

Monsod, Toby C. et al.

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How to change a constitution by hand-waving (Or, the unbearable lightness of evidence in support of lifting foreign ownership restrictions)

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**How to change a constitution by hand-waving
(Or, the unbearable lightness of evidence in support of lifting
foreign ownership restrictions)**

by

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Abstract

This paper provides a review of the empirical evidence cited in the current public discussions on removing the remaining constitutional restrictions on foreign-equity ownership in certain economic sectors. A fuller appreciation of the given evidence shows that lifting equity restrictions is not a necessary condition for explaining the inward stocks of foreign direct investment (FDI) in the cited countries, including the Philippines. While restrictive equity rules may represent a hindrance to FDI, their potential effects are small and sometimes insignificant in comparison to other explanatory variables such as the ease of doing business, physical infrastructure, and perceived corruption. The paper cautions against an uncritical mindset towards FDI, discussing how consistent empirical evidence of the positive effects of FDI on host economies has proved elusive and that knowledge and technological spillovers from FDI are highly context-specific, not unconditional, and not without cost. Instead, a more discriminating approach, focusing on the quality of multinational enterprises and its activities, rather than simply on the volume of FDI, is recommended. Finally, the paper warns that the push for legislative flexibility, while attractive on the surface, can be self-defeating since it also has the potential of increasing investment uncertainty, particularly given the idiosyncrasies of Philippine political economy.

Key words: foreign direct investment; multinational enterprises; foreign equity restrictions, constitutional change, empirical models of investment distribution; influences on the distribution of direct foreign investments; rules versus discretion

JEL Codes: F14, F21, F23, F60

⁺ We thank our colleagues, Adrian Mendoza, Anthony Sabarillo, Gabby Domingo, and Maria Socorro Gochoco-Bautista for helpful comments. All errors are ours.

I. Motivation

This paper is a comment on the quality of the arguments being put forward in favor of lifting foreign ownership limitations contained in the 1987 Constitution. We were impelled to write after observing how much of what passes for economic analysis on the issue has been dominated by casual opinion, loose reasoning, and an incomplete appreciation of empirical evidence. Considering the gravity of any proposal to change the fundamental law of the land, those in power are obliged to at least ensure they are thoroughly and accurately informed of the risks and benefits of any potential action.

We are well aware of the opinion that economic cha-cha could be nothing but a red herring and that the real object of charter change proponents is to amend term limits and other political provisions of the Constitution.¹ We take no position on that issue in this paper. Our sole aim is to improve the tenor of debate on the subject by contributing to a more discerning, fully informed public discussion as befits a pending momentous decision. We think this is a worthwhile exercise regardless of the true motives of those who promote economic cha-cha. The opportunity may still arise, before any decision to amend our fundamental law is made, for a sober, multidisciplinary conversation on the deep institutional parameters and rigidities affecting the country's development trajectory, which could include a rigorous and systematic review of the 1987 Constitution in its entirety. At whatever time that opportunity arises, this paper we hope will have contributed to the effort.

More immediately, as we observe current public discussions, two prominent assertions have been made and repeated that appear particularly troubling.

First is the contention that “removing restrictions is a *necessary first step*” (our emphasis) towards increasing foreign direct investments (FDIs) or stimulating economic activity—alternatively, “it is a necessary but not sufficient condition”—as has been asserted by some resource persons at the House of Representatives (HOR) during the hearings of the 19th Congress Committee of the Whole House (RBH7), and even by Representatives themselves.² NEDA itself has said as much. On Day 2 of the

¹ This view is reasonable given the laudatory announcements accompanying the release of the IRR of the Public Services Act, as amended, last March 2023. NEDA stated that, “together with complementary measures”, such as the amendments to the Foreign Investment Law (in July 2022) and Retail Trade Liberalization Act (in March 2022), the passage of CREATE (in May 2021), and others, “we are confident that the Philippines will be able to attract much needed capital and technology, sustain its high-growth trajectory, and generate high-quality jobs enabling rapid poverty reduction in the next six years.” (<https://neda.gov.ph/neda-releases-public-service-act-irr/>).

² As one Representative explained (RBH7 hearings, Day 2, part 2, around the 3:20 hour mark): “*Kinakailangan natin[g] buksan ang pintuan, pero komo’t binuksan natin ang pintuan ay hindi naman ibig sabihin nun ay ‘matic maganda ang loob ng bahay. Kelangan natin[g] pagandahin pa ang loob ng bahay, siguraduhin na may running water, siguraduhin na may ilaw, etsetera.*” A less flattering metaphor will liken the effort to change constitutional equity restrictions to the hostel owner who spends a lot of money to landscape the grounds before repairing the roof that has caved in.

RBH7 hearings (February 27, 2024), when asked directly whether more FDI could be induced without amending the Constitution if only other issues related to the ease of doing business, corruption, quality of infrastructure, stability of government policies and others could be properly addressed—the NEDA officials present said no.³

The thing is, if there are statutory restrictions, then that is the first gate, or barrier. So, if closed *na siya* by statutory restrictions, then [even properly addressing] the other factors would not matter.

The second assertion that raises eyebrows is that having restrictive economic provisions enshrined in the Constitution rather than in ordinary legislation is the *main reason* that the Philippines has lagged economically behind its peers in Southeast Asia.⁴ To wit:

... [T]heir (other nations') having greater legislative flexibility in the enactment of laws pertaining to business and economy accounts for their relative success in comparison to us.⁵

The reasoning seems to be that since the Philippines is the only country in the region with foreign equity restrictions in its Constitution, and since it has (subsequently) been receiving the smallest portion of FDI into the ASEAN, then the former must have caused the latter—an obvious *post hoc* fallacy.⁶ Implicit in this story is a belief that differences in statutory equity restrictions are the main factor explaining the dispersion of FDI across the ASEAN. A further implicit assumption is that “legislative flexibility” is superior to constitutional rules when it comes to the economy.

Wittingly or not, these statements also convey the impression to the public that any and all foreign direct investments bring unmitigated benefits. In public discussions, including during the RBH7 hearings, FDI has been variously described as the solution to the country's low saving and investment rates; a source of technology and managerial know-how; a driver of better jobs; a measure to break local monopolies; and the means by which the country can shift to a higher growth path, in emulation of Vietnam. It is true some people catch themselves in time and prudently state that FDIs are “not a panacea”. Still, such surprising modesty is difficult to reconcile with the supposed wonders an open-door FDI policy is likely to achieve.

³ RBH7 hearings, Day 2, Part 2, around the two-hour mark.

⁴ <https://www.pna.gov.ph/articles/1218281>.

⁵ <https://www.philstar.com/business/2024/02/13/2332855/why-we-need-amend-restrictive-economic-provisions-continued-last-week>. “In the immediate postwar period, we were equal to or ahead of these other countries in terms of economic achievements. However, today, we are at the tail-end of economic accomplishments when compared with all of them! There are many reasons for this. But their having greater legislative flexibility in the enactment of laws pertaining to business and economy accounts for their relative success in comparison to us.” This reflects the view in Sicat [2005].

⁶ *Post hoc ergo propter hoc* is a logical fallacy in which one event is said to be the cause of a later event simply because it occurred earlier.

In our assessment, the available evidence that statutory foreign equity restrictions can explain the dispersion of FDI across the ASEAN is weak at best. Improvements in the business regulatory environment, combined with improvements in infrastructure, have effects on FDI that dwarf the size of those coming from any change in foreign equity restrictions. One paper estimates the potential effects on FDI of improving perceptions of public sector corruption to be 8 times stronger than the potential effect of lifting equity restrictions. So, lifting Constitutional restrictions may at best be described as nice, but can hardly be called “necessary”.⁷

The somewhat uncritical enthusiasm for FDIs apparent in recent public discussions could also stand some moderation in our view. The by now extensive scientific literature has produced no clear answer whether a direct causal relationship exists between FDI and economic growth in developing economies (Narula and Pireli [2018], Carkovic and Levine [2004], among others). The knowledge and technological spillovers from FDI are seen to be highly context-specific, not unconditional, and not without cost. The key message to policymakers is to take care not to assume that any and all forms of FDIs will be good for national development and have a net contribution to economic welfare and efficiency. Instead, what research indicates is the need to focus on the quality and appropriateness of FDI, rather than merely on its volume. It suggests a role for thoughtfully crafted and executed industrial policy or a system of industrial priorities as a mechanism to enable domestic producers to assimilate the technology and knowledge of multinational enterprises (Morrissey [2012], OECD [2002], among others).

We organize the rest of this paper as follows. The next two sections address the issue of statutory foreign equity restrictions. We provide a brief look at how the Philippines stands as measured by what is known as the OECD FDI Regulatory Restrictiveness Index. This is followed by a discussion of the available evidence on the possible links between such restrictions and the dispersion of FDI in the ASEAN, and on inward FDI stock among advanced and emerging economies more generally. We then move to a discussion of the link between FDI and economic growth—which some authors have termed “elusive”—and its implication for policymakers in the fourth section. We end with some remarks on legislative flexibility.

⁷ A “necessary” condition (X) is one that must be present for another (Y) to occur. That is, without X, Y cannot occur or operate; so, Y requires X. On the other hand, a “sufficient” condition is anything that is capable of producing a change in Y on its own. If X represents changing statutory equity restrictions, and Y is FDI allocations, then we discuss how the available evidence does not support that X was a necessary condition for Y among the ASEAN-5 for the period studied. At best, X may be one sufficient condition among others for Y, albeit a very weak one. Changing statutory restrictions is not “necessary” in the sense that other sufficient conditions may operate even without such statutory changes. From this follows the practical choice for policymakers to focus their attention on which among several sufficient conditions has the largest and most significant impact on Y. (We thank Gabby Domingo for pointing out the need to make this clarification.)

II. FDI Regulatory Restrictiveness Index: equity restrictions in the Philippines

The FDI Regulatory Restrictiveness Index (henceforth, simply Restrictiveness Index or RRI), is a summary measure of statutory FDI restrictiveness, originally developed for OECD countries in 2003 then extended to non-OECD countries later in the decade. The RRI assigns scores to four types of statutory restrictions:

- (a) foreign equity limitations (the largest component);
- (b) screening and approval requirements;
- (c) restrictions on the employment of foreign key personnel; and
- (d) other operational restrictions (e.g. limits on land-ownership, branching, capital repatriation, etc.).

All in all, 22 economic sectors excluding education and health are scored on these four dimensions (a)-(d). The simple average of the 22 sector scores then becomes the “total” score for each type of restriction; the four totals are then combined to become the score of the overall RRI.

The variable of specific interest in what follows is component (a) of RRI, and we shall call it the Equity Index. It is important to note that only overt regulatory restrictions are scored. The level of actual enforcement or implementation is not taken into consideration. Other aspects of the regulatory framework, i.e., the extent of state ownership, the nature of corporate governance, and institutional or informal restrictions, which may impinge on the investment climate are also not incorporated [Kalinova, Palerm, and Thomsen 2010]. Comparable measures of the RRI—and therefore the Equity Index—are available from 1997 onward for OECD countries and from 2001 for some non-OECD countries, including some members of the ASEAN.⁸

The latest (2020) scores for the Philippines on foreign equity restrictions (i.e., the Equity Index) can be seen in Table 1. The country’s score is 0.282, with sector scores ranging from 0.00 to 1.00. The scoring rule is that if no foreign equity is permitted, the score is 1 (sector is closed); if majority foreign control is not allowed, the score is 0.5; if there is a requirement of a domestic minority holding, it is 0.25. Scores are scaled down (i.e., improved) if or when foreign equity limits affect only a portion of the sector. The bases for OECD’s scoring (as of 2018) are provided in the last column.⁹ The effect of laws passed after 2020 (e.g. CREATE in 2021, etc.) is not considered in the scoring.

The table also provides the scores for Vietnam, which has a total score of 0.074, or a little more than one-fourth that of the Philippines. Vietnam is often held up as a benchmark in current public

⁸ The data series is publicly available at <https://stats.oecd.org/Index.aspx?datasetcode=FDIINDEX>. The first OECD Investment Policy Review for the Philippines [OECD 2016] provides RRI values from 1987-2014 for the Philippines, Malaysia, and Indonesia but scores do not seem to match those in the main database.

⁹ This information comes from the pilot ASEAN FDI Regulatory Restrictions database and is available for 2017 and 2018 only. See https://qdd.oecd.org/subject.aspx?Subject=ASEAN_INDEX

discussions owing to its aggressive outward orientation since 1986, the higher average annual level of FDI inflows it receives (e.g. about twice that of the Philippines between 1990 and 2022 ¹⁰), and the performance of its manufactured exports, described as a “manufacturing miracle”, for which FDI accounts for about 90 percent.¹¹ The table also shows the difference in scores between the two countries: the larger is the positive “gap with Vietnam”, the tighter the statutory equity restrictions in the Philippines.

Finally, the table also highlights in bold font the sectors covered by the Articles in the Constitution¹² that are proposed for amendment under Resolution of Both Houses (RBH) Nos. 6 and 7 from the Senate and House of Representatives, respectively. Scores that are asterisked are those with equity restrictions found in ordinary law or administrative rules.

1. At the top end of the restrictiveness scale for the Philippines are Media (S16) at 0.788 and Business Services (S21) at 0.750, followed by Agriculture (S1) at 0.675. Next in the order are Forestry (S2), Fisheries (S3), and Mining (S4), and Real Estate Investment (S22) all of which have scores of 0.500. The constitutional restrictions in Media are well known and its sector score reflects both the 100-percent Filipino ownership rule in mass media and the laxer 60-40 and 70-30 rule for private radio and advertising, respectively. The foreign equity limits of 40 percent for real estate and the primary sectors (agriculture, forestry, fishing, and mining) are also well known. However, among the latter, Agriculture is scored as more restrictive than the rest because the corporate practice of agriculture as a profession is not explicitly allowed in the 11th Regular Foreign Investment Negative List issued in 2018.¹³ On the other hand, the 11th Negative List explicitly states that 100 percent foreign ownership is allowed through financial and technical assistance agreements (FTAA) with the President, but that has apparently not been factored into the score for mining by OECD.
2. The statutory restrictions in the Business Services sector - that is, Legal, Accounting & Audit, Architectural and Engineering services - may be less well-known. The Constitution reserves the practice of all professions to Filipino citizens “save in cases prescribed by law”, and Accounting, Architecture and Engineering do allow practice by foreigner professionals subject to reciprocity conditions, e.g. ASEAN Mutual Recognition Arrangements are already operational for these professions.¹⁴ Still, the OECD gives Accounting and Engineering services a score of 1.00 because

¹⁰ Based on FDI net inflows (BOP figures in current US\$), sourced from <https://data.worldbank.org>

¹¹ <https://www.brookings.edu/articles/vietnams-manufacturing-miracle-lessons-for-developing-countries/>

¹² Specifically, Article XII Section 11 on franchises for public utilities, Article XIV Section 4 on education, and Article XVI Section 11 on the advertising industry. These currently limit foreign ownership to at most 40% or 30%.

¹³ Executive Order 65. The issuance of a regular foreign investment negative list, which specifies investment areas open to foreign investors and/or reserved for Filipino nationals, is mandated by the Foreign Investment Act of 1991, as amended. The 12th Negative list was issued in 2022.

¹⁴ Filipino accountants, architects and engineers may apply to be recognized in ASEAN countries. See <https://www.prc.gov.ph/asean-mra>

the corporate practice by foreigners is not explicitly (or completely) allowed in the 11th Negative List. The practice of Law is also scored 1.0 because non-Filipino citizens cannot become members of the Bar in any case.

3. On the other hand, all manufacturing sectors—Food, Oil ref./Chemicals, Metals/Machinery, Electronics, and Transport Equipment (S5 to S9)—as well as Wholesale and Retail (S11, S12) and Insurance and Other Finance (S19, S20), are free of restrictions. Banking (S18) at 0.125 is restricted to some degree; foreign banks may enter the market subject to conditions.¹⁵ Electricity generation, a component of the Electricity sector (S10), is also restriction-free. Somewhere in between are Transport (S14) at 0.492, Communications (S17) at 0.488, and Construction (S11) at 0.375.
4. Vietnam trumps the Philippines in Business Services, Agriculture, Media, other primary sectors (Fisheries, Mining, Forestry) and Construction, in that order. Vietnam also has less restrictive scores in Electricity (S10) but this is because electricity distribution (including transmission) is scored 0.500 for the Philippines and 0.00 for Vietnam. The latter however does not mean that Vietnam allows foreign ownership in the sub-sector. In fact, Vietnam has always maintained a state monopoly on electricity transmission and distribution (through Vietnam Electricity, a state-owned enterprise or SOE).¹⁶ What is likely happening here is that the OECD scoring methodology does not (yet) incorporate the extent of state ownership, and since state-ownership does not, per se, overtly discriminate against foreign entities (as OECD reasons), a score of 0.0 is assigned [Kalinova et al. 2010].
5. On the other hand, the Philippines does just as well, if not less restrictive, in Banking, Other Finance, Retail, Wholesale, *all* five Manufacturing subsectors, and Insurance. The Philippines has scored 0.00 for statutory equity restrictions in Manufacturing and Wholesale since the index was measured in 1997.

Surprisingly, the scores of the two countries with respect to Transport and Communications are not all that different; the gaps are at 0.084 and 0.125, respectively.¹⁷ Vietnam has maintained the tightest

¹⁵ Among others, reciprocity and that at least 60% of the resources or assets of the entire banking system is held by domestic banks which are majority-owned by Filipinos (RA 10641 of 2014).

¹⁶ As of May 2022, private investors can build new segments of Vietnam's electrical grid and operate those segments without the direct involvement of the state, although the State retains its monopoly over the management of the national power grid system. However, "compliance requirements are stringent" owing to significant national security concerns and "compliance and regulatory risks are heightened for foreign investors..." <https://www.aseanbriefing.com/news/vietnam-s-amended-electricity-law-sparks-new-opportunities-for-foreign-investment/>

¹⁷ The small gap suggests the similarity of equity restriction regimes in both countries. Yet it is surprising how these statutory restrictions have become the whipping boy for the inefficiencies and monopoly that people observe in Transport and Communications—while at the same time extolling Vietnam's performance in these sectors. Clearly something is wrong in this argument.

statutory restrictions in Transport since 1997, despite its score dropping marginally between 2010 and 2020.¹⁸ Its level of restrictions in Communications has stayed the same since 2010 while the Philippines' score dropped (i.e. improved) in 2018.

Table 1. OECD FDI Restrictiveness Index: Equity Restrictions by sector, Philippines and Vietnam, 2020

ID	Sector	Philippines	Vietnam	Distance to Vietnam	Equity restrictions, Legal provisions (as of 2018)
S1	Agriculture	0.675*	0.063	0.612	40%, Art XII Sec.2; 40% in the processing of rice/corn after 30 years (PD 194). 0% foreign equity in the practice of profession by corporations (not listed for corporate practice in 11 th negative list.)
S2	Forestry	0.500	0.063	0.437	40%, Art XII Sec 2.
S3	Fisheries	0.500	0.000	0.500	40%, Art XII Sec 2.
S4	Mining & Quarrying (incl. Oil extraction)	0.500	0.000	0.500	40%, Art XII Sec 2. The 100% provision for FTAA "is assumed to be rather an exceptionally accepted condition" and does not change the score.
S5	Mfg: Food and other	0.000	0.025	-0.025	
S6	Mfg: Oil ref. & Chemicals	0.000	0.000	0.000	
S7	Mfg: Metals, machinery and other minerals	0.000	0.000	0.000	
S8	Mfg: Electric, Electronics and other instruments	0.000	0.000	0.000	
S9	Mfg: Transport equipment	0.000	0.000	0.000	
S10	Electricity	0.250	0.000	0.250	
	<i>Electricity generation</i>	0.000	0.000	0.000	
	Electricity distribution (includes transmission)	0.500	0.000	0.500	40%, Art XII, Sec 2 and 11
S11	Construction	0.375*	0.000	0.375	40% (up from 25% until 2018) for the construction and repair of locally-funded public works (Sec 1 of Commonwealth Act No 541, LOI No 630, and RA 7718). Foreign equity is allowed without restrictions in other construction-related activities
S12	Wholesale	0.000	0.025	-0.025	
S13	Retail	0.000	0.038	-0.038	
S14	Transport	0.492	0.408	0.084	40%, Art. XII, Sec 11
	Surface	0.475	0.331	0.144	"
	Maritime	0.500	0.413	0.087	"
	Air	0.500	0.481	0.019	"
S15	Hotels & restaurants	0.250*	0.038	0.212	40% in tour operators and professional congress organizers (Rules and Regulations to Govern the Accreditation of Travel and Tour Services)
S16	Media	0.788	0.188	0.600	
	<i>Radio & TV broadcasting</i>	0.725	0.125	0.600	0% except for private radio (40%). Art VI, Sec 11, RA 3846.
	Other media	0.850	0.250	0.600	30% for advertising
S17	Communications	0.488	0.363	0.125	40%, Art XII, Sec 11
	Fixed telecoms	0.475	0.363		

¹⁸ The sectors in Vietnam with the tightest restrictions in 1997 were Transport, Banking, Other Finance, Real Estate. In 2010, these were Transport, Real Estate, Communications. In 2020, Transport, Communications, Banking.

	Mobile telecoms	0.500	0.363	
S18	Banking	0.125	0.250	-0.125
S19	Insurance	0.000	0.000	0.000
S20	Other finance	0.000	0.044	-0.044
S21	Business services	0.750*	0.031	0.719
	Legal	1.000*	0.063	0.937
	Accounting & audit	1.000*	0.063	0.937
	Architectural	0.000	0.000	0.000
	Engineering	1.000*	0.000	1.000
S22	Real estate investment	0.500	0.167	0.333
<div> <div>- Citizenship is required for admission to the Bar</div> <div>- 0% in the practice of profession by corporations for Law, Accountancy, Engineering, which are not listed for corporate practice in the 11th negative list.</div> <div>40% for private land, Art XII, Sec 7</div> </div>				
Total Equity Index		0.282	0.077	0.204

Source: Columns 2 and 3: <https://stats.oecd.org/Index.aspx?datasetcode=FDIINDEX>; Column 4: https://qdd.oecd.org/subject.aspx?Subject=ASEAN_INDEX. Notes: Sectors in bold are targeted by RBH 6 or 7 of the Senate and House. Scores marked with an asterisk are for sectors restricted by ordinary law or administrative policy.

Given that statutory equity restrictions are comparable in Manufacturing (i.e., no restrictions), Transport (restricted to less than 50 percent), Communications (restricted to less than 50 percent), and, possibly, electricity distribution (restricted to less than 50 percent in the Philippines, while transmission is state-owned; state-owned and -operated in Vietnam), the question arises as to how statutory restrictions *per se* can be argued to have been decisive in the miracle of Vietnam's manufacturing exports relative to the Philippines' mediocre performance. Consequently, one must ask whether lifting statutory restrictions in transport, communications, and electricity distribution—as intended by RBH 6 and 7—will serve the purpose of helping the Philippines keep pace or catch up with Vietnam.

A further point to note is that both the Executive and Legislative even before and up to now have the opportunity to lift equity restrictions in some key sectors—if only they wanted to do so. For instance, business services (and even agriculture) could have been liberalized by coordinating the simplification of rules for the individual and corporate practice of professions. Construction could have been expanded by removing barriers found in relevant laws. Tourism could be liberalized by simply relaxing accreditation rules.

III. Statutory foreign equity limitations and FDI in ASEAN

We now discuss results from three working papers that were cited during the RBH7 hearings as providing an empirical basis for lifting equity restrictions (or, in the case of the first paper, as **not** a basis for being **against** economic cha-cha.¹⁹) These are the papers by Parcon-Santos, Amador, and Romarate [2021], Lacaza [2023], and Mistura and Roulet [2019].²⁰ The first, which the authors have

¹⁹ RBH7 hearings, Day 2, Part 2, around the 3:14 hour mark.

²⁰ These are, respectively, a BSP (Bangko Sentral ng Pilipinas) Discussion Paper, a CPBRD (Congressional Policy and Budget Research Department) Discussion Paper, and an OECD (Organization of Economic Co-operation and Development) Working Paper.

made clear was not written with the current debate in mind,²¹ analyzes the determinants of FDI “outward positions” of the top FDI source countries to recipient economies in the ASEAN-5—Indonesia, Malaysia, Philippines, Thailand and Vietnam—over the period 2009 to 2019. The second paper, which was written with economic cha-cha in mind, does the same thing for the period 2010–2020. The third paper examines determinants of bilateral inward FDI stocks and cross-border mergers and acquisitions (M&A) investment stocks among a set of 60 advanced and emerging economies, including the Philippines, over the period 1997 to 2016.²²

The measure of FDI used in the first two papers, “FDI outward position”, may require some explanation. What it refers to is the total accumulated level of direct investment from the source economy, say Japan, at the end of the year, by destination (or host) country, say the Philippines.²³ Direct investment position is a stock, i.e., the value of the resident investor’s equity in and net loans to enterprises in the foreign destination country held at the end of the reference period; FDI stocks are thought to better capture the “optimal level of capital allocation across countries than FDI flows”.²⁴ The data used by these two papers come from the IMF’s Coordinated Direct Investment Survey (CDIS), which has direct investment by source-country to each member of the ASEAN-5 by year, yielding a panel across time and across countries.²⁵

All three papers employ either the OECD’s Equity Index of the RRI or the overall RRI itself as one of their explanatory variables. They all apply an augmented “gravity model”, which has been described as “the workhorse model in the empirical literature analyzing the determinants of FDI across

²¹ RBH7 hearings, Day 2, Part 2, around the 3:17 hour mark. Dr. Parcon-Santos is explicit in saying that they were only interested in why the Philippines was lagging behind in terms of FDI and did not write to support any position on economic charter change. She made clear that the study dealt with overall FDI; whether or not easing restrictions in the sectors contemplated under RBH7 would increase their respective FDI would require a different study. In line with this, she urged “a careful assessment of the sectors that we are trying to open up to foreign investors before taking any action...”

²² Mistura and Roulet [2019] note that the previous literature on restrictions and FDI was confined to the experience of advanced economies, and when emerging economies were included, “fairly simplistic measures of capital controls” were used. A review of literature is provided in Box 2 of the paper.

²³ [Foreign] Direct investment is a category of cross-border investment associated with a resident in one economy having control or a significant degree of influence on the management of an enterprise interest (10 percent or more of voting stock) that is resident in another economy [IMF Balance of Payments and International Investment Position Manual, 6th Edition]. A direct investment is distinguished from a portfolio investment, which is the purchase of, say, stocks and bonds of entities located in another country, often to make a short-term speculative gain.

²⁴ In contrast, flows are more likely to be influenced by the business cycle and other short-term adjustments as well as single events (e.g. large cross-border mergers and acquisitions) (Parcon-Santos et al. [2021], Mistura and Roulet [2019]).

²⁵ CDIS includes only direct investment position (stock) data. “Mirror” data on inward (outward) direct investment positions of their counterpart economies can be derived, using outward (inward) direct investment positions reported by CDIS participant economies, CDIS data have a number of limitations, including that they are self-reported and voluntary. See documentation at <https://data.imf.org/?sk=40313609-f037-48c1-84b1-e1f1ce54d6d5&sid=1390288795525>

countries”.²⁶ In its barest formulation, the FDI gravity model posits that bilateral FDIs are positively related to the product of the market sizes of the host and source countries and negatively related to the distance between them. The former proxies for supply and demand forces and the latter “accounts (roughly) for transaction costs and other frictions in bilateral investments” [Mistura and Roulet 2019: 18]. Researchers augment the simple gravity variables with other research-specific variables, then estimate the model using what is known as the Poisson pseudo-maximum likelihood (PPML) estimator. Owing to the specification of their models, almost all of the estimated coefficients generated by the PPML in the cited papers are simple “elasticities” which measure the responsiveness of the variable to be explained to changes in the explanatory variables included in the regression: the coefficient is interpreted as the percentage increase in FDI for every one percent increase in, say, the Equity Index. A larger elasticity denotes the greater importance of a variable as a determinant. As in most exercises of this nature, all three papers estimate statistical associations or correlations between the variables, rather than causation.²⁷

Differences in statutory foreign equity restrictions among the ASEAN-5 may help explain some of the observed distribution of FDI from source countries since 2009, but they cannot be considered as the main explanatory factor and can hardly be called necessary.

Parcon-Santos, Amador, and Romarate [2021] examine the dispersion of FDI among the ASEAN-5 coming from their top 15 FDI source-countries for the period 2009-2019 and asks these broad questions: “What factors explain differences in FDI across ASEAN-5 countries” and “How do different foreign direct investors choose across potential host countries?”²⁸ The second question is a reference to the different types of FDI, i.e., whether resource-seeking, market-seeking (horizontal), efficiency-seeking or export-platform (vertical), or strategic-asset seeking.²⁹ The presumption is that each type of FDI may assign different degrees of importance to potential host country characteristics. For instance, market size may be expected to carry greater weight for market-seeking FDI; relative costs and productivity of inputs may matter more for efficiency-seeking and export-platform FDI, and

²⁶ Gravity models were originally developed to explain bilateral flows of trade in goods. They were later also applied to explain foreign investment flows.

²⁷ Correlation is a statistical association between variables. Causation means that a change in one variable causes a change in another variable. Estimating causal effects requires an instrumental variable strategy, which the studies do not undertake. However, two of the studies – Parcon-Santos et al [2021] and Mistura and Roulet [2019] – undertake panel data regressions with country fixed effects, at least as a test of robustness, which can attenuate omitted variable bias. The latter paper also reports a dynamic gravity model as an additional test (which we discuss on p. 17).

²⁸ They also ask, “Are sovereign credit ratings useful in determining a country’s attractiveness for FDI?”, which was actually a key motivation.

²⁹ Natural-resource seeking FDI are interested in exploiting locally available natural resources; horizontal FDI pursue access to domestic markets to sell final products or intermediate goods ; vertical FDI seek availability and cost advantages for production for export back to the source country or to third party countries (export-platform); strategic asset-seeking FDI acquire or access local knowledge, distribution networks, technology and other strategic assets (Dunning and Landon [2008] and Ekholm, Forslid, and Markusen [2007]).

so on. The authors use this lens to interpret their findings even if their data for FDI (from the CDIS) cannot distinguish FDI by motive or by industrial sector. This is a limitation of their paper.

In their base model,³⁰ the authors include traditional gravity variables (real GDP of host and source countries, geographical distance between capital cities) and host-country factors that may matter to investment costs of source countries: corporate tax rate, cost and quality of labor (minimum wage, human capital index), macroeconomic stability (inflation), and economic openness, as measured by the Equity Index of the RRI. Successively added are variables that measure public governance (Corruption Perception Index, Rule of Law); business regulatory environment (Ease of Doing Business-Trading Across Borders); and the quality of hard/soft infrastructure (Roads Index and Telecoms Infrastructure Index).

What do the reported results reveal about the role of statutory FDI restrictions? These are our interpretation of the reported results, understanding that an in-depth look at statutory FDI restrictions was not the focus of the paper.

1. The Equity Index is found to be negative and statistically significant in the base model (columns 1 and 2, Table 2). This means that changes in the Equity Indices across the ASEAN-5 do help explain changes in the distribution of FDI outward position of source countries to them. The negative sign means relaxing (reducing) statutory foreign equity restrictions is associated with an increase in a source country's outward FDI position, holding other factors fixed. The estimated coefficient of -0.4999 means that a 10 percent reduction in equity restrictiveness, as measured by the Equity Index, is associated with an average 5 percent increase in FDI outward position.
2. However, the statistical and policy significance of the Equity Index *weakens* as institutional and infrastructure variables are added, all of which are statistically significant in their own right (Table 2, columns 3 to 10). The effects of improvements in Corruption Perception, Rule of Law, Ease of Doing Business, and Road and Telecoms Infrastructure are *stronger*, implying they are comparatively of greater importance as determinants of FDI. The difference is particularly stark in the case of Ease of Doing Business-Trading Across Borders (EDB): a 10 percent improvement in the EDB score is associated with a 15.1 to 15.8 percent increase in FDI outward position, holding the base and other governance variables fixed (Table 2, columns 5 and 6). This effect is 3.7 times greater than the response associated with relaxing equity restrictions (now estimated at a smaller 4.1 to 4.3 percent increase in FDI outward position).

³⁰ Parcon-Santos et al. [2021] implement many specifications. Here we highlight here only those that are relevant for our discussion.

Table 2 Correlates of FDI outward position from the Top 15 Source Countries to the ASEAN-5, 2009-2019, as estimated by Parcon-Santos et al. [2021]

Explanatory variables	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
Market size, source	-0.594	-0.446	-0.508	-0.509	-0.517	-0.515	-0.547	-0.485	-0.507	-0.536
Market size, host	0.853***	0.927***	0.943***	0.999***	1.009***	1.029***	0.888***	1.049***	1.042***	0.968***
Distance	-0.469***	-0.481***	-0.447***	-0.442***	-0.443***	-0.442***	-0.451***	-0.462***	-0.450***	-0.446***
Corp Tax Rate	-1.182***	-0.943***	-1.214***	-1.023***	-0.795***	-0.717***	-1.134***	-1.031***	-0.649*	-0.820**
Min Wage	-0.074**	-0.062*	-0.02	-0.015	-0.023	-0.023	-0.026	0.025	-0.018	-0.026
Human Capital Index	4.328***	2.986***	2.399***	2.199**	1.178	1.17	2.147***	1.053	0.71	1.243
Equity Index	-0.499**	-0.509**	-0.422*	-0.361	-0.431*	-0.409*	-0.337	-0.266	-0.403*	-0.384
Inflation		-0.054**	-0.037	-0.03	-0.024	-0.023	-0.02	-0.058**	-0.03	-0.018
Corruption Perc			0.688*		0.312					
Rule of Law				0.970*		0.418				
EDB					1.579***	1.510**			1.834**	1.322**
Road infra							0.589**			0.316
Telecoms infra								0.570**	0.141	
R2	0.82	0.83	0.83	0.83	0.83	0.83	0.83	0.83	0.83	0.83
Observations	700	700	700	700	700	700	700	700	700	700

Source: Parcon-Santos, Amador, and Romarate [2021: Table 5.2]

Notes: (1) Dependent variable: FDI outward position of source to host country; (2) *, **, and *** - denote significance at 10%; 5%; and 1% levels, respectively; (3) year and source dummies included, but not shown; (4) infrastructure variables are highly correlated with the governance indicators, hence they are not included in the same estimation [ibid: 23]

- When Telecoms Infrastructure is taken into account, FDI outward position becomes even more responsive to improving the ease of doing business: a 10 percent improvement in EDB is now associated with an 18.3 percent increase in FDI outward position. (Table 2, column 9). This is 4.6 times greater than the response associated with relaxing equity restrictions (i.e. now estimated at an even smaller 4.0 percent increase in FDI outward position). If Road Quality is accounted for along with EDB, the response of FDI outward position to a 10 percent improvement in EDB is not as large— an increase of about 13.2 percent—but this is still 3.6 times larger than the response associated with relaxing equity restrictions, i.e. estimated at a 3.8 percent increase in FDI outward position (Table 2, column 10).
- Indeed, it is notable that the coefficient of Equity Index in the last specification (Table 2, column 10) is statistically *insignificant*. This means that changes in the measure of equity restrictiveness across the ASEAN-5 do not help explain changes in the dispersion of FDI outward position from source countries to them. The Equity Index is also statistically insignificant when Rule of Law,

Road Quality, or Telecoms Infrastructure quality are added to the base model individually (Table 2, columns 4, 7 and 8). When the overall RRI is used as a proxy of economic openness, it is also statistically *insignificant* for all investors once macroeconomic stability, quality of institutions, and quality of infrastructure are accounted for (Appendix Table 2)

In sum, differences in foreign equity restrictions across the ASEAN-5, as measured by the Equity Index, may help explain *some* of the observed dispersion of FDI outward position from source countries over the period, but they *cannot* be considered as the main explanatory factor and can hardly be called necessary.³¹ Improvements in the business regulatory environment, combined with improvements in infrastructure, not only have effects that dwarf the size of those coming from any change in foreign equity restrictions, but changing restrictions may not even have a significant bearing on outcomes.³²

The authors implement other specifications (e.g. segregating Asian and non-Asian source countries, exploring the role of industrial agglomeration, technological innovation, and bilateral investment treaties, and so forth) that will not be discussed here but which are rich in insight. It is enough to make the obvious observation that different types of FDI will have different sensitivities to various locational factors, including statutory equity restrictions. This should suggest to policymakers the importance of understanding the different types of FDI and what attracts them so that measures can be designed for those that will best serve policy goals. This presupposes that the country's policies towards FDI are not solely about "the attraction of FDI, as if it were simply a matter of capital" but are closely integrated with industrial policy.³³ "[Not] every dollar of FDI has the same potential to promote development" [Narula 2014: 13, 8].

Among the ASEAN-5, the potential effects on FDI of taking action on other fronts, such as improving perceptions of public sector corruption, are far stronger than the potential effect of lifting equity restrictions.

Lacaza [2023] draws heavily from the approach of Parcon-Santos et al. [2021] in terms of choice of host countries, source countries and period of study (with minor adjustments), dependent variable

³¹ That is, the lifting of equity restrictions is one of several "sufficient" conditions affecting FDI allocation. But even its status as a "sufficient" condition is tenuous given the fact that it becomes insignificant in some of the specifications. For the same reason, it can be argued that it is not "necessary" as an explanation of FDI allocation in the crude sense that other (likewise sufficient) factors can operate independently and with greater effect on the dependent variable even in the absence of changes in equity restrictions. (Please see footnote 7). The research design of a correlation study limits how far "necessity" can be precisely inferred. A more rigorous test would have been to interact equity restrictions with other factors, say, infrastructure, to see whether the latter continues to exert an influence on investment even when equity restrictions are binding.

³² In other words, X may be a sufficient condition for Y, but relative to other sufficient conditions, it is a weak one.

³³ There are divergent views on the matter of industrial policy. We comment on this in the next section.

and source data. But it departs from the earlier paper in the choice of explanatory variables.³⁴ For instance, Rule of Law, Ease of Doing Business, and variables of infrastructure quality are not considered, despite the findings of the earlier paper. At the same time, a new variable, “common colonizer”, is included. No conceptual or practical justification however is given for these modelling choices.³⁵

Estimated coefficients have the expected signs and statistical significance (Table 3). Viewed against the third (most comparable) specification of Parcon-Santos et al. [2021], estimated coefficients are markedly greater in magnitude. For instance, the coefficient of the Equity Index is 0.765 (versus 0.422 in the specification of Parcon-Santos et al.). Thus Lacaza [2023] finds that “a 10 percent reduction in foreign equity restrictions is projected to generate an average increase of around 7.7 percent in the FDI outward position from source countries to host countries”.

Ideally, these large differences should have been examined by the paper itself.³⁶ In any event, the estimated elasticity of 0.77 for the Equity Index variable is what has been bandied about in the House of Representatives to illustrate what sort of bump in FDI could be obtained if the Philippines reduced its Equity Index by 70 percent to the level of Vietnam’s (or, what FDI the Philippines would potentially forego if it did not lift equity restrictions). In one instance, it was stated during the hearings that “improving the foreign equity restrictions score of the Philippines from 0.281 to 0.077, or by 70 percent ... will be equivalent to an additional FDI of US\$6.7 billion, or ₱323 billion” from a base of about ₱600 billion.³⁷ (N.B. The amount of ₱323 billion is 53.9 percent ($=0.77 \times 70$ percent) of ₱600 billion.)

³⁴ There is also a significant change in the list of source countries, although the original intent seems to have been to simply expand the list of the earlier paper. The source countries in Parcon-Santos et al. [2021] are the “top 15” of ASEAN, namely, Japan, USA, Singapore, China, Hong Kong (HK), the Netherlands, Luxembourg, United Kingdom, South Korea, Malaysia, Taiwan, Australia, India, Indonesia, Canada. Lacaza [2023] expands this to the “top 20”, adding Switzerland, Thailand, Ireland, France, and Belgium. However, Singapore, Hong Kong, Taiwan, and Belgium are omitted “due to incomplete or unavailable data on the FDI restriction index and other relevant variables” (p. 9).

³⁵ “Common colonizer” may have been borrowed from Mistura and Roulet [2019], who explain that similarities in administrative practices due to a common colonial linkage could facilitate cross-border investment. Other distance variables featured in Mistura and Roulet [2019] however are not adopted by Lacaza [2023].

³⁶ Since the paper drew heavily from the earlier work, this should have been the standard practice. Besides, the methodological choices made in Lacaza [2023] raise questions regarding their impact on results. For instance, what was the effect of omitting Singapore, Hong Kong, and Taiwan as source countries given that they accounted for upwards of 18 percent of total FDI into ASEAN for the period.

³⁷ 19th Congress Committee of the Whole (RBH7), Day 3, Part 2, somewhere at the 3:51 hour mark. Lacaza explains (in personal correspondence), that ₱600 billion is, roughly, the peso equivalent of US\$11.983 million, the net inward FDI flows in 2021 as reported in <https://data.worldbank.org>.

Table 3 Correlates of FDI from Top FDI Source Countries to ASEAN-5:
2010-2020, as estimated by Lacaza [2023], and 2009-2019, as estimated by Parcon-Santos et al. [2021]

Correlates	Parcon-Santos et al. [2021]	Lacaza [2023]
	(3)	
Market size, source	-0.508	-0.113
Market size, host	0.943***	1.835***
Distance	-0.447***	-0.864***
Corporate Tax Rate	-1.214***	-1.861**
Minimum Wage	-0.02	
Human Capital Index	2.399***	10.85***
Equity Index	-0.422*	-0.765*
Inflation	-0.037	-0.623***
Corruption Perception	0.688*	6.053***
Rule of Law		
EDB		
Road infrastructure		
Telecoms Infrastructure		
Common Colonizer		0.764***
Constant	10.607	-17.32
<i>R</i> ²	0.83	0.439
Observations	700	770

Source: Table 3, this paper, and Lacaza [2023]. Notes: (1) Dependent variable: FDI outward position of source to host country; (2) *, **, and *** - denote significance at 10%; 5%; and 1% levels, respectively; (3) year and source dummies included, but not shown, and (4) To understand how the two sets of source countries differ, please refer to footnote 34.

Such illustrations must be explained carefully, however. It should be remembered that coefficient estimates from these and similar empirical exercises are potential *average effects* across countries, and may not apply exactly to specific countries, much less to specific sectors within a country.³⁸ But as long as the estimated elasticities of this paper are to be utilized by the author to draw attention to the potential benefits of relaxing restrictions, then the illustration must also include the finding that a much larger increment in FDI can be obtained through far simpler means—for instance, by lowering the perceived levels of public sector corruption. This can be inferred from the model's large estimated coefficient of the Corruption Perception Index (CPI). It implies that a *10 percent improvement* in countries' CPI is associated with a whopping *60.5 percent average increase* in FDI outward position, holding all other factors fixed - about *8 times larger* than the 7.7 percent increase in FDI associated with a 10 percent improvement in the Equity Index. Thus, to go along with using the same ₱600

³⁸ Estimated coefficients must also be used appropriately. In this case, the 0.77 estimate refers to the sensitivity of a stock variable, FDI outward position. Net inward FDI flows on the other hand are a flow variable. CDIS or UNCTAD data on FDI inward stock to the Philippines as of end-2021 would be more appropriate. To make simple comparisons, however, we use the same (inappropriate) base figure in our illustration.

billion as a base, a 10 percent improvement in the CPI, could potentially generate an additional ₱363 billion in FDI, or about ₱40 billion more than what is estimated from reducing Equity Restrictions by 70 percent. It is also a feasible route: improving our CPI score by 10 percent means raising it from 34/100 (in 2020) to between 37/100 and 38/100, a feat the country *already achieved in 2014*.³⁹ Doing so again is not inconceivable therefore and does not require amending the Constitution.

One might also simulate the potential effects of lowering the corporate income tax (CIT) from 25 percent to 20 percent,⁴⁰ which has been Vietnam's CIT since 2016, although, again, it would only be for illustration purposes as coefficient estimates are average effects and may not apply exactly to each country. However, the main point has hopefully already been made: as estimated, the potential effects on FDI of taking action on other fronts, such as perceptions of public sector corruption, are likely to be much stronger than the potential effect of lifting equity restrictions.

On a global level, the relationship between inward FDI stock and statutory foreign equity restrictions is not straightforward. The significance of the latter seems to depend on the type of FDI by motivation, manner of entry, and industrial sector involved.

Mistura and Roulet [2019] is not a paper exactly comparable to the other two. Observing that many primary and service sectors “remain off-limits to foreign investors” in various parts of the world, the authors are concerned about the “unfinished FDI liberalization agenda” and set out to estimate potential costs in terms of foregone investments of keeping statutory barriers in place. It therefore uses a more macro approach, investigating the determinants of bilateral inward FDI stocks among a large group of 60 advanced and emerging economies, over the period 1997 (or 2001) to 2012. It should be noted that how these determinants may be weighed by specific FDI source countries interested in the ASEAN as a region is beyond its scope.

The upside is that the paper is able to investigate possible industrial sector-specific nuances in the sensitivities of FDI which Parcon-Santos et al. [2020] is not able to do. This is because data on cross-border merger and acquisition (M&A) investments stocks, which the paper uses alongside data on bilateral inward FDI stock, permits a sectoral look.⁴¹ M&A data is described as “representative of the

³⁹ The country's CPI slid down from 38/100 in 2014 to 35/100 in 2015, then further to 34/100 in 2017. In 2021 and 2022, it went down further to 33/100 before recovering to 34/100 in 2023.

⁴⁰ The coefficient estimate for CIT suggests that a 20 percent reduction in CIT (i.e., from 25 percent to 20 percent) could potentially generate an average 37.2 percent increase in bilateral FDI outward positions, all other factors held fixed. CREATE reduced the CIT to 25 percent, retroactive to July 1, 2020, and will reduce it by 1 percent annually for domestic corporations and resident foreign corporations (RFC), reaching 20 percent by 2027.

⁴¹ Bilateral data on nominal inward FDI stock are from OECD and UNCTAD. Bilateral M&A inward investment stock data are from a commercial data provider (Dealogic). This is supported by research but is not subject to official vetting by authorities. Coverage may also be uneven across time and countries thus the authors urge “caution” when interpreting results. The authors also note that the data have not been netted for cases where

international market for corporate control of profit-generating assets rather than development of new (greenfield) ones which had traditionally been the focus of the literature. The authors contend that “much FDI currently takes the form of cross-border M&As”. The paper investigates the determinants of bilateral inward M&A investment stocks for the whole economy, as well as for the primary, manufacturing and services sectors individually, over the period 2001-2016.

The paper’s variable of interest is the RRI, as a whole and by each of its components. The model is run using the overall index and then, alternately, using indices by type of restriction (i.e., equity restrictions, screening, and other restrictions) to assess the implications, if any, for the attractiveness to FDI. Several other variables are included in the baseline model, such as traditional gravity measures (market size, distance, contiguity, common language, common colonizer), along with measures of remoteness, trade openness, membership in trade agreements, dissimilarities in factor endowments, natural resource endowments, corporate tax rate, real bilateral exchange rate, and governance. Governance is represented by a synthetic variable created by averaging five of six World Governance Indicators developed in Kaufmann et al. [2003] and is expected to have a positive effect.⁴²

We make five observations about the paper’s reported results.

1. With inward FDI stocks as the dependent variable, the baseline model finds a negative and statistically *significant* relationship with FDI restrictiveness as measured by the RRI (Appendix Table 3). It is estimated that actions to reduce RRI by 10 percent could increase bilateral inward FDI stocks by around 2.08 percent on average. By component, equity restrictions have the *strongest* effect, with a coefficient of -0.287, against -0.107 for screening restrictions (and -0.008 for other restrictions, which is not significant.) The coefficient of -0.0287 means that actions that improve the equity index by 10 percent, could increase bilateral inward FDI stocks by around 2.87 percent on average.
2. For M&A inward investment stocks economy-wide, overall RRI remains negative and statistically significant. That is, M&A inward investment stocks are expected to increase 3.05 percent given a 10 percent reduction in the RRI (Appendix Table 4). But here equity restrictions are strikingly no longer material: the coefficient of the Equity index is statistically and economically *insignificant*, with a coefficient of just -0.04. In contrast, the two other components of RRI are highly

the target and acquired firm are located in the same country but the equity seller is in a third country, and so differ from FDI statistics which are net of divestments.

⁴² The authors do not explain why the five indicators were combined instead of tested individually. This may be because governance is not a main variable of interest. The five WGI indicators chosen were Voice and Accountability, Political Stability, Regulatory Quality, Rule of Law and Control of Corruption. Government Effectiveness was excluded.

significant: a 10 percent reduction in “screening restrictions” and in “other restrictions” could increase M&A inward investment stock by 1.79 percent and 1.08 percent, respectively.⁴³

3. In regressions that distinguish between industrial sectors (i.e., primary, manufacturing, and services) the Equity Index *remains insignificant* (Appendix Table 5).⁴⁴ In contrast, the estimated coefficients of the overall RRI and its sub-indices for screening restrictions and for other restrictions are negative and strongly significant for services, though less so for manufacturing. All indices are insignificant (and positive) for the primary sector.
4. The measure of human capital dissimilarity is statistically significant and carries the expected negative sign. This means a greater gap in human capital endowments between origin and destination countries is associated with less FDI or M&A inward stocks. The authors note that this could suggest the predominance of horizontal FDI and M&A investments.
5. The synthetic Governance indicator is *not significant* and has an unexpected negative sign in the baseline model, whether bilateral FDI inward stock or M&A investment stock is used as the dependent variable. The authors do not comment on this result. They are also silent when the coefficient on the Governance variable turns *positive and strongly significant* in a dynamic gravity model that is estimated using a GMM estimator, in a test of robustness of the original results (Appendix Table 3).⁴⁵

Along with the marked change in the significance of the Governance variable, the results of the dynamic gravity model also indicate a *weakening* of the statistical significance of the RRI and Equity Index (from the 1 percent level to 10 percent). The estimated coefficients in this model are not simple elasticities and so more information is needed to say whether foreign equity restrictions or Governance has a greater (or lesser) effect on FDI inward stock. Unfortunately, this test of robustness is used by the authors only to confirm the sign and statistical significance of the main variables of interest, which Governance is not, and nothing more.⁴⁶

⁴³ The authors suggest that this could reflect some more genuine differences between greenfield and M&A investments. For instance, that greenfield investors are typically less willing to share the rents with local equity partners, or M&A investors are potentially more asset-specific and more responsive to the windows of opportunities for acquiring suitable targets and less sensitive to competing locations or to the overall investment climate as signaled by restrictions, and so forth.

⁴⁴ Estimated coefficients are statistically insignificant and small at -0.081 and -0.019 for manufacturing and services, and statistically insignificant (and positive) for the primary sector.

⁴⁵ A dynamic model is estimated following the literature which argues that ignoring the dynamic nature of FDI could lead to an overestimation of the effect of bilateral factors. Results are reported for inward FDI stocks (if a similar test was done for M&A inward investment stocks, it was not reported). Parcon-Santos et al. [2021] perform a number of tests of robustness but not this one.

⁴⁶ The only comments the authors make on the results of dynamic model are that “most of the results are consistent” with the PPLM results and that “other types of restrictions” has become significant at the 10% level.

Nonetheless, what we come away with from these results is a confirmation that the relationship between inward FDI stock and foreign equity restrictions is not straightforward. Their importance will depend on the type of FDI (whether horizontal, vertical, etc.), the manner of FDI entry (acquisitions versus greenfield investment), as well as industrial sector or sub-sector involved. Differences in the way greenfield investments versus mergers and acquisitions respond to equity restrictions may be especially salient in view of the decrease in volume of the former over the last two decades. In developing countries, the value of announced greenfield investments has shrunk from more than double FDI inward flows (in the early 2000s) to about half at the onset of the pandemic [Berger and Ragoussis 2022]. Meanwhile, acquisitions, or *brownfield* investments more generally, have doubled as a share of FDI in low- and middle-income countries over the past 10 years [WB 2020]. Brownfield FDI refers to any purchase by a foreign entity of assets that corresponds to more than 10 percent of total assets of a target company.⁴⁷ While a minority share does not necessarily grant control over the firm, “shareholders can significantly influence the firm strategies and managerial decisions at ... thresholds, generally over 30 percent” [WB 2020: 59]. Berger and Ragoussis [2022: 3] write how “evidence has shown that it (brownfield investment) can be significant in the medium term, which invites a reassessment of incentives and framework conditions to foster its potential.”

The paper also confirms that governance, as measured, matters, although the paper does not concern itself with further investigating how important governance can be relative to equity restrictions.

To sum up what we gather on statutory equity restrictions and FDI from the working papers just discussed, we have the following:

1. Differences in foreign equity restrictions may help explain *some* of the observed distribution of FDI from source countries to the ASEAN-5 since 2009, but they *cannot* be considered as the main explanatory factor and can hardly be called necessary. *If* the economic charter change is *premised* on the *necessity* of lifting equity restrictions as a condition for improved economic performance, then this could be considered as evidence against it.⁴⁸
2. Among the ASEAN-5, improvements in the business regulatory environment, combined with improvements in infrastructure, have effects on FDI that dwarf the size of those coming from any change in foreign equity restrictions. One paper estimated the potential effects on FDI of improving perceptions of public sector corruption to be 8 times stronger than the potential effect of lifting equity restrictions.

⁴⁷ 10 percent is the threshold for a foreign investment to be considered FDI as per the IMF and OECD. “The purchase can be friendly or unfriendly and result in various combinations of outcomes in terms of creating a new legal entity, including a simple acquisition or a merger. Joint ventures do not fall under the category of brownfield foreign investment because they refer to the establishment of new facilities—greenfield investment— involving a local and a foreign entity.” [WB 2020: 59].

⁴⁸ Refer to footnotes 7, 31 and 32.

3. On a global level, the relationship between inward FDI stock and foreign equity restrictions is not straightforward. The significance of the latter seems to depend on the type of FDI by motivation (whether horizontal, vertical, etc.), by manner of entry (M&A/brownfield or greenfield investment), as well as industrial sector or sub-sector involved. For instance, although statistically significant on the whole, foreign equity restrictions appear to be statistically and economically insignificant for mergers and acquisitions and perhaps brownfield investments more generally. This suggests the importance of understanding the different types of FDI and what attracts them as well as the extent to which each type may (or may not) serve a country's policy goals. More on this in the next section.

IV. Foreign direct investment and economic growth

Since foreign equity restrictions may matter differently or not at all to various types of FDI, it may be argued it would be best to just open the gates to all and just lift all restrictions. Alternatively, perhaps Congress should be the given power to craft and change the rules as and when it sees fit? Each of these options is founded on premises that need to be carefully examined. The first presumes that any and all foreign direct investment carries unmitigated benefits. The second presupposes that “legislative flexibility” is superior to constitutional rules when it comes to the economy. We comment on this last point in the final section, but here we shall deal with the first.

Foreign direct investment as a *sine qua non* for development is a precept that seems to have entered conventional wisdom in the late 1970s and 1980s. The idea was especially amplified when financial assistance to developing countries from the World Bank and IMF was made conditional on the implementation of structural adjustment or stabilization programmes that required an FDI-friendly policy regime, among others. By 1990, a blanket endorsement of FDI was one of ten policies identified in what became known as the Washington Consensus [Williamson 1990]. Since then, many developing country governments have since made attracting multinational enterprises (MNEs) through FDI a key component of development policy [Narula [2014], Morrissey [2012]].

It is interesting to note however how more nuanced shade is thrown on the idea by the actual historical experience of latecomer industrialization in the previous century. Not even the World Bank's [1993] canonical description of the “East Asian Miracle”, which enumerates the successful policies of the first-tier Newly Industrialized Economies, lists among them a blanket openness to FDI *per se*. Rather what mattered was an openness to *foreign technology*, which in some cases was achieved through FDI and in other cases through various other means (e.g., technology licensing).⁴⁹

⁴⁹ To wit: “Governments encouraged improvements in technological performance by keeping several channels of international technology transfer open at all times, *even though some, such as direct foreign investment, were restricted or closed for varying periods* [WB 1993:300-301] (Emphasis supplied). Countries that depended more on FDI for technology acquisition included Hong Kong, Singapore, Indonesia, and Thailand. By contrast,

Foreign investment in Taiwan during its heyday the 1960s, for example, amounted only to six percent of gross capital formation⁵⁰ [WB 1990: 132]. More important than the volume of investment was its focus on manufacturing, a sector that allowed Taiwan to capitalize on its facilitated transfers of technology and development of skills.

It is nonetheless the current belief among many policymakers that FDI is not only a direct (and debt-free) source of capital financing but also a means to transform a country's production and employment structures and accelerate GDP growth (Alfaro et al. [2010], Narula and Pineli [2018]). MNEs are assumed to be better equipped relative to domestic firms with best-practice technology, management practices, and organizational arrangements that can improve a country's productivity. They are also thought to create positive externalities which can lead to increasing returns in production and long-run growth.⁵¹ Positive externalities accrue to host countries through the adoption of knowledge and foreign technology, which operates through spillovers to domestic firms via imitation, employee turnover, horizontal and vertical linkages between firms, and competition ⁵² [ibid]. Because of their greater potential for such external effects, "knowledge and technology transfers are expected to be the most important mechanisms through which FDI promotes growth in the host country" [de Mello 1997: 9].

On the other hand, other writers also warned that in the presence of pre-existing distortions in trade, prices, and finance, FDI could in some cases prove counterproductive, even hurting resource allocation and slowing growth. For instance, distortions may bias FDI away from activities where a country has a comparative advantage [Balasubramanyam et al. 1996].⁵³ Investment incentives that favor faster rather than more efficient factor accumulation may jeopardize the role of FDI as a means for advanced technology transfer. "If rents can accrue to the foreign investor using older technologies due to price distortions, there is very little incentive for the foreign investor to engage in inventive activities in the host country or to transfer more modern technologies" [de Mello 1997: 26]. Greater foreign activity could also negatively affect the productivity of wholly domestically owned firms in

South Korea, Taiwan, and China relied more on licensing, capital goods imports, and foreign training [WB 1993: 21].

⁵⁰ This also qualifies the notion that foreign investment should be regarded as a major solution to the country's low saving and investment rates. Most of the investment by the NIEs were in fact financed by domestic saving.

⁵¹ This is suggested by endogenous growth theory (e.g. Romer [1986]). In contrast, FDI can only affect the level of income, leaving the long-run growth rate unchanged in neoclassical growth models a la Solow [1956]. A good discussion is found in de Mello [1997].

⁵² For instance, when the existing stock of knowledge is augmented by domestic firms that invest in learning to keep abreast, this could compel MNEs to bring in better technology, and so forth [Balasubramanyam et al. 1996].

⁵³ See also Easterly [1993] and Borensztein et al. [1998].

the same industry due to competition effects [Aitken and Harrison 1999].⁵⁴ Foreign investment may also decrease national welfare due to the repatriation of profits [Reis 2001].⁵⁵

Much time has passed since the 1970s and 1980s when enthusiasm for FDI ran at an uncritical high. In the meantime, the profession has had the chance to test these hypotheses given the actual long-term experience with FDI. The verdict is that on the whole—and “not for the lack of trying” to find it—consistent evidence of the positive effects of FDI on host economies has proved “elusive” (Benetrix, Pallan, and Panizza [2023], Narula and Pireli [2018], Bruno, Campos, and Estrin [2019]).⁵⁶ The *macro-empirical literature*, which focuses on identifying a causal relationship between FDI flows or stocks and aggregate economic growth, finds no or only weak support for the claim that FDI per se accelerates economic growth (Carkovic and Levine [2005] and Durham [2004]).⁵⁷ FDI has on average a detrimental effect on long-term income levels in developing countries, with the “growth-limiting effects of FDI exceed[ing] growth-enhancing effects” in most countries, including the Philippines [Herzer 2012].⁵⁸ Iamsiraroj and Ulubaşoğlu [2015] report slightly different findings documenting a positive and statistically significant effect of FDI on growth globally. However, even these effects are “economically limited.”⁵⁹ Iamsiraroj [2016] finds evidence of a “virtuous cycle” with FDI contributing to economic growth and growth attracting FDI inflows, although results vary across different groups of countries (e.g. negative and insignificant for Asia and Australasia, negative and significant for Latin America and the Caribbean, etc.)⁶⁰

⁵⁴ This can happen, even if technology transfers take place, when multinationals attract demand away from domestic firms, which then have to reduce production and move up their average cost curves [Aitken and Harrison 1999]. If multinationals purchase less inputs locally than the domestic firms they displace, FDI leads to a decrease in input variety and host-country productivity [Rodríguez-Clare 1996]. Crowding-out effects may also occur when multinational companies compete with domestic firms for scarce resources (skilled labor, logistics, energy), increasing input costs for local firms and squeezing them out of the market [Li et al. 2017].

⁵⁵ In this model, foreign investment increases welfare only if the increase in productivity is great enough to compensate for the loss of profits.

⁵⁶ This is not disputed and is what drives continuing research on the matter. Benetrix et al. [2023] describe a google search that yielded 5000 articles on the subject. Paul and Feliciano-Cestero [2021] is a recent review of the literature. Our discussion here is only a snapshot of what is out there.

⁵⁷ These two studies emerged to contradict the majority of macroeconomic evidence of a beneficial effect [Kotarridi and Stengos 2010]

⁵⁸ Herzer [2012] estimated the long-run relationship between GDP and FDI/GDP for 44 developing countries using data for 1970–2005. The group mean estimate was negative and significant. Country specific coefficients were negative for 26 countries, of which 20 were significant, including for the Philippines.

⁵⁹ As described in Bruno et al. [2019]. Iamsiraroj and Ulubaşoğlu [2015] estimate that a 1 percentage point increase in FDI's share in GDP in a country in a given five-year period leads to a .76 percentage point increase in growth of GDP per capita compared to another country in the same region (see Table 4, column 7 of the paper). Data are from a sample 140 countries for the period 1970 to 2009.

⁶⁰ The paper examines FDI-growth associations using a simultaneous systems of equations approach, employing the three-stage least squares estimator, of 124 cross-country data for the period 1971–2010. See Appendix Table 6 for an example of the variation in their findings.

What this literature generally suggests is that FDI may be growth-enhancing only if certain local conditions or absorptive capacities are present. These include an outward-oriented development strategy [Balasubramanyan et al. 1996]; a minimum level of human capital [Borenzstein et al. 1998]; and well-developed local financial markets (Alfaro et al. [2010], Alfaro et al. [2004]).⁶¹ Iamsiraroj [2016] do not find evidence that human capital is an important channel, and instead finds trade openness and a friendly investment climate to be critical. Benérix, Pallan, and Panizza [2023] confirm the original findings of Borenzstein et al. [1998] and Alfaro et al. [2010] and demonstrate in addition that the relationship between FDI and growth, as well as the mediating effect of education and financial depth, varies over time. The mediating effect may no longer hold in the post-1990 period and the correlation between FDI and growth appears to become insignificant in the 2000s.⁶²

The *micro-empirical literature* on FDI which focuses on spillovers, may have arisen in part from the failure of aggregate cross-country studies to find large and robust evidence on FDI's contribution to growth in low-income countries [Morrissey 2012]. The evidence on the existence of positive productive externalities has itself been “sobering” however (Alfaro et al [2010], Gorg and Greenaway [2004], Narula [2014], etc.). Reviews of literature and meta-analyses of studies on FDI productivity spillovers have indicated “weak regularity in terms of estimated effects, with the only exception being the general negligible effects of the presence of foreign MNEs on the productivity of their competitors (horizontal spillovers)” [Narula and Pineli 2018].⁶³ Vertical spillovers, in turn, are observed to vary considerably across countries, “but they tend to be positive and economically significant when it comes to supplier industries (backward spillovers), whereas the effects on buyer industries (forward spillovers) are economically irrelevant on average”. Mixed findings persist even when more easily measured outcome variables—such as the entry, survival or exit of domestic firms, or their propensity to export and innovate—are used, although the results on export and innovation spillovers are described as “more favorable to FDI, or at least is less blurred than in the case of productivity spillovers” [Ibid: 7].

The failure to find unambiguously positive effects could be due to data and measurement instruments which are not refined enough to probe “what really matters”, e.g., absorptive capacity of domestic

⁶¹ This means that the direct effect of FDI on growth can be zero (or negative), but when interacted with human capital, financial development, or trade, it might have a positive effect on growth [Borenzstein et al. 1998].

⁶² That is, for the period 1998 to 2019. This vanishing effect is hypothesized to be due “the second unbundling”, i.e., starting from the 1990s, better communication allowed MNEs to coordinate complex activities across borders, giving rise to the global value chain (GVC) revolution that has changed the nature of FDI [Benetrix et al. 2023].

⁶³ The rest of this paragraph draws heavily from Narula and Pireli [2018]. The authors cite the meta-analyses of Isrova and Havranek [2013], Havranek and Isrova [2011], and Meyer and Sinani [2009]. Wooster and Diebel [2010] is another. Meta-analysis is a quantitative method of research synthesis. Meta-analyses employing different estimation methods can yield quite different results however [Narula and Pineli 2018].

firms, ownership characteristics of subsidiaries, and so on [Gorg and Greenaway 2004].⁶⁴ Panel data studies which attempt to account for the heterogeneity of firms (domestic firms, foreign subsidiaries, MNEs) do reveal a more nuanced, although still not unambiguous, picture. For domestic firms, studies indicate that only those with high levels of absorptive capacity – e.g., firms with a higher educated workforce or smaller technological gaps to foreign subsidiaries – benefit from spillovers [Rojec and Knell 2018].⁶⁵ For foreign subsidiaries, spillovers appear to be stronger when subsidiaries are competence-creating rather than competence-exploiting (although this may not apply in technology intensive sectors),⁶⁶ domestic market- rather than export-oriented subsidiaries (although evidence is not uniform), and cross-border M&A rather than greenfield investment (in the case of Japanese and Swedish affiliates). The extent of FDI spillovers may also depend on the sectoral structure of inward FDI, i.e., FDI in some sectors (services) may produce more spillovers than in others (manufacturing), and there is heterogeneity even then.⁶⁷ With respect to the issue of equity restrictions, it may be of relevant interest that empirical studies that explicitly take ownership structure into account find that partial foreign ownership ventures and minority foreign-owned affiliates “produce better results” with regard to spillovers to local firms [Ibid: 596].⁶⁸

Regarding MNEs, it would appear that potential benefits may not be equal across investors from different countries, e.g. investors from far-off countries create more beneficial linkages, while some investors (e.g. Japanese, Korean) tend to minimize local procurement relative to others (Narula and Pireli [2018], Havranek and Isrova [2011]). It also appears that the motivation of MNEs⁶⁹ will matter for associated spillover effects, although empirical evidence on this is “intriguingly scarce” [Narula and Pineli 2018]. For instance, export-oriented FDI are less likely to develop links with domestic companies versus market-seeking FDI (Sanchez-Martin et al. [2015], Farole and Winkler [2012]).⁷⁰ Natural-resource seeking FDI tend to have even less potential for spillovers. This is to be expected because resource-seeking FDI are typically more interested in extraction than in production, and MNE activity tends to develop in enclaves, limiting the scope for linkages to domestic firms. Thus, this type of FDI “provides few benefits other than direct employment [for unskilled] and (a share of) export earnings” (Morrissey [2012], Morrissey [2010]).

⁶⁴ It is also possible that spillovers are simply unimportant in reality, or that multinational corporations are effective at ensuring that firm-specific assets and advantages do not spill over.

⁶⁵ The rest of this paragraph draws heavily from Rojec and Knell [2018].

⁶⁶ “Competence-creating” subsidiaries are those which have the mandate to generate new technology in accordance with the comparative advantage in innovation of the host country. “Competence-exploiting” subsidiaries depend on the competence of their parent companies, i.e., home-base exploiting” [Cantwell and Mudambi 2005].

⁶⁷ For instance, FDI in telecoms may have notable benefits versus FDI in utilities, where “linkages other than employment are limited.” [Morrissey 2012]. However, even in telecoms, benefits are not linkages but better access to the service. “It is the use of mobile phones that generates the benefits, not learning from the foreign firms that provide the service.” [ibid: 29]

⁶⁸ This point is also noted in the meta-analysis of Isrova and Havranek [2012] and Havranek and Isrova [2011].

⁶⁹ Motives are market-seeking, efficiency-seeking or export-platform, natural resource-seeking, or strategic-asset seeking. See footnote 29.

⁷⁰ See the papers listed in Rojec and Knell [2018] which deal with the market-orientation of foreign subsidiaries.

Implications

Ultimately, understanding the nexus between FDI and economic growth in full detail will require going beyond average effects, allowing for heterogeneity among both host and source countries, and studying country experiences longitudinally [Narula and Pineli 2018]. Indeed, Kottaridi and Stengos [2010] note that “the way FDI affects growth differs across and within countries. The relationship seems to be complex and the impact varies according to a country’s level of FDI.... [P]arameter heterogeneity may exist in the sense that the effect of a change in a particular variable is not the same.... In other words, there exists a different FDI-growth nexus in different countries.”⁷¹

Moreover, there might not be a direct causal relationship between FDI and economic growth per se. The observed relationship may be, simply, that *the determinants of FDI happen to be the determinants of GDP growth* [Narula and Dunning 2010].⁷² A kinder interpretation however is that

[T]here is an important concatenation between the two. Simply put, MNE (or FDI) activity is not a condition *sine qua non* for development. Instead, the link between MNEs and development is an indirect one: Where inward MNE activity results in positive externalities, and *when* domestic firms have the capacity to usefully internalize these externalities, and *if* the non-firm sector supports domestic capacity building, there will be industrial development [Narula 2014:8].

The key message to policymakers at this time is to take care not to assume that any and all types of FDI will be good for development. FDI spillovers are a “context-specific phenomenon” [Narula and Pireli 2018]. They are not unconditional and are not without potential costs. This is because “not every multinational firm is a good source of externality and not every domestic firm is equally well placed to benefit from multinational activity” [Castellani and Zanfei 2005]. It implies that national governments seeking to realize maximum benefits from FDI must ensure that domestic absorptive capacity exists [Morrissey 2012: 27].⁷³ It further suggests that a more discriminating approach to FDIs should be considered, one that features identifying what sort of technology and knowhow can be of use to local firms, and proactively seeking out the same. This means focusing on the quality of MNE and its activities, rather than simply on the volume of FDI—a pivot that may be necessary in any case given global trends. As Berger and Ragoussis [2022:5] observe: “An indiscriminate focus on

⁷¹ Li, Chen, and Shapiro [2013] on China, or Nguyen, Sun, and Anwar [2017] on Vietnam are examples of country case studies. Joo and Shawl [2023] demonstrate how the FDI-growth nexus for the period 1997 to 2018 differs across BRICS.

⁷² To quote these authors directly: “Unless these intervening mechanisms between MNE activity and development are properly understood, all that can be said with certainty is that the determinants of FDI are also the determinants of development” [Narula and Dunning 2010: 265].

⁷³ Unless otherwise indicated, the rest of this paragraph and the next draw heavily from Morrissey [2012]

investment volume is increasingly futile in the face of stagnating FDI flows, weaker development impact, and longer-term political risks.”⁷⁴

Effective spillovers also require MNEs that are willing to transfer some of their knowhow—“implicitly, by not being overly secretive or isolated, if not explicitly”⁷⁵—as well as domestic firms that want to learn and are able to. Mere involvement with global value chains is no guarantee that supplier firms will necessarily benefit in terms of knowledge transfer, innovation, and increasing value added. Comparing the Philippines and Thailand, for example, Mendoza [2023] has pointed to the importance of the governance structures and power balance existing between foreign lead firms and their local suppliers. Product and functional upgrading—potentially large sources of spillovers—are negatively affected when lead foreign firms exert a tight and hierarchical control over their suppliers. At the same time, however, control structures tend to be more lax when local suppliers show superior capabilities. This implies that countries like the Philippines whose firms and industries show weak industrial and innovative capabilities are likely to derive fewer benefits from their links to global value chains and stagnate in their product niches.

The mechanism to facilitate a transfer to, and utilization by, domestic firms will typically require some sort of government support. Some have suggested that “industrial policy is the mechanism that enables domestic producers to assimilate (adopt and adapt) the technology and knowledge of MNEs” [Morrissey 2012: 30].⁷⁶ This is not the place for a full-scale discussion of the size and shape of industrial policy, which itself has a wide literature.⁷⁷ The point however is to disabuse the public of the notion that any and all forms of FDIs will be good for national development and a net contribution to economic welfare and efficiency. For this reason, there is room for government policy to guide foreign investments into areas that bring the most gains to the country and to create an external social and regulatory environment that encourages foreign firms to share their technology and facilitate upgrading. Noting the inherent power imbalance between foreign lead firms and their domestic suppliers, Mendoza [2023: 25] points to the need for “active institutional and network support for innovation and capacity building...to create a [value-chain] environment conducive for upgrading and sustainable growth”. At a minimum, an emphasis on the retention and expansion of existing MNE investment and deepening their linkages with the domestic economy would be essential [Berger and Ragoussis 2022]. Aldaba and Quejada [2022] suggest the same for the Philippines by proposing streamlining ecozone regulations that currently affect the transactions, and impede the creation of backward linkages, between MNEs located inside zones and domestic companies outside

⁷⁴ Berger and Ragoussis [2023] propose a rethinking of narratives and policies about FDIs.

⁷⁵ Morrissey [2012] discusses how China’s FDI delivers few linkages and almost no spillovers in sub-Saharan Africa (SSA). Chinese firms have increased investments in SSA, particularly in the oil sector and infrastructure construction. However, “chinese firms typically bring their own machinery, equipment and even workers – there are minimal linkages.” [p. 29]

⁷⁶ This is also discussed in OECD [2002].

⁷⁷ A flavor of divergent yet nondogmatic views on the matter can be found in the discussion between Justin Lin and Ha-joon Chang [Lin and Chang 2009].

economic zones. More directly, government may provide fiscal support in various forms to priority innovations and R&D activities in line with industry roadmaps and an overall national innovation policy [Mendoza *ibid.*].

Our objective was to address the assertion that lifting foreign ownership restrictions in the Constitution is a necessary condition for improving economic performance and catching up with Vietnam and other ASEAN neighbors. We have discussed the available empirical evidence which in our view provides only weak support for such an assertion. We have also discussed the literature on the elusive link between FDI and economic growth, making the point that policymakers should take care not to assume that any and all forms of FDI will be good for national development and have a net contribution to economic welfare and efficiency, and pursue quality and appropriateness of FDI rather than quantity.

It should be clear however that we are by no means opposed to FDI and that we do see its potential to make a significant contribution to development. But this is only if we are clear-eyed about what and from where benefits from FDI are to be expected, what the real barriers to investment are, and what supporting institutions and policies are needed so that society can derive the most benefit from it.

We close here with a remark on legislative flexibility.

V. Legislative “flexibility” versus constitutional “rigidity”

Resolutions of Both Houses (RBH) Nos. 6 and 7 propose to amend constitutional articles dealing with foreign-ownership restrictions by appending the phrase “unless provided by law” to the relevant articles.⁷⁸ This expedient is thought to open the possibility of subsequent changes in foreign ownership rules through the enactment of simple statutes.

At first blush, the idea of providing the legislature with the “flexibility” to change rules must seem a definite improvement compared to the “rigidity” of having such rules enshrined in a constitution. For nothing prevents Congress—if it is so minded—from keeping the restrictions as they are. The only difference is that it now allows itself the possibility of changing the status quo in the future. In economic terms, this is akin to expanding the opportunity set of actions, with the former set of actions being a strict subset of the new one. How can this be anything but a win-win?

⁷⁸ This expedient was suggested by Juan Ponce Enrile (now presidential legal counsel) (see, e.g., https://malaya.com.ph/news_news/jpe-makes-cha-cha-easy-just-add-unless-otherwise-provided-by-law/) On the other hand, former chief justice Reynato Puno has argued that this recourse would open congress to judicial challenge, since it would effectively mean congress could amend the constitution through ordinary legislation without subjecting the issue to a plebiscite. (see: <https://newsinfo.inquirer.net/1910382/puno-on-suggestions-to-not-use-unless-provided-by-law-in-economic-cha-cha>)

Words can be tricky, however, and the same choice between “flexibility versus rigidity” can be recast as a choice between “discretion versus rules”. Put this way, the matter requires more careful thought. There is after all a great amount of scholarship, mostly dealing with monetary policy,⁷⁹ that concludes that in many cases, adhering to a rule can paradoxically be superior to giving one’s self discretion.

The problem with granting discretion always lies in how it throws a spotlight on the credibility of the actor (in this case Congress) and how its newfound discretion changes people’s expectations of what might happen. Giving oneself the power to do something implies the power to change and even undo the rules, adding to uncertainty through several channels.

First there is short-run uncertainty. Suppose the “unless-provided-by-law” amendments pass smoothly enough. What would that mean to a foreign investor? Immediately—nothing. Congress would still have to deliberate on and pass specific laws that further open certain hitherto semi-closed sectors.⁸⁰ Allowances must also be made for implementing rules to be drawn up, not to mention possible legal challenges to be met.⁸¹ One effect of this waiting period however is to put foreign investments in limbo until the shape and form of more “liberal” laws become known. Investors otherwise eager to jump in may decide to postpone their decisions if there is the prospect of an improvement over the current regime of ownership laws. A would-be investor who may have been perfectly willing to develop a seaport under the old 40-60 rule may instead decide to postpone their decision because a prospective law might offer the possibility of full ownership. This is a case where the anticipation of the best (from the investor’s viewpoint) becomes the enemy of the good. Exactly how long this interregnum will last—between the change in the constitutional amendments and the effective implementation of the new statutes—cannot be known.

Depending on the shape of laws passed, moreover, further uncertainty may be introduced. Suppose the new law gives some regulatory agency, or Congress itself, the authority to approve which specific foreign investments or which investors might qualify for full ownership—in a process similar to, say, obtaining a congressional franchise. Such an approach might seem prudent as a means to screen out less than desirable investors (e.g., those that represent a threat to national security).⁸² But on the other hand, affording such discretionary power to government would be a virtual invitation to lobbying—a prospect bound to lift the hearts of many a corrupt politician, bureaucrat, or (more neutrally) certain law firms, without necessarily contributing to the greater good. Lobbying itself, of

⁷⁹ Seminal contributors include Kydland and Prescott [1978] and Calvo [1978].

⁸⁰ For instance, public utilities, such as electricity distribution and transmission, water and wastewater pipeline distribution system including sewerage, petroleum and petroleum products pipeline transmission systems, seaports, and public utility vehicles.

⁸¹ Such challenges may be nontrivial considering the comments of former Chief Justice R. Puno cited in footnote 78.

⁸² That compliance and regulatory hurdles are raised, owing to national security concerns, may even be expected at least for certain backbone services. An interesting commentary on this is provided by S. CuUnjieng at <https://www.youtube.com/watch?v=px7CWsUGcQQ>

course, is an expedient fraught with both expense and uncertainty, particularly when bribes provide no assurance of success. This can happen when jurisdictions overlap, members of the legislature change, or when, as often happens, politicians do not stay “bought” [Shleifer and Vishny 1993].⁸³

The well-known idiosyncrasies of Philippine political economy—such as the President’s overbearing influence over the civil service, Congress, and the justice system; the bureaucracy’s vulnerability to powerful but narrow political influence; dynastic politics; the absence of stable ideologies and parties that can temper careerist politics and clientelism—all these cast an extra tinge of uncertainty and unpredictability to politics and policies that color the investment atmosphere for Filipinos and foreigners alike.⁸⁴ Hence not even clearing all initial regulatory hurdles can guarantee continued operational certainty, much less success, nor even guard against virtual expropriation. Whether originating from Congress or the executive, compliance and regulatory risks are par for the course and present rent-seeking opportunities. As recent examples show—notably the nonrenewal of the franchise of the venerable ABS-CBN (and the recent controversy over the Son of God’s less venerable SMNI)—not even sunk investments are entirely secure in this country.⁸⁵ What both cases reveal, in opposite ways, is an investment atmosphere—one directly influenced by Congress—that is highly variable depending on the way the political winds blow, one weighed down not only by mundane rent-seeking but also by exceptional favoritism or its converse, exceptional political targeting and vendetta.

⁸³ There is also the matter of whether regulatory capacity is in place to perform screening functions. As it stands, there seems to be more whimsy and less coherence in economic policymaking, especially of late, e.g. the 2023 rice price caps, the absence of economic cost-benefit analyses of lifting equity restrictions in specific sectors, and so forth.

⁸⁴ This is quite apart from the plain political pressure to legislate visibly and hastily—without sufficient study or long-term perspective—only for critical issues to surface soon after or for these to be walked back subsequently. A recent example is the Maharlika Investment Fund, depicted as a tool for economic development that would promote fiscal stability through strategic and profitable investments, which was passed in 17 days in the HOR, and signed into law in July 2023, only to have its two state bank-funders (which had supported the creation of the MIF) file for “regulatory relief” from the BSP’s capital requirements a couple of months later (<https://www.rappler.com/business/explainer-landbank-development-bank-philippines-challenge-after-funding-maharlika/>). One is also reminded of the institution of the K-12 system in education in 2013, depicted as a panacea for skills mismatch, if not a solution to poverty itself, which is now facing quiet legislation that proposes to revert to the pre-K-12 system.

⁸⁵ This is in sharp contrast to the sunk and other costs of Piatco-Fraport which were, arguably, overcompensated for after the Philippine government expropriated the 96-percent completed NAIA 3 from them in 2003, on the basis of graft, poor work and breach of the constitutional limit of 40 percent on foreigners in public utilities. The Philippine government won its cases at the International Chamber of Commerce in Singapore and the International Centre for Settlement of Investment Disputes in Washington DC. But it did not win at home when the Supreme Court, in 2012, computed “just compensation” for the expropriation to be US\$510.3 million (P25 billion), more than triple the government’s estimate of \$149.5-million based on an audit of Piatco-Fraport’s duly receipted expenses. See <https://www.philstar.com/opinion/2015/09/27/1504694/government-always-won-against-piatco-until>.

The essence of discretion is that what is given can be taken away. In considering whether and how much to invest in the country, foreign corporations will not be oblivious to the manner in which even Filipino corporations can be whipsawed by political or bureaucratic discretion, a concern supported by Ma and Wei [2020].⁸⁶ The picture they see will hardly be reassuring, whether full equity ownership is granted or not.

In the end, the “legislative flexibility” contemplated by RBH Nos. 6 and 7 only makes “discretion” itself the rule, thus inviting greater rent-seeking and creating greater uncertainty in the investment process.

⁸⁶ Ma and Wei [2020] use a model to explain the endogenous composition of capital inflows and find that poor institutional quality leads to both an inefficiently low share of equity financing and an inefficiently high volume of total inflows consisting mostly of debt. Equity investment is more vulnerable to expropriation risk than is debt investment, which is why expropriation risk is particularly important in the case of equity inflows.

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Appendices

Appendix Table 1 Scoring of Equity Restrictions of FDI Restrictiveness Index

Foreign equity limits		Scores
	Start-ups and acquisitions	
No foreign equity allowed		1
Foreign equity < 50% of total equity		0.5
Foreign equity > 50% but < 100% of total equity		0.25
	Acquisitions	
No foreign equity allowed		0.5
Foreign equity < 50% of total equity		0.25
Foreign equity > 50% but < 100% of total equity		0.125

Source: Kalinova et al [2010]

Notes: 1. The score is scaled down when foreign equity limits affect only a portion of the sector.

2. Restrictions on the purchase of land are recorded in two ways: if they concern restrictions on real estate, they are recorded as an equity restriction in the real estate sector; if they impinge on the use of land for business purposes, they are recorded under other operational restrictions in all sectors concerned

Appendix Table 2. Robustness using total FDI Restrictiveness by Parcon-Santos et al. [2021],

Explanatory variables	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
Market size, source	-0.506	-0.419	-0.494	-0.508	-0.502	-0.507	-0.542	-0.481	-0.497	-0.536
Market size, host	0.836***	0.869***	0.889***	0.954***	0.950***	0.976***	0.852***	1.053***	1.047***	0.897***
Distance	-0.456***	-0.472***	-0.440***	-0.436***	-0.436***	-0.435***	-0.441***	-0.453***	-0.443***	-0.437***
Corp Tax Rate	-1.336***	-1.297***	-1.563***	-1.368***	-1.166**	-1.112**	-1.351***	-1.173**	-1.000*	-1.187**
Min Wage	-0.070*	-0.053	-0.006	0.005	-0.009	-0.004	-0.016	0.045	0.027	-0.014
Human Capital Index	3.635***	2.222***	1.547***	1.179**	0.36	0.359	1.622**	0.451	-0.162	0.902
Equity Index	-0.505***	-0.351	-0.225	-0.102	-0.230	-0.165	-0.240	-0.185	-0.198	-0.235
Inflation		-0.043	-0.029	-0.024	-0.017	-0.016	-0.009	-0.053	-0.034	-0.007
Corruption Perc			0.736**		0.370					
Rule of Law				1.105**		0.614				
EDB					1.512***	1.274**			1.227	0.866
Road infra							0.668**			0.498*
Telecoms infra								0.682***	0.446**	
R2	0.815	0.822	0.819	0.82	0.82	0.82	0.824	0.825	0.823	0.823
Observations	700	700	700	700	700	700	700	700	700	700

Source: Personal correspondence with H. Parcon-Santos

Notes: dependent variable: FDI outward position of source to host country; *, **, and *** - denote significance at 10%; 5%; and 1% levels, respectively; s1-s10 refer to specifications 1-10 (see Table 2, this paper)

Appendix Table 3. Signs, significance and (selected) coefficients of determinants of bilateral inward FDI stock, 1997/2001 to 2012: Baseline PPLM versus Dynamic system GMM, in Mistura and Roulet [2019]

Variables	PPLM Model				Robustness test: Dynamic system GMM gravity model			
	1	2	3	4	1	2	3	4
FDI Inward (t-1)	-				(+) ^{***}	(+) ^{***}	(+) ^{***}	(+) ^{***}
FDI index (-1)	0.208 ^{***}				-0.013*			
FDI_equity		0.287 ^{***}				-0.017*		
FDI_screening			0.107 ^{***}				-0.014 ^{***}	
FDI_others				-0.008				-0.018 ^{**}
GDP_origin	(+) ^{***}	(+) ^{***}	(+) ^{***}	(+) ^{***}	(+) ^{***}	(+) ^{***}	(+) ^{***}	(+) ^{***}
GDP_destination	(+) ^{***}	(+) ^{***}	(+) ^{***}	(+) ^{***}	(+) ^{***}	(+) ^{***}	(+) ^{***}	(+) ^{***}
GDP growth potential	(+) ^{**}	(+) ^{**}	(+) ^{**}	(+) ^{**}	(+) ^{***}	(+) ^{***}	(+) ^{***}	(+) ^{***}
SIM	(+)*	(+)*	(+)*	(+)*	(-)*	(-)	(-)	(-)*
Distance	(-) ^{***}	(-) ^{***}	(-) ^{***}	(-) ^{***}				
Border	(-)	(-)	(-)	(-)				
Language	(+) ^{***}	(+) ^{***}	(+) ^{***}	(+) ^{***}				
Colony	(+) ^{***}	(+) ^{***}	(+) ^{***}	(+) ^{***}				
Remote 1	(-)	(-)	(-)	(-)	(-) ^{***}	(-) ^{***}	(-) ^{***}	(-) ^{***}
Remote 2	(-) ^{**}	(-) ^{**}	(-) ^{***}	(-) ^{***}	(-) ^{***}	(-) ^{***}	(-) ^{***}	(-) ^{***}
Trade openness	(+) ^{**}	(+) ^{***}	(+) ^{**}	(+) ^{**}	(+) ^{***}	(+) ^{**}	(+) ^{**}	(+) ^{***}
FTA_1	(-)	(-)	(-)	(-)	(+)	(-) ^{***}	(-) ^{***}	(-) ^{**}
FTA_0	(-) ^{***}	(-) ^{***}	(-) ^{***}	(-) ^{***}	(-)	(-) ^{***}	(-) ^{***}	(-) ^{***}
FTA_rel	(-)	(-)	(-)	(-)	(+) ^{***}	(+) ^{***}	(+) ^{***}	(+) ^{***}
FD	(-)	(-)	(-)	(-)	(-) ^{***}	(-) ^{***}	(-) ^{***}	(-) ^{***}
HCD	-0.870 ^{**}	-0.859 ^{**}	-0.850 ^{**}	0.853 ^{**}	(-)	(-)	(-) ^{**}	(-) ^{***}
Natural Resources								
Rent	(-)	(-)	(-)	(-)	(+) ^{***}	(+) ^{***}	(+) ^{***}	(+) ^{***}
Corporate Tax Rate	0.295	0.278	0.324*	0.246	-0.085*	0.189 ^{***}	0.128 ^{***}	0.141 ^{***}
RBER	(-)	(-)	(-)	(-)	(-)	(-)	(-) ^{***}	(-) ^{***}
Governance	-0.475	-0.644	-0.689	-0.443	0.153 ^{***}	0.156 ^{***}	0.184 ^{***}	0.143 ^{***}

Source: Tables 3 and A1.1, Mistura and Roulet [2019]

Appendix Table 4. Signs, significance and (selected) coefficients of determinants of bilateral inward M&A investment stock, 2001-2016, in Mistura and Roulet [2019]

Variables	1	2	3	4
	-			
FDI index	0.305**			
FDI_equity		-0.04		
FDI_screening			-	
FDI_others			0.179***	
				-0.108**
GDP_origin	(+)**	(+)**	(+)**	(+)**
GDP_destination	(+)**	(+)**	(+)**	(+)**
GDP growth potential	(-)**	(-)**	(-)**	(-)**
SIM	(-)	(-)	(-)	(-)
Distance	(-)**	(-)**	(-)**	(-)**
Border	(+)	(+)	(+)	(+)
Language	(+)**	(+)**	(+)**	(+)**
Colony	(+)*	(+)*	(+)*	(+)*
Remote 1	(+)**	(+)**	(+)**	(+)**
Remote 2	(-)	(-)	(-)	(-)
Trade openness	(+)	(+)**	(+)	(+)*
FTA_1	(-)**	(-)**	(-)**	(-)**
FTA_0	(-)**	(-)**	(-)**	(-)**
FTA_rel	(+)	(+)	(+)	(+)
FD	(+)	(+)	(+)	(+)
		-		
HCD	-0.613*	0.604*	-0.614*	-0.617*
Natural Resources				
Rent	(+)	(+)	(+)	(+)
Corporate Tax Rate	(-)	(-)	(-)	(-)
RBER	(+)*	(+)**	(+)**	(+)
Governance	-0.295	-0.346	-0.299	-0.371
C	(-)**	(-)**	(-)**	(-)**
R2	0.635	0.635	0.636	0.634
Obs	34948	34948	34948	34948

Source: Table 3, Mistura and Roulet [2019]

Appendix Table 5. Determinants of bilateral M&A inward investment stock by sub-sector, in Mistura and Roulet [2019]

	Panel B1: Primary sector				Panel B2: Manufacturing				Panel B3: Services			
	[1]	[2]	[3]	[4]	[1]	[2]	[3]	[4]	[1]	[2]	[3]	[4]
FDI_RI _{j,t-1}	0.216 (0.99)	-	-	-	-0.163* (-1.64)	-	-	-	-0.387** (-2.35)	-	-	-
FDI_RI_EQ _{j,t-1}	-	0.176 (0.86)	-	-	-	-0.081 (-0.77)	-	-	-	-0.019 (-0.20)	-	-
FDI_RI_SC _{j,t-1}	-	-	0.056 (0.67)	-	-	-	-0.089* (-1.90)	-	-	-	-0.254*** (-4.93)	-
FDI_RI_OTH _{j,t-1}	-	-	-	-0.011 (-0.16)	-	-	-	-0.011 (-0.22)	-	-	-	-0.139*** (-2.87)
R-square	0.515	0.515	0.515	0.514	0.631	0.631	0.631	0.631	0.633	0.632	0.634	0.630
Obs.	31749	31749	31749	31749	34325	34325	34325	34325	34948	34948	34948	34948

Note: This table shows the results of estimating Poisson Pseudo-Maximum Likelihood (PPML) models for a cross sectional unbalanced panel data on bilateral M&A inward investment stock by sub-economic sectors (i.e., primary, manufacturing and services) from 60 countries over 2001–2016. Origin country, destination country and year fixed effects are included, but coefficients are not reported. i denotes the origin country, j the destination country and t a given year. All explanatory variables are one year lagged. *, ** and *** indicate statistical significance at the 10%, 5% and 1% levels, respectively. Z-scores are reported in parentheses.

Source: Table 4, Mistura and Roulet [2019]

Appendix Table 6. Direct, Potential, and Total Effects on Growth, 1971-2010, in Iamsirarov [2016]

Variables	Developing countries			Asia and Australasia			Latin America and Caribbean		
	<i>direct effects</i>	<i>potential effects</i>	<i>Total</i>	<i>direct effects</i>	<i>potential effects</i>	<i>total</i>	<i>direct effects</i>	<i>potential effects</i>	<i>total</i>
FDI inflows/GDP	4.11*	n/a	4.11*	-0.18	n/a	-0.18	-2.45*	n/a	-2.45*
Growth	n/a	0.33*	0.33*	n/a	+0.06*	+0.06*	n/a	-0.51*	-0.51*
Log (initial GDP/cap)	0	n/a	0	-2.78*	n/a	-2.78*	-4.84*	n/a	-4.84*
labor growth	0	n/a	0	0	n/a	0	-0.44*	n/a	-0.44*
log (labor force)	n/a	0	0	n/a	0	0	n/a	0	0
Primary attainment	-0.05*	-0.12*	-17*	0	0	0	0.17*	0.32*	0.49*
secondary attainment	0	0	0	0.10*	-0.01*	0.09*	0	0.32*	0.32*
tertiary attainment	-0.17*	n/a	-0.17*	0	n/a	0	0	n/a	0
FDI/GDPx primary	-0.05*	n/a	-0.05*	0	n/a	0	0	n/a	0
FDI/GDPx secondary	-0.04*	n/a	-0.04*	0	n/a	0	0.05*	n/a	0.05*
FDI/GDPx tertiary	-0.03*	n/a	-0.03*	0	n/a	0	0.05*	n/a	0.05*
domestic investment/GDP	0.17*	0	0.17*	+0.17*	-0.02*	+0.15*	0.09*	0	0.09*
Trade/GDP	0	0.29*	0.29*	0	-0.01*	-0.01*	0.09*	0	0.09*
Govt expenditure/GDP	0	n/a	0	0	n/a	0	-0.28*	n/a	-0.28*
Credit in private sector	-0.03*	n/a	-0.03*	0	n/a	0	0	n/a	0
Economic freedom	1.04*	2.84*	3.88*	+1.79*	-0.17*	+1.62*	0	-3.53*	-3.53*
Log (telephone lines)	n/a	-6.41*	-6.41*	n/a	+0.10*	+0.10*	n/a	0	0
log (exchange rate)	n/a	0	0	n/a	0	0	n/a	0	0

Source: Iamsirarov [2016] Table 1 and authors' computations. Notes: Direct effects are the estimates of the growth equation from Table 1 of the paper. Potential effects are estimated by multiplying each coefficient from the FDI equation in Table 1 with the estimated direct effect of FDI on growth. Total effects are the sum of the direct and the potential effects.