TNC's PLANS REGARDING FDI DURING 2009-2011. INVESTMENT POLICY MEASURES

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Abstract:
Deepening economic and financial integration between emerging and advanced economies manifested itself, among other ways, in the recent surge in private capital flows from advanced economies to emerging markets, but also in the reverse flows of capital from emerging market countries. Volatility of prices (especially raw materials), geopolitical instability and threats to personal safety were also perceived by TNCs as having a significant potential impact on FDI. On the other hand, the risks of food or environmental crises were not perceived as posing a potentially strong threat to FDI over the next three years. Recent measures by some emerging markets attest to these countries' concerns about the impacts of global macroeconomic imbalances on their economies.

Key words: *FDI flows, TNCs, investment policy measures.*

JEL classification: *F21, F23, G24*

1. INTRODUCTION

In a period of crisis such as the present one, companies also face (or perceive) a high level of uncertainty. This may lead them to adopt risk-averse investment strategies, and prompt them to reduce their investments further. It is thus interesting to determine which kinds of risks are perceived by TNCs as having the greatest potential impact on their FDI prospects. To do so, two different dimensions of risk were analysed separately: (i) the probability of particular risks materializing; and (ii) the potential impacts of those risks, should they materialize, on investment plans (figures 1).

Regarding the probability of given risks, TNCs were especially concerned about large exchange rates fluctuations, the price volatility of petroleum and raw materials, a worsening of the economic crisis and growing financial instability, as well as rising protectionism and price volatility in general. General risks, such as war, geopolitical instability, or food and environmental crises, were not perceived as very probable in the short term (figure 1).

The expected strong impact of a potential rise in FDI protectionism is also worth noting. Some political tensions have been observed in recent years over such matters as the acquisition of domestic companies by foreign interests (especially hedge funds and State-owned enterprises including sovereign wealth funds) and the protection of natural resources from foreign ownership. This has led to a rising, although still limited, wave of measures restricting FDI, especially in some Latin American countries as well as in the Russian Federation. Some companies are clearly concerned that the ongoing crisis could trigger additional restrictions on FDI (UNCTAD, 2009).

TNCs' responses point to a start in the recovery of their FDI expenditures as early as 2010, and this trend might even accelerate in 2011. While the majority of respondent TNCs expected their FDI to be lower in 2009 than in 2008, this percentage falls to 42% with regard to FDI in 2010 and to 19% in 2011. More than half of the

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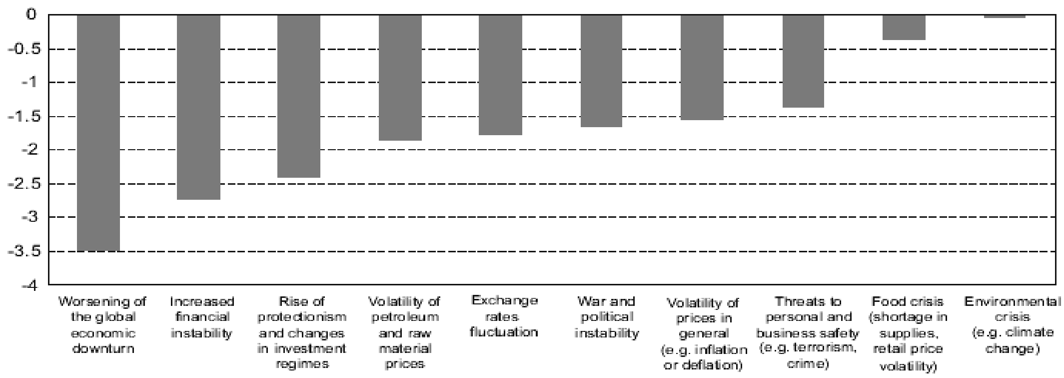
companies reported their intention to invest more abroad in 2011 than they did in 2008, as against 33% and 22% in 2010 and 2009, respectively.

Figure 1. Importance of risk factors for FDI decisions, 2009–2011



Source: UNCTAD Survey 2009.

The first reason for this recovery is TNCs' view that the global FDI environment will improve over time. For instance, more than 40% of respondent companies expressed overall optimism for the global FDI environment in the year 2011, against less than 10% for 2010 and 0% in 2009. In other words, a majority of companies seemed to believe that, after a very difficult year in 2009, the environment would begin to improve slightly in 2010, and even more in 2011.

In addition, in general, companies appeared to be less pessimistic about their own future than they were about their overall environment. 57% of them had a negative view about their own company's investment prospects for 2009, to be compared to 90% expressing pessimism about the global FDI environment. This difference could mean that individual TNCs are quite confident in their own capabilities both to resist the crisis and to take advantage of the economic upturn better than the average TNC.

2. FDI PROSPECTS BY 2011

Buffeted by the growing global financial and economic crisis, TNCs around the world reduced their FDI in 2008, compared to 2007, thus ending nearly a five-year period of uninterrupted growth. This decline, most pronounced in developed economies, was also apparent in developing economies where the rate of growth of FDI slowed down markedly to a flat 2% (Table 1). FDI prospects are affected in similar ways, regardless of the home region of the company.

Table 1. FDI outflows and cross-border M&A purchases, (billions of dollars)

	FDI outflows			Cross-border M&A purchases		
Region/economy	2007	2008[a]	Growth rate (%)	2007	2008[a]	Growth rate (%)
World	**2 063.4**	**1 868.9**	**- 9.4**	**1 699.8**	**1 205.4**	**-29.1**
Developed economies	**1 743.4**	**1 536.4**	**- 11.9**	**1 447.6**	**986.0**	**-31.9**
Europe	1 270.7	990.3	- 22.1	856.0	647.5	-24.4
United States	313.8	298.6	- 4.8	402.6	166.5	-58.7
Japan	73.5	127.4	73.2	38.8	64.3	65.6
Developing economies	**268.8**	**274.1**	**2.0**	**199.4**	**181.1**	**-9.1**
Africa	5.3	..	..	9.4	14.3	51.2
Latin America and the Caribbean	52.1	36.1	- 30.7	48.7	20.3	-58.3
Asia and Oceania	211.4	239.6	13.4	141.2	146.6	3.8
West Asia	44.8	..	..	47.9	37.4	-21.9
South, East and South-East Asia	166.5	185.2	11.2	93.3	108.3	16.1
Transition economies	**51.2**	**58.3**	**13.9**	**25.2**	**25.0**	**-0.5**

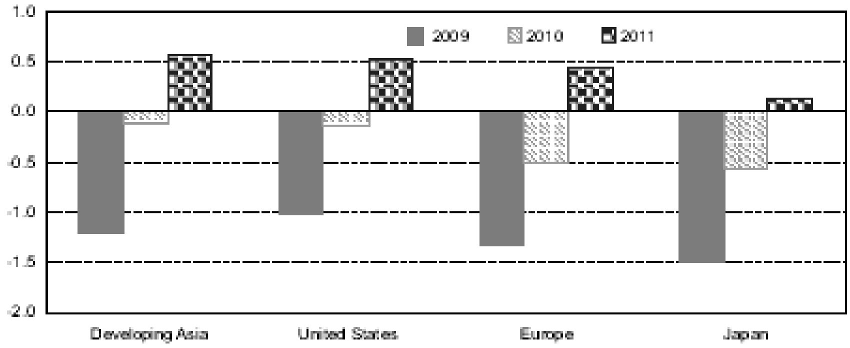
Source: UNCTAD, 2009.

Respondent companies from all home regions expressed very negative views concerning their business environment and global FDI prospects in the short term (figure 1). In all regions, a large majority of TNCs also reported that the ongoing economic downturn had already exerted a negative impact on their FDI plans.

Consequently, respondent TNCs worldwide expected a decline in their FDI expenditures in 2009, with no regional exception (figure 1). Preliminary FDI data for the first quarter of 2009 confirm a sharp decline in FDI outflows, compared to the same period in 2008, in most of the 26 countries for which figures were available, regardless of the region to which they belong.

As noted, the views of TNCs on their global FDI environment and on their own FDI prospects improve markedly over time. This progressive return to optimism can be observed for all home regions. Only a minority of companies from developing Asia, Europe, Japan and the United States reported that they intended to invest less abroad in 2011 than in 2008.

Figure 1. TNCs' views on global FDI prospects, by home region 2009-2011



Source: UNCTAD Survey, 2009.

Respondent companies from all home regions stated their intentions to increase by 2011 the share of foreign countries in their sales and employment as well as in their FDI expenditures and assets. This is especially true for TNCs in Japan and the United States, which appear to be intent on increasing their internationalization in terms of the four major variables analyzed in this survey: sales, employment, investments and assets. TNCs from developing Asia and North America seem more optimistic about the rebound in their FDI than Japanese and European TNCs. Beyond these common features, FDI plans for the three years ahead present some differences by home region.

Prospects for FDI in 2011 by European TNCs seem fairly moderate. Following the marked decline already observed in 2008 (-22%), FDI outflows continued to decrease in the first quarter of 2009 (for the countries for which data are available). From responses to the survey, European companies appear to hold a relatively pessimistic view on the medium-term evolution of their FDI environment (figure 1). The deep recession in Europe, decreasing profits and tougher external financing conditions explain why European TNCs anticipate only a slow recovery in their FDI expenditures after the low point reached in 2009.

TNCs from developing Asia plan a steady recovery in their FDI in 2011. After rapidly increasing over the past few years, FDI outflows from developing countries rose from less than 8% of the world total in 1998 to about 13% in 2007. In 2008, they showed resilience to the overall decline of FDI, with a 2% increase compared with 2007. This marked drop in 2009 is mainly due to decreasing sales and exports to developed markets, faltering cash flows and limited access to credit.

However, TNCs from developing Asia intend to rapidly resume their ambitious internationalization strategies: 57% of them intend to invest more abroad in 2011 than they did in 2008 – one of the highest percentage for all regions in the survey (figure 1).

TNCs from the United States and Canada seem to be quite confident that their international investments will rebound. Outward FDI flows from the United States fell by about 5% in 2008 as a result of repatriations of reinvested earnings and debt by foreign affiliates of United States TNCs, while new investments abroad were halted. Responses by United States TNCs point to probable further cuts in investment programs in 2009. However, their FDI plans remain quite ambitious, as 71 % of respondents reported that they expected the level of their outward FDI to be higher in 2011 than in 2008. At first glance, these expectations may seem quite optimistic in view of the present recession affecting the United States. However, they are consistent with other sources that point to a possibly strong and even rapid recovery of the United States economy, which may boost revenues and facilitate further FDI.

Japanese TNCs expect only a moderate recovery in their FDI in 2011. However, the significance of this apparently bleak outlook must be viewed in the context of recent trends. There was a dramatic increase in FDI outflows from Japan in 2008, due largely to a record level of cross-border M&A purchases by cash-abundant Japanese companies ($64 billion). But responses by Japanese TNCs indicate a marked pullback from these high levels in 2009, followed by a very timid recovery (figure 1). Data for the first quarter of 2009 confirm a 42% drop in Japanese FDI outflows compared to the same period in 2008. Problems in the domestic economy, decreasing sales prospects in other developed-country markets and reduced access to credit largely explain this cautious attitude, which is confirmed by other sources (Jetro, 2009).

Table 2. Percentage of companies with investments in different regions, by home region (per cent of responses)

Home region	Host region				
	All respondents	Europe	North America	Japan	Developing Asia
Developed countries					
EU-15	78	81	70	91	59
New EU-12	35	54	30	21	6
Other European countries	32	41	41	18	18
North America	75	67	93	88	53
Other developed countries	36	27	44	61	18
Developing countries					
North Africa	19	33	11	12	..
Sub-Saharan Africa	17	21	15	15	..
Latin America and the Caribbean	44	44	63	48	18
West Asia	37	39	37	39	35
South, East and South-East Asia	65	53	74	82	71
South-East Europe and CIS	**38**	**53**	**26**	**30**	**12**
Average number of regions where the companies is present	4.3	4.7	4.6	4.6	2.6

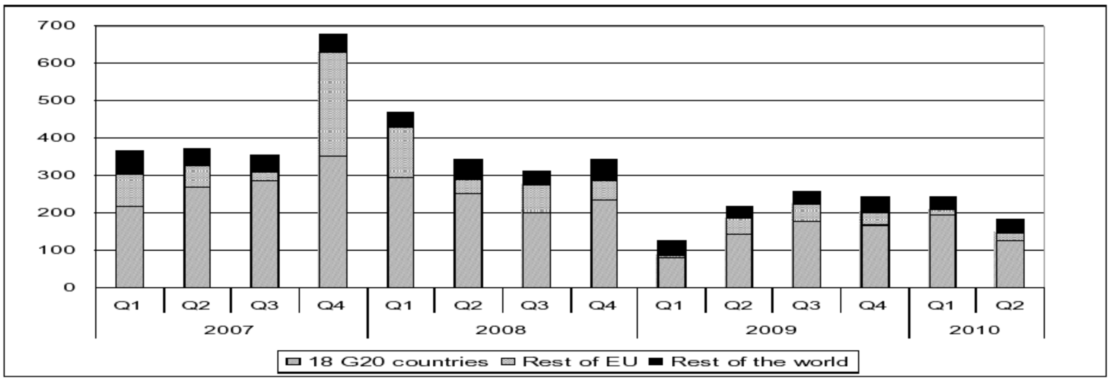
Source: UNCTAD Survey, 2009

Respondent European companies are relatively more concentrated than average, in terms of their present assets, in their home region (especially in the new EU-12, other Europe and CIS/SEE) as well as in Africa (Table 2). They also have a very strong presence in North America. Regarding their future FDI plans, they also showed a greater preference than average for EU-15 and new EU-12 countries, and to a lesser extent for the Commonwhealth of Independent States and South-East Europe (CIS/SEE) and Africa (figure 2). However, they intend to increase significantly the level of priority given to developing regions where they have less presence, notably Asia and Latin America.

3. INVESTMENT POLICY MEASURES

Foreign direct investment (FDI) flows to G20 countries declined sharply by 36% in the second quarter of 2010, after four quarters of modest recovery in the wake of the financial crisis (Figure 1). As the economic recovery remains fragile and new risk factors (such as competitive devaluations) are emerging, G20 and global FDI flows for 2010-2011 as a whole are estimated to remain stagnant. That implies that 2010-2011 FDI flows will still be some 25% lower than the average of the last three pre-crisis years (2005-2007). A new FDI boom remains a distant prospect.

Figure 1. Global FDI inflows by group of countries, 2007/Q1-2010/Q2 (USD billion)



Source: UNCTAD, Fourth Report on G20 Investment Measures, November 2010.

Table 3. Investment and investment-related measures taken or implemented between May 2010 and October 2010

	Investment-specific measures	Investment measures related to national security	Emergency and related measures with potential impacts on international investment*	International investment agreements
Argentina				
Australia	•		•	
Brazil	•			
Canada	•		•	•
China	•			•
France			•	•
Germany			•	•
India	•			
Indonesia	•			
Italy			•	•
Japan			•	
Korea, Republic of	•		•	•
Mexico				
Russian Federation			•	•
Saudi Arabia	•			
South Africa			•	
Turkey				•
United Kingdom			•	•
United States			•	
European Union				•

Source: UNCTAD, Fourth Report on G20 Investment Measures, November 2010.

During the May 2010 – October 2010 reporting period, G20 members took some sort of investment policy action (investment-specific measures, investment measures relating to national security, emergency and related measures with potential impacts on international investment, international investment agreements). Emergency measures with potential impacts on international investment continued to account for most of the measures during the period (Table 1).

3.1. Investments specific measures

Eight G20 members took investment-specific measures (those not designed to address national security or emergency concerns) during the reporting period. Measures include the following:

- Australia tightened the rules applicable to foreign investment in residential real estate.
- Brazil reinstated restrictions on rural land-ownership for foreigners by modifying the way a law dating back to 1971 is to be interpreted. The reinterpreted law establishes that, on rural land-ownership, Brazilian companies which are majority owned by foreigners are subject to the legal regime applicable to foreign companies.

- Canada removed foreign ownership restrictions regarding international submarine cables, earth stations that provide telecommunications services by means of satellites, and satellites.
- China increased the threshold that triggers central level approval for foreign-invested projects in the "encouraged" or "permitted" categories. China also extended existing business permits of foreign-controlled companies for retail distribution to online sales over the internet.
- India sought to make its foreign investment regulations more accessible to investors by consolidating regulations relating to FDI and cross-border capital flows.
- Indonesia amended its rules that determine to what extent foreigners can invest in specific industries in the country. Among others, the changes further liberalize foreign investment in construction services, film technical services, hospital and healthcare services, and small scale electric power plants.
- The Republic of Korea extended FDI zones for the services sector.
- Saudi Arabia allowed foreign investors to invest in an exchange-traded fund of Saudi Arabian shares.

Three countries took measures designed to reduce the volatility of short term capital flows:

- Brazil doubled the tax levied on non-residents‘ investment in fixed-income securities to 4%.
- Indonesia introduced a one-month minimum holding period on Sertifikat Bank Indonesia (SBIs), a debt instrument, and tightened banks‘ net foreign exchange positions.
- The Republic of Korea introduced limits on forward exchange positions of banks; restricted the use of foreign currency loans granted by financial institutions established in the Republic of Korea to residents to overseas purposes; and tightened regulations on banks‘ foreign exchange liquidity ratio.

The measures show some continued moves toward eliminating restrictions and improving clarity for investors (Canada, China, India, Indonesia, the Republic of Korea and Saudi Arabia), but also some steps toward increasing restrictions (Australia, Brazil, Indonesia, and the Republic of Korea).

3.2. Investment measures related to national security

None of the G20 members took investment measures related to national security in the reporting period.

3.3. Emergency and related measures with potential impacts on international capital movements

Emergency measures continued to be the most frequent measure covered by this report (Table 4). While the report does not record cases of overt discrimination against foreign investors in the design of these programs, discrimination might be present in their implementation. In addition, these measures have direct impacts on competitive processes, including those operating through international investment.

Two countries introduced new emergency schemes: Italy reintroduced a scheme for the financial sector that it had discontinued earlier, and the United States established a new support scheme. Many schemes, especially broad support schemes for the real economy, remain open to new entrants. Only three G20 members, Australia, Japan and the United States, closed one or more support schemes for the financial sector during the reporting period. Also, emergency schemes dedicated to non-financial sectors are, for the most part, still open for new entrants.

Table no. 4 Status of emergency measures in financial and non-financial sectors

	Financial sector				Non-financial sectors			
	At least one emergency scheme was closed for new entry of firms in the reporting period	At least one emergency scheme continued to be open for new entrants on 15 October 2010	At least one new scheme was introduced in the reporting period	Legacy assets still held by government on 15 October 2010	At least one emergency scheme was closed for new entry of firms in the reporting period	At least one emergency scheme continued to be open for new entrants on 15 October 2010	At least one new scheme was introduced in the reporting period	Legacy assets still held by government on 15 October 2010
Argentina								
Australia	•			•				
Brazil								
Canada				•		•		•
China								
France				•		•		•
Germany		•		•		•		•
India								
Indonesia								
Italy		•	•	•		•		•
Japan	•	•		•		•		•
Korea, Republic of		•		•		•		•
Mexico								
Russian Federation						•		•
Saudi Arabia								
South Africa						•		•
Turkey								
United Kingdom				•		•		•
United States	•		•	•	•	•	•	•
European Union								

Source: UNCTAD, Fourth Report on G20 Investment Measures, November 2010.

In the financial sector, public expenditure commitments for certain individual companies represented hundreds of billions of USD. For instance, the German government‘s financial commitment for a special purpose vehicle – “bad bank”– exceeds USD 220 billion, and a British bank benefits from a guarantee of assets of over GBP 280 billion. In the United States, Government Sponsored Enterprises operating in the mortgage lending sector now benefit from an explicit unlimited guarantee.

Some governments have begun to unwind financial positions – assets or liabilities - acquired as part of their crisis response. These actions took several forms: sales by governments of their stakes in companies (United Kingdom and United States) or paying down of loans or relinquishing state guarantees by companies participating in the programs (France, Germany, and the United States). Only one country – India – has so far dismantled all emergency programs for the financial sector and has no outstanding legacy assets or liabilities. Two countries have dismantled guarantee or capital injection programs for the financial sector, but still have outstanding legacy assets or liabilities left over from these programs (Australia and the United Kingdom). Three countries have guarantee or capital injection programs that are still open for new entrants (Germany, Italy, and Japan).

In France, Germany and the United States, financial institutions have repurchased government participations at predetermined prices at the moment of their choice. The United States has also disposed of some positions on the market through sales agents and has auctioned off warrants.

3.4. International investment agreements

During the reporting period, G20 members continued to negotiate or pass new international investment agreements (IIAs), thereby further enhancing the openness and predictability of their policy frameworks governing investment. Between 21 May and 15 October 2010, six bilateral investment treaties (Canada, China, Russian Federation, Turkey) and other agreements with investment provisions were concluded by G20 members (Canada, France, Germany, Italy, Republic of Korea, Mexico, EU, UK).

These agreements differ in terms of content, ranging from the Canada-Panama FTA that includes substantive investment provisions that are typically found in BITs (and that also grants pre-establishment rights) to the EU agreement with the Republic of Korea that takes a commercial presence approach and includes provisions on the transfer of funds.

4. CONCLUSIONS

G20 members have continued to honor their pledge not to retreat into investment protectionism. On the contrary, the majority of investment measures taken during the review period carry on the trend towards investment liberalization and facilitation.

However, these findings provide no grounds for complacency. Recent measures by some G20 emerging markets attest to these countries‘ concerns about the impacts of global macroeconomic imbalances on their economies. If these imbalances and related risks for other countries are not dealt with in a credible manner, the resulting policy tensions could degenerate into a protectionist spiral. In non-financial sectors, risks of discrimination against foreign investors are still real as well. G20 Leaders will want to continue their vigilance in this area. Managing the investment impacts of emergency measures taken in response to the crisis still constitutes a great challenge for G20 governments. These measures could be applied in a discriminatory way toward foreign investors. In addition, they pose serious threats to market competition in general and to competition operating through international investment in particular.

Governments have, in some cases, begun dismantling and unwinding emergency schemes. This process will take several years. Again in this phase, risks of protectionism may arise. Governments‘ choice of the approach and timing of unwinding will determine the prevalence of these risks and thus the trust and confidence that investors will have in governments‘ fairness and openness.

There are also grounds for concern that support policies are becoming an entrenched feature of the policy landscape in some countries. The fact that many emergency schemes are still operating two years after the crisis points to the political dilemmas facing governments. Although there may be a few cases where concerns about systemic stability persist, there is now a growing risk that governments are being captured by a logic for subsidization from which it is difficult to escape.

Leaders should also be mindful of the risks for international investment resulting from global macroeconomic imbalances. These pose two types of problems for international investment policy makers. First, in a general way, global macroeconomic imbalances and related policy tensions detract from investor confidence and therefore dampen investment, both domestic and international. Second, countries have begun adopting policies (capital controls and financial regulations with similar effects) aimed at buffering their economies from volatility of foreign exchange markets and capital flows induced by these imbalances. Such policies will, if they become entrenched, lead to fragmentation of international capital markets along national lines and may be difficult to dismantle once in place.

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