# A Critical Assessment of Direct Investments Abroad (DIA) and the Changing Nature of Foreign Direct Investments (FDI)[1]

## Introduction

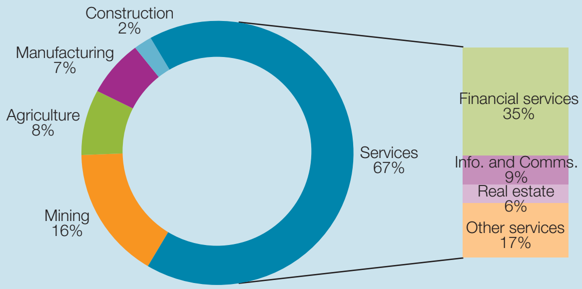
Building on from previous articles on the performance of Malaysia's direct investments abroad (DIA)[2] and investment incentives framework[3], this article presents a critical assessment on the positive spillovers and policy challenges of DIA and FDI to the Malaysian economy. A broad framework in assessing the costs and benefits of both DIA and FDI is applied, combining quantitative and qualitative perspectives. This includes measurable impacts such as investment, exports, value added, and employment; and associated costs such as tax revenue foregone, and investment income payments. We also take into consideration the less tangible benefits and costs associated with DIA and FDI, and the overarching backdrop of rapidly-changing global economic, industrial, and technological trends. The article concludes with a discussion on policy strategies, with an eye on ensuring the country maximises the economic and financial benefits from these ventures, and minimises potential exposure to risks.

### I. Developments and Drivers of Direct Investments Abroad (DIA)

DIA by Malaysian companies has increased at a rapid pace, reflecting the maturity of domestic firms and limited domestic natural resources, facilitated by strategic national policy initiatives. Since 2001, on average, the stock of Malaysia's DIA increased by 20.7% per annum, from RM31.7 billion in 2001, to register outstanding DIA of RM522.5 billion as at end-2017. Between 2005 through 2014, DIA flows have averaged RM39.1 billion per annum, or 4.7% of nominal GDP. Since 2015, however, DIA flows have moderated somewhat, with average outflows amounting to RM33.7 billion per annum, or 2.7% of GDP between 2015 and 2017, reflecting a more cautious approach given greater uncertainty in the global growth environment and low global oil and commodity prices since December 2014. The depreciation of the ringgit in this period, which rendered investments abroad more expensive for domestic firms, may have also contributed to the moderation. As at end-2017, DIA was accumulated mainly in the financial services sub-sector (34.7% of outstanding DIA), followed by the mining and agriculture sectors (15.8% and 7.8%, respectively), and the information and communication services sub-sector (9.1%). By destination[4], DIA was channelled mainly to Southeast Asian economies, particularly Singapore and Indonesia, followed by European countries, and North America, particularly to Canada (Chart 1)[5].

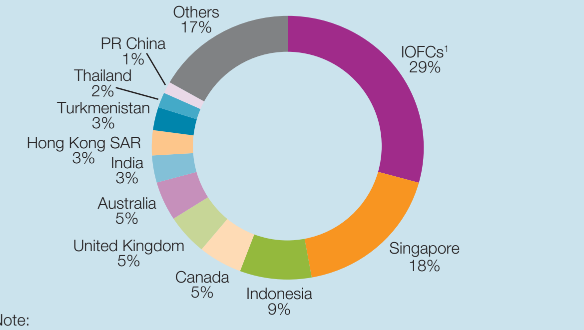
Chart 1: Outstanding Direct Investments Abroad

**i) By economic sectors: DIA largely concentrated in the services sector**




Note:
Banks and insurance companies account for 23% of DIA stock in the financial services sub-sector (or 8% of total DIA stock). The remaining 77% (27% of total DIA stock) comprise investment holding companies. Figures may not add up due to rounding.

**ii) By immediate destination countries: Southeast Asia, Europe and North America are the largest destinations for Malaysian DIA**




Note:
International Offshore Financial Centres (IOFCs) include Mauritius (7%), Cayman Islands (6%), Isle of Man (5%), Bermuda (5%), British Virgin Islands (3%), Netherland Antilles (2%), Marshall Islands (1%), Bahamas (1%), Jersey and Seychelles (1%). Figures may not add up due to rounding.

Source: Department of Statistics, Malaysia

1 This article was written in collaboration between the Economics and Foreign Exchange Administration Departments.
2 BNM Annual Report, 2016. 'Payoffs from Going Global: Assessing the Returns from Malaysia's DIA'.
3 BNM Quarterly Bulletin, 3Q 2017. 'Rethinking Investment Incentives'.
4 In line with the 6th Edition of the IMF's Balance of Payments and International Investment Position Manual (BPM6), Malaysia's DIA data is recorded by immediate destination basis, and not the ultimate country of destination.
5 DIA intermediated through IOFCs account for 29% of outstanding DIA stock. Investment via IOFCs, where investable funds are pooled before being directed to economic sectors in various locations, is a common global practice for companies operating internationally.

DIA was initially driven by the pursuit of natural resources in the 1980s and 1990s, mainly undertaken by Government-linked companies (GLCs) in the oil and gas and palm oil industries. Since the mid-2000s, however, private companies, particularly in the financial services and telecommunication industries, began to display greater interest and capability in venturing abroad to expand into new markets and customers, achieve greater economies of scale, and acquire strategic assets. These developments took place amid increased regional economic cooperation through bilateral and regional agreements, and are complemented by national policy initiatives, particularly the progressive liberalisation of foreign exchange administration (FEA) rules on residents' investments abroad in 2005. The flexibility to mobilise foreign currency funds was a key enabler for Malaysian firms to pursue opportunities abroad and strategic tie-ups with established international industry players, access new markets, acquire technical know-how, and fast-track technological transfers in various phases of the production process. Additionally, domestic industrial policies have nurtured market leaders well-placed to advance the strategic interests of the country in key industries. Furthermore, the development of the financial system in Malaysia has given rise to a strong banking system and large base of capable institutional investors, including provident and pension funds, and private and public asset managers, who invest the nation's savings abroad to maximise returns and diversify risk exposures. DIA was further supported by macroeconomic push factors, such as the strengthening of the ringgit between 2005 and 2013, and, after the Global Financial Crisis, the lower interest rate environment and relatively strong growth of emerging markets, which led to more attractive valuations of foreign assets.

**II. Spillovers from DIA to the Malaysian Economy**

(i) Establishment of the Malaysian Brand in the Global Market

In the past few years, we have begun to witness positive spillovers from DIA through the establishment of the Malaysian brand in the global market, and the increased benefits accruing to large Malaysian conglomerates. These companies, who are already market leaders in their respective industries, have investments that span across the globe and have since been recognised as capable industry players in their own right. As a result, fourteen Malaysian companies are ranked in the "2017 Forbes Global 2000" list of the world's largest public companies[6]. Unsurprisingly, the country's home-grown oil and gas company was the 125$^{th}$ largest corporation by total revenue on the "Fortune Global 500" list, topping the rank for Malaysia. The Bank's industrial engagements have also uncovered some anecdotal evidence of more intangible benefits, in the form of technological and knowledge transfers in selected industries like the utilities, financial services, leisure and hospitality, and tourism industries (please refer to the 'Information Box on Case Study of Top Resident Investors' at the end of this article, for more details).

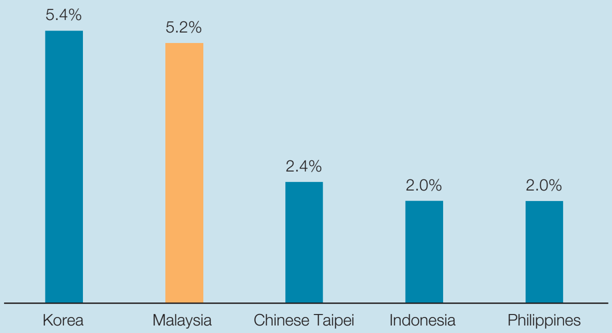
(ii) Limited Evidence of Domestic Spillovers and Forward Linkages

Malaysia's DIA has generated a return on its outstanding assets (return on assets, ROA) of 5.2% per annum, between 2010 and 2017. Compared to regional peers, Malaysian corporates have performed relatively well on their investments abroad (Chart 2). The investment income accrued from DIA has helped offset some of the primary income payments in the current account. While the primary income deficit has remained sizeable (amounting to an average of RM32.1 billion per annum between 2010 and 2017), without the commensurate increase in income receipts from DIA, these deficits would have been almost double (at RM63 billion per year, on average). From the international investment position (IIP) perspective, DIA has also diversified Malaysia's external asset composition. In 2004, the proportion of external assets was heavily dominated by official foreign exchange reserves (60.6% of total external assets in the IIP; DIA share: 11.7%). As at end-2017, however, the DIA share of total external assets increased to 31%, with reserves accounting for a smaller share (24.6%). The diversification of external assets is important, given that the large portion of external liabilities is accounted for by domestic corporations and banks. A more balanced risk portfolio in terms of the composition of external assets and liabilities ensures that the country is not solely reliant on reserve assets to balance its external liabilities exposure.

[6] By order, these companies are Malayan Banking Berhad, Tenaga Nasional Berhad, Public Bank Berhad, CIMB Group Holdings Berhad, Sime Darby Berhad, Genting Berhad, Petronas Chemicals Group Berhad, RHB Bank Berhad, Hong Leong Financial Group Berhad, Axiata Group Berhad, MISC Berhad, Maxis Berhad and AmBank Group and Petronas Gas Berhad, as listed.

Chart 2: Return on Assets of Direct Investments Abroad

**Malaysia's DIA one of the best performers in the region**




Notes:
1. Average return on DIA between 2010 and 2016 for Chinese Taipei
2. DIA stock for Indonesia and Philippines as at end-3Q 2017
3. Approximated 2017 annual income data for Philippines

Source: Department of Statistics, Malaysia, National Authorities, and Bank Negara Malaysia estimates

Economic theory, however, suggests that investments abroad should enhance trade and investment linkages and performance, foster internationally-competitive firms, increase high-technology industrial clusters and high-skilled employment domestically, and even increase the Government's tax revenue through stronger and more sustainable growth. Of interest, studies on the domestic impact of DIA on home countries have been relatively limited, compared to studies on the impact of FDI on host countries. This is partly due to the lack of comparable and reliable data, particularly for emerging and developing economies. For advanced economies, while findings are generally rather mixed, literature indicates that DIA tend to have positive spillovers in the home country, in terms of economic and domestic investment growth, high-skilled job creation, technology transfers, and exports performance. More recently, a few studies reported that Korean DIA has been found to have a positive impact on exports, domestic productivity, and employment. These trends may be different, however, for different sectors in which DIA has taken place, and even according to the different investment destinations[7].

For Malaysia, the domestic economic spillovers of DIA are not yet discernable. Findings from empirical studies indicate DIA has not been found to have a positive correlation with Malaysia's growth or trade performance, raising concerns that DIA may have come at the expense of growth domestically. Low domestic spillovers may also point to the limited formation of deeper backward linkages[8]. This may be due to the fact that DIA is largely concentrated in the services sector, which may offer fewer opportunities to form backward linkages, compared to sectors like manufacturing. Insights from industrial engagements allude to other structural constraints, such as the relatively lower capabilities of domestic firms to provide products and services meeting both the needs of Malaysian firms conducting businesses abroad and foreign firms operating in the country. These studies also point to the difficulties in quantifying the domestic impact of outward investments by resident companies. Even with tangible impacts like exports, investment, and employment, data limitations may limit deeper quantitative analysis, while more qualitative indicators like technology and knowledge transfers, and upgrading of value chains present an even bigger challenge.

Low repatriation from income and dividends earned from investments abroad is another factor that underscores the low impact of DIA on the domestic economy (for more details, please refer to the Information Box on 'Case Study of Top Resident Investors'). Between 2010 and 2016, DIA have accumulated income amounting to RM149.4 billion, of which 30.1% are retained abroad for reinvestment and 51.8% are declared as dividends.

7 Kim, S (2000) and Ahn et al (2005). Positive correlation with trade is more statistically significant for 'high-tech' and 'medium-tech' industries. While DIA is positively correlated with total factor productivity and employment in general, DIA into PR China displays a negative effect.

8 Goh and Wong (2014), Goh et al (2013), Wong (2013) and Chen et al (2012).

Estimates using internal data on cross-border banking flows indicate that only 51% of income are repatriated back to Malaysia. Out of these, an even smaller proportion are permanently retained in Malaysia to be re-channelled into further expansion of domestic operations or investment in domestic activities. In sum, the cost and benefit analysis of DIA must account for a wider set of considerations, and extend beyond simplistic profitability considerations for the investor.

(iii) Challenges and Concerns Surrounding DIA

On occasion, a few DIA projects have also been confronted with external headwinds and exposure to regulatory uncertainty, which may have affected the viability and profitability of these particular investments, and attracted prominent media attention. These include regulatory changes and restrictions in host countries, stiffer-than-expected competition in certain sectors, acquiring investments at high valuations, and venturing into assets beyond core business sectors or mandates. In addition, the rapid expansion of domestic banking groups across borders has contributed to greater interlinkages and increased complexity in managing potential risks to financial stability. These include increased complexities in terms of ensuring compliance with regulatory developments, managing enterprise-wide capitalisation, liquidity and business risks, and undertaking recovery and resolution planning. These observations, however, should not be generalised to represent the entirety of Malaysia's DIA. As noted earlier, on the whole, Malaysia's DIA has performed relatively well. At 5.2% between 2010 and 2017 ROA is slightly above the average global growth of 3.9% in the same period, and comparable to average regional[9] growth rates of 5.3%.

**III. Developments and Drivers of Foreign Direct Investments (FDI)**

Foreign direct investments have been a key driver facilitating Malaysia's productive expansion from a commodity-dependent, agriculture-based economy into an industrialised economy with a vibrant manufacturing base well-positioned in the regional and global trade value chain. The rapid industrialisation of developing countries in the 1970s-1980s was a pivotal period, with significant investments by multinational corporations in Malaysia, particularly in the manufacturing and mining sectors. These developments were shaped by the intensification of global manufacturing value chains, technological progress, a favourable demographic profile, and modern domestic infrastructure. At the same time, key domestic policies such as the Promotion of Investments Act 1986, liberalisation of foreign equity rules in the manufacturing sector, and the gradual liberalisation of foreign equity rules in selected services sub-sectors have continued to attract foreign investments and enhance the competitive environment in domestic industries. In the last 16 years, outstanding FDI in Malaysia increased by 9.9% per annum, from RM129.1 billion in 2001 to RM565 billion as at end-2017. In terms of economic sectors, FDI has been channelled mainly into the manufacturing sector (41% of outstanding FDI), followed by the financial services, wholesale and retail trade, and mining sectors (21.3%, 7.2%, and 6.9%, respectively). Most FDI flows are from regional economies like Singapore, Japan, and Korea, again underscoring the importance of regional trade and investment ties; followed by investments from Europe and North America (Chart 3).

**IV. Benefits and Costs Associated with FDI**

(i) A Catalytic Force in Malaysia's Economic Development

FDI is widely-acknowledged to have been a game-changer in Malaysia's economic development and came at the right time for Malaysia to partake in the globalisation surge that began in the 1980s. The increase in FDI, which, at its peak, registered flows amounting to 10.5% of GDP in the 1990s, brought a corresponding rise in the share of manufactured exports, employment, and income per capita. According to newly-released Inward Foreign Affiliates Statistics 2016 (Inward FATS 2016) published by the Department of Statistics, Malaysia (DOSM), exports generated by foreign firms amounted to RM292.8 billion, or 31.8% of gross exports in goods and services in 2016. Foreign firms have also created job opportunities, directly employing 847,300 workers (approximately 5% of total employment)[10]. The productivity of FDI firms are also significantly higher than the national average, with value added per worker at approximately three times higher than national productivity levels, at RM237,000 per worker per year on average between 2010 to 2016, compared to RM72,520 per worker nationally.

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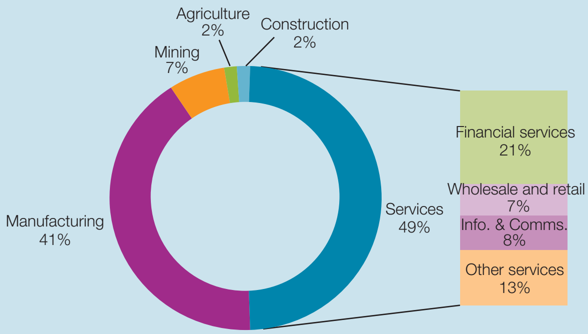
[9] Regional countries refer to Indonesia, Phillipines, Singapore and Thailand, which account for 29% of Malaysia's outstanding DIA stock.

[10] A key difference between FATS and direct investment data from the BOP is the equity threshold applied. Under BOP, a direct relationship is established at a 10% minimum equity stake in a related enterprise. Under FATS, control of an affiliate by an ultimate parent company arises when equity interest is more than 50%.

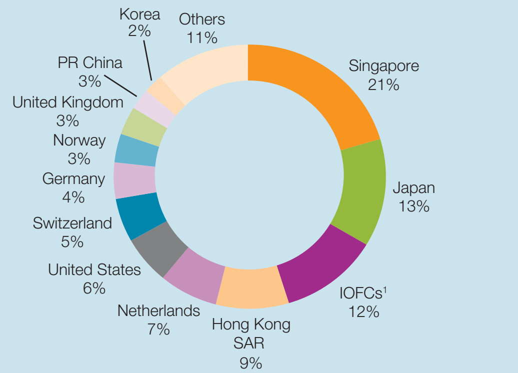
Chart 3: Outstanding Foreign Direct Investments

**i) By economic sectors: FDI channelled mainly into the services and manufacturing sectors**




Note:
Banks and insurance companies account for 63% of FDI stock in the financial services sub-sector (or 13% of total FDI stock). The remaining 37% (8% of total FDI stock) comprise investment holding companies. Figures may not add up due to rounding.

**ii) By source countries: Largest FDI investors are from regional countries, Europe and North America**




Note:
International Offshore Financial Centres (IOFCs) include British Virgin Islands (4%); Bermuda (3%); Jersey (2%); Cayman Islands (1%); Bahamas (1%); and Mauritius, Barbados, Panama, Samoa and Isle of Man (1%). Figures may not add up due to rounding.

Source: Department of Statistics, Malaysia

These investments have facilitated Malaysia's diversification away from a reliance on agriculture and minerals. This, in turn, has contributed to the fundamental strength of the economy. With the help of FDI and a rich and deep domestic ecosystem of production facilities, infrastructure, supporting services and talent, Malaysia is now firmly entrenched in the regional and global trade value chain.

(ii) Increasing Indication of Diminishing Net Benefits to the Economy

However, there is evidence that benefits to the country have been narrowing. The prevalence of labour-intensive and low-cost modes of production have led to the slow development of domestic value chains and ancillary services, and high reliance on imported goods, services, and foreign workers. This is evidenced by the slowing growth of domestic content in exports and lower spending on research and development by foreign MNCs. According to data compiled by the OECD, domestic content in Malaysia's gross exports is lower than regional average and regional economies (60.9% in 2014; regional average: 69%; Philippines: 76.3%; PR China: 70.7%). R&D spending by US FDI companies in Malaysia has also declined since 2012 (4.6% of total output; 3.6% share of output in 2014), and is lower than regional economies (India: 11.1%; Chinese Taipei: 4.9%; PR China: 4.5%)[11], indicating that technology transfers by foreign companies have plateaued. Inward FATS also point to other examples of waning benefits to the domestic economy, for example in declining shares of value added from foreign companies (2010: 19.5% of total value added; 2016: 18%), and investment (2010: 22.4% of gross fixed capital formation; 2016: 20.1%). Foreign firms have also contributed to the general trend of increased participation of low-skilled foreign workers in domestic industries[12]. While these trends are also contributed by local firms, unchecked reliance on low-skilled foreign workers have led to deep distortions, including the prevalence of low-skilled job creation and depressed wages in the Malaysian economy. The wider impact of these issues, such as stagnant wages amid rising cost of living, is disproportionately felt by the most vulnerable members of society. For example, reliance on low-skilled foreign workers tends to displace local workers in the low-skilled category, who also tend to be members of households in the bottom 40% of the household income distribution (B40). These industrial trends lead to the slow development of value creation among domestic suppliers and service providers, low pace of innovation and technological adoption, and wage and price distortions, which tend to outweigh some of the benefits of FDI.

[11] For a more detailed account, refer to Box Article on 'Rethinking Investment Incentives' in BNM's 3Q 2017 Quarterly Bulletin.
[12] For a more detailed account, refer to Box Article on 'Low-Skilled Foreign Workers and Its Distortions to the Economy'.

(iii) Costs and Leakages to the Economy

These concerns are especially stark when taking into account the cost of attracting foreign investments into the country. Over the years, the Government has deployed broad-based investment incentives to develop strategic industries and encourage desired economic activities. As previously estimated by Bank Negara Malaysia, the cost of incentives ranged between RM10 billion to RM15 billion annually, over the past five years, and account for up to approximately 9% of total Government tax revenue. These resources could have been channelled to improve public infrastructure and services, which are critical components in attracting and facilitating investments in the first place. There also appears to be a mismatch between the investments the country is receiving, and new growth areas in which the nation should be cultivating. For example, there is emerging evidence of increasing FDI in less productive sectors such as real estate and property development, particularly in segments in which policymakers have identified imbalances. FDI in the real estate and construction sector has risen in terms of share, from an average of 6.3% of annual FDI flows in 2010-2015, to 19.1% in 2016 and 2017. Industrial engagements suggest these investments are channelled mainly in the higher-end property segments. Other leakages include low domestic spillovers due to the high rate of income repatriation by foreign companies and high remittances from foreign workers, both of which are structural factors which weigh on Malaysia's current account balance.

Furthermore, the prevalence of fiscal incentives as a means to attract investment has come under scrutiny by international organisations, amid concerns of a 'race to the bottom' and wide-ranging changes in the regulatory environment aiming to discourage harmful tax practices. This also gives multinational companies the upper hand when it comes to deciding on an investment destination, and puts pressure on Governments to give in to the other immediate demands of industry, at the cost of strategic policy direction.

**V. Policy Implications: A New Framework for Thinking about Investments**

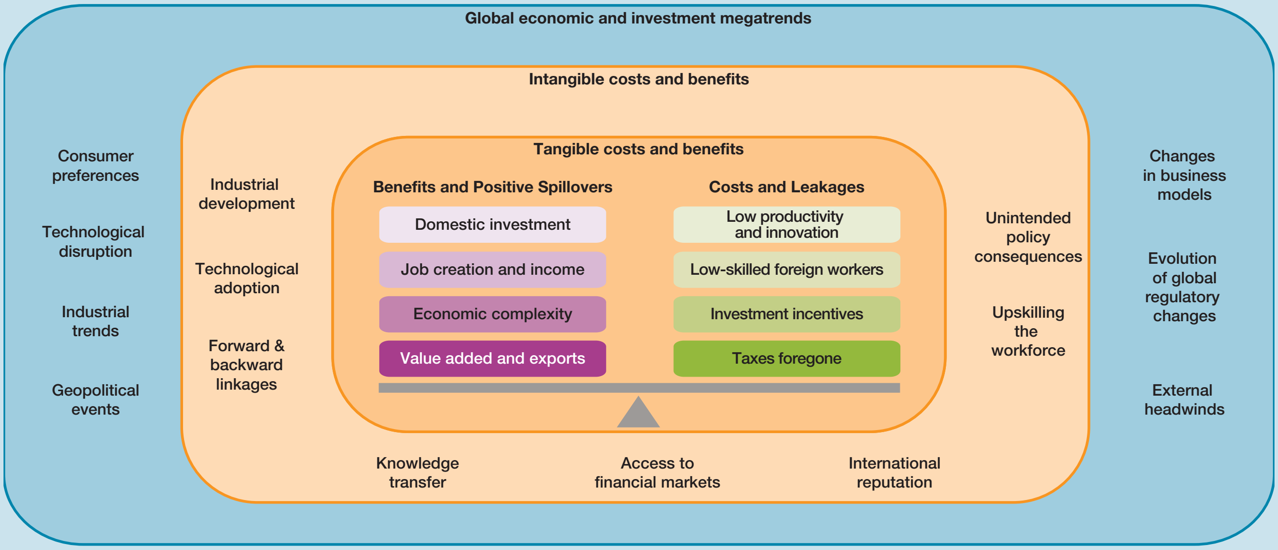
In the current highly-dynamic and complex economic environment, there is little room for complacency. Globalisation and technological disruption is rapidly changing consumer preferences, industrial trends, and business models. A fresh approach is needed, and policymakers must adapt to a new framework for thinking about investments. While traditionally, policymakers tended to place more emphasis on FDI, Malaysia is facing an interesting turning point. Aside from ensuring FDI remains an important contributor to economic development, we must also consider strategies to maximise backward and forward spillovers from DIA. These are challenging mandates but they are not insurmountable. The way forward lies in undertaking a rethinking of the national investment strategy and adopting a new approach to the cost and benefit analysis framework for both inward and outward investments. There also needs to be greater clarity in the direction of labour policy, particularly with regard to the role of low-skilled foreign workers in the economy. Communication on the Government's strategy on foreign workers need to be enhanced, alongside ease of obtaining information about current regulations, and offer clearly defined timelines on the gradual implementation of future regulations. At the highest level, however, policymakers have to agree on how Malaysia's DIA and FDI can best fit into global industrial trends and strategise accordingly, as regional countries such as PR China and Singapore have done.

Towards this end, a broad framework in assessing the net benefits of both DIA and FDI is envisioned, combining quantitative and qualitative perspectives, and an overarching backdrop of rapidly-changing global economic, industrial, and technological trends (Illustration 1). Costs and benefits associated with both FDI and DIA includes measurable impacts such as investment, exports, value added, employment, and associated costs such as tax revenue foregone and investment income payments. We also take into consideration the less tangible benefits and costs associated with DIA and FDI, particularly the benefits brought about by technological adoption, development of industrial clusters, and potential distortions to industrial behaviour from previous regulatory barriers.

This new framework in weighing costs and benefits highlights several policy implications. Firstly, the effectiveness of the current strategy to attract investments needs to be reflected upon. Regulations must spur investors to innovate, adopt new technologies, and serve emerging consumer preferences and industrial trends. FDI and prospective investments should deepen linkages in the domestic supply chain and build new value clusters. These investments should also exhibit desirable characteristics such as high-skilled job creation, and lift economic complexity and product sophistication[13]. Towards this end, a rethinking of the investment incentives framework is called for[14]. The decision on whether or not to award investment incentives should strike a balance between a nimble and flexible principles-based approach and a more decisive, performance- and outcome-based approach. Incentives awarded should be time-bound and tied to indicators on innovation, productivity, quality employment, and economic complexity. Malaysia cannot continue to rely on low-cost strategies to attract foreign investments, in an environment of increasing competition from other countries around the region.

Illustration 1: An Aspirational Cost-Benefit Analysis Framework

**Considerations for investments must be broader than immediate impacts and profitability**




Note: The indicators mentioned in the above framework are by no means exhaustive and serve as an illustrative example of a comprehensive perspective to assess the costs and benefits of both DIA and FDI.

Secondly and perhaps more challenging to achieve is the objective of maximising domestic spillovers from DIA. Efforts to promote two-way flows from investment activities and promote backward and forward linkages in the domestic economy must be strengthened. Part of this effort includes optimising the performance of Malaysian companies investing abroad. Korea, for example, facilitates local companies and SMEs in venturing abroad by offering investment consultancy services, which provides pertinent context on the social and political backgrounds of countries in which companies invest in. Through investment promotion agencies, the Government provides advisory services in terms of laws and regulations, and common challenges faced by foreign firms entering these markets. These services aim to reduce the incidence of companies falling into legal and regulatory pitfalls which could have been avoided, and prepare them for sector-specific challenges. Strategic and transparent communication of investment plans, particularly among GLCs and national institutional investors, would also be beneficial given the important roles that these companies play in the Malaysian economy. As discussed, a more dynamic investment incentives framework is needed to support this objective, coupled with more effective monitoring and enforcement to ensure performance measures are achieved, in line with investment approvals requirements and FEA regulations. This is complicated by the fact that domestic spillovers resulting from DIA activities may not be readily quantifiable due to data limitations and current frameworks for assessing the viability of investments abroad. Thus, a list of clear, principles-based requirements to complement quantitative indicators is warranted to comprehensively assess the

[13] For a more detailed account, refer to Box Article on ‘Complexity and Growth: Malaysia’s Position and Policy Implications’.
[14] For a more detailed account, refer to Box Article on ‘Rethinking Investment Incentives’ in BNM’s 3Q 2017 Quarterly Bulletin.

likely financial and economic impact of investments abroad by domestic companies. Adoption of these policies will require implementation in a highly coordinated and cohesive manner to maximise the effectiveness of institutional support for DIA.

Finally, industry associations could also play a more constructive role in policy dialogue, either through providing industrial insights to national agencies, or by participating in policy ideation. Firms operating in the Malaysian economy must do so with a view of building a more facilitative industrial ecosystem, enhancing the functioning of domestic labour markets and continuously improving productivity. Initiatives by the Government such as the recently-introduced Employment Insurance System is necessary to enhance the flexibility of the labour market and encourage more efficient channelling of private savings. It has been observed that given the deep preponderance for low-cost models, there have often been strong industry pushback to Government-initiated reforms to lift labour or industrial standards. Corporate buy-in and meaningful participation is crucial in ensuring these key economic reform initiatives are implemented successfully. It is important to keep in mind that investments and economic progress in the economy must ultimately benefit the people and bring not only economic development, but also social progress.

## Conclusion and Future Areas for Research

In summary, DIA has proven advantageous for certain domestic corporations, with some evidence of domestic spillovers in selected sectors. However, evidence of wide-ranging economic benefits of DIA have been inconclusive. On FDI, while the benefits to the economy are clearer, they are by no means constant or automatic. There is evidence that the net benefits to the economy is decreasing, amid the high costs of attracting foreign investments. Investment policy needs to be recalibrated such that the country does not rely solely on cost-pull factors to attract foreign investments, and to minimise economic leakages. The policy framework on investment needs to be reconsidered for both DIA and FDI, to ensure the country remains on track in its aspiration towards becoming a high-income nation. This would require that the country continues to invest in infrastructure and human capital and remove domestic impediments, so that it is always well positioned to ride the next wave of technological disruption and global economic megatrends. Going forward, a more concerted effort is needed to better quantify and assess the costs and benefits of both FDI and DIA. This includes conducting more research on the less-explored area of domestic complementarities of DIA, improving information collection and compilation methods to better quantify and take into account intangible impacts, and instituting greater discipline in enforcing a more comprehensive cost-benefit analysis framework which focuses on the wider impact of these investments. These policy tweaks to enhance backward linkages and spillovers from DIA and FDI are important, and they are a complementary effort in the long-run pursuit of efficient and functioning markets and high-quality infrastructure. Enhanced coordination between Government agencies and improved collaboration between the public and private sectors are necessary to strengthen the attractiveness of the domestic investment ecosystem for the sustainable long-term prospects of the Malaysian economy.

## Case Study on Top Resident Investors

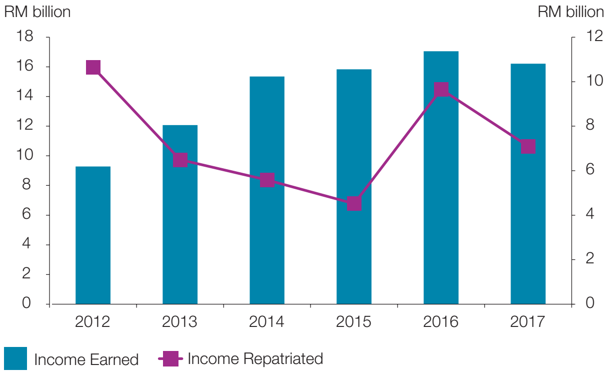
A series of industrial engagements and surveys on large DIA firms comprising of 52 companies which contributed to 60% of the total outstanding DIA stock as at 1H 2017[1] were conducted. The survey was aimed not only to gain insights into the financial performance of Malaysia's DIA but also to assess the intangible benefits of DIA to the domestic economy.

**Moderate repatriation of financial returns**

- Despite a challenging global economic environment, income on DIA remained stable for the past 6 years since 2012 reflecting the resilience of these investments. Of the DIA income earned, 51% (RM44.0 billion)[2] was repatriated with roughly equal share between GLCs and private companies. The remaining 49% (RM41.8 billion)[3] of DIA income retained overseas were used for reinvestment or paying off borrowings. Minimal conversion into ringgit is observed[4] from the repatriated income as it is generally kept in foreign currency to be re-channelled into new investments abroad, effectively leaving marginal amount for domestic utilisation.
- The moderate growth in investment income is also reflective of the relatively early stage of Malaysian DIA. Initially, DIA was mostly undertaken via greenfield ventures in which the payback periods were relatively long, ranging between three and 18 years. Following long gestation periods, some DIA started to yield return only recently. Over time, Malaysian corporates with increasing maturity started to undertake overseas expansion via brownfield ventures with shorter payback period ranging between three to five years.

Chart 1: Income Earned and Repatriated

**Relatively stable income from DIA**




Source: Bank Negara Malaysia

**DIA has more apparent benefits in selected industries, as some sectors have benefited from technology transfer**

- DIA can potentially expedite the technology transfer to Malaysia, especially in Malaysia's fledgling renewable energy sector. Acquisition of two brownfield projects in the United Kingdom and Turkey by the national power company can spur the development of Malaysia's own solar and wind power generation through technology transfer from global energy players. This is in line with the national strategy to develop renewable sources of energy as outlined in the Green Technology Master Plan Malaysia 2017-2030.
- Similarly, DIA in the leisure and hospitality sector has helped to develop a unique world class theme park in Malaysia through the participation of international producers and distributors of motion pictures. This bodes well for Malaysia's efforts to boost the tourism industry.

1 For the purpose of this article, companies incorporated in Wilayah Persekutuan Labuan are classified as non-residents, in line with treatment under FEA regulations.
2 Figure excludes income earned by financial institutions and FEA treatment of Labuan as non-resident.
3 Source: Bank Negara Malaysia.
4 Source: Feedback from surveyed companies.

**DIA not yet a catalyst for Malaysian exports**

- While it is often acknowledged that DIA should facilitate greater market access, contribution to Malaysian exports via DIA has yet to be a reality. Only the plantation sector recorded some DIA related exports of equipment, machineries and fertiliser amounting to RM121 million between 2014 and 2016[5]. This amount is negligible compared to total exports from the country of RM2,330 billion in the corresponding period[6]. From this perspective, DIA has failed to spur Malaysian exports.

**DIA in infrastructure projects abroad promotes Malaysia's brand and goodwill**

- The success of Malaysian companies undertaking large scale overseas projects such as highways, power plants, and residential and commercial projects help to establish and elevate Malaysian corporates' reputation abroad. As at March 2017, Malaysia's corporates successfully completed 866 international projects with a combined value of RM92 billion and there are 55 projects still in the pipeline worth RM25 billion[7].

**DIA benefits yet to be fully realised**

- DIA flows are generally one way, as even repatriated income would be ploughed back into new investments, thus permanently impairing domestic liquidity in the process. There needs to be not only higher repatriation of DIA income but more importantly its conversion into ringgit should increase to replenish domestic liquidity and contribute towards more balanced flows in the onshore foreign exchange market. Based on anecdotal evidence, despite our GLCs and private companies undertaking large scale projects and huge investments overseas, the country's exports are yet to show a corresponding improvement due to DIA activities.

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5 Source: Feedback from surveyed companies.
6 Source: Department of Statistics. Malaysia.
7 Source: Construction Industry Development Board.

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