New Zealand data show that there has been New Zealand IFDI stock from Korea and Taiwan over the last 5 years, although the value of investment has been kept confidential. Non-confidential Statistics New Zealand data show that in 1999 there was NZ\$2 million FDI stock in New Zealand from Korea, and NZ\$21 million from Taiwan.

Singapore investment has been mainly in the service industries. Taiwan and South Korea investment in New Zealand has been mostly in tourism, timber, and food processing, while Taiwanese investment in New Zealand is for the most part in relatively small-scale niche investments.⁸

3.2.3 Hong Kong and China

The value of Hong Kong FDI stock in New Zealand appears to have decreased slightly since 1993. In 2006, Hong Kong companies held NZ\$724 million New Zealand IFDI stock, down from NZ\$999 million in 1993. In April 2008, Hong Kong's Cheung Kong Infrastructure Holdings announced it would purchase Vector's Wellington electricity network for NZ\$785 million, resulting in an almost overnight doubling of the value of Hong Kong IFDI stock in New Zealand.⁹

The values of most flows and stock of China OFDI are confidential, but Statistics New Zealand released data showing NZ\$15 million of FDI flowed from China to New Zealand in 2005. In 2005, China FDI stock in New Zealand was NZ\$129 million, approximately 0.18% of New Zealand total IFDI stock.

Chinese FDI in New Zealand appears to be largely in the forestry and construction sectors. In 2007, Chinese firm Wenita Forestry Limited owned NZ\$31 million in net assets in New Zealand.¹⁰ There are a small number of large construction firms owned, or part owned, by Chinese investors, in New Zealand, such as Richina.¹¹

⁸ Gupta, S 2003. Investment New Zealand. Asian Foreign Direct Investment: Taiwan

⁹ The National Business Review. April 28, 2008 Vector's Wellington network sold for \$785 million

¹⁰ Wenita Forestry limited company accounts 2008, from New Zealand Companies Office

¹¹ New Zealand Companies Office

3.3 Sectors where Asian firms invest in New Zealand

Table 1 Industry of non-Australian Asian investment in New Zealand 2002 / 2003

	Japan	Singapore	S. Korea	Taiwan	China	Malaysia
Finance	X					
Leisure / tourism		X	X	X		
Automotive	X					
Retail		X				
Construction		X			X	
Beverages	X	X				
Industrial	X					
Food processing	X		X	X		X
Seafood	X		X			X
Forestry / timber	X		X	X	X	X
Horticulture						X
Hides / skins			X			

Source: Derived from Gupta. S 2003. Asian Foreign Direct Investment: Investment New Zealand Working Papers, NZIER

As can be seen in Table 1, forestry is a common area for investment for nearly all of the countries discussed above.¹² Services are often the common sector for investment by the more developed of the Asian economies. Singaporean, South Korean and Taiwanese firms all have New Zealand holdings in leisure and tourism, including interests in hotels and golf courses. Japanese companies have also invested in the financial sector.

¹² Data on Hong Kong were not available

4. Discussion

These data show that Asian OFDI grew steadily through the 1980s up until the Asian financial crisis. Since 2003, Asian aggregate OFDI has been growing rapidly. During a period of increasing world FDI, the Asian share of the world total has been increasing. Underlying this has been the increasing wealth of Asian firms, as their home economies develop, and the liberalisation of controls over capital movement in Asia.

Asia has grown in significance as the source of New Zealand IFDI since the early 1990s, and particularly since 2003. However, removing Australia from this analysis, New Zealand IFDI from Asia has increased only slightly since 1993.

4.1 Determinants of FDI

Generally speaking, FDI takes place for two main reasons:

- Efficiency seeking – investment is undertaken to take advantage of low cost inputs to production, particularly labour
- Market seeking – investment is undertaken to gain better access to the destination country's markets.

Resource seeking, investment to gain access to resources, could be added as a third category, although it is, strictly speaking, a form of efficiency seeking.

4.1.1 Efficiency seeking

A considerable amount of non-Australian Asian resource or efficiency seeking New Zealand IFDI has been in forestry and associated products, and in food processing.

Asian demand for forestry and related products is likely to increase with growing populations and incomes. Increased demand for the end products may encourage more investment in this industry in New Zealand.

Most of the investment in forestry to date has been through mergers and acquisitions (M&A) of existing forests. Most of the land which is suitable for planting has already been planted, leaving little opportunity for new green-field investment. Future investments in forestry will likely follow a similar pattern, transferring ownership of existing assets rather than, of more economic benefit, creating new ones.

Of possibly greater benefit to New Zealand and investing Asian companies, is the comparative advantage New Zealand has in wood and wood processing technology. Ministry of Agriculture & Forestry(MAF) suggest that there has been some substantial investments in the top end production of this market, as firms

look to add value to wood and wood products.¹³ Asian investors may benefit from accessing this technology through New Zealand investments. New Zealand firms could benefit substantially from gaining exposure and access to large and growing markets.

Asian investment in the food processing sector is generally done to guarantee the investing company supply and quality of food products. Behind the growing Asian demand for the food produced in New Zealand are the changing tastes of many Asian consumers. The consumption of dairy products in China, for example, nearly doubled in the 5 years to 2007. Typically, demand for protein and dairy products increases with wealth, suggesting Asian demand for New Zealand food-stuffs will continue to increase. This demand may influence FDI.

Food processing FDI has both immediate and longer term benefits to New Zealand. The immediate benefit is a market for New Zealand goods. A longer term benefit is the facilitation of access to global distribution networks such investment brings. Food technology is also an area where New Zealand holds some comparative advantage. IFDI in food technology may further improve this comparative advantage and provide more markets for product development.

4.1.2 Market seeking

The majority of New Zealand IFDI stock is market seeking. A 2001 Boston Consulting Group report suggested that up to 85% of New Zealand inflow of FDI are in either the non-tradable sector, or otherwise orientated towards the domestic market.¹⁴ Many of the large New Zealand enterprises in telecommunications, banking, transportation and other areas, are owned by foreign investors.

It is unlikely that many firms will undertake new greenfield investment to gain access to New Zealand markets. The new opportunities that our markets provide tend to be in niche areas, rather than big operations suitable for large-scale investment. Large scale manufacturing is not practical here, due to the relatively high costs of labour, and limited opportunities for economies of scale. FDI is sometimes used to circumnavigate trade barriers; however, this is for the most part not the case in New Zealand.

Tourism is an area where new market seeking FDI may be attracted to New Zealand. Singaporean companies already own a number of hotels in New Zealand. The other NIEs also have investments in New Zealand tourism and leisure. As more Asian economies develop, and diversify away from manufacturing and more towards services, this area may attract more Asian IFDI.

¹³ MAF 2003, contribution of land based industries to New Zealand's economic growth <http://www.maf.govt.nz/mafnet/rural-nz/profitability-and-economics/contribution-of-land-based-industries-nz-economic-growth/>

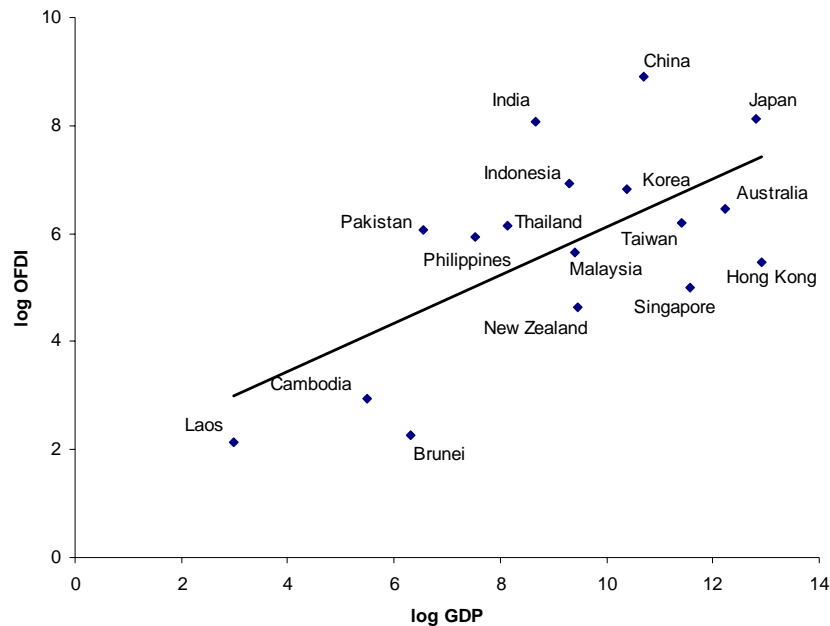
¹⁴ The Boston Consulting Group 2001 Building the Future

4.1.3 Other factors

Intuitively, as a nation gets richer, so too do the firms operating in that economy. This provides the capital for expansion off-shore. The relationship between OFDI and the GDP of 17 Asian nations is shown in Figure 11.¹⁵

Figure 11 Log GDP and Log OFDI with trend line for 17 Asian nations

2003 or 2004 Log total GDP and log total OFDI with trend line for 17 Asian nations.



Source: UNCTAD FDI database, Penn World Tables, NZIER calculations

Short and medium term GDP growth in non-Japan Asia is predicted to average over 5% per annum in the short to medium term.¹⁶ GDP growth in China and India is expected to grow at around 8% per annum until 2013.¹⁷ As these economies grow, the value of their OFDI is very likely to increase. As noted above, as these economies develop the pattern of their OFDI may also change.

Another factor which influences the foreign investment decisions of a company is the distance between the FDI destination and source countries. As noted above, firms tend to expand into neighbouring markets when they first undertake FDI. There is empirical evidence on Asian investment patterns supporting this theory.¹⁸ This is probably a key factor explaining the high involvement of Australian investors in New Zealand.

¹⁵ This chart seeks to establish that a relationship does exist rather than

¹⁶ NZIER Quarterly Predictions June 2008

¹⁷ NZIER ibid

¹⁸ Hiratsuka. D 2006 Outward FDI from and Intraregional FDI in ASEAN: Trends and Drivers.

Although being on the periphery of Asia, New Zealand may be able to take advantage of being the closest country to most of Asia to specialise in the sectors where we have comparative advantage.

One of the other catalysts of OFDI from many Asian economies was the liberalisation of capital controls and markets. This both enabled and encouraged FDI. The last section of this report discusses the role of governments in FDI.

5. The role of Government in FDI

5.1 Agreements

New Zealand is involved in a number of Free Trade Agreements (FTAs) with other Asian nations. FTAs tend to encourage FDI directly, by establishing the rules of cross-border investment, and indirectly, by promoting market growth and development.

New Zealand is involved in the following Asian FTAs:¹⁹

- Australia and New Zealand Closer Economic Relations (CER) - 1983
- New Zealand and Singapore Closer Economic Partnership (NZSCEP) - 2001
- New Zealand and Thailand Closer Economic Partnership (NZTCEP) - 2005
- Trans-Pacific Strategic Economic Partnership (Trans-Pacific SEP) - 2005
Brunei/Chile/New Zealand/Singapore
- New Zealand-China Free Trade Agreement (NZ-China FTA) - 2008

Other Asian agreements currently under negotiation or consideration are:

- ASEAN-Australia/NZ Free Trade Agreement
- New Zealand and Malaysia Free Trade Agreement
- New Zealand and Hong Kong Closer Economic Partnership
- New Zealand and India Free Trade Agreement
- New Zealand and Korean Free Trade Agreement
- New Zealand and Japan feasibility study of a Closer Economic Partnership

New Zealand has double tax agreements with Australia, China, India, Indonesia, Japan, South Korea, Malaysia, the Philippines, Singapore, Taiwan and Thailand.²⁰

¹⁹ MFAT Trade Agreements website

²⁰ The New Zealand Inland Revenue Department. <http://taxpolicy.ird.govt.nz/international/DTA/index.html>

5.2 Government policies

Many governments of developing Asian economies have liberalised capital account transactions, foreign ownership, and foreign exchange policies, to encourage FDI. There are a number of Asian countries which have actively sought FDI by offering tax breaks and other forms of assistance to foreign companies looking for somewhere to invest. OFDI from some Asian nations has also been encouraged through financial and fiscal incentives, as well as other forms of assistance.

The New Zealand government has also offered subsidies and tax breaks to attract FDI to New Zealand. Although recently some of these policies were assessed as providing only modest success and hence discontinued.²¹

On 30th August 2007, the Minister for Economic Development, Trevor Mallard noted that New Zealand's stock of IFDI was similar to other small developed economies when measured as a share of GDP. However, he also expressed concern at the low levels of New Zealand OFDI stock. In response the Government is changing focus from assisting foreign firms wanting to invest in New Zealand to assisting New Zealand firms investing offshore.

This is not to say that all policies to attract IFDI will be scrapped. In some areas, such as biotechnology and screen production, assistance is continuing, or even increasing.

How government policies have influenced previous Asian FDI flows to New Zealand, and how discontinuing them would influence future flows, is not clear. Such policies are only one of a number of factors considered by potential investors. It is probable that any likely changes in policy will have only a small, if any, effect on New Zealand IFDI from Asia. Other factors, of more importance, identified previously are efficiency seeking, market seeking, the growth of Asian home economies and the liberalisation of controls over capital investment in Asia.

5.2.1 The New Zealand FDI environment

In many ways New Zealand appears an attractive destination for IFDI. As discussed above, from the mid 1980s, the laws governing FDI were relaxed. New Zealand constantly ranks highly as one of the easiest countries in the world to start and run a business.²² New Zealand rates well with regards to capital controls, political stability and exchange rate conversion.²³

Governance issues may have made New Zealand a less attractive destination for IFDI. While some researchers suggest the quality of New Zealand's infrastructure,

²¹ Cabinet Economic Development Committee 2007. Internationalisation and Investment

²² Doing Business <http://www.doingbusiness.org/economyrankings>

²³ Boston consulting Group. 2001. Building the Future

in particular in energy supply, hampers New Zealand IFDI²⁴ this effect may be over-stated as electricity supply is generally stable.

More concerning for potential investors is government intervention to prevent IFDI. In 2008 the New Zealand government stopped a Canadian Investment fund from purchasing a 40% stake in Auckland International Airport Limited. The government claimed it intervened to prevent foreign ownership of 'strategically important' infrastructure. Although, some assets which seem strategically important may not be deemed so by the government. There was no intervention to stop the sale of Vector to a foreign buyer only a few weeks after the Auckland International Airport deal was prevented. Such government intervention sends an un-welcome signal to potential investors.

Moreover, for international investors interested in owning and managing essential facilities like electricity and gas distribution, telecommunications, ports and airports, the somewhat idiosyncratic regulatory regime relating to monopolies may have acted as a barrier. Some potential investors have undoubtedly concluded the costs of understanding the New Zealand regime outweighed the potential returns from doing so, given the small size of the New Zealand economy and hence the comparatively small size of such businesses in this country. This is not to say the regulatory regime has not been the right one for New Zealand. The point is that it being tailored for New Zealand's small size and conditions has probably inhibited international investment in essential facilities.

6. Summary

Asian aggregate OFDI has been trending up since 2003. Most of the more developed Asian economies are steadily increasing their share of world OFDI. A number of following economies, China especially, have been rapidly investing off-shore. This trend looks set to continue as Asian companies become wealthier, and markets are further liberalised.

The Asian companies which, to date, are responsible for the lion's share of New Zealand IFDI all originated in the more developed economies of Asia. Australia holds over half of New Zealand IFDI stock. Companies from Japan, Hong Kong and Singapore all own reasonable amounts of New Zealand's FDI stock. The dominance of Australia as a source of New Zealand IFDI is probably largely due to proximity. The relative wealth of Japan and the NIEs undoubtedly explains why firms from these countries, rather than other less developed Asian nations, have so far invested in New Zealand.

It is almost certain that more OFDI will come from developing Asian countries as they become wealthier and some of this FDI may be attracted to New Zealand. There is already Asian investment in forestry and food processing sectors. This is an area which could potentially attract more investment. Our tourism market has

²⁴ See for example Castalia 2006. Foreign Direct Investments Effects.

attracted investment from a number of more developed Asian economies. This is possibly an area where other, still developing, Asian economies may invest in the future.

To encourage Asian FDI into New Zealand care needs to be taken of our reputation as a destination for IFDI. Government intervention in, on some occasions, blocking FDI and other occasions accepting FDI sends the wrong signal to potential investors. Increasing awareness of the possibilities available to Asian investors may help to attract IFDI. Focusing on strengthening links between Asia and New Zealand in trade and migration will also undoubtedly be of benefit.

Appendix A A note on FDI data

The data used in this report has been sourced largely from the United Nations Conference on Trade and Development (UNCTAD) and Statistics New Zealand. While these are both reliable sources of data, there are a number of factors which can lead to FDI data being under or over-stated:

- not all forms of FDI are reported
 - FDI includes new foreign equity flows, intra-company debt transactions, and reinvested earnings. It is not uncommon for only new equity flows to be reported as FDI
 - the value of a considerable amount of New Zealand IFDI is not made publically available due to confidentiality reasons.
- planned rather than actual FDI is sometimes reported
 - departments measuring IFDI often record planned investments by foreign entities, rather than actual FDI flows.
- FDI stock can fluctuate when there is no real change to FDI
 - FDI stock measures the value of an asset at a point in time, and can change if a different valuation method is used, or with depreciation, when there is no actual change in FDI.
- the source or destination country of FDI is not always the same as the source of the capital or the final destination of the investment
 - FDI can be sent from one country to another via a third country. As an example, capital originating in China may be sent to Hong Kong, and then sent back to China as FDI. Some commentators suggest this accounts for a large portion of the measured FDI between Hong Kong and China.²⁵

A further issue is that Statistics New Zealand, in keeping with international guidelines, changed its definition of FDI, from owning 25% of an asset to owning 10% of an asset, from the June quarter 2000. As a result, data up to March 2000 is not directly comparable with data from 2001 on.

For these, and other reasons, precise values of FDI may differ from reported values. However, with the exception of Hong Kong-China FDI, it is unlikely that these issues significantly distort the trends observed in the data.

²⁵ UNCTAD, Hattari. R & R. S. Rajan 2008.

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