Dragoman Digest

US securities regulator unveils draft mandatory climate-risk disclosure regime
If adopted, the regime would set a major international precedent

The **US** Securities and Exchange Commission (SEC) has proposed rule changes that, if adopted, would require publicly traded companies to report on their Scope 1, 2 and in some cases, Scope 3 emissions. Scope 3 emissions include emissions that occur throughout a company's value chain from assets not owned or controlled by the organisation, including the emissions of customers in using the company's product. The regime will be based on existing frameworks such as the Taskforce on Climate-Related Financial Disclosures (TCFD) and will be finalised by the end of this year.

Under the proposal, companies will have to disclose their Scope 3 emissions if they are deemed "material", or if they are included in the company's stated net zero targets. This will increase compliance costs but may also cause some suppliers to adopt more aggressive emissions targets. The SEC's new framework will require firms to report their exposure to, and management of physical climate and transition risks.

Similar reporting regimes have been introduced in the **UK** and **New Zealand,** whilst the **EU** announced earlier this month that it will draft additional reporting criteria for companies "with relevant activities in high-risk sectors" – including mining, minerals, agriculture and textiles. It also agreed to widen the scope of the scheme to include all large, listed companies. There will be greater scrutiny on companies' performance against stated targets, with implications for underperformers on their social license to operate.

The Philippines relaxes foreign investment rules
The changes have been broadly welcomed by the foreign business community

Outgoing **Philippines** President **Rodrigo Duterte** has approved an amendment to the nation's Foreign Investment Act, removing the nation's 40 percent foreign ownership limits on key public utilities including airlines, railways, and telecommunications. This came after the Retail Trade Liberalisation Act was amended in January, lowering the minimum paid-up capital requirement for foreign companies from US$2.5 million to US$490,000.

The Philippines currently ranks as the most restrictive investment regime in Asia, according to the Organisation for Economic Cooperation and Development's foreign direct investment regulatory restrictiveness index. One factor has been the persistent influence of powerful family-based conglomerates who have long sought to limit FDI to protect their own interests. In helping to shepherd through the changes, Duterte expressed his hope to make the country competitive with its "progressive neighbours in ASEAN". In 2020, Manilla attracted US$6.5 billion (1.8 percent of GDP) and will have some ground to make up compared to **Vietnam**'s US$15.8 billion (5.8 percent of GDP).

Despite the policy change, the Philippines still presents challenges for investors. Skills gaps, reliable energy supply and infrastructure gaps are material constraints. Nonetheless, if the reaction from foreign businesses in the Philippines is anything to go by, this is a clear step in the right direction. According to local analysts, "various foreign chambers…are frankly ecstatic" with these changes having been pursued by the business committee "for decades".

Volkswagen announces investments to reduce reliance on China
Volkswagen pivot comes amidst general shift towards an emphasis on more resilient growth and supply chains

Lockdowns, semiconductor shortages, and shortages of raw materials have all caused considerable supply chain headaches for car manufacturers. **Germany**'s Volkswagen provides a case study. Following the lockdowns in its major manufacturing hubs in **China**, the company recorded an 18 percent reduction in production in 2020, and a further 7 percent loss in 2021 as global semiconductor shortages wreaked havoc.

A key plank of Volkswagen's response has been to shift investment to potentially less lucrative, but notionally more reliable markets. While the company will maintain its existing China operations, Volkswagen has pledged to invest over US$7 billion in the **US**, with the objective of doubling its share of the US electric vehicle market to at least 10 percent. It also flagged the potential for increased investment in Europe, as part of an overall directive to reduce the company's dependence on China. The Chinese market accounts for at least 50 percent of Volkswagen's annual profits.

Intense pressure on companies to exit Russia after the invasion of Ukraine has also forced Volkswagen to reassess risk fundamentals. In what would present an existential crisis for the company, Volkswagen is increasingly concerned that a wholesale rupture in Western relations with Beijing could lead to similar pressure to exit China.

Opting for a slightly different approach, **US** carmaker Stellantis announced earlier this month its plan to expand its stake in its joint venture with China's GAC group from 50 percent to 75 percent. It will, however, move towards an "asset light" approach, shifting towards imports rather than increased local production to limit its exposure to "any geopolitical risks". Whilst China is too lucrative to miss, the risks associated with overdependence are proving difficult to ignore.

Supply Chain Resilience Initiative takes further incremental steps
SCRI is one plank in a broader, emerging economic architecture under the aegis of the Quad

Earlier this month **Japan, Australia,** and **India** committed to developing "principles" to strengthen supply chain management across the Indo-Pacific region. The meeting was part of the Supply Chain Resilience Initiative (SCRI) trilateral agreement that was launched last year by the three countries as part of an implicit push to reduce reliance on **China**.

The principles in question are intended to underpin standards for logistics collaboration and data sharing, including on carbon emissions, and will be finalised next year. Another focus is on joint projects in the automotive, electronic, and healthcare sectors. The leaders also welcomed an investment promotion event which attracted stakeholders across the three economies. Whilst progress has so far been limited, there are clear benefits to collaboration based on the economic complementarities of the three countries. Australia has large supplies of raw materials, Japan high-end manufacturing capability, whilst India has assembly and manufacturing capabilities in the automotive, electronics (particularly mobile phones) and pharmaceutical sectors.

The meeting comes after the Quad grouping already committed late last year to an initiative to diversify the supply chains of critical technologies and materials, including semiconductors. Bilateral arrangements are also in the offing, as Australia and India look set to conclude an interim trade deal, after negotiations stalled six years ago. A more serious signifier of intent will be major funding commitments.