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Inward and Outward FDI Country Profiles

Inward and Outward FDI Country Profiles

Edited by Karl P. Sauvant, Thomas Jost, Ken Davies, and Ana-Maria Poveda-Garces (New York: VCC, 2011).

This compilation contains a series of standardized country profiles of inward and outward foreign direct investment (FDI), peer-reviewed by a global network of experts. The publication is intended to contribute to the analysis of trends in foreign direct investment and policy issues related to them. The reports, which cover inward and outward FDI for 22 countries (13 developed economies and 9 emerging markets), include statistics on FDI stocks and flows, output and employment of foreign affiliates, and sectoral and geographical FDI distributions. The reports also list principal foreign affiliates (for inward FDI), principal multinational enterprises (for outward FDI), together with lists of recent major M&As and greenfield investments. The standardized template used to produce the reports is also included. This volume is designed to become a reference tool for anyone interested in foreign direct investment.

Vale Columbia Center
on Sustainable International Investment

A Joint Center Of Columbia Law School And
The Earth Institute, Columbia University

Inward and Outward FDI Country Profiles

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Karl P. Sauvant
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Ana-María Poveda Garcés

January 2011

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VALE COLUMBIA CENTER
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A JOINT CENTER OF COLUMBIA LAW SCHOOL AND
THE EARTH INSTITUTE AT COLUMBIA UNIVERSITY

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The Vale Columbia Center on Sustainable International Investment (VCC) seeks to be a leader on issues related to foreign direct investment (FDI) in the global economy, paying special attention to the sustainability dimension of this investment. It focuses on the analysis and teaching of the implications of FDI for public policy and international investment law. Its objectives are to analyze important topical policy-oriented issues related to FDI, develop and disseminate practical approaches and solutions, and provide students with a challenging learning environment. For more information, please see http://www.vcc.columbia.edu.

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Acknowledgments

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We would like to thank the authors, Ram C. Acharya, José Eduardo Alatorre, Christian Bellak, Gabriel R.G. Benito, Octavio de Barros, Filip de Beule, Subrata Bhattacharjee, Louis Brennan, Benjamin Chavez, Jaime Dupui, Carolina Fernandez, Philippe Gugler, Khalil Hamdani, Ralph Hirdina, Kalman Kalotay, Oleksiy Kononov, Alexey V. Kuznetsov, Marco Mutinelli, Ray Mataloni, Susanne Mayer, Cecilia Nahon, Beatriz Nofal, Andrei Panibratov, Miguel Posada, Lucia Piscitello, Pramila Raghavendran, Someshwar Rao, Carlos Razo, Magdolna Sass, Premila Nazareth Satyanand, Xavier Tinguely, Daniel Van Den Bulcke, Rakhi Verma, Leila Wright, and Zbigniew Zimny for their inspiring contributions.

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Thomas Jost
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Columbia FDI Profiles is a peer-reviewed series. We would like to acknowledge our deep appreciation for the contributions of all the peer-reviewers, most of whom work in the field of international investment as academics or practitioners. Their insightful comments have strengthened the *Profiles* series and this volume. We thank:

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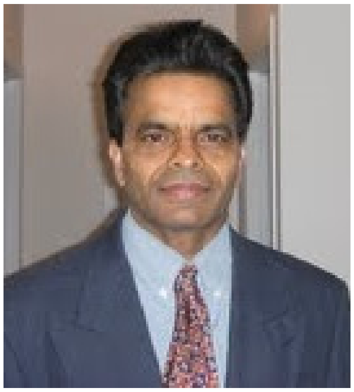

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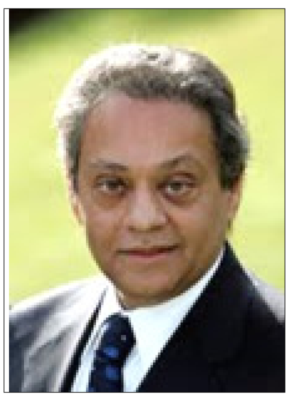

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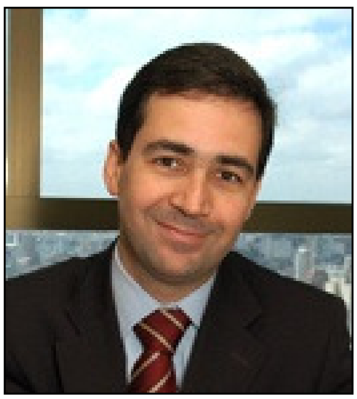

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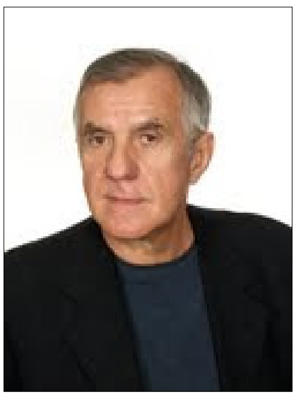

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Foreword

Corporate executives, policy-makers, academic researchers – all eagerly await good news of foreign direct investment (FDI). The economic crisis brought the bad news of a slump in global FDI flows. The *Columbia FDI Profiles* published by the Vale Columbia Center on Sustainable International Investment have helped us understand the magnitude and distribution of this decline, including the good news of countries for which the FDI decrease was small or where recovery has begun.

Be the news bad or good, we need to understand on a continuous basis both the salient features of total FDI flows and their rivulets. This is a major task: some 200 countries are FDI recipients, and many are also FDI originators. This volume gives many snapshots of these flows in countries that are of particular interest because of their size, like the United States, Brazil or China, or because they are trend bellwethers such as Belgium, Chile or Canada.

We can never have enough valid, reliable and comparable data to keep track of what is happening to FDI. This compendium of national chapters is unique in providing us with timely, rich and concise information that can help our understanding, our research and both public and private policies related to FDI. Since this investment affects our economic well-being, these chapters hopefully also have an impact on public opinion and the views of stakeholders.

Each country has its own story to tell, and the national profiles with their standard set of tables provide us also with interesting insights that enrich our knowledge of the overall FDI phenomenon and remind us of how numerous, complex and interacting the factors are that bear on outward and inward foreign direct investment. Without these insights about particular countries, industries, companies, policies, and public sentiments, FDI data are lifeless numbers.

So, as past and future readers, let us express our gratitude to the in-country experts who prepared this volume's chapters which give us a succinct overview of FDI and the issues it raises in the minds of countless researchers, corporate advisors and executives and policy-makers all over the globe.

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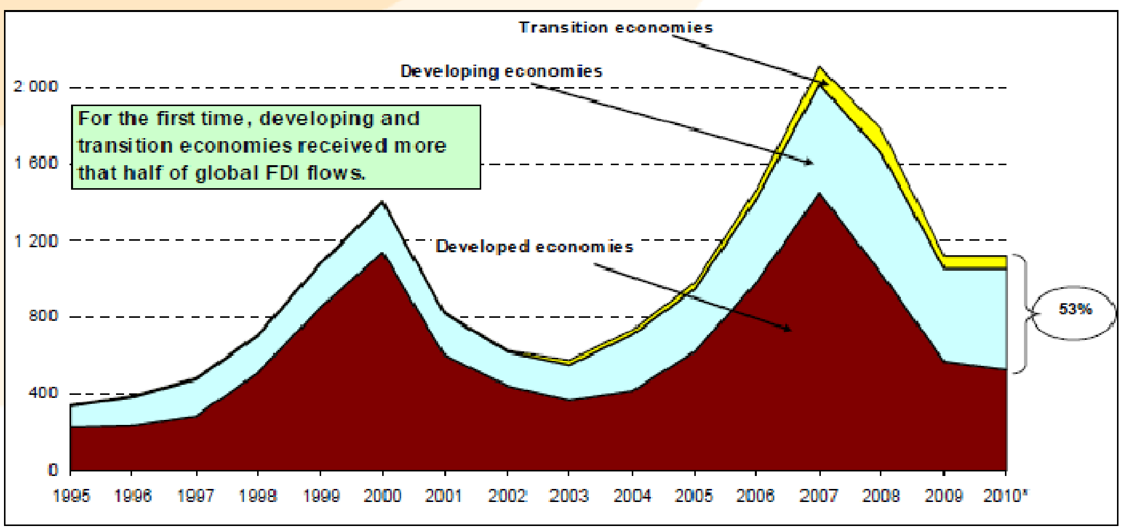
Preface

Over the past year, the *Columbia FDI Profiles*, a series of country profiles of inward and outward foreign direct investment issued by the Vale Columbia Center on Sustainable International Investment, have contributed to the analysis of trends in foreign direct investment (FDI) and policy issues related to them.

The *Profiles* series has been authored and peer-reviewed by a growing global network of scholars who, in a standardized format, have focused discussion on FDI trends and developments, corporate players, the policy scene, the global financial crisis, and the outlook for each country, in either outward or inward FDI.

International investment has become an increasingly important feature of the globalized economy in the past 20 years, having grown much faster than world GDP. Global FDI inflows more than quintupled from US$ 208 billion in 1990[1] to US$ 1.1 trillion in 2010.[2] The total stock of FDI rose from just under US$ 2 trillion in 1990 to nearly US$ 18 trillion by end-2009.[3]

Figure 1. FDI inflows, global and by group of economies, 1995-2010
(Billions of dollars)



Source: UNCTAD, Global Investment Trends Monitor, at http://www.unctad.org/en/docs//webdiaeia20111_en.pdf.

[1] UNCTAD FDI Statistics, available at http://unctadstat.unctad.org.
[2] UNCTAD, Global Investment Trends for January 17, 2011, available at http://www.unctad.org/en/docs//webdiaeia20111_en.pdf.
[3] UNCTAD FDI Statistics, available at http://unctadstat.unctad.org.

While trade issues remain the main focus of attention when looking at international economic relations, international investment has become roughly twice as important as trade in delivering goods and services across frontiers. In 2009, world exports of goods and services totaled US$ 16 trillion, while global sales of foreign affiliates were US$ 29 trillion.[4]

Global FDI has grown faster than world GDP partly as a result of policy changes in recipient countries. As countries – notable developing countries and formerly centrally-planned economies – have abandoned autarky or import-substitution policies, many have opened their economies to foreign investment. Most countries have now also adopted active FDI attraction strategies through a proliferation of investment promotion agencies at both national and sub-national levels.

In recent years, while most regulatory changes have been in the direction of FDI liberalization and promotion, there has been a tendency of late to reconsider the costs and benefits of FDI, and this has led to an increase in the proportion of regulatory changes that tend to restrict FDI. At the same time, a strong international investment law and policy regime has been created, consisting of a plethora of international investment agreements, including bilateral investment treaties and free trade agreements with investment clauses. This regime strengthens the rule of law in the international investment area.

This volume seeks to help our understanding of the growing role of FDI in the world economy by looking at salient features of inward and outward FDI of individual countries (both developed ones and emerging markets), paying special attention to the national policy framework for this investment. Moreover, as work on the preparation of such profiles continues, both in the form of updates to the profiles in this volume and of profiles of countries not yet covered, they will be posted on Vale Columbia Center's website at http://www.vcc.columbia.edu. We hope that this volume will become a reference tool for all those interested in foreign direct investment.

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New York, January 2011

[4] IMF World Economic Outlook database October 2010, available at http://www.imf.org

List of abbreviations

BIT - bilateral investment treaty

BRIC - Brazil, Russia, India, China

FDI - foreign direct investment

IFDI - inward foreign direct investment

OFDI - inward foreign direct investment

FTA - free trade agreement

GDP - gross domestic product

IMF - International Monetary Fund

M&A - mergers and acquisitions

MNE - multinational enterprise

NAFTA - North American Free Trade Agreement

OECD - Organisation for Economic Co-operation and Development

R&D - research and development

SME - small and medium-sized enterprise

SOE – state-owned enterprise

SWF - sovereign wealth fund

UNCTAD - United Nations Conference on Trade and Development

WTO - World Trade Organization

PART I

DEVELOPED ECONOMIES

Chapter 1 – Austria

Inward FDI and its policy context, 2010

Christian Bellak and Susanne Mayer

Since World War II, inward foreign direct investment (IFDI) has played an important role in Austria, contributing substantially to overall investment. Austria's IFDI stock increased every year except in two. The most recent decline occurred in 2008 as a result of the economic and financial crisis. In fact, valuation adjustments led to a fall of the country's IFDI stock by 4%. Yet, in real terms, as measured by employment, IFDI rose even during 2008, and projections for 2009 suggest renewed growth of the country's IFDI stock. This short Profile highlights a number of stylized facts on IFDI and describes the country's FDI policy environment.

Trends and developments

Country-level developments

In Austria, foreign affiliates traditionally have played an important role. In the mid-1970s, the share of foreign capital in the manufacturing sector was roughly one third, while the other two thirds were held by the state and the private sector in equal proportions. These shares have changed since, due to the privatization policy, the structural transformation toward a service economy and the increase in international mergers and acquisitions (M&As). IFDI still contributes considerable amounts to gross fixed capital formation (GFCF) (in 2009, the share of IFDI flows in GFCF was 13%).

Turning to more recent developments, in 2007 Austria's aggregate IFDI stock grew by 47% to US$ 163 billion (annex table 1) or to 41% in relation to its GDP. In 2008, the upward trend stopped and Austria's IFDI stock decreased. But already in 2009, it picked up again, almost reaching the value of 2007. Part of the decline in 2008 in dollar terms is due to the depreciation of the Euro against the dollar. In 2009, net IFDI flows to Austria (annex table 2) amounted to US$ 7.3 billion. They consisted of new equity of US$ 4.4 billion and equity divestments of US$ 5.0 billion (hence net equity investments decreased by US$ 0.6 billion), reinvested earnings of US$ 4.4 billion and other capital (US$ 3.5 billion).

Data for the first quarter of 2010 show a net IFDI flow of US$ 5.8 billion, which is a strong increase compared to the first quarter of 2009 (US$ 2.5 billion). Yet, on an annual basis, a sharp upswing cannot be expected, due to the low economic growth rates in some of the home economies of Austrian IFDI.

The sectoral distribution of Austria's IFDI stock clearly reflects the structural transformation of the country's economy and its geographical advantages (annex table 3). In terms of total capital at market prices, the manufacturing sector accounts for only 14% of the total stock (in 1989 its share was 40%). Thus, today most IFDI is directed toward the services sector, with "professional, scientific and technical services" accounting for 45% of the total IFDI stock – a share that has increased strongly during the past decades (see annex table 3 for details). This sector *inter alia* includes engineering, applied research and consulting services. Also, the share of "financial intermediation" increased substantially, with important foreign banks taking over Austrian banks.

In contrast to the sectoral distribution, which has changed considerably over the past decades, the geographical distribution of the home countries of foreign investors in Austria has changed little. The figures presented in annex table 4 reveal that IFDI is still a very regional phenomenon.[5] The three neighboring countries (Germany, Switzerland, Italy) accounted for more than 50% of the total IFDI stock (US$ 159 billion) in 2007. Other European countries – except for the Netherlands, with a stake of US$ 9 billion – own negligible amounts, except the United Kingdom. Among the non-European home countries, even the stocks of large countries like Japan and the United States together amounted to only US$ 21 billion (or 11%) in 2007.

It should, however, be mentioned that transactions which seem to be unrelated to Austria at first glance may affect the regional composition of IFDI considerably. This can be illustrated by two large transactions that recently took place. First, between 2006 and 2007, Japanese FDI stock in Austria rose from US$ 1.8 billion to US$ 6.9 billion, mainly due to a takeover of British Tobacco by Japan Tobacco[6] as well as a direct investment of Japan Tobacco in Austria Tabak. Second, the takeover of Bayerische Hypo-Vereinsbank (of Germany) by the Italian Unicredit Group in 2006 led to a strong regional shift of foreign investors in Austria. So far, this investment was counted as a German investment. Due to the "ultimate beneficial owner principle" applied to inward investment, Bank Austria had to be re-classified as an Italian rather than a German investment – despite still being owned by Bayerische Hypo-Vereinsbank. This ended the relative dominance of Germany in Austria's IFDI stock, which accounted for almost one third of the total IFDI stock until 2006.

Few operational data on foreign affiliates in Austria are available in a concise manner, most notably data on employment, sales and profitability. After reaching a peak in 2000 with 252,400 employees, employment in foreign affiliates in Austria steadily decreased until 2007, to 235,200, back to the level of the early 1990s. In contrast, aggregate sales of foreign affiliates in Austria (due to the small market size only about US$ 137 billion in 2007) grew steadily. Concerning profitability, the overall median return on equity was 11.6% in 2007, with the median value for mature investments being twice as high as for young firms. Unfortunately, no comparable figures are available for the performance of domestic Austrian firms or the total population of firms. The only value – which is not directly, but closely comparable – is the median value for the return on equity in manufacturing, which was 18.5% in 2007; it is not known how the primary and the tertiary sectors together would influence this value and hence no firm conclusion based on this comparison can be drawn.

A distinctive feature of Austrian IFDI is the large importance of "special purpose entities" (SPEs) or "shell companies". According to the current version of the Organization for Economic Co-operation and Development (OECD) benchmark definition, corporations without any economic

[5] Please note that the latest figures available in the required country classification are for 2007. Figures on the geographical distribution of FDI for 2008 are also available, yet they are classified differently.

[6] This is a merger by two foreign companies, which ultimately affects the ownership of an Austrian company.

activity in the host economy are termed “SPEs”. These are holding companies located in Austria owned by non-residents that in turn hold shares of non-resident enterprises abroad. Austria is chosen by SPEs due to its favorable tax treatment of such investments. In 2005, the inclusion of only five SPEs resulted in an increase of Austria’s IFDI stock by approximately US$ 71 billion. In 2007 and 2008, SPEs were still very important, accounting for about 40% of the total IFDI stock.[7]

Another particular feature of IFDI in Austria are regional holding companies. These Austrian firms are set up by a foreign-owned parent company to engage in domestic activities in Austria as well as in FDI. For example, Bank Austria is a “bridgehead” for Central and Eastern European markets; that is why the Italian owner (Unicredit) has placed its affiliates in Central and Eastern European countries under Bank Austria’s control. These bridgeheads are important. If they were counted separately, Austria’s IFDI stock would be adjusted by as much as US$ 61 billion. According to the Austrian Central Bank, multinational enterprises (MNEs) from over 30 countries have established their bridgeheads or regional headquarters in Austria.

SPEs and regional holding companies make up for the largest share in Austrian IFDI, the remaining share is accounted for by foreign firms either targeting the Austrian market or engaging in vertical FDI. The shares of SPEs and regional holding companies in IFDI are much smaller, if calculated on the basis of employment and of the number of investments.

According to a survey of Austrian Central Bank[8], and in line with “objective” location advantages of Austria, such as a high per capita income, favorable relative unit labor costs (despite high wage costs, which are, however, compensated by high productivity), a highly-skilled labor force, and the vicinity to the Central- and East European markets. Market-seeking motives play a smaller role in explaining foreign investments in Austria (20% in terms of total capital invested), whereas labor costs, taxation and sourcing account for 56%.

The corporate players

Annex table 6 lists the most important M&As during the past three years. In 2007, the outstanding transactions were first the shift of ownership of Bank Austria from a German to an Italian owner (described above) and second the transfer of ownership from Unicredit to Bank Austria of most of its activities in Central and Eastern Europe. The effect of this latter transaction was not only an increase in Austria’s IFDI stock, but also a rise in the country’s outward foreign direct investment (OFDI) stock due to the regional headquarter function of Bank Austria for the affiliates in Central and Eastern Europe. During 2008 and 2009, no comparable large transactions took place, which is reflected in much lower IFDI flows.

The most recent large divestment was reported in late 2009 and early 2010, when Hypo Alpe-Adria-Bank, owned by Bayerische Landesbank, went bankrupt and was re-nationalized by the Austrian Government. Only in 2007, Bayerische Landesbank had acquired a stake (50% plus 1

[7] OeNB, *Internationale Vermögensposition Österreichs 2008* (Vienna: Statistiken Sonderheft, 2009), table 1a.
[8] www.oenb.at/de/stat_melders/datenangebot/aussenwirtschaft/direktinvestitionen/direktinvestitionen.jsp#tcm:14-149053.

vote) of the Austrian Hypo Alpe-Adria-Bank (equal to a transaction amount of US$ 2.4 billion).[9] The whole transaction amounted to US$ 2.2 billion, of which US$ 1.2 billion were provided by Bayerische Landesbank and US$ 658 million by the Austrian Government, as well as the Carinthian local government and private firms. Therefore, the investor,[10] Bayerische Landesbank, gained from profits of its investment in Austria in earlier years, but did not have to bear the full losses. As in other countries, this event stimulated a new discussion in Austria about the role of the state in a market economy, where the Austrian Government provided large "rescue packages" for the banking sector ("too big to fail"), but not for other industries.

Effects of the current global crisis

The economic crisis led to a convergence of market and book values[11] of Austria's IFDI stock: the ratio approached one in 2008, while it had been 1.2 on average during 2005 to 2007. Stagnating or declining demand abroad required write-offs of assets of foreign affiliates, especially of an export-platform nature, due to lower expected future profitability. Capacity utilization in the Austrian economy is still low and, therefore, expansion can be achieved with existing assets. In addition, for a particular type of IFDI, i.e. affiliates set up by foreign firms in Austria as bridgeheads for markets in Central- and Eastern Europe, uncertainty about future growth prospects increased during the crisis.

Yet, the economic crisis did not have negative effects only, as the following example of "crisis-induced restructuring of MNEs" in the form of concentration of production shows. As Austria has no "own" automobile manufacturers (but a strong automotive supplier industry), international developments in the automobile industry have a very direct repercussion on large parts of the manufacturing sector. In this respect, the restructuring of GM's Europe activities is of interest, since Opel (a subsidiary of GM) owns a large plant in Austria. As far as one can assess the current restructuring of Opel's activities in Europe, the Austrian plant seems to benefit from the closing of other plants in Europe. It should be noted that the Austrian Government – at least so far – has not been willing to provide any subsidies to GM for keeping its plant in Austria.

The policy scene

Attracting FDI has always been high on the agenda of the Government, independently of its political orientation. While Austria was quite successful in attracting IFDI in the past, with few exceptions, it never introduced policies or laws specific to IFDI. Rather, the approach was to create an economic environment conducive to investment in general. Nevertheless, there are several areas in which policies have contributed directly to attracting IFDI, including those related to taxation, investment protection and research and development (R&D).

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[9] Reported figures on the value of the transactions vary slightly, depending on the date of publication and type of media (see also next footnote.)

[10] See e.g."HGAA-Deal: Österreich verstaatlicht Krisen-Tochter der BayernLB", *Spiegel Online*, August 24, 2010, available at: www.spiegel.de/wirtschaft/unternehmen/0,1518,666864,00.html.

[11] It should be noted that the most recent detailed figures refer to 2007 and were released by the Austrian National Bank in late 2009. This publication has brought major changes in the reporting practice, like the use of market values for listed firms. Thus, it should be kept in mind that de-listings (most recently Bank Austria; and Austrian Airlines which was acquired by Deutsche Lufthansa) have a big effect on the market values of Austrian IFDI, apart from business cycle effects. In addition, an extension of capital included in "other FDI capital", as well as the inclusion of the new category of FDI, namely "special purpose entities" and a change in the classification of "indirect" FDI, were introduced.

As a member of the European Union, the four freedoms of the Single Market apply (with restrictions of the freedom of movement of people), and hence there are no restrictions on IFDI from other EU members. Austria has steadily built a network of bilateral investment treaties (BITs), with 59 Austrian BITs in force in September 2010. The latest BIT was concluded in 2004 (with Ethiopia), and the latest BIT came into force in 2006 (with Algeria).[12] Currently, several BITs are under negotiation.[13]

The need to include the high environmental, social and labor standards codified in Austrian legislation into BITs has been argued in public debate, and an Austrian model BIT has been drafted, which includes provisions for investor conduct regarding the environment (art. 4)[14] and labor (art. 5).[15] Yet, so far, none of these provisions has been included in actual BITs.[16]

Austria offers a number of investment incentives in the areas of regional assistance, small and medium-sized enterprises (SMEs) (e.g. through loan guarantees), technology promotion (e.g. through grants and tax incentives), education, and training. Most of the incentives are granted to domestic and foreign firms alike without discrimination by ownership. The sophisticated system of export promotion developed in Austria also benefits foreign investors, since a considerable amount of IFDI is export oriented. Initially set up for exporters and outward investors, this system increasingly serves inward investors as well, through export credits granted by the Oesterreichische Kontrollbank AG, acting as the Austrian export credit agency on behalf of the Austrian Federal Ministry of Finance.

Austria increasingly feels the locational competition from neighboring countries in Central and Eastern Europe – even if many of its location factors are still very different from those of the latter. The Austrian Government has reacted with several measures to this competition from new locations. This is clearly visible, for example, in the drastic reduction of the statutory corporate

[12] See Austrian Federal Ministry of Economy, Family and Youth, "Bilaterale Investitionsschutzabkommen – Länder", available at: www.bmwfj.gv.at/Aussenwirtschaft/Investitionspolitik/Seiten/BilateraleInvestitionsschutzabkommen-Länder.aspx.

[13] However, the Austrian Government does not reveal publicly, which countries are involved.

[14] This model BIT has never been published officially. However, from an unauthorized copy, the following quote is taken: "The Contracting Parties recognize that it is inappropriate to encourage investment by weakening or reducing the protections afforded in domestic environmental laws. Accordingly, each Party shall strive to ensure that it does not waive or otherwise derogate from, or offer to waive or otherwise derogate from, such laws in a manner that weakens or reduces the protections afforded in those laws as an encouragement for the establishment, acquisition, expansion, or retention of an investment in its territory. If a Party considers that the other Party has offered such an encouragement, it may request consultations with the other Party and the two Parties shall consult with a view to avoiding any such encouragement."

[15] See previous footnote for source. "The Parties recognize that it is inappropriate to encourage investment by weakening or reducing the protections afforded in domestic labor laws." Accordingly, each Party shall strive to ensure that it does not waive or otherwise derogate from, or offer to waive or otherwise derogate from, such laws in a manner that weakens or reduces adherence to the internationally recognized labor rights referred to in paragraph 2 as an encouragement for the establishment, acquisition, expansion, or retention of an investment in its territory. For the purposes of this Article, "labour laws" means each Party's statutes or regulations, that are directly related to the following internationally recognized labor rights:(a) the right of association; (b) the right to organize and to bargain collectively; (c) a prohibition on the use of any form of forced or compulsory labour; (d) labour protections for children and young people, including a minimum age for the employment of children and the prohibition and elimination of the worst forms of child labour, and (e) acceptable conditions of work with respect to minimum wages, hours of work, and occupational safety and health."

[16] The national contact point for the OECD Guidelines for Multinational Enterprises provides information material at: http://www.bmwfj.gv.at/Aussenwirtschaft/Investitionspolitik/Seiten/OECD-LeitsaetzefuermultinationaleUnternehmen.aspx. ABA – Invest in Austria (governmental agency) provides information at:
http://www.aba.gv.at/EN/ABA-Invest+in+Austria.aspx.

tax rate from 34% to 25% in 2005 and subsequent changes in the tax law. Today, the favorable tax environment in Austria includes provisions like the cross-border intra-group loss relief ("Gruppenbesteuerung"), the international participation exemption and special legislation on trusts and foundations ("Stiftungsrecht") – all measures conducive to the establishment of SPEs and holding companies. Besides these purely national changes in the tax law, the number of double taxation treaties (DTTs) has increased steadily, and a number of treaties are currently being negotiated.[17]

Austria has set up a federal investment promotion agency in order to co-ordinate its inward investment promotion activities.[18] In addition, each of the nine provinces has set up some kind of regional agency. This is important, as there are substantial regional variations in subsidies and incentive schemes. The investment agency fulfils an important role in the provision of information. Over time, it has developed a one-stop-shop concept in order to facilitate investor attraction. The activities of these federal and local bodies are especially important in times of crisis, when foreign investors are reluctant to engage in new activities or to expand existing ones.

Whilst a big issue in other countries as well as in the Austrian political discussion and the media, sovereign wealth fund (SWF) investments in Austria are rather rare. Only the Abu Dhabi Investment Authority and the Libyan Investment Authority have undertaken FDI in Austria.[19] This low number explains why public action (e.g. a special law) has not emerged, but this topic will continue to be debated.

Conclusions and Outlook

IFDI in Austria was only slightly affected by the global economic and financial crisis as no major divestments occurred, yet strong valuation adjustments contributed to declining growth rates. The outlook for further growth of existing as well as new IFDI is positive as Austria's economic environment and the favorable taxation of companies are highly competitive with other locations in Europe. Thus, much will depend on developments in other countries, as a large part of Austria's IFDI is efficiency-seeking and export oriented.

Additional readings

Austrian Federal Ministry of Economy, Family and Youth, ed., *Jahrbuch: Österreichs Außenwirtschaft*. (Short English version: *Austria's External Economic Relations)* (Vienna, 2009).

Bellak, Christian, "The investment development path of Austria," *Transnational Corporations*, vol. 10, no. 2 (2001), pp. 107-134.

Greul, Erich and René Dell'mour, *Statistik der Auslandsunternehmenseinheiten* (FATS-Statistik), available at:

[17] See Austrian Federal Ministry of Finance, "Liste der österreichischen Doppelbesteuerungsabkommen auf dem Gebiet der Steuern vom Einkommen und vom Vermögen", available at: www.bmf.gv.at/steuern/fachinformation/internationalessteu_6523/diesterreichischend_6527/_start.htm.

[18] See Austrian Business Agency, available at: www.aba.gv.at.

[19] "Libysche Investoren werden stärkste Unicredit-Aktionäre", Die Presse, 05.08.2010 and "Gaddafi-Fonds kauft sich in Österreich ein", Die Presse, 14.09.2009.

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OeNB, "Direct investment 2007," *Statistiken, Special Issue* (Vienna: September 2009), available at: www.oenb.at.

Pfaffermayr, Michael, Christian Bellak and Michael Wild, "Firm performance after ownership change: a matching estimator approach," in *Applied Economics Quarterly*, vol. 52, no. 1 (2006), pp. 29-54.

Useful websites

For FDI data: Austrian Central Bank, available at: www.oenb.at/de/stat_melders/datenangebot/aussenwirtschaft/direktinvestitionen/direktinvestitionen.jsp#tcm:14-149053.
For the most recent publication on Austrian FDI: http://www.oenb.at/de/img/shst_2010_09_mon_tcm14-207927.pdf

Statistical annex

Annex table 1. Austria: inward FDI stock, 2000-2009 (US$ billion)

Economy	**2000[a]**	**2001[a]**	**2002[a]**	**2003[a]**	**2004[a]**	**2005[a]**	**2006[a]**	**2007[a]**	**2008[a]**	**2009[a, b]**
Austria	31	35	45	58	70.7	83	111	163	148	161
Memorandum: comparator economies										
Germany	272	272	298	395	512.1	476	592	676	701	….
Slovakia	5	6	9	15	21.9	28	34	45	46	….
Switzerland	87	89	125	162	197.7	170	265	338	374	….

Source: UNCTAD's FDI database, available at: http://stats.unctad.org/fdi; OeNB, 2010, zip file Stand/Beschäftigte der österreichischen ausländischen Direktinvestitionen nach Branchen – NACE 2003 von 1990 bis 2008, available at: www.oenb.at.
[a] Currency conversion rates US$ per Euro used for Austria: 2000: 0.9305, 2001: 0.8813, 2002: 1.0487, 2003: 1.2630, 2004: 1.3621, 2005: 1.1797, 2006: 1.3170, 2007: 1.4721, 2008: 1.3917, 2009: 1.4406.
[b] The value for 2009 is preliminary, since 2009 FDI flows were added to 2008 stocks.

Annex table 2. Austria: inward FDI flows, 2000-2009 (US$ billion)

Economy	2000	2001	2002	2003	2004	2005	2006	2007	2008[a]	2009[a]
Austria	8.8	5.9	0.4	7.1	3.9	10.8	7.9	29.6	11.9	7.3
Memorandum: comparator economies										
Germany	198.3	26.4	53.5	32.4	-10.2	47.4	57.1	56.4	24.9	….
Slovakia	1.9	1.6	4.1	2.2	3.0	2.4	4.7	3.3	3.4	….
Switzerland	19.3	8.9	6.3	16.5	0.9	-1.0	30.8	49.2	17.4	….

Source: UNCTAD's FDI database, available at: http://stats.unctad.org/fdi; and OeNB, *Pressedienst 30.4.2010: Österreichs Außenwirtschaft in ruhigerem Fahrwasser* (Vienna, 2010).
[a] Currency conversion rate US$ per Euro 2008: 1.4717, 2009: 1.3928.

Annex table 3. Austria: distribution of inward FDI stock, by economic sector and industry, 2000, 2008 (US$ million)

Sector/industry	2000[a]	2008[a]
All sectors/industries	**31,165**	**147,785**
Primary	**290**	**404**
Agriculture, mining	290	404
Secondary	**6,514**	**17,963**
Food products, beverages, tobacco products	182	1,150
Textiles and textile products, leather and leather products	193	335
Wood, paper, printing	618	2,597
Chemicals, petroleum products, pharmaceuticals	1,374	4,764
Non-metallic mineral products	458	710
Basic metals and fabricated metal products	505	1,253
Computers, electronic and optical products	1,983	2,035
Machinery and equipment	628	1,960
Manufacture of transport equipment	285	572
Other products, repair and installation	147	264
Electricity, water supply, waste collection and treatment	30	2,127
Construction	112	198
Tertiary	**24,359**	**129,418**
Trade	6,258	20,920
Transport and storage, postal and courier services	169	931
Accommodation and food services	143	391
Information and communication services	2,213	1,925
Financial intermediation	6,231	42,503
Real estate activities	924	3,116

Professional, scientific and technical services	8,125	58,097
Administrative and support services	287	1,557
Public and other services	9	-21

Source: OeNB, 2010, zip file Stand/Beschäftigte der österreichischen/ausländischen Direktinvestitionen nach Branchen – NACE 2003 von 1990 bis 2008, available at: www.oenb.at.

[a] Currency conversion rate US$ per Euro 2000: 0.9305, 2008: 1.3917.

Annex table 4. Austria: geographical distribution of inward FDI stock, 2000, 2007
(US$ million)

Region/economy	**2000**	**2007**
World	31,165	159,111
Developed economies	30,136	141,204
Europe	27,411	116,755
European Union	24,297	104,235
Germany	14,168	40,007
North America	1,925	16,464
Canada	41	1,980
United States	1,884	14,484
Other developed countries	801	7,986
Australia	20	120
Japan	782	6,873
Developing economies	797	13,301
Africa	1	3,314
Asia and Oceania	678	9,204
Latin America and Caribbean	117	783
South East Europe and the CIS	232	4,606

Source: OeNB, "Direct Investment 2007," Statistiken, Special Issue, (Vienna, September 2009), available at: www.oenb.at and information provided by René Dell'mour of the Austrian Central Bank.

Annex table 5. Austria: foreign affiliates, ranked by assets, 2008 (US$ million)

Rank	**Name**	**Industry**	**Total assets**
1	Bank Austria	Banking	5,003
2	GM - Opel	Car industry	n.a.
3	Siemens AG Österreich	Electronics	4,547
4	Bawag	Finance and insurance	n.a.
5	BMW Magna	Automotive supplier industry	n.a.
6	T-Mobile	Communications	n.a.

Source: Information provided by the companies.

Annex table 6. Austria: main M&A deals, by inward investing firm, 2007-2009
(US$ million)

Year	Acquiring company	Home economy	Target company	Target industry	Shares acquired (%)	Estimated / announced transaction value
2009	Adesso AG	Germany	CFC	Prepackaged software	100.00	3.4
2009	Novo Invest Co Srl	Romania	Wettpunkt	Amusement and recreation services	100.00	7.4
2009	Bilfinger Berger AG	Germany	MCE AG	Special industry machinery, nec	100.00	515.2
2009	Aragon AG	Germany	MLP Finanz-dienstleistungen AG	Investment advice	100.00	7.3
2009	Barracuda Networks Inc	United States	Phion AG	Prepackaged software	79.75	13.9
2009	SIBUR Holding	Russia	CITCO Waren-Handels GmbH	Petroleum and petroleum products wholesalers, nec	100.00	269.8
2009	Novartis AG	Switzerland	Ebewe Pharma GmbH-Specialty	Pharmaceutical preparations	100.00	1,272.9
2009	Michael Huber Muenchen GmbH	Germany	Micro Inks GmbH	Printing ink	100.00	0.02
2009	Deutsche Lufthansa AG	Germany	Austrian Airlines AG	Air transportation, scheduled	53.84	1,443.7
2009	Deutsche Lufthansa AG	Germany	Austrian Airlines AG	Air transportation, scheduled	41.56	207.8
2008	Union Investment Real Estate	Germany	ARCOTEL Kaiserwasser	Hotels and motels	100.00	42.4
2008	IDEX Corporation	United States	iPEK Spezial TV GesmbH & CO KG	Electronic components, nec	100.00	42.3
2008	Net 1 UEPS Technologies Inc	South Africa	BGS Smartcard Systems AG	Personal credit institutions	80.10	106.6
2008	Radiant Systems Inc	United States	Orderman GmbH	Computer peripheral equipment, nec	100.00	30.9
2008	YIT Corp	Finland	MCE AG-Building Technology	Special industry machinery, nec	100.00	85.6
2008	Unicredito Italiano SpA	Italy	Bank Austria Creditanstalt AG	Banks	3.65	1,272.4

2008	Criteria CaixaCorp SA	Spain	Erste Group Bank AG	Banks	4.90	916.8
2008	Dubai Aerospace Entrp	United Arab Emirates	F:WZ	Prepackaged software	100.00	25.0
2008	Unibail-Rodamco SE	France	Shopping City Sued	Operators of nonresidential buildings	100.00	954.9
2008	Hungarian Telephone & Cable	United States	Memorex Telex Communications	Telephone communications, except radiotelephone	95.70	129.6
2007	Novartis AG	Switzerland	Intercell AG	Biological products, except diagnostic substances	9.80	214.0
2007	VA Tech WABAG Ltd	India	VA Tech Wabag GmbH	Water supply	100.00	100.0
2007	Constantia Packaging BV	Netherlands	Constantia Packaging AG	Primary production of aluminum	12.83	147.2
2007	Mondi Packaging Paper Swiece	Poland	Unterland Flexible Packaging	Laminated plastics plate, sheet and profile shapes	100.00	100.0
2007	Investor Group	United Kingdom	ONE GmbH	Radiotelephone communications	82.55	1,876.7
2007	BayernLB Holding AG	Germany	Hypo Alpe-Adria-Bank	Banks	50.00	2,185.9
2007	Basic Element Co	Russia	Strabag SE	Industrial buildings and warehouses	30.00	1,427.2
2007	Rasperia Trading Ltd	Russia	Bauholding Strabag SE	Industrial buildings and warehouses	30.00	1,637.3
2007	Wacker Construction Equipment	Germany	Neuson Kramer Baumaschinen AG	Mechanical power transmission equipment, nec	n.a.	828.8
2007	Westcore Properties LLC	United States	Koninklijke-Ppty Portfolio	Operators of nonresidential buildings	100.00	108.0
2007	Investor Group	United States	BAWAG	Banks	100.00	4,209.6

Source: Thomson ONE Banker. Thomson Reuters.

Annex table 7. Austria: main greenfield projects, by inward investing firm, 2007-2009
(US$ million)

Year	Investing company	Home economy	Industry	Estimated / announced investment value
2009	International Petroleum Investment Company (IPIC)	United Arab Emirates	Plastics	107.6
2009	O. N. Sunde	Norway	Plastics	50.7
2009	International Petroleum Investment Company (IPIC)	United Arab Emirates	Plastics	75.3
2009	Accor	France	Hotels and tourism	58.2
2009	Dialog Semiconductor	Germany	Semiconductors	50.9
2009	Valiant Machine & Tool Inc	Canada	Automotive Components	66.6
2009	Four Seasons Hotels & Resorts	Canada	Hotels and tourism	59.8
2009	International Petroleum Investment Company (IPIC)	United Arab Emirates	Plastics	51.8
2009	HiPP	Germany	Food and tobacco	57.1
2009	Baxter	United States	Biotechnology	112.0
2008	Novartis	Switzerland	Pharmaceuticals	70.9
2008	Google	United States	Software and IT services	252.8
2008	Mahle	Germany	Automotive components	63.9
2008	Motel One Hotels & Resorts (Astron Hotels & Resorts)	Germany	Hotels and tourism	60.3
2008	Hotusa	Spain	Hotels and tourism	60.3
2008	Carlyle Group	United States	Real estate	159.2
2008	Sol Melia Hotels & Resorts	Spain	Hotels and tourism	60.3
2008	NH Hotels (NH Hoteles)	Spain	Hotels and tourism	60.3
2008	Wacker	Germany	Industrial machinery, equipment and tools	86.0
2008	ProLogis	United States	Real estate	103.8
2008	Brixxon	Hungary	Automotive OEM	236.4
2008	UniCredit (UniCredito Italiano)	Italy	Financial services	128.1
2008	Sony	Japan	Consumer electronics	111.5

2007	Viessmann Werke	Germany	Industrial machinery, equipment and tools	79.0
2007	General Motors (GM)	United States	Engines and turbines	80.9
2007	Global Crossing	Bermuda	Communications	133.9
2007	MAN	Germany	Automotive OEM	147.1
2007	McArthurGlen	United Kingdom	Real estate	196.0
2007	Fomento de Construcciones y Contratas (FCC)	Spain	Industrial machinery, equipment and tools	132.2
2007	O. N. Sunde	Norway	Plastics	83.2
2007	Rexam	United Kingdom	Metals	131.4
2007	Magna International	Canada	Healthcare	129.9
2007	International Petroleum Investment Company (IPIC)	United Arab Emirates	Plastics	84.0

Source: fDi Intelligence, a service from the Financial Times Ltd.

Outward FDI and its policy context, 2010

Christian Bellak and Susanne Mayer

As a latecomer in OFDI, Austria's firms were mostly export-oriented until the mid-1990s. When Austria joined the European Union (EU) in 1995 OFDI started to grow. This process was further stimulated by the effects of the opening up of Eastern European markets. Austria's OFDI stock revealed positive growth rates ever since the 1990s. Still in 2008, Austria's OFDI flows recorded their second largest value in history and pushed the small Austrian economy among the 20 largest foreign investors globally.[20] *Yet, a substantial change occurred in 2008, when the growth of its OFDI stock stopped – mainly due to valuation adjustments in the aftermath of the crisis. Austrian economic policy is conducive to FDI in general and recently the Austrian tax environment has been revised with several measures benefiting Austrian parent companies.*

Trends and developments

Country-level developments

Until the mid-1990s, OFDI was limited in Austria as few firms set up foreign affiliates and the number of foreign affiliates per firm was low. OFDI then started to grow. In 2007 Austrian OFDI stock[21] increased no less than 41% year-on-year (annex table 1). One transaction accounted for more than half of the increase in Austria's OFDI stock in 2007. Both 2006 and 2007 were boom years as Austria's OFDI stock abroad reached record values. During the crisis year of 2008, Austria's OFDI stock remained constant measured in nominal US-dollar values. In 2009, OFDI stock started to grow again (by about US$ 10 billion).[22] Yet, this does not mean that the current economic crisis has had no effect on Austria's OFDI. As usual, the macro picture does not reveal the underlying changes of the aggregate OFDI stock on the industrial and geographical as well as the financial level. For example, the divestment/investment ratio[23] changed dramatically compared to the previous years, from 20% in 2007 to 81% in 2009.

The recent development in Austria's OFDI stock is clearly reflected in OFDI flows (annex table 2). In 2008, Austrian OFDI flows reached the second largest value ever (US$ 31 billion)[24], which at first glance seems to stand in contrast with the slow growth of the OFDI stock in 2008 reported above. The difference between the OFDI flow and the change in the stock between 2007 and 2008 can be explained by considerable valuation adjustments (caused by the current

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[20] BMWFJ, *Direktinvestitionen Oesterreichs 2008* (Vienna, 2008), available at: http://www.bmwfj.gv.at/Aussenwirtschaft/Aussenhandelsdaten/Seiten/default.aspx

[21] Bellak, Christian, "Austrian manufacturing MNEs: long term perspectives", *Journal of Business History*, vol. 39, no. 1 (1997), pp. 47-71.

[22] Estimate of the Austrian Central Bank (OeNB).

[23] The difference between investment and divestment equals net outward FDI flows, which are revealed in annex table 2.

[24] OeNB, *Pressedienst 30.4.2010: Österreichs Außenwirtschaft in ruhigerem Fahrwasser* (Vienna, 2010); and OeNB, *Pressedienst 17.9.2009: Direktinvestitionen 2009 deutlich schwächer* (Vienna, 2010); see also Bundesministerium für Wirtschaft, Familie und Jugend, *Die Entwicklung der österreichischen Direktinvestitionen 2008* (Vienna 2010).

economic crisis) and substantial exchange rate losses.[25] The situation changed in 2009, when OFDI flows dropped to US$ 6.7 billion. New equity investments of US$ 22.9 billion and reinvested earnings of US$ 1.8 billion were offset by outflows consisting of equity diverstments of US# 15.4 billion and other capital outflows of US$ 2.7 billion. Available data for the second quarter of 2010 show net OFDI flows of only US$ 1.5 billion, compared to US$ 5.7 billion in the second quarter of 2009.

In terms of sectoral distribution, Austrian OFDI stock originates from and is directed to the services sector, including the financial, trading or holding industry (partly for tax reasons) (annex table 3). The manufacturing sector, on the other hand, accounted for only one fifth of capital invested, but for 37% of employment in foreign affiliates in 2008. The steady increase in the share of the services sector in OFDI reflects the structural transformation of the Austrian economy towards a services economy.

Despite the strong increase during the last decade, Austrian OFDI remains largely regional rather than global. Austrian MNEs focus on other EU countries and on Central, East and South East European countries (annex table 4). Ranked by employment in 2008, the Czech Republic, Hungary and Romania are the three most important host countries for Austrian OFDI (with 81,000, 80,000, and 69,000 employees respectively) even before the larger and neighbouring Germany (67,000 employees). Ranked by capital, Austria is the most important foreign investor in six countries (Slovenia, Croatia, Bosnia Herzegowina, Romania, Serbia and Bulgaria); in turn, Austria ranks as the second in terms of OFDI stock in Slovakia and third in Hungary and the Czech Republic.

Few operational data of foreign affiliates are available, most notably data on employment, sales and profitability.[26] The number of employees in Austrian foreign affiliates has more than doubled since 2001, to slightly more than half a million employees working in 3,699 foreign affiliates. In contrast to the strong growth of employment abroad, employment in Austrian MNEs at home has remained stable since 2002, at about 300,000 employees. The increase in employment abroad has occurred primarily in the services sector, while the manufacturing sector has experienced a decrease (e.g. in the chemical and wood-products industries).

During the period 1998-2007, aggregate sales grew five-fold, reaching US$ 193 billion in 2007. This implies that the sales per foreign affiliate investment grew from US$ 12 million in 1998 to US$ 52 million in 2007, indicating a rise in the average size of investments. Data on the profitability of Austrian OFDI show on average a remarkable return on equity of about 11% in 2007, a year when many other affiliates already suffered from the crisis effects. The fact that the median value is only 7.8% confirms that the high profitability is due to the larger (and more mature) affiliates abroad and hence smaller and newer foreign affiliates are less profitable. During 1998-2007, Austrian foreign affiliates earned US$ 51 billion in total. More than half of these earnings (US$ 28 billion) were earned in Central and East European Countries (CEECs). Due to the Parent Subsidiary Directive of the EU, almost all income earned by Austrian foreign affiliates located largely in old and new EU member states is tax exempt in Austria. This implies

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[25] OeNB, Presseaussendung 22. 7. 2010 by Johannes Turner, *Massive Wertberichtigungen stoppen das Wachstum der Direktinvestitionen: Ergebnisse der Direktinvestitionsbefragung der OeNB 2008* (Vienna, 2010).
[26] The most recent figures refer to 2007.

that income earned abroad is not penalized compared to income earned in Austria and thus it does not influence the location choice abroad – as long as it is within the EU.

The corporate players

Austria has few large and global MNEs, unlike other small countries such as Switzerland or the Netherlands. There are only about 25 foreign affiliates listed as joint stock companies on foreign stock exchanges, including those like OMV (primary sector), Wienerberger AG (secondary sector) and Bank Austria (tertiary sector). Second, a good deal of Austrian OFDI is constituted by foreign-owned MNEs, which have been analyzed separately from 2006 onwards only. Hence, about one-third or approximately 280 Austrian affiliates abroad are owned by Austrian firms, which are themselves affiliates of foreign MNEs. These account for 37% of equity capital and 34% of employment of Austrian total OFDI.[27]

"Foreign controlled" affiliates fall into two distinct types of foreign control. One type is Regional Holding Companies (RHCs), Austrian firms set up by a foreign-owned parent company to engage in domestic activities in Austria as well as in FDI.[28] The second type is Special Purpose Entities (SPEs) or "shell companies", including private trusts.[29]

The overarching motive for Austrian firms to engage in OFDI is the market motive, as Austria is a small open economy relying heavily on exports. The importance of the market motive applies to affiliates in EU markets as well as CEECs alike. Measured in terms of capital invested, about 50% of FDI is carried out to secure sales abroad, partly complementing and partly replacing exports. Other motives like efficiency (labor costs, taxation) or sourcing are much less important (with about one third accounting for "other" reasons). Firms seem to overstate the market motive understating the weight of efficiency-seeking with regard to CEEC markets. Case study evidence[30] suggests that Austrian firms have taken advantage of the lower wage level in neighbouring countries, often coupled with local market supply in the CEECs. Wages can be considered the only location factor, where Austria may have a disadvantage compared to several other European countries.[31]

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[27] Austrian National Bank figures, calculated from: http://www.oenb.at/de/stat_melders/datenangebot/aussenwirtschaft/direktinvestitionen/direktinvestitionen.jsp#tcm:14-149053.

[28] These RHCs are included in the FDI figures. According to the Austrian Business Agency (http://www.aba.gv.at/DE/Headquarters/Headquarters-Standort+%c3%96sterreich.aspx), about 300 foreign firms have set up regional headquarters to serve the CEEC markets, among them about 28 Fortune 500 companies. More than 1000 international firms coordinate their CEEC activities from Austria (e.g. Siemens, Beiersdorf, Eli Lilly, Henkel or FedEx). For example, Bank Austria, owned by the Italian Uno Credito – and thus an inward FDI – is responsible for the activities of Uno Credito in Central and Eastern Europe, and thus a major outward investor with substantial activities in Austria.

[29] According to the current version of the OECD benchmark definition, corporations – contrary to Regional Holding Companies (listed under the first type) – without any economic activity in the host country are termed SPEs. These are not included in the FDI figures. They are holding companies located in Austria owned by non-residents that in turn hold shares of non-resident enterprises abroad. In 2005, the inclusion of only five SPEs resulted in an increase of Austria's OFDI stock by approximately US$ 88 billion. In 2007, they accounted for 40% of the OFDI stock.

[30] Christian Bellak, Elisabeth Beer and Wilfried Altzinger, "Fallstudien zu den Auswirkungen der Ostöffnung auf Beschäftigung und Zahlungsbilanz Österreichs", *Research Report*, Project funded by Jubiläumsfonds der Oesterreichischen Nationalbank, No. 6700 (Vienna, 2000).

[31] In contrast, Austria's infrastructure, education, productivity, and taxation advantages among others are superior to most other countries in Europe, where the bulk of Austrian OFDI is located.

Annex table 5 lists the most important Austrian corporate players. Few firms are "truly global" (among them Wienerberger AG, the World's largest brick manufacturer), whilst most firms are rather regional MNEs. Annex table 6 shows that M&A activity in 2008 continued and is widespread across the service and manufacturing sector. M&As contributed considerably to the strong increase of the Austrian OFDI stock in 2007 (annex table 6). Greenfield transactions are concentrated in resource and real estate sectors (annex table 7).

Effects of the current global crisis

A major economic crisis like the current one may affect the growth of Austria's OFDI in both financial and real terms, the sectoral and regional structure of OFDI, and its actual and expected profitability.

As market-oriented FDI usually takes the form of long-term projects, the fact that the OFDI stock show positive growth rates even during the crisis years 2008 and 2009 may simply reflect earlier management decisions, which result in investments spread over a certain number of years. Accordingly, Austria's OFDI stock did not decline (annex table 1).

The current economic crisis may affect the market valuation of foreign affiliates, but since only very few Austrian foreign affiliates are listed on the stock exchange (the precise number is not published by the Central Bank and is believed to be around 25 affiliates), the crisis has not so far affected the "market to book value" ratio of Austrian investments abroad (1.1 on average in 2005-2008). Another important effect of the crisis was the shift of the financing structure of OFDI from equity or loans to reinvested earnings, which clearly reflects the reluctance of parent companies to invest beyond the earnings of their foreign affiliates.

The development in financial terms reported in the previous paragraph went hand in hand with the development in real terms. In 2008, Austrian investors set up 50 additional foreign affiliates alone in Germany (worth US$ 1.9 billion), which accounted for about 17,000 jobs. In 2007 and 2008, total employment in Austrian foreign affiliates increased by 100,000, with the manufacturing sector contributing 23,000 jobs.[32] It seems that investments were not immediately put on hold in reaction to the financial crisis. Therefore, we conclude that neither in financial terms, nor in real terms, the effects of the crisis on Austrian OFDI were particularly strong.

The strong investment by Austrian investors and Austrian banks in particular in the Central and East European Countries has been criticized by some commentators for their large exposure in Eastern Europe – so large that it even might endanger macro-economic stability (e.g. Paul Krugman[33]). Yet, a so-called "stress test" applied to Austrian banks by the Bank of International Settlements using the "exposure/GDP"-ratio shows that Austrian banks rank lower than Swiss, Irish, Dutch, Belgium, Swedish, UK, and French banks (1.2 compared to a range between 3.7 and 1.3).[34] Austrian Central Bank has explained Austria's favourable ranking by the strong

[32] Figures for 2009 and 2010 are not yet available.
[33] http://krugman.blogs.nytimes.com/2009/04/15/austria/.
[34] See e.g., Rodrigo Alfaro and Mathias Drehmann , "Macro stress tests and crises: what can we learn?" *Bank of International Settlements (BIS), Quarterly Review*, part 3 (Basle, 2009).

concentration of Austrian banks on Central and Eastern Europe, which has kept them from investing large amounts in “toxic assets”, e.g. in Iceland, Spain etc.

In 2009, Austrian investors continued to expand their activities in the CEECs and the South and East European Countries (SEECs). Due to its regional focus, OFDI is likely to slow in line with the severe crisis in these markets. Projections of the Vienna Institute of International Comparative Studies (WIIW) show that GDP growth in CEECs will be 3.3% in 2011, while only a 1.6% growth rate is expected in the EU.[35] Therefore, many Austrian firms will try to survive the short term impacts of the crisis in order to participate in positive growth in the medium-term.

Third, the profitability of OFDI has been strongly affected by the crisis as earnings of Austrian foreign affiliates decreased by US$ 5.1 billion between 2007 and 2008. This is quite dramatic as only one fifth (US$ 1.3 billion) of profits was earned in the EU-15 countries, while 71% was earned in the CESEE-20 region. For example in Hungary, Austrian firms made a loss on aggregate. The only two countries where earnings of Austrian FDI increased markedly in 2008 were the Czech Republic and Germany. Expectations of a recovery of profitability seem premature, but some companies have announced a restructuring of their activities abroad (e.g., the MWS Industrieholding GmbH in the metal industry), which may lead to more efficiency and ultimately higher profitability.

The effects of the current economic crisis have been mixed. They are certainly less drastic than in many other countries, as Austria’s OFDI stock has increased throughout the crisis. Growth rates, however, were dampened, which suggests that certain investment projects have been postponed or cancelled.

The policy scene

OFDI became a major policy topic in Austria only in the 1990s, before the policy focus was on promoting exports. Even when OFDI started to grow in the mid-1990s no major policy interventions occurred. Instead, the export promotion system was extended and adapted to serve OFDI (see below). As an EU member, Austria enjoys the four freedoms of the Single Market, including no restrictions on OFDI.

In the aftermath of the current crisis, public concern arose about declining growth rates and lower profitability of OFDI, viewed from the perspective of possible adverse effects on domestic parent firms. No laws or regulations have been so far passed to deal with the effects of the crisis, partly because it is largely unclear what is the “right” policy intervention?

While it has not produced laws or policies focused exclusively on OFDI, the Austrian Government has undertaken several measures that are conducive to OFDI. It has steadily built a network of BITs and 59 Austrian BITs are now in force. The latest BIT was concluded in 2004 (with Ethiopia) and the latest BIT came into force in 2006 (with Algeria).[36] Several BITs are currently being negotiated. Many double taxation treaties (DTTs) have been concluded,

[35] WIIW, “Will exports prevail over austerity?” *WIIW current analysis and forecasts*, No. 6 (Vienna, 2010).
[36] Austrian Federal Ministry of Economy, Family and Youth, “Bilaterale Investitionsschutzabkommen – Länder”, available at: www.bmwfj.gv.at/Aussenwirtschaft/Investitionspolitik/Seiten/BilateraleInvestitionsschutzabkommen-Länder.aspx.

guaranteeing favourable tax treatment of the proceeds from FDI in addition to the Parent-Subsidiary Directive of the EU.[37] Third, the long-established network of trade delegates (Handelsdelegierte) of the Austrian Chamber of Commerce abroad has also increasingly helped Austrian firms to establish more permanent activities abroad. Most importantly, the export guarantee system has been extended to guarantee investments abroad. The “Oesterreichische Kontrollbank AG” (OeKB) is acting as Austria’s export credit agency on behalf of the Austrian Federal Ministry of Finance. Since exports and OFDI are closely linked, the larger MNEs are the main “customers” or “beneficiaries” of the OeKB. The OeKB’s Investment Guarantee G 4 provides political risk insurance related to the establishment of a new venture or the acquisition of/or investment in a company abroad.[38] [39]

The "go international" initiative of the Austrian government[40] in co-operation with the chamber of commerce includes a wide variety of measures, ranging from subsidies to the provision of information for investment opportunities. This initiative intends to stimulate exports as well as direct investment abroad. A special focus is put on the “TUBRICS” countries (Turkey, Ukraine, Brazil, Russia, India, China and South Africa) as well as the North American Free Trade Area (NAFTA).

The employment effects of investment by domestic and foreign holding companies in Austria are deemed so important[41] as to justify the reform of policy measures which should increase the quality of “headquarters location Austria”. Such measures are primarily related to the tax environment. Today, the tax environment in Austria includes provisions on cross-border intra-group loss relief, international participation exemptions, special legislation on trusts and foundations and has been conducive not only directly to outward investment, but also to the establishment of special-purpose entities (SPEs) and holding companies, as described above. Since the area of direct taxation in the EU is largely in the realm of the nation state, this policy field is a primary decision variable for the attraction and sustainability of OFDI for national governments.

The need to include the high environmental, social and labor standards codified in Austrian legislation into BITs has been argued in the public debate and an Austrian model BIT has been drafted, yet not published officially, which includes provisions for investor conduct in these areas (Article 4: Investment and the environment and Article 5: Investment and labor). Recently,

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[37] Some DTTs are currently under negotiation, for an up-to-date number, see Austrian Federal Ministry of Finance, “Liste der österreichischen Doppelbesteuerungsabkommen auf dem Gebiet der Steuern vom Einkommen und vom Vermögen”, available at: www.bmf.gv.at/steuern/fachinformation/internationalessteu_6523/diesterreichischend_6527/_start.htm.

[38] These can be minority stakes or investments which are fully-owned by the investing company as well as shareholder loans. The contribution can be made in cash, in kind or a combination of both. The political risk insurance covers risks such as: total or partial deprivation of equities or shareholder loans due to nationalization, expropriation, confiscation; total or partial destruction for political reasons of the project's tangible assets to an extent that prevents the business to be operated without loss; restrictions on the free disposal or transfer of dividends, proceeds or repayment of capital and payment of interest on shareholder loans, or proceeds of any disinvestment.

[39] See http://www.fdi.net/documents/WorldBank/databases/pri-center_mockup/oekb.html.

[40] http://www.go-international.at/go-international/foerderprogramme/index.php

[41] Susanne Sieber, Österreichs Attraktivität für ausländische Direktinvestitionen sowie als Standort für Headquarters-Funktionen, WIFO Studie im Rahmen des Leitprojekts "Forschungsschwerpunkt Internationale Wirtschaft (FIW)" des Österreichischen Instituts für Wirtschaftsforschung im Auftrag des Bundesministeriums für Wirtschaft und Arbeit, available at: www.fiw.ac.at/fileadmin/Documents/Publikationen/fiwstudie21.pdf .

an arbitration case between an Austrian outward investor and Macedonia has arisen. Unfortunately, no details about the current status are available, except that it is "pending".[42]

Conclusions and Outlook

The growth and the profitability of Austria's OFDI suffered during the crisis. While raising the profitability of foreign affiliates abroad may not seem to be a primary policy goal of the home country government at first glance, a greater regional diversification of Austrian FDI abroad could guarantee the success of FDI. Greater regional diversification means that Austrian parent firms may cross-subsidize foreign affiliates, as markets normally develop at different speeds. The government should adopt measures to increase the level of diversification to prevent negative repercussions of low market growth abroad on Austria. Measures should suit specific market failures. The concentration on a few markets abroad is inter alia due to market failure in the form of information asymmetries. This justifies government intervention in the form of the provision of information (e.g. about industry-specific market developments) or the creation of incentives for regional diversification (e.g. insurance schemes), especially in areas where the costs of collecting such information are high and smaller firms therefore would not gather such market-related information.

A major policy issue coming up – not specific to Austria, but affecting Austria as well – is the new competence of the EU for "investment", including FDI. In an extreme case, this could imply the shift of BITs to the supranational level and thus lead to a major policy shift in this area towards a new "level playing field".

Additional readings

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http://www.fiw.ac.at/index.php?id=533

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[42] See EVN AG v. The Former Yugoslav Republic of Macedonia (ICSID Case No. ARB/09/10, available at: www.encharter.org/index.php?id=469) for details about Electricity distribution ("expropriation" under the Energy Charter).

Pfaffermayr, Michael, with Peter Egger and Yvonne Wolfmayr-Schnitzer, "The International Fragmentation of the Value Added Chain: The Effects of Outsourcing to Eastern Europe on Productivity and Wages in Austrian Manufacturing," *The North American Journal of Economics and Finance*, vol. 12, no. 3 (2001), pp. 257-272.

Useful websites

For FDI data: Oesterreichische Nationalbank, available at: www.oenb.at/de/stat_melders/datenangebot/aussenwirtschaft/direktinvestitionen/direktinvestitionen.jsp#tcm:14-149053.

For the most recent publication on Austrian FDI: http://www.oenb.at/de/img/shst_2010_09_mon_tcm14-207927.pdf

Statistical annex

Annex table 1. Austria: outward FDI stock, 2000-2009 (US$ billion)

Economy	2000[a]	2001[a]	2002[a]	2003[a]	2004[a]	2005[a]	2006[a]	2007[a]	2008[a]	2009[a, b]
Austria	24.8	28.5	42.5	56.0	69.8	71.8	105.7	148.8	148.6	160.6
Memorandum: Comparator economies										
Germany	541.9	617.8	695.8	830.7	925	927.5	1,081.3	1,294.5	1,450.9	n.a.
Slovakia	0.4	0.4	0.5	0.8	0.8	0.6	1.3	1.5	1.9	n.a.
Switzerland	232.2	252.2	292.2	341.4	400.6	432.0	559.9	657.9	724.7	n.a.

Source: UNCTAD's FDI database, available at: stats.unctad.org/fdi/; and OeNB, 2010, zip file Stand/Beschäftigte der österreichischen ausländischen Direktinvestitionen nach Branchen – NACE 2003 von 1990 bis 2008, available at: www.oenb.at.

[a] Currency conversion rates US$ per Euro end-of-year used for Austria: 2000: 0.9305, 2001: 0.8813, 2002: 1.0487, 2003: 1.2630, 2004: 1.3621, 2005: 1.1797, 2006: 1.3170, 2007: 1.4721, 2008: 1.3917, 2009: 1.4406.

[b] The value for 2009 is preliminary, since FDI flows 2009 were added to 2008 stocks.

Annex table 2. Austria: outward FDI flows, 2000-2009 (US$ billion)

Economy	2000[a]	2001[a]	2002[a]	2003[a]	2004[a]	2005[a]	2006[a]	2007[a]	2008[a]	2009[a, b]
Austria	5.7	3.1	5.8	7.1	8.3	11.1	13.7	33.4	30.5	6.7
Memorandum: Comparator economies										
Germany	56.6	39.7	18.9	5.8	20.5	75.9	127.2	179.5	156.5	n.a.
Slovakia	0.0	0.1	0.0	0.2	0.0	0.1	0.5	0.4	0.3	n.a.
Switzerland	44.7	18.3	8.2	15.4	26.3	51.1	75.8	49.7	86.3	n.a.

Source: UNCTAD's FDI database, http://stats.unctad.org/fdi/; and OeNB, 2010, Austrian Direct Investment Abroad (active), available at: www.oenb.at.
[a] Currency conversion rates US$ per Euro averages used for Austria: 2000: 0.9240, 2001: 0.8956, 2002: 0.9444, 2003: 1.1308, 2004: 1.2433, 2005: 1.2458, 2006: 1.2557, 2007: 1.3706, 2008: 1.4717, 2009: 1.3928.
[b] Revised value.

Annex table 3. Austria: distribution of outward FDI stock by economic sector and industry, 2000, 2008 (US$ million)

Sector/industry	2000	2008
All sectors/industries	**24,821**	**148,622**
Primary	**212**	**1,950**
Agriculture, mining	212	1,950
Secondary	**6,667**	**40,400**
Food products, beverages, tobacco products	460	2,790
Textiles and textile products, leather and leather products	84	202
Wood, paper, printing	736	4,550
Chemicals, petroleum products, pharmaceuticals	1,110	10,626
Non-metallic mineral products	1,083	4,114
Basic metals and fabricated metal products	1,302	3,038
Computers, electronic and optical products	639	3,642
Machinery and equipment	461	2,494
Manufacture of transport equipment	158	1,016
Other products, repair and installation	74	775
Electricity, water supply, waste collection and treatment	168	2,532
Construction	392	4,622
Services	**17,940**	**106,270**
Trade	4,032	15,967
Transport and storage, postal and courier services	34	668
Accommodation and food services	107	199
Information and communication services	193	4,611

Financial intermediation	9,852	66,495
Real estate activities	415	4,524
Professional, scientific and technical services	2,292	9,295
Administrative and support services	911	3,467
Public and other services	104	1,044

Source: OeNB, 2010, zip file Stand/Beschäftigte der österreichischen/ausländischen Direktinvestitionen nach Branchen – NACE 2003 von 1990 bis 2008, available at: www.oenb.at.

Annex table 4. Austria: geographical distribution of outward FDI stock, 2000, 2007
(US$ million)

Region/economy	**2000**	**2007**
World	24,821	151,014
Developed economies	21,909	113,643
Europe	19,380	106,607
European Union	17,690	98,124
Germany	4,718	21,671
North America	2,194	5,280
Canada	185	816
United States	2,010	4,465
Other developed countries	335	1,756
Australia	308	1,351
Japan	5	94
Developing economies	2,178	11,733
Africa	19	125
Asia and Oceania	646	8,905
Latin America and Caribbean	1,513	2,710
South East Europe and the CIS	733	25,625
Croatia	451	10,206

Source: OeNB, "Direct Investment 2007," Statistiken, Special Issue, (Vienna, September 2009), available at: www.oenb.at.

Annex table 5. Austria: principal foreign investors, 2008

(US$ million)

Rank	Name	Industry	Foreign assets
1	Wienerberger	Building material	n.a.
2	Erste Group Bank	Banking	n.a.
3	OMV	Energy	n.a.
4	Swarovski	Crystal cutting	n.a.
5	Raiffeisen Zentralbank	Banking	n.a.
6	AGRANA Zucker	Food	n.a.
7	Strabag	Banking	n.a.
8	Verbund	Electricity	n.a.
9	Wiener Städtische	Insurance	n.a.
10	Telekom Austria	Telecommunications	n.a.
11	Baumax Essl	Retail	n.a.
12	Immoeast	Real estate	n.a.

Source: authors calculations.
n.a.: not available.

Annex table 6. Austria: main M&A deals, by outward investing firm, 2007-2009
(US$ million)

Year	Acquiring company	Target company	Target industry	Target economy	Shares acquired (%)	Estimated / announced transaction value
2009	Investor Group	Colonia RE AG-RE Portfolio	Operators of apartment buildings	Germany	100.0	95.6
2009	bwin Interactive Ent AG	Gioco Digitale SpA	Amusement and recreation services	Italy	100.0	164.0
2009	UNIQA Versicherungen AG	Claris Assicurazioni SpA	Life insurance	Italy	90.0	106.1
2009	Verbund	E ON AG-Hydro Power Plants	Electric services	Germany	100.0	1,931.6
2009	Verbund	Poweo SA	Electric services	France	13.4	63.2
2009	Asamer Holding AG	Libyan Cement Mnfg JV Co	Cement, hydraulic	Libya	56.0	145.2
2009	DCM DECOmetal Intl Trading	Australian Zircon NL	Miscellaneous metal ores, nec	Australia	70.5	27.2
2009	Erste Donau-Dampfschiffahrts-gesellschaft	AD Jugoslovensko Recno	Water transportation of freight, nec	Yugoslavia	67.0	31.7
2009	Investor Group	Baskent Elektrik Dagitim AS	Electric services	Turkey	100.0	1,220.0
2009	Kapsch TrafficCom AG	Q-Free ASA	Electronic parts and equipment, nec	Norway	20.5	16.0
2008	VIG	BCR Asigurari SA	Accidental and health insurance	Romania	88.5	345.0
2008	Polytec Holding AG	Peguform GmbH	Automotive parts, supplies	Germany	100.0	280.5
2008	Raishop Holding	Poslovni sistem Mercator dd	Grocery stores	Slovenia	23.0	405.3
2008	Intercell AG	Iomai Corp	Pharmaceutical preparations	United States	100.0	176.6
2008	Strabag SE	Strabag AG	Residential construction, nec	Germany	21.1	343.9
2008	Labelux Group	Bally International AG	Women's footwear, except athletic	Switzerland	100.0	600.0
2008	Raiffeisen PPP Infrastruktur	Allami Autopalya Kezelo	Bridge, tunnel, and elevated highway construction	Hungary	n.a.	169.0
2008	CA Immobilien Anlagen AG	Vivico Real Estate GmbH	Real estate investment trusts	Germany	100.0	1,520.8
2008	Rail Cargo	MAV Cargo Zrt	Railroads, line-	Hungary	100.0	590.00

	Austria AG		haul operating			
2008	Bank Austria Creditanstalt AG	OJSC Ukrsotsbank	Banks	Ukraine	94.2	2,231.2
2007	Telekom Austria AG	Mobile Digital Communications	Telephone communications, except radiotelephone	Belarus	70.0	1,033.3
2007	Sparkassen Immobilien AG	Citec Immobilien-Residential	Operators of apartment buildings	Germany	100.0	251.6
2007	Immofinanz Immobilien Anlagen	Undisclosed logistics centres	Land subdividers and developers, except cemeteries	Germany	100.0	372.1
2007	OMV AG	MOL Group	Crude petroleum and natural gas	Hungary	8.6	1,346.4
2007	Bank Austria Creditanstalt AG	ATF Bank JSC	Banks	Kazakhstan	95.6	1,661.0
2007	Bank Austria Creditanstalt AG	International Moscow Bank	Banks	Russia	10.0	229.4
2007	Conwert Immobilien Invest SE	Undisclosed real estate	Real estate agents and managers	Germany	100.0	213.7
2007	Verbund	EnerjiSA	Electric services	Turkey	49.99	326.2
2007	Bank Austria Creditanstalt AG	Aton Institutional Business	Security brokers, dealers, and flotation companies	Russia	100.0	424.0
2007	CA Immobilien Anlagen AG	Hessen-Property Portfolio	Land subdividers and developers, except cemeteries	Germany	100.0	986.6

Source: Thomson ONE Banker. Thomson Reuters.

Annex table 7. Austria: main greenfield projects, by outward investing firm, 2007-2009
(US$ million)

Year	Investing company	Industry	Source economy	Estimated / announced investment value
2009	OMV	Coal, oil and natural gas	Romania	716.6
2009	Immofinanz	Real estate	Russia	281.7
2009	OMV	Coal, oil and natural gas	Kazakhstan	250.6
2009	OMV	Coal, oil and natural gas	Germany	211.6
2009	OMV	Coal, oil and natural gas	Turkey	663.2
2009	OMV	Coal, oil and natural gas	Romania	472.9
2009	OMV	Alternative / renewable energy	Romania	570.6
2009	Kapsch Group	Communications	Belarus	675.0
2009	Egger Group	Alternative / renewable energy	Romania	598.2
2009	Spinelli Euro Freight	Transportation	Russia	218.9
2008	OMV	Coal, oil and natural gas	Germany	870.9
2008	Supernova	Real estate	Croatia	720.3
2008	OMV	Coal, oil and natural gas	Turkey	740.0
2008	A-Tec Industries	Industrial machinery, equipment and tools	United Kingdom	645.2
2008	Asamer	Real estate	Ukraine	941.2
2008	intico solar	Electronic components	Germany	954.5
2008	OMV	Coal, oil and natural gas	Turkey	781.0
2008	Immofinanz	Real estate	Russia	715.1
2008	Kolm Pfluger	Food and tobacco	Serbia	776.3
2008	Kelag	Alternative / renewable energy	Romania	621.2
2007	Kronospan	Wood products	Russia	440.4
2007	Bau Holding Strabag	Building and construction materials	Hungary	286.7
2007	Bau Holding Strabag	Metals	Russia	254.1
2007	Meinl Bank	Coal, oil and natural gas	Hungary	222.2
2007	EVN	Alternative / renewable energy	Albania	1,500.0

2007	Immofinanz	Real estate	Romania	404.3
2007	Meinl Bank	Real estate	Russia	406.1
2007	Erste Bank	Real estate	Slovakia	243.0
2007	Erste Bank	Real estate	Hungary	394.1
2007	Erste Bank	Real estate	Bulgaria	283.3

Source: fDi Intelligence, a service from the Financial Times Ltd.

Chapter 2 – Belgium

Inward FDI and its policy context, 2010

Filip De Beule and Daniel Van Den Bulcke

As a small open economy, Belgium has been actively and successfully attracting IFDI since the 1960s and consequently has one of the most internationalized economies in the world. Foreign affiliates represent approximately 35% and 21% of manufacturing and services jobs as well as 42% and 24% of value added by the manufacturing and services sector, respectively. Despite an overall drop in competitiveness of Belgian industry, the introduction of a new and innovative incentive, the notional interest deduction scheme, to lower corporate income tax for all firms in 2005 has led to an increase of inflows of equity capital from 2006 onward, although the financial crisis took its toll on inflows in 2008 and 2009. In addition, the risk capital allowance has done much to promote Belgium's role as a financial conduit, allowing a large proportion of the authorized capital to flow back to other countries in the form of loans. This trend was reinforced by the global financial crisis.

Trends and developments

Country-level developments

According to UNCTAD, Belgium has been among the top ten recipients of IFDI flows for many years. At the end of 2009, Belgium ranked fifth in terms of IFDI stock, behind the United States, the United Kingdom, France, and Hong Kong (China). With an IFDI stock of roughly US$ 830 billion (annex table 1), the country was ahead of such large economies as Brazil, Mexico, Russia, and China.[43] Largely as a result of its policy of attracting IFDI since the 1960s, Belgium has one of the most internationalized economies in the world. According to UNCTAD's transnationalization index, in 2005 Belgium ranked at the top of the list of the most "globalized" developed countries and second, only after Hong Kong (China) in the combined list of developing and developed economies.[44]

Despite its relatively small economic size of less than 3% of the European Union's GDP, Belgium also has a strong FDI position in the EU. Belgium attracted between 5% and 20% of EU's IFDI flows in the period 2002-2009, a higher share than that of most other similar-sized European countries. It is one of the most important host countries (third position) for IFDI in the EU, accounting for over 11% of cumulative EU IFDI. The highly globalized Belgian economy is characterized by a regionalized concentration of the source countries with investments in Belgium. The lion's share of Belgium's IFDI comes from European Union countries, especially

[43] UNCTAD, *World Investment Report 2010: Investing in a Low-Carbon Economy* (New York and Geneva: United Nations, 2010).
[44] UNCTAD, *World Investment Report 2008: Transnational Corporations and the Infrastructure Challenge* (New York and Geneva: United Nations, 2008).

from Belgium's immediate neighbors. These neighboring countries account for about two-thirds of the country's IFDI, distributed as follows: France 25%, Germany 20%, the Netherlands 19%, and the United Kingdom 4%. US firms constitute one of the largest non-European sources of IFDI in Belgium, although their importance is waning.[45] This regional concentration of IFDI is related to Belgium's central geographical location, to the importance of Brussels as the political and administrative capital of the EU and, most importantly, to Belgium's role in the distribution of goods and services across the European continent.

IFDI flows into Belgium have been on a rising trend since 2002 (annex table 2).[46] In the crisis year of 2008, Belgium was able to maintain its level of FDI inflows at US$ 110 billion, while other countries like the Netherlands experienced a sharper drop. However, in 2009 Belgium's FDI inflow collapsed to US$ 34 billion (see also the section on the effects of the current global crisis on IFDI).

The majority of foreign affiliates in Belgium are services sector affiliates (annex table 3). These employ more than 336,000 people, with about 145,000 in the manufacturing sector and 190,000 in the service sector, which represents about 35% and 21% of sector employment, respectively. In terms of value added, foreign affiliates in both sectors contribute about US$ 15 billion each, which represents about 42% and 24% of the total value-added in the manufacturing and service sectors, respectively. The most important foreign affiliates in terms of size – as measured by total assets, turnover and employment – are in the chemical and pharmaceuticals sector, the automotive sector, personnel services, and coordination centers. Coordination centers usually have large total assets without much turnover or employment, while temporary personnel service companies have large employment figures without much turnover or total assets.

Europe is the predominant source of FDI flows into Belgium. In 2007, before FDI bore the brunt of the economic crisis, according to Bank of Belgium statistics, Europe was the source of US$ 99 billion of Belgium's US$ 105 billion inflows, while the United States supplied US$ 6 billion (annex table 4). The list of the most important foreign direct investors in terms of numbers of projects is headed by US companies, with 38 out of 142. Firms from Belgium's neighboring countries have also established a sizeable number of greenfield projects: France 17, Germany and the Netherlands 13 each, and the United Kingdom 11. The United States and Belgium's neighbors together represent about two-thirds of all greenfield investment projects in Belgium. Intra-European investments are the most important source of investment in Belgium, although firms from emerging economies like Brazil and China also seem to have discovered investment advantages in Belgium. Flanders has traditionally been the most successful region in attracting investment, although by 2009 Wallonia, with 57 greenfield investment projects, had almost caught up with Flanders' 64 such projects. Wallonia reportedly has less cumbersome environmental and spatial planning policies, making it easier for firms to invest there.

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[45] AMCHAM, *US Direct Investment in Belgium Report 2009* (Brussels: AMCHAM Belgium, 2009).

[46] Separate data for Belgium have only been available since 2002. Before 2002, the data were reported for the Belgium-Luxembourg Economic Union (BLEU). In January 2006, the National Bank of Belgium (NBB) switched to a new system for collecting the FDI data needed to draw upon balance-of-payment data. This revamped data collection system also required adjustments to the technical method of producing the balance of payments. The new system conforms to the administrative simplification requirement introduced by the Government. This means that financial institutions report only transactions for their own account and no longer for their clients; while specific surveys are used to supplement all components of the balance of payments. A change in the data collection method inevitably entails methodological breaks. Strictly speaking, it is therefore incorrect to compare data published since 2007 with the data available until 2006.

The corporate players

Many foreign chemical companies have plants in two or even all three of the Belgian regions. The chemical industry in the Flemish region represents 73% of the total sales of the chemical sector in Belgium. The port of Antwerp is located in the world's biggest and most diversified petrochemical cluster, the Antwerp-Rotterdam region. The chemicals sector in the Walloon region represented 19% of total turnover of the Belgian chemical sector in 2005. Base chemical manufacturing activities are mainly concentrated in the province of Hainaut. In addition, Wallonia has an important biotechnology pole and high-tech pharmaceutical industry in the province of Walloon Brabant and the North Hainaut area. Wallonia-based companies account for 28% of the total R&D expenditure of the chemical sector in Belgium. Although it makes a comparatively modest contribution to the sector's turnover (8%), the Brussels-Capital region remains an essential link in the chain of activities of the chemical sector in the country. This region has only few chemical production facilities but is home to various head offices, like those of BASF and Statoil (annex table 5), which are near to several international organizations and institutions. Brussels is clearly the preferred location for the establishment of regional headquarters (coordination centers), although there are some in other parts of the country.

Another sector in which Belgium has attracted large amounts of foreign investment is the automotive industry. US companies, such as Ford and General Motors (GM), have played an important role. Although GM was already assembling cars in Belgium a century ago, US firms intensified their search for market opportunities at the time of the establishment of the European Common Market at the end of the 1950s, as they sought to take advantage of economic growth and leap over the common external tariff. In Flanders, they found reliable workers who - at that time - were cheaper than in Wallonia and less prone to strike. Most European automotive companies, including Volkswagen, Renault and Volvo, also established production plants in Belgium. As the European automotive market became oversaturated and overcapacity was created in developed countries, these production plants have come under heavy strain. Renault, for instance, disinvested its Vilvoorde plant in 1997. GM recently decided to close down its Opel plant in Antwerp. Others were able to survive after restructuring. Volkswagen restructured its plant in Vorst, near Brussels, to produce the Audi A1. Ford Genk, the largest branch (of Ford Europe, Germany) plant in Belgium, is still in business after major downsizing a few years ago. The Volvo plant in Gent became a subsidiary of Geely Automotive of China when it acquired the former Swedish brand from the Ford group in 2010. Perhaps because of Geely's commitment to run Volvo as a multi-domestic business, the Volvo plant in Gent seems to have survived the recession unscathed. Meanwhile, the reduced activity of the car assemblers in Belgium due to disinvestments has affected the suppliers to this industry and caused much indirect unemployment.

In 2009, the largest foreign acquisition was in the banking sector, where BNP Paribas acquired 75% of Fortis Bank for US$ 12.8 billion. Other M&As included the purchase of a 51% stake in SPE by the French energy company EDF for US$ 1.8 billion and a variety of other deals in various sectors, including electrical services, courier services, machine manufacturing, software, pharmaceuticals, and clothing (annex table 6).

An analysis of the number of greenfield investment projects by sector (annex table 7) shows that sales and marketing activities lead the list in most years. The second place is taken up by manufacturing (production), while the third position is held by the logistics sector. Belgium has also proven an attractive location for European headquarters of MNEs as well as for their distribution centers. This attractiveness is not only the result of the large number of EU and international institutions based in Brussels and the country's geographic location in the center of Western Europe, but also of investment incentives for holding companies and regional headquarters, the so-called "coordination centers" (see below), although these incentives were phased out by the end of 2010 to comply with EU rules. Since 2005, these four sectors have taken up the top four positions of greenfield investments in Belgium.

The total of greenfield projects and M&A deals declined from around 300 a year in 2005-2007 to 250 in 2008 and 224 in 2009. Greenfield investments outnumbered acquisitions, although between a quarter and half of the greenfield investments were expansion projects by foreign firms already present in the country.[47]

Effects of the current global crisis

IFDI flows in Belgium declined during the economic and financial crisis, although the IFDI stock grew sharply in 2009. FDI inflows peaked at US$ 118 billion in 2007 before declining to US$ 110 billion in 2008 and US$ 34 billion in 2009. A detailed analysis of the monthly net inflows of FDI indicates that equity capital investments remained rather stable in 2008 and 2009, while other capital flows, such as intra-company loans, occasionally turned extremely negative. These data suggest that coordination centers and other affiliates in Belgium were used as a conduit for intra-company loans in an effort to support their corporate parents or other affiliates (see further on the impact of the notional interest deduction scheme). Annex table 4 also indicates that these negative flows of IFDI were mainly due to non-European countries, while Europe sustained its equity investment in Belgium.

The policy scene

Belgium has traditionally welcomed foreign investment. The Belgian Government currently encourages new foreign investment as a means to promote innovation and employment. The Belgian federal government provides tax breaks for R&D and investment in capital goods, as well as fiscal incentives for hiring employees. As a result of some regional devolution, Flanders, Brussels and Wallonia now have substantial autonomy in courting potential foreign investors, as each deems appropriate. For more direct support, all three regions offer financing and subsidies that aim to attract new businesses and generate employment. The regions may favor certain industries when allocating subsidies, as part of their overall economic policy. These preferred investments are often environmental, biotechnology and information and communications technology projects, or others using innovative technologies.

The part of R&D expenditures by foreign-controlled firms is about 1.5 times the part of domestic-controlled firms. In the period 2000-2006, the annual growth rate (before correction for inflation) of FDI in R&D equaled 0.9%, and the share of R&D expenditures of foreign affiliates

[47] Ernst & Young, *Barometer van de Belgische Attractiviteit 2010* (Brussels: Ernst and Young, 2010).

in the total of the business expenditures for R&D (BERD) remained stable at around 59%. However, the recent employment growth in foreign affiliates has declined since 2006.[48] FDI in R&D from other EU member states (and especially France and the Netherlands) decreased sharply, whereas the share of IFDI in R&D by US firms increased (despite the decrease in absolute terms of their investments). Together, Europe and the United States account for nearly 95% of total IFDI in R&D in Belgium. Until 2006, FDI in R&D from emerging and developing economies in Belgium were minor. More recently, the takeovers of Arcelor by Mittal Steel and of Hansen Transmissions by Suzlon are examples with implications of foreign control by emerging markets (in this case India) over R&D expenditures in Belgium.

In order to attract regional headquarters of MNEs and to enhance Belgium's attractiveness as a favorable location for FDI in general, the Government began a fiscal incentive scheme at the beginning of the 1980s, when the "coordination centers" legislation was enacted.[49] When the European Commission ruled that the fiscal relief scheme had to be discontinued, the Belgian Government succeeded in obtaining a transition period (which ended in 2010), and it switched to a new promotional tool, the "notional interest deduction" (NID) to attract risk capital.[50] This measure was introduced in 2006 and applies to the existing capital stock.[51] Under the NID - an innovative measure in international tax law - all companies subject to Belgian corporate income tax are allowed to deduct from their taxable income an amount equal to the interest they would have paid on their capital in the case of long-term debt financing.

This measure was to a large extent intended to convince MNEs that perform coordinating activities on behalf of their groups to remain or establish themselves in Belgium, although all firms can take advantage of it. Around 280 coordination centers were active during the lifetime of the coordination center regime, most of which were European, although US firms constitute the single largest nationality.[52] As the Government and the industry itself feared that the end of the Belgian coordination center regime would create a negative image of the investment climate in Belgium, the worst case scenario was that the industry would vanish altogether and job losses were estimated in a range of 10,000-20,000 jobs.[53] With the new regime, Belgium wanted to keep existing coordination centers while also attracting new ones. Although data indicate that the number of coordination centers has dropped dramatically from around 250 in the mid 1990s and around 200 in 2005 to around 75 by 2008, the most important – in terms of employment and capital – coordination centers are still active using the NID scheme while other finance centers

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[48] According to Ernst & Young, 3,357, 3,391 and 4,379 jobs were created by foreign affiliates in Belgium in 2009, 2008 and 2007, respectively. See, Ernst & Young,, op. cit..

[49] From 1983, after discussions with the European Commission, the Belgian authorities applied a favorable tax regime, including lower corporation tax, capital duty, property tax, and withholding tax, to these establishments. In 2003, the European Commission declared that the reliefs amounted to state aid and did not comply with the EC Treaty. Coordination centers whose ten-year period of approval was under way were allowed to avail themselves of the benefits of the scheme until the end of that period until December 31, 2010 at the latest. The EU Commission banned Belgium from renewing approvals when they expired after the end of 2005.

[50] Ministry of Finance, *NotionalIinterest Deduction: AnIinnovative BelgianTtaxIincentive* (Brussels: Ministry of Finance, 2009).

[51] Christian Valenduc, Les intérêts notionnels: une réforme fondamentale et controversée', *Courrier hebdomadaire* (Brussels : CRISP, 2009).

[52] M.P. Styczen, *A Comprehensive Case Study of Multinationals' Financial Centers in Belgium* (Oslo: Norway School of Economics and Business Administration, 2010).

[53] M. Quaghebeur, "Officials hope new tax regime will attract multinationals", *Tax Notes International*, January, 2005, pp. 140-41; B. Springael, "Notional interest deduction: investment in Belgian risk capital rewarded", *IBFD Derivatives and Financial Instruments,* January/February, 2006, pp. 47-56.

have picked up some of the slack. If Belgium can attract new finance centers belonging to multinational groups, that could stimulate employment and offset the job losses in coordination centers whose capital and activities have been transferred abroad. These new finance centers currently employ few people.

Since its introduction, the notional interest deduction has been criticized for its high budgetary cost, estimated at more than US$ 2 billion, although the net budgetary impact was estimated at between US$ 200 and US$ 500 million after taking account of payback effects.[54] Since the risk capital allowance was introduced, there has been a noticeable rise in the authorized capital and hence in the shareholders' capital of companies established in Belgium. The considerable contribution of capital from other countries led to a rise in the authorized capital of Belgian companies while strengthening their financial autonomy, at least at the national level. These capital inflows partly reflect a move to substitute capital injections for current loans granted by foreign companies. In addition, the risk capital allowance has done much to encourage the formation of finance companies, allowing a large proportion of the authorized capital to flow back to other countries in the form of loans. The record capital contributions from abroad seem to indicate that the risk capital allowance has succeeded in making Belgium attractive from the tax angle. However, critics have claimed that it was not effective in preventing a decline in R&D and employment during the crisis years, and should therefore not be applicable for companies that have lain off their workforces. A bill was proposed, but never passed.[55]

Belgium is also quite active in terms of international investment agreements. Belgium is in the top ten signatory countries of BITs. It has also concluded and renewed several BITs and double taxation treaties (DTTs) in recent years in order to renegotiate the agreements with additional provisions covering broader economic activities.[56]

Conclusions and Outlook

Although IFDI in Belgium has been strongly influenced by MNEs using Belgium as a financial platform for investments in other countries, it is important in most sectors of the Belgian economy and in the technologically-oriented sectors in particular. Since the 1980s, when it was created, the coordination centers framework promoted both inward and outward investment in Belgium. As this incentive scheme was brought to an end by a decision of the European Commission as part of its program against unauthorized state aid, the extent to which the new "notional interest" measure will be able to keep up Belgium's reputation as a country with a large "welcome mat" for FDI remains to be seen. IFDI for the Belgian economy is likely to remain important, provided Belgium succeeds in keeping up with the other EU countries in attracting foreign affiliates and convinces firms from emerging markets to locate in Belgium as a platform for conquering the European market. While Belgium's high labor costs may be a handicap, they may largely be offset by the high productivity of its workers and operational and environmental advantages such as excellent infrastructure and favorable living conditions.

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[54] K. Burggraeve, Ph. Jeanfils, K. Van Cauter, and L. Van Meersel, "Macroeconomic and fiscal impact of the risk capital allowance," *Economic Review*, September 2008, p. 41 (Brussels: National Bank of Belgium, 2008).
[55] M. Arena, M. Mathot and G. Coëme, "Wetsvoorstel betreffende de notionele interestaftrek," *Doc 52, 2482/001*, p. 9 (Brussels: Belgische Kamer van Volksvertegenwoordigers, 2010).
[56] UNCTAD, "Recent developments in international investment agreements," *IIA Monitor*, No. 3, p. 15 (Geneva and New York: United Nations, 2009).

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Statistical annex

Annex table 1. Belgium: inward FDI stock, 2002-2009 (US$ billion)

Economy	**2002**	**2003**	**2004**	**2005**	**2006**	**2007**	**2008**	**2009**
Belgium	230	351	467	378	481	593	519	830
Memorandum: comparator economies								
Austria	45	58	71	83	111	163	159	169
Denmark	83	100	116	116	134	161	151	158
Netherlands	350	427	477	451	517	728	639	597

Source: UNCTAD’s FDI/TNC database, available at: http://stats.unctad.org/fdi/
Note: Data for Belgium are not available prior to 2002, as they were only reported as part of the Belgium Luxembourg Economic Union (BLEU).

Annex table 2. Belgium: inward FDI flows, 2000-2009 (US$ billion)

Economy	2002	2003	2004	2005	2006	2007	2008	2009
Belgium	16	33	44	34	59	118	110	34
Memorandum: comparator economies								
Austria	0	7	4	11	8	31	11	7
Denmark	7	3	-10	13	3	12	3	8
Netherlands	25	21	5	48	8	115	-8	27

Source: UNCTAD's FDI/TNC database, available at: http://stats.unctad.org/fdi/
Note: Data for Belgium are not available prior to 2002, as they were only reported as part of the Belgium Luxembourg Economic Union (BLEU).

Annex table 3. Belgium: sectoral distribution of inward FDI, by sector aggregates of foreign affiliates, 2005

Sector / industry	Number	Employment	Net value added (US$ million)
All sectors / industries	3,355	336,412	30,550
Primary	30	1,134	150
Secondary	682	145,208	14,960
Services	2,643	190,070	15,450

Source: Filip De Beule and Ilke Van Beveren, "Belgium's competitiveness: A comparison of foreign and domestic enterprises", in D. Van Den Bulcke, A. Verbeke and W. Yuan, eds, *Handbook on Small Nations in the Global Economy: The Contribution of Multinational Enterprises to National Economic Success* (Cheltenham: Edward Elgar, 2009), pp. 30-49.

Annex table 4. Belgium: geographical distribution of inward FDI flows, 2007-2009
(US$ million)

Region/economy	2007	2008	2009
World	105,334	95,978	20,592
Europe	99,237	77,389	42,245
EU-27	88,926	71,149	21,335
Other European countries	10,311	6,240	20,910
Africa	-269	-1,145	-4,921
North Africa	-353	59	-691
Other African countries	83	-1,204	-4,229
America	6,048	6,915	-5,764
North and Central America	6,045	5,840	-5,612
South America	3	1,075	-152
Asia	-1,798	12,714	-11,207
Near and Middle East	201	1,010	-1,851
Other Asian countries	-1,999	11,704	-9,356
Oceania	2,116	102	239
Other	52	12,748	-16,040

Source: National Bank of Belgium's, available at http://www.nbb.be/app/cal/E/belgohome.htm
Note: Not including reinvested earnings, which are not available.

Annex table 5. Belgium: main foreign affiliates, ranked by the sum of total assets, employment and turnover, 2008

Name	Employment	Turnover (US$ million)	Total assets (US$ million)	Home economy	Industry
Exxonmobil Petroleum & Chemical	2,176	28,972	42,339	United States	Manufacture of refined petroleum products
Hewlett-Packard Coordination Center	23	3	72,676	United States	Activities of head offices
Arcelormittal Finance And Services Belgium	34	4	61,285	Luxembourg	Activities of head offices
Petrofina	551	21,054	19,662	France	Manufacture of refined petroleum products
Toyota Motor Europe	2,415	26,831	9,602	Japan	Activities of head offices
BASF Antwerpen	3,432	6,446	22,982	Denmark	Manufacture of other organic basic chemicals
Atlas Services Belgium	6	3	32,815	France	Activities of head offices
Suez-Tractebel	172	157	31,120	France	Engineering, architectural, and surveying services
Gdf Suez Cc	376	68	29,382	France	Activities of head offices
Glaxosmithkline Biologicals	5,748	3,753	16,302	Great Britain	Pharmaceutical and medicine manufacturing
Ikea Service Center	43	7	25,404	Netherlands[a]	Activities of head offices
BASF Coordination Center	58	25	21,432	Denmark	Activities of head offices
Statoil Asa	53	8	21,347	Norway	Activities of head offices
Carrefour Belgium	10,993	6,449	3,533	France	Grocery stores
Centre De Coordination Carrefour	16	1	19,768	France	Activities of head offices
Petrofina International Group	32	6	19,474	France	Activities of head offices
Randstad Belgium	15,372	973	2,352	Netherlands	Temporary employment agency activities
Janssen Pharmaceutica	3,913	5,242	9,272	United States	Pharmaceutical and medicine manufacturing
Eni Coordination Center	30	16	17,147	Italy	Activities of head offices
Arcelor Mittal Belgium	7,400	4,336	5,155	Luxembourg	Manufacture of basic iron and steel and of ferrous-alloys
Royal Park Investments	3	0	15,813	France	Miscellaneous business services
Gmr	2	1	14,512	France	Miscellaneous business services
Sabelfi	9	2	12,082	Canada	Business credit institutions
Manpower (Belgium)	11,491	344	103	United States	Temporary employment agency activities
Adecco Personnel Services	10,688	595	109	CH	Temporary employment agency activities

Source: Authors' calculations, based on the Amadeus database (Bureau Van Dijk).
[a] IKEA is owned by INGKA Holding B.V., a Dutch corporation; its operational headquarters are in Sweden.
Note: Unconsolidated accounts.

Annex table 6. Belgium: main M&A deals, by inward investing firm, 2009

Acquiring company	Target company	Target industry	Source economy	Shares acquired (%)	Transaction value (US$ million)
BNP Paribas SA	Fortis Bank SA/NV	Banking	France	74.9	12,765.3
EDF	SPE SA	Electric services	France	51.0	1,848.3
Centrica Overseas Holdings Ltd	Segebel SA	Electric services and other combined	United Kingdom	50.0	972.4
CVC Capital Partners Ltd	De Post-La Poste	Courier services	Luxembourg	49.9	478.2
Dean Foods Co	Alpro NV	Soybean oil mills	United States	100.0	448.0
Ecofin Ltd	Hansen Transmissions Intl	Machinery manufacturing	United Kingdom	10.0	115.0
Canon Europa NV	IRIS Group SA	Prepackaged software	Netherlands	17.0	99.0
Aquiline Capital Partners LLC	Clear2Pay NV	Prepackaged software	United States	n.a.	74.1
Sally Beauty Holdings Inc	Sinelco Group NV	Service establishment equipment	United States	100.0	36.6
Celesio AG	Laboratoria Flandria NV	Pharmaceuticals	Germany	n.a.	35.4
Amplifon SpA	Dialogue	Medical, dental, and hospital equipment	Italy	100.0	19.5
Investor Group	Cardio3 BioSciences SA	Biological products	Luxembourg	n.a.	17.9
Dorel Industries Inc	Baby Art bvba	Clothing and accessories	Canada	100.0	5.4
Skidata AG	Orcus	Prepackaged software	Austria	100.0	3.0
BNP Paribas SA	Fortis Insurance Belgium SA	Insurance	France	25.0	1.9
Logan Oil Tools Inc	Diamant Drilling Services SA	Metalworking machinery	United States	100.0	0.7

Source: Thomson ONE Banker, Thomson Reuters.

Annex table 7. Belgium: main greenfield projects, by inward investing firm, 2009

Investing company	**Target industry**	**Business activity**	**Source economy**	**Estimated transaction value** (US$ million)
GlaxoSmithKline (GSK)	Pharmaceuticals	Manufacturing	United Kingdom	542
ExxonMobil	Coal, oil and natural gas	Electricity	United States	449
COFRA Holding	Real estate	Construction	Switzerland	196
COFRA Holding	Real estate	Construction	Switzerland	196
France Telecom	Communications	Customer contact center	France	142
Eneco	Alternative/renewable energy	Electricity	Netherlands	128
Caterpillar	Industrial machinery, equipment and tools	Manufacturing	United States	126
TPG	Transportation	Logistics, distribution and transportation	Netherlands	80
Ciblex	Transportation	Logistics, distribution and transportation	France	80
Avient	Transportation	Logistics, distribution and transportation	United Kingdom	80
Astre	Transportation	Logistics, distribution and transportation	France	79
Pierre & Vacances	Hotels and tourism	Construction	France	58
Inditex	Consumer products	Retail	Spain	54
Hema	Consumer products	Retail	Netherlands	54
IKEA	Consumer products	Retail	Sweden	54
Inditex	Consumer products	Retail	Spain	54
DSM	Rubber	Manufacturing	Netherlands	51
Asahi Glass	Ceramics and glass	Manufacturing	Japan	48
Ashland	Chemicals	Manufacturing	United States	37
PolyOne	Chemicals	Manufacturing	United States	35

Source: fDi Intelligence, a service from the Financial Times Ltd.

Annex table 7a. Belgium: Number of greenfield projects and acquisitions in Belgium, 2005-2009

Entry mode	**2005**	**2006**	**2007**	**2008**	**2009**
Greenfield	179	185	175	142	146
Acquisition	119	106	126	108	78
Total	298	291	301	250	224

Source: Ernst & Young, *Barometer van de Belgische Attractiviteit 2010* (Brussels: Ernst and Young, 2010); Zephyr database, Bureau Van Dijk.

Annex table 7b. Number of greenfield projects in Belgium, by sector, 2005-2009

Sector	**2005**	**2006**	**2007**	**2008**	**2009**
Sales and marketing	56	63	71	48	60
Production	47	66	38	36	27
Logistics	43	28	28	33	26
Headquarters	8	9	20	8	8
Research and development	12	4	5	7	11
Services	13	15	13	10	14
Total	179	185	175	142	146

Source: Ernst & Young, *Barometer van de Belgische Attractiviteit 2010* (Brussels: Ernst and Young, 2010).

Chapter 3 – Canada

Inward FDI and its policy context, 2010

Ram C. Acharya, Someshwar Rao, Subrata Bhattacharjee, and Leila Wright

Canada has actively participated in the corporate globalization process and is a major importer of foreign direct investment (FDI). Canada's high levels of IFDI over the past 25 years reflect its improved business climate, reduced restrictions on foreign ownership and a prospering economy. Like other developed economies, Canada experienced declining FDI inflows in 2008 and 2009, largely due to the dramatic fall in M&As and the global economic recession. The outlook for 2010 and beyond however is promising because of the expected economic expansion in Canada and other countries, and improved global financial markets. Moreover, the Canadian Government has sent strong signals to foreign investors that Canada is open for business by, among other things, lifting restrictions on previously protected sectors and increasing the financial thresholds for the review of foreign investments.

Trends and developments

IFDI in Canada has risen steadily over the past decade, with cross-border M&As driving the most recent upsurge, especially in the primary sector. Canada is one of the G-7 economies most open to IFDI: slightly more than one-fifth of Canada's total assets are controlled by foreign companies. The ratio of the IFDI stock to the Canadian gross domestic product (GDP) was 34% in 2008, compared with, for example, a ratio of 37% for the United Kingdom. The impact of the global financial and economic crisis reduced IFDI in 2008 and 2009. Nevertheless, though still weaker than in the previous year, the Canadian M&A market strengthened in the third quarter of 2009, posting a 27% increase in deal value over the second quarter of 2009.

Country-level developments

Between 2000 and 2008, Canada's stock of IFDI grew by 120%, reaching US$ 474 billion by the end of 2008 (annex table 1). By way of comparison, growth of U.S. stock was much lower, while that of the United Kingdom was slightly higher. In contrast, Mexico's IFDI stock grew at nearly twice the pace of Canada's.

Between 2000 and 2008, Canada's IFDI flows were lowest in 2004 when they hit a negative value (because foreigners sold more of their existing interest in Canada than they bought), and highest in 2007 when they reached US$ 108 billion. There was a massive surge in foreign acquisitions of Canadian firms in 2006 and 2007, following the strong increase in commodity prices (annex table 2). In addition to the improved Canadian business climate, reduced restrictions on IFDI also contributed to the rise in M&A activity.

IFDI in Canada is concentrated largely in the service sector (44%), followed by manufacturing (34%) and the primary sector (22%) (annex table 3). The manufacturing sector's share of the stock of IFDI declined by 14 percentage points since 2000, due to a diversion of investments into the primary sector and, to a lesser extent, the service sector. Within manufacturing, the decline was most marked in the computer and electronics, transportation equipment, textiles, clothing, wood and paper industries. In the computer and electronics industry, Canada's IFDI stock in 2008 was lower than its 2000 level due to a post-2000 meltdown of asset values. In the primary sector, MNEs typically invest in Canada's oil and gas and other mining industries. Cross border M&As boosted investment in 2007, driven by rising commodity prices.

Canada's IFDI stock comes overwhelmingly from developed countries. In 2008, these accounted for 92% of inward stock; however, this share was six percentage points below the 2000 level (annex table 4). Of this FDI, 58% came from the United States and 26% from European Union countries. Developing countries, on the other hand, accounted for only 5% of Canada's IFDI stock in 2008, up from 2% in 2000. This growth is largely attributable to Brazil's growing investment in Canada. In more recent years, companies from Asia, particularly from China, and, to some extent from India, are acquiring Canadian companies especially in the resource sector.

The corporate players

Foreign affiliates are increasingly active in Canada. In 2007, 21% of assets and 29% of revenue in Canada were under foreign control. In 2007, about one-fifth of all foreign-controlled assets in Canada were in the primary sector, a disproportionately large share compared to its contribution to Canada's GDP, increasingly concentrated in the oil and gas and other mining industries. The shares of these two industries in foreign controlled assets rose by almost four percentage points between 2000 and 2007. The share of foreign controlled assets in the manufacturing sector, in comparison, declined from 33% in 2000 to 25% in 2008. The share of foreign assets in the service sector has remained more or less constant at 18%, and is concentrated predominantly in the wholesale, retail, real estate, renting, and leasing industries.

A list of the top 20 largest foreign companies operating in Canada (ranked by revenue) is provided in annex table 5. Among them, two are operating in the energy (oil and gas) and the metals and mining industries; three in the automobile industry; two in computer services; and one in the IT service industry.

There were 60 mega-deals (value of US$ 1 billion or more) with a combined value of US$ 275 billion announced in 2007 alone, a record high in terms of both volume and value. Of the total value of announced deals that year, 78% was cross-border in nature; all of the ten largest deals had an international component. The value of foreign-led acquisitions, the largest of which was worth US$ 48 billion (BCE) (annex table 6), surpassed the acquisitions by Canadians in foreign countries by a 2-to-1 margin. The pace of cross-border M&A activity declined dramatically in 2008 however, falling to less than one-third of its 2007 value. The decline continued through the first quarter of 2009, but had begun to rebound by the third quarter of 2009.

Annex table 7 provides a list of greenfield investments in Canada over the past three years (2007-2009).[57] In 2008, greenfield investments occurred mainly in the insurance industry, followed by the retail service industry. In 2009, in contrast, greenfield investment targeted the oil, metal and energy industries.

Effects of the current global crisis

The negative impact of the global economic and financial crisis is visible in the precipitous drop in IFDI flows in 2009. These were negative in the first half of 2009, as sales of assets by foreign investors were higher than incoming FDI. In the first quarter, FDI inflows into Canada were only US$ 743 million, while disinvestment amounted to US$ 1.1 billon in the second quarter. FDI inflows rose to US$ 19.3 billion by the end of 2009, but flows were still less than half the level attained in 2008, which in turn was less than in 2007 (annex table 1).

The fourth quarter of 2009 was the third consecutive quarter in which the Canadian M&A market expanded, ending a volatile year on a positive note and possibly indicating that financial markets have stabilized.[58] Strong M&A activity in the third quarter reflected a continued improvement in a number of market fundamentals, including the financing conditions for buyers, buyers' confidence, and company valuations.[59] The third quarter's largest and second largest M&As included China's Investment Corporation's investment in Teck Resources Ltd. and the US$ 1.5 billion takeover of Eldorado Gold Corp. by Australia-based Sino Gold Mining Ltd. The largest inward cross border M&A in the fourth quarter of 2009 was Korean National Oil Corporation's US$ 4.1 billion acquisition of Calgary-based Harvest Energy Trust. Despite the improvements in M&A markets over the second half of 2009, M&A activity remains well below the levels experienced prior to the global financial crisis and recession.[60] Consistent with the historical trends, the total number of acquisitions made by Canadian companies abroad exceeded the number of foreign takeovers of Canadian companies by a margin of 2.2 to 1.

The policy scene

Non-Canadians who acquire control of an existing Canadian business or who intend to establish a new Canadian business must comply with the Investment Canada Act (ICA). Canada has historically had relatively high regulatory barriers to IFDI among developed economies, including in services such as banking. However, through recent amendments to the ICA, the Canadian Government has revised its approach to foreign investment regulation to create a more liberal regime aimed at increasing its share of IFDI not just from traditional sources, such as the United States, but also from emerging markets, especially Brazil, Russia, India, and China.[61] Review thresholds will be increased significantly, reducing the number of investments subject to a review. Nevertheless, Canada continues to rely on sector-specific restrictions and its powers to review sovereign investments and any other foreign investments with the potential to threaten

[57] Data on shares acquired and the transaction value are not available as they are confidential
[58] Crosbie, "M&A quarterly report-Q4/09", available at: http://www.crosbieco.com/pdf/ma/MA_Q409.pdf
[59] Ibid.
[60] Ibid.
[61] Note that these amendments were made in response to recommendations of the Competition Policy Review Panel. For further information see Competition Policy Review Panel, *Terms of Reference*, available at: http://www.ic.gc.ca/eic/site/cprp-gepmc.nsf/eng/h_00004.html.

national security. In particular, when guidelines were introduced in 2007, the ICA did not include a national security review power. However, the recent amendments have added a stand-alone national security review test to the ICA.

This test is separate from the net benefit test that is generally applicable to reviewable investments under the ICA, and applies to a much broader range of proposed transactions. The national security test subjects investments that "impair or threaten to impair national security" to Ministerial and potentially Cabinet review, though no definition of what constitutes "national security" is given in the ICA or the regulations made thereto.[62] However, it is possible that investments impacting Canada's sovereignty, national defense and potentially strategic sectors of the economy (such as natural resources), and investments by state-owned enterprises (SOEs) may be considered under the national security test. Concerns have been raised that the test has the potential to be used as a tool for protectionism, given the high level of discretion provided to the Government. However, to date there has been no action taken to substantiate this concern.

Conclusions and Outlook

Canada's sound macro environment (including its fiscal, monetary and tax policies), its efforts to stimulate economic growth and open its borders to IFDI, an improved business climate, and a favorable natural resource endowment all contributed to the large increase in FDI in Canada over the past 20 years. Like other developed countries, cross-border M&As into Canada, and hence IFDI flows, were hit hard by the financial crisis and recession. The outlook for IFDI in 2010 and beyond looks promising because of the expected expansion of the Canadian and other economies, the improved situation in global financial markets and increased demand for resources. Canada still has higher barriers to IFDI compared to many developed countries in key services industries. Any progress on this front would be expected further to increase FDI in Canada.

Additional readings

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[62] *National Security Review of Investments Regulation*, S.O.R./2009-271.

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Industry Canada, *Backgrounder:* “Guidelines for state-owned enterprises”, available at: http://www.ic.gc.ca/eic/site/ic1.nsf/eng/02060.html.

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Statistical annex

Annex table 1. Canada: inward FDI stock, 2000, 2008 (US$ billion)

Economy	**2000**	**2008**	**Growth (percent)**	**Share in GDP (percent)**	
				2000	**2008**
Canada	215	474	120	33	34
Memorandum: comparator economies					
US	1,257	2,279	81	14	16
Mexico	97	295	203	20	27
UK	439	983	124	30	37

Source: UNCTAD's FDI/TNC database, available at: http://stats.unctad.org/fdi/. The GDP data for all countries are taken from World Bank's World Development Index.

Annex table 2. Canada: inward FDI flows, 2000-2008 (US$ billion)

Economy	**2000**	**2001**	**2002**	**2003**	**2004**	**2005**	**2006**	**2007**	**2008**
Canada	66.8	27.7	22.1	7.5	-0.4	25.7	59.8	108.3	44.8
Memorandum: comparator economies									
US	314.0	159.5	74.5	53.1	135.8	104.8	237.1	271.2	316.1
Mexico	18.0	29.8	23.7	16.5	23.7	21.9	19.3	27.3	21.9
UK	118.8	52.6	24.0	16.8	56.0	176.0	156.2	183.4	96.9

Source: UNCTAD's FDI/TNC database, available at: http://stats.unctad.org/fdi/

Annex table 3. Canada: distribution of inward FDI stock, by economic sector and industry, 2000, 2008 [a] (US$ million)

Industries based on NAICS [b] classifications	2000	2008	Growth (percent)
Primary	***23,009***	***103,322***	***349***
Agriculture, forestry, fishing and hunting	764	1,145	50
Oil and gas extraction	15,194	69,494	357
Mining (except oil and gas)	4,184	25,634	513
Construction and utility	2,867	7,049	146
Secondary	***104,071***	***160,970***	***55***
Chemical manufacturing	13,347	23,492	76
Computer & electronic manufacturing	9,948	6,119	-39
Transportation equipment manufacturing	16,224	18,685	15
Other manufacturing—group 1 [c]	41,416	57,887	40
Other manufacturing—group 2 [d]	23,135	54,786	137
Services	***87,813***	***206,554***	***135***
Transportation and warehousing	2,014	4,265	112
Information and cultural industries	5,408	8,170	51
Finance and insurance	25,057	56,704	126
Management of companies and enterprises	17,881	57,014	219
Other services industries	37,452	80,402	115
Unspecified	0	2760	
All sectors/industries	**214,893**	**473,606**	**120**

Source: Statistics Canada: CANSIM, Table No. 376-0052.

[a] The original data were in Canadian dollars and were converted into US dollars using average annual exchange rates (Canadian dollar per US dollar of 1.485 for 2000 and 1.066 for 2008).

[b] North American Industry Classification System.

[c] Other manufacturing—group 1 includes nine NAICS 3-digit industries: (1) food, (2) beverage & tobacco, (3) textile mills, (4) textile products, (5) clothing, (6) leather, (7) wood product, (8) paper, (9) petroleum and coal product manufacturing. Other manufacturing—group 2 includes eight NAICS 3-digit industries. They are: (1) plastics and rubber, (2) non-metallic mineral, (3) primary metal, (4) fabricated metal, (5) machinery, (6) electrical equipment, appliance and component, (7) furniture related and (8) miscellaneous manufacturing.

[d] Other services industries include the following five NAICS industries: (1) wholesale trade, (2) retail trade, (3) real estate and rental and leasing, (4) professional, scientific and technical services, (5) accommodation of food services.

Annex table 4. Canada: geographical distribution of inward FDI stock, 2000, 2008
(US$ million)

Region/economy	2000	2008	Growth (%)		2000	2008	Growth (%)
World	**214,893**	**473,606**	**120.4**				
Developed economies	***210,599***	***435,973***	120	*Asia/Oceania*	*2,815*	*9,575*	240
Europe	72,073	142,921	107	Hong Kong , China	2,272	[a]	
European Union	64,579	124,376	98	India	12	959	7809
Austria	153	229	93	Malaysia	79	64	-20
Belgium	1,939	2,314	50	China	129	2582	1897
Cyprus	NA	1,749		Philippines	1	2	39
Denmark	261	841	223	Saudi Arabia	[a]	2	
Finland	339	1189	251	Singapore	98	179	82
France	24,914	17,392	-30	Rep. of Korea	156	810	418
Germany	4,966	8,793	77	Taiwan Province of China	65	91	39
Ireland	710	646	-9	Thailand	1	5	597
Italy	616	1,226	99	UA Emirates	[a]	4,883	
Luxemburg	2,012	5,311	164	*Latin America and Caribbean*	*1,245*	*12,462*	901
Netherlands	10,327	3,1754	207	Argentina	[a]	41	
Poland	8	7	-19	Bahamas	133	337	154
Spain	440	271	-38	Barbados	162	370	129
Sweden	1763	1600	-9	Brazil	418	11,182	2574
United Kingdom	16,131	51053	216	British Virgin Islands	63	249	293
North America	*130,405*	275,430	111	Cayman Islands	22	[a]	
United States	130,405	275,430	111	Chile	6	[a]	
Other developed economies	*15,615*	36,167	132	Colombia	2	1	-54
Australia	1,152	3,840	233	Jamaica	1	[a]	
Bermuda	1,391	1,964	41	Mexico	145	231	59
Israel	197	721	267	Nether. Antilles	228	5	-98
Japan	5,415	12,207	125	Panama	63	47	-25
Liechtenstein	86	169	97	Peru	1	[a]	
New Zealand	68	38	-43	Venezuela	3	[a]	
Norway	3,370	2,843	-16	***Transition economies***	***6***	***348***	5642
Switzerland	3,937	14,384	265	Russian Federation	6	348	5642
Developing economies	***4,139***	***22,683***	448	***Unspecified***	***149***	***14,602***	9712
Africa	*79*	646	713				
South Africa	79	646	713				

Source: Statistics Canada: CANSIM, Table No. 376-0051
[a] Suppressed due to confidentiality.

Annex table 5. Canada: top 20 largest foreign affiliates in Canada, ranked by revenue, 2008

Rank	Company	Industry	Revenue [a] (US$ billion)	% of foreign ownership
1	Imperial Oil Limited	Oil and gas	29.3	69
2	Husky Energy Inc.	Energy	23.2	71
3	Wal-Mart Canada Corp.	Consumer services	15.6	100
4	Novelis Inc.	Metals and mining	10.9	100
5	Honda Canada Inc.	Automobile	10.8	100
6	Direct Energy Marketing Limited	Energy	10.7	100
7	Ultramar Ltd.	Oil and gas	10.4	100
8	Costco Wholesale Canada Ltd.	Consumer services	9.5	100
9	Ford Motor Company of Canada, Ltd.	Automobile	7.8	100
10	Canada Safeway Ltd.	Food retail	6.4	100
11	Home Depot Canada	Retailing	5.7	100
12	Gerdau Ameristeel Corporation	Metals and mining	8.5	66
13	Cargill Limited	Financial services	5.5	100
14	Best Buy Canada Ltd.	Computer	5.2	100
15	IBM Canada Ltd.	IT Services	5.1	100
16	Toyota Canada Inc.	Automobile	5.0	100
17	Hewlett-Packard (Canada) Co.	Computer	4.9	100
18	Sears Canada Inc.	Retailing	5.4	90
19	Conoco Phillips Canada Resources Corp.	Oil and gas	4.7	100
20	HSBC Bank Canada	Banks	4.0	100

Source: Financial Post Magazine, FP 500, 2009, Toronto.
[a] "Revenue" refers to sales by the Canadian business only, and not to the global revenue of the parent companies.

Annex table 6. Canada: M&A deals, by inward investing firm, 2007-2009

Year	Acquiring company	Target company	Target industry	Source economy	Shares acquired (%)	Estimated/ announced transaction value (US$ billion)
2009	Canada Pension Plan (Canada)	Macquarie Communications Infrastructure Group (Australia)	Financial services	Australia	100%	7.6
2008	Teck Cominco Limited (USA)	Fording Canadian Coal Trust (Canada)	Mining	USA	100%	13.2
2007	Western Oil Sands Inc. (Canada)	Marathon Oil Corporation (USA), WesternZagros Resources Ltd. (Canada)	Oil and gas	USA	100%	6.6
2007	- Madison Dearborn Partners, LLC (Chicago, Ill, USA) - Providence Equity Partners Inc. (Providence, New York, Los Angeles, London, Hong Kong and New Delhi) - Ontario Teachers' Pension Plan (Ontario, Canada)	BCE Inc. (Canada)	Communications	USA, UK, India	- OTPP 52% - Providence Equity Partners 32% - Madison Dearborn Partners 9% - Other, unidentified Canadian investors hold the balance of the equity.	48.1
2007	Rio Tinto Group (UK)	Alcan Inc. (Canada)	Aluminum production	UK	95.82%	38.1
2007	The Thomson Corporation (Canada)	Reuters Group PLC (England)	Financial news	UK	53%	17.4
2007	The Toronto-Dominion Bank (Canada)	Commerce Bancorp, Inc. (USA)	Financial services	USA	100%	8.5
2007	IPSCO Inc.	SSAB Svenskt Stal AB	Steel pipe manufacturer	Sweden	100%	7.7
2007	Alcoa Inc.	Alcan Inc.	Aluminum production	USA	100%	33.0
2007	Ontario Municipal Employees Retirement System (Canada), Apax Partners (International)	Thomson Learning assets The Thomson Corporation (vendor)	Higher education	International: North America, Europe, Asia	100%	7.8

Source: **Financial Post Crosbie: Mergers & Acquisitions database in Canada, 2009: available at: www.fpinfomart.ca**

Annex table 7. Canada: main greenfield projects, by inward investing firm, 2007-2009 [a]

Investing company	Joint venture partner (if any)	Target industry	Home economy
2009			
Bruno Blervaque		Management	France
Shanghai Zhongrong Property Group	Baizheng Song	Metals and mining	China
Pilatus Energy AG		Oil and gas	UAE
Renewable Energy Holdings PLC		Energy	Isle of Man
Takeda Canada, Inc.		Pharmaceuticals	Japan
DEGI Homburg Harris Limited Partnership		Real estate	Germany
2008			
AXIS Reinsurance Company		Insurance	Bermuda
Dunlop Sports Group Americas, Inc.		Retail	UK
Partner Reinsurance Company Ltd.		Insurance	Bermuda
Partner Reinsurance Europe Limited		Insurance	Ireland
Great Lakes Pork, Inc.		Farming	US
Cardiff-Assurances Risques Divers		Insurance	France
Cardif Assurance Vie		Insurance	France
Triton Insurance Company		Insurance	US
Bed Bath & Beyond Canada L.P.		Retail	US
EDS Group Holdings Limited		Other	UK
Louis Dreyfus Canada Ltd.		Other	US
Lowe's Companies, Inc.		Retail	US
2007			
ABC Learning Centres Limited		Real estate	Australia
Plavor III B.V.		Real estate	Netherlands
Alan Minty		Oil and gas	UK
Concession A25, L.P.		Construction	US
CS Automotive Tubing Inc.		Automobiles	Republic of Korea
Universal Power Transformer Inc.		Energy	India
Dalkia International S.A.		Health care	France
PMI Mortgage Insurance Co.		Insurance	US
Host International of Canada, Ltd.	Cancouver Uno, S.L. and Aldeasa Canada Inc.	Retail	Spain
BBPP North America S.a.r.l.		Construction	Channel Islands
Laing Investments Management Services		Financial	UK

Source: Industry Canada.
[a] Data are confidential.

Outward FDI and its policy context, 2010

Ram C. Acharya, Someshwar Rao, Subrata Bhattacharjee, and Leila Wright

Canada was a major net importer of foreign direct investment prior to 1996. The stimulus for the surge in Canada's OFDI came from profitable investment opportunities abroad. Canada has diversified significantly its OFDI away from the United States over the past 20 years. The financial crisis significantly affected Canada's FDI outflows, but OFDI seems to have rebounded in the second half of 2009. While Canadian investment has historically gone mainly to developed countries, recent changes in Government policies seem to suggest that Canada is looking to build closer ties with developing countries as well. Canada has a longstanding commitment to multilateral cooperation and actively supports the World Trade Organization (WTO) framework as a way to promote international trade and investment. At the same time, Canada continues actively to negotiate foreign investment promotion and protection agreements (FIPAs).

Trends and developments

Country-level developments

In 2008, Canada was the tenth largest global investor measured by the value of its OFDI stock. Between 2000 and 2008, Canada's OFDI stock grew by 116%, reaching US$ 520 billion (annex table 1). However, the growth in Canada's OFDI stock during 2000-2008, though almost double that of the United Kingdom's (UK), was lower than the growth of the United States' (US) stock, and only one quarter that of Mexico's.[63] Despite growing more slowly than its continental neighbors, Canada's share of North America's OFDI stock (including intra-regional FDI stock) remained stable at around 15%.

In terms of the ratio of the OFDI stock to GDP, the United Kingdom stands out among the same four comparator countries. In 2008, the ratio of the OFDI stock to GDP was 57% for the UK, 43% for Canada, 22% for the US, and 4% for Mexico (annex table 1). Everything else being the same, smaller countries generally tends to be more outward-oriented in terms of both trade and FDI, which may explain why Canada's OFDI orientation is higher than that of the US. As regards the UK, it is not clear whether relatively weaker investment opportunities at home, better investment opportunities abroad, or a more market-seeking nature of UK companies would explain the UK's relatively high OFDI orientation.

Between 2000 and 2008, Canada's annual OFDI flows fluctuated between a low of US$ 23 billion in 2003 and a high of US$ 78 billion in 2008 (annex table 2a). There was a substantial

[63] We have chosen the United States, Mexico and the United Kingdom as comparator countries, for two reasons. First, the United States and Mexico are partner countries of the North American Free Trade Agreement, and it is interesting to know how Canada compares with them. Second, the United Kingdom is the most outward FDI oriented country among the G7 countries, and hence a benchmark country.

increase in FDI outflows in 2007 and 2008. High commodity prices and the resulting increases in Canadian companies' stock valuations may have enabled Canadian firms to acquire more assets abroad.

With regard to sectoral distribution, Canadian companies tend to concentrate their cross-border investments in the primary and tertiary sectors, with FDI in the secondary sector playing only a minor role. Between 2000 and 2008, the share of the primary sector in Canada's total OFDI stock increased from 13% to 18%. Similarly, the share of services rose from 55% to 63%, while the share of the manufacturing industry fell from 32% to 13% (annex table 3). All industries except chemicals contributed to manufacturing's relative decline. The largest decline (10 percentage points in just eight years) occurred in computers and electronic manufacturing. The deterioration in the competitive position of Canada's manufacturing industry and the decline of its importance in most potential host countries seem to have contributed to the decline of the manufacturing industry in Canada's outward flows.

Within the service industry, OFDI in the finance and insurance industry grew the most rapidly: its share in the total OFDI stock rose from 28% in 2000 to 40% in 2008. The deregulation of the financial services industry that took place in many countries around the world in the past decade may have paved the way for a massive increase in this sector's share, as both occurred during the same time period. However, there is no particular study (that we know of) that looks at the relationship between financial deregulation in other countries and Canada's OFDI flows. The increase in OFDI in the primary sector could be mainly due to post-2005 commodity price increases as Canadian firms were able to acquire more foreign firms, especially in the oil and gas extractive industries,

The geographical composition of Canada's OFDI stock in 2008 has changed little from 2000. The largest share, 79%, was destined to developed countries. The remaining 20% was invested in developing countries, with only a negligible share going to transition economies (annex table 4). The United States remains by far the largest destination market for Canada's OFDI, absorbing 49% of Canada's OFDI stock in 2008. Canada's historically close economic ties with the United States could be a major contributing factor for the US dominance. The other determinants might include geographical proximity, similarities in the regulatory climates and a common language.[64] Among other developed countries, the European Union (EU) received a little less than one-quarter of Canada's OFDI stock, with the remaining 7% broadly distributed among other industrialized OECD countries. In 2008, two countries accounted for about half of Canada's total OFDI stock in the developing world: Barbados and Cayman Islands, both tax havens. Canada's OFDI in all other developing countries was very small; the largest share was in Brazil (1.4%).

Altogether, four offshore centers −Barbados (7.1%), Bermuda (3.5%), Cayman Islands (3%), and Bahamas (2% in 2007, the data for 2008 are suppressed) − were the destination for 16% of

[64] This fact is related to the assumptions underpinning gravity models, which hold that the size of two countries and the distance between them can be core determinants of FDI flows between two countries. The basic message of the model is that, after controlling for the influence of other variables, both trade and FDI flows between any two countries are positively correlated with the size of the two economies and negatively related with the distance between them. See, for example James E. Anderson, "Gravity, productivity and the pattern of production and trade", NBER Working Paper No. 14642, January 2009.

Canada's OFDI stock in 2008.[65] The outward investments made in these offshore jurisdictions then make their way to other jurisdictions. Finally, Canada's low FDI in developing countries is not unusual compared to other developed countries, most of which likewise invest primarily in other developed countries.

The corporate players

Canadian companies are actively engaged in cross-border M&As. Between 2007 and 2009, there were approximately 20 M&A deals worth more than US$ 1 billion each (annex table 5). Twelve of those mega-deals were concluded in 2009. The acquisitions were in various sectors. Six of them were in oil and mineral resources, indicating Canadian companies' strong comparative advantage in these industries.

The data show that sales of goods and services of foreign affiliates of Canadian MNEs rose by 74% between 2000 and 2007, reaching US$ 430 billion (annex table 6). The largest increase was in the primary sector affiliates' sales, which rose by 277%. Out of total sales of all Canadian affiliates, the share of affiliates in the US fell from 65% in 2000 to 52% in 2007.[66] Foreign affiliates of Canadian companies employed 1.13 million people in 2008. The employment in these affiliates rose by 28% during 2000-2007, much more than the growth realized in domestic employment during the same time period (with a growth of 16%).

Effects of the current global crisis

Canadian FDI outflows did not feel the impact of the global financial crisis and the recession that followed in 2008. Outflows were about US$ 39 billion in both the first and the second half of that year, making Canada an exception among most other developed countries, where OFDI fell in the second half of 2008. As a matter of fact, in 2008, outflows were at their highest level since 2000. These outflows were mainly greenfield investments, which contributed to 51% of total OFDI flows, while M&As contributed 29% and the remaining part was contributed by reinvested earnings. The relatively low contribution of reinvested earnings was possibly a consequence of falling profits abroad (annex table 2a). Yet, the other components, net outflows (which may include greenfield, M&A and loan investment as well), were quite strong, at almost double what they were in 2007.

The crisis did, however, result in a marked drop of Canadian OFDI flows in the first six months of 2009: they were less than US$ 6 billion in the first two quarters. But flows bounced back to US$ 41 billion by the end of 2009.

The renewed strength since the third quarter of 2009 was primarily attributable to a pickup in acquisition activity. In 2009, for the first time in five years, the "balance of trade" for cross-border M&A transactions favored Canadian buyers. The aggregate value of Canadian-led cross-

[65] Large investments in these offshore centers are motivated by special reasons (legal tax minimization, holding companies, offshore financial centers, special purpose entities). The FDI data for these offshore centers are corrected for flows to third countries from these centers. Otherwise, their share in Canada's OFDI would be even higher. However, the correction may not be 100%, because holding companies may not fully disclose where the capital flows from these offshore centers.

[66] There are no data on the share of Canadian MNEs' real activities in other countries. There is also no information available on sales in host countries, and exports/imports to/from their Canadian parent companies and their affiliates in other countries.

border deals was higher than the value of foreign acquisitions of Canadian companies by a margin of 1.2:1. Moreover, Canadian companies were involved in a number of mega-deals (annex table 6).

Canadian firms mainly targeted the US for their M&As in 2009. This increased investment was facilitated by the sizeable appreciation of the Canadian dollar vis-à-vis the US dollar and the signs of an economic recovery in the United States in the third quarter. In spite of the rebound since the third quarter, Canadian OFDI flows in 2009 were only about half of what they were in 2008 (US$ 41 billion versus US$ 78 billion).

Overall, OFDI allows Canadian firms to expand their production in international markets. Since trade and OFDI are complements, one helps to increase the other.

The policy scene

Canada is continually looking for ways to expand its economic presence internationally. In this effort, the Canadian Government actively promotes outward foreign investment through FIPAs, multilateral investment and trade agreements and institutional assistance abroad. Historically, Canada has focused its efforts on rule-based investment agreements with other developed economies. However, recent negotiations suggest that Canada is also looking to build stronger ties with key developing economies.

Canada has a longstanding commitment to multilateral cooperation and actively supports the WTO framework as a way to promote international trade and investment. At the same time, Canada continues to negotiate FIPAs, i.e. bilateral agreements aimed at protecting and promoting foreign investment through legally-binding rights and obligations. FIPAs accomplish their objectives by setting out the respective rights and obligations of the countries that are signatories to a treaty with respect to the treatment of foreign investment. Canada currently has 23 FIPAs in place. Since 2007, Canada has concluded negotiations with India, Jordan, Kuwait, Madagascar, and Peru. Negotiations are ongoing with Indonesia, Mongolia, Tanzania and Vietnam, while those with China are in the final stages. Exploratory discussions are being pursued with a number of countries in Asia, Africa and the Middle East. Furthermore, Canada has FIPAs with six of the new European Union member states (the Czech Republic, Hungary, Latvia, Poland, Romania, and Slovakia).

NAFTA is a significant tool for investment promotion among Canada, Mexico and the United States. Chapter 11 establishes a framework to provide NAFTA investors with rule-based investment, predictability and dispute settlement procedures. Increasingly, though, Canada is actively engaged in negotiations to establish FTAs with key countries outside of North America. For example, in early 2009, Canada and India agreed to initiate exploratory talks on an economic partnership agreement, and Canada and the EU announced in May 2009 their intentions to negotiate a Comprehensive Economic and Trade Agreement (the “CETA”). The CETA is expected to include, among others, competition policy, trade promotion and investment facilitation. Negotiations are currently underway.

The Canadian Government's new Global Commerce Strategy[67] highlights the importance of increasing both inward and outward flows of investment to enhance future Canadian competitiveness and productivity. Canada recently increased the size of its network of investment and trade commissioners posted in foreign locations, so as to assist Canadian companies seeking to enter and establish themselves in foreign markets. Historically, Export Development Canada (EDC) and the Canadian Commercial Corporation, both public agencies, have assisted in financing Canadian exports, particularly for large infrastructure projects and major procurements.[68] EDC currently has only a limited number of OFDI financing initiatives. However, new regulatory changes are expected to enhance EDC's ability to invest in private equity and venture capital funds. This reform should help Canadian companies expand and grow their businesses internationally, particularly in emerging markets.

Conclusions and Outlook

Canada has been a net exporter of FDI since 1996, with approximately half of its OFDI destined for the United States. In recent years, Canada's FDI outflows have been increasingly concentrated in the mining, oil and gas and finance and insurance industries. Lower commodity prices compared to 2008 may dampen somewhat Canadian investment in mining and oil industries at home and abroad. Similarly, as a result of the global financial crisis, foreign banking industries are expected to attract tighter regulations, which could discourage Canadian foreign investment in this industry.

Additional readings

Acharya, Ram C. and Someshwar Rao, "Foreign direct investment trends: a Canadian perspective," Industry Canada, Working Paper (2009), available at: www.ic.gc.ca/eic/site/eas-aes.nsf/eng/ra02066.html.

Competition Policy Review Panel, "Compete to win," Final Report (2008), available at: www.ic.gc.ca/eic/site/cprp-gepmc.nsf/eng/home.

Foreign Affairs and International Trade Canada, "Canada-European Union: trade and investment enhancement agreement," available at: www.international.gc.ca/trade-agreements-accords-commerciaux/agr-acc/eu-ue/index.aspx.

Foreign Affairs and International Trade Canada, "Investment," available at: www.international.gc.ca/trade-agreements-accords-commerciaux/invest/index.aspx?lang=en.

[67] Foreign Affairs and International Trade Canada, "Seizing global advantage," available at: http://www.international.gc.ca/commerce/strategy-strategie/index.aspx.
[68] *Ibid.*

Useful websites

For information on the Investment Canada Act: Industry Canada (www.ic.gc.ca/eic/site/ica-lic.nsf/eng/home).

Statistical annex

Annex table 1. Canada: outward FDI stock, 2000, 2008

(US$ billion)

Economy	2000	2008	2009	Growth 2000-2009 (%)	Share in GDP (%)		
					2000	2008	2009
Canada	238	524	567	138	33	35	42
Memorandum: comparator economies							
US	2,694	3,104	4,303	60	28	22	30
Mexico	8	46	53	562	1	4	6
UK	898	1,531	1,652	84	62	58	76

Source: UNCTAD's FDI/TNC database, available at: http://stats.unctad.org/fdi/. The GDP data for all countries are taken from the World Bank's World Development Index.

Annex table 2. Canada: outward FDI flows, 2000-2008

(US$ billion)

Economy	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
Canada	44.7	36	26.8	22.9	43.3	27.5	44.4	59.6	80.8	38.8
Memorandum: comparator economies										
US	142.6	124.9	134.9	129.4	294.9	15.4	224.2	393.5	330.5	248.1
Mexico	0.4	4.4	0.9	1.3	4.4	6.5	5.8	8.3	1.2	7.6
UK	233.4	58.9	50.3	62.2	91	80.8	86.3	318.4	161.1	18.5

Source: UNCTAD's FDI/TNC database, available at: http://stats.unctad.org/fdi/.

Annex table 2a. Canada: outward FDI flows, by category of transaction, 2000-2008

(US$ billion)

Item	2000	2001	2002	2003	2004	2005	2006	2007	2008
Total outflows	**44.7**	**36.0**	**26.8**	**22.9**	**43.3**	**27.5**	**44.4**	**59.6**	**77.7**
Reinvested earnings	5.2	1.5	4.5	6.0	11.0	13.4	16.6	22.0	16.2
Other outflows	39.5	34.6	22.2	16.9	32.3	14.1	27.8	37.6	61.6

Source: Statistics Canada: CANSIM Table No.: 376-0015.

Annex table 3. Canada: distribution of outward FDI stock, by economic sector and industry, 2000, 2008 (US$ million)[a]

Sector/industry	2000	2008	Growth (%)
Primary	***32,215***	***109,926***	***241***
Agriculture, forestry, fishing and hunting	312	4,972	1491
Oil and gas extraction	12,578	56,553	350
Mining (except oil and gas)	16,647	31,661	90
Construction and utility	2,677	16,739	525
Secondary	***76,100***	***79,814***	***5***
Chemical manufacturing	3,563	14,323	302
Computer & electronic manufacturing	27,663	12,016	-57
Transportation equipment manufacturing	10,301	13,123	27
Other manufacturing—group 1[b]	15,398	19,021	24
Other manufacturing—group 2[c]	19,176	21,332	11
Tertiary	***131,311***	***378,299***	***188***
Transportation and warehousing	12,244	16,068	31
Information and cultural industries	21,281	19,696	-7
Finance and insurance	68,143	240,964	254
Management of companies and enterprises	15,018	64,189	327
Other services industries[d]	14,624	37,383	156
Unspecified	**445**	**29,785**	
TOTAL	**240,071**	**597,825**	**149**

Source: Statistics Canada: CANSIM Table No. 376-0052.

[a] The original data were in Canadian dollar and were converted into US dollar using average annual exchange rates (Canadian dollar per US dollar) of 1.485 for 2000 and 1.066 for 2008.

[b] Other manufacturing—group 1 includes nine NAICS 3-digit industries: (1) food, (2) beverage & tobacco, (3) textile mills, (4) textile products, (5) clothing, (6) leather, (7) wood product, (8) paper, and (9) petroleum and coal product manufacturing.

[c] Other manufacturing—group 2 includes eight NAICS 3-digit industries. They are: (1) plastics and rubber, (2) non-metallic mineral, (3) primary metal, (4) fabricated metal, (5) machinery, (6) electrical equipment, appliance and component, (7) furniture related, and (8) miscellaneous manufacturing.

[d] Other services industries include the following five NAICS industries: (1) wholesale trade, (2) retail trade, (3) real estate and rental and leasing, (4) professional, scientific and technical services, and (5) accommodation and food services.

Annex table 4. Canada: geographical distribution of outward FDI stock, 2000, 2008 (US$ million)

Region/economy	2000	2008	Growth (%)
World	**240,071**	**597,825**	**149**
Developed economies	**189,799**	**464,782**	**145**
Europe	**57,001**	**141,574**	**148**
European Union	**53,486**	**127,928**	**139**
Austria	432	493	14
Belgium	2022	1988	-2
Cyprus	73	85	17
Czech Republic	63	201	221
Denmark	52	536	933
Finland	30	248	717
France	3126	17575	462
Germany	3079	9858	220
Greece	328	S	-100
Hungary	2960	10102	241
Ireland	4886	19189	293
Italy	3307	1126	-66
Luxembourg	1066	3012	183
Netherlands	7,064	7,880	12
Poland	81	277	242
Portugal	315	166	-47
Romania	1	233	n.a.
Spain	451	2,330	417
Sweden	784	1,997	155
United Kingdom	23,684	50,632,	114
North America	**119,827**	**291,471**	**143**
United States	119827	291,471	143
Other developed economies	**153,721**	**421,762**	**1741**
Australia	2,090	6,625	217
Bermuda	6,385	20,886	227
Iceland	n.a.[a]	1,029	n.a.
Israel	307	341	11
Japan	3,780	2880	-24
New Zealand	409	1005	146
Norway	282	850	201
Switzerland	2,119	8560	3042
Developing economies	**47,699**	**112,887**	**137**
Africa	**402**	**1,869**	**365**
Algeria	68	205	201
Burkina Faso	15	n.a.[a]	n.a.
Egypt	26	361	1275
Eritrea	2	n.a.[a]	n.a.
Ghana	93	n.a.[a]	n.a.
Libya	19	n.a.[a]	n.a.
South Africa	10919	1,275a	1069
Tunisia	51	n.a.[a]	n.a.
Zimbabwe	18	28	55

Region/economy	2000	2008	Growth (%)
Asia/Oceania	**9,394**	**20,354**	**117**
China	380	3,358	783
Hong Kong , China	2,518	5,658	125
India	87	751	765
Indonesia	1,624	1,883	16
Korea, Republic of	512	755	48
Malaysia	340	1049	208
Mongolia	n.a.	255	n.a.
Pakistan	n.a.[a]	30	n.a.
Papua New Guinea	182	281	55
Philippines	265	629	137
Singapore	2137	2731	28
Taiwan Province of China	223	n.a.[a]	n.a.[a]
Thailand	663	1220	84
Turkey	463	1596	245
Vietnam	2	158	7701
Latin America and the Caribbean	**37,903**	**90,665**	**139**
Argentina	3,382	3,249	-4
Bahamas	4,718	n.a.[a]	n.a.
Barbados	13,244	42,200	219
Bolivia	35	123	251
Brazil	4,490	8,624	92
British Virgin Islands	188	717	281
Cayman Islands	2,585	17,984	596
Chile	3651	6036	65
Colombia	605	992	64
Costa Rica	78	38	-52
Dominican Republic	133	1498	1029
Ecuador	164	42	-74
Guyana	98	19	-81
Honduras	6	103	1603
Jamaica	399	n.a.[a]	n.a.[a]
Mexico	2,597	3,651	41
Netherland Antilles	81	139	70
Peru	1,296	2,212	71
Trinidad and Tobago	65	2241	3367
Venezuela	221	798	261
Transition economies	**340**	**507**	**49**
Kazakhstan	156	n.a.[a]	n.a.[a]
Russian Federation	185	507	175
Unspecified	**2,234**	**19,648**	**780**

Source: Statistics Canada: CANSIM Table No. 376-0051.
[a] Suppressed due to confidentiality.

Annex table 5a. Canada: trade and employment of Canadian foreign affiliates, 2000, 2007

Sector	Value of sales (US$ billions)			Number of employees (thousands)		
	2000	2007	Growth (%)	2000	2007	Growth (%)
Primary	30.4	111.8	267.6	122	171	4.6
Secondary	122.2	175.1	43.3	444	527	18.7
Tertiary	94.5	143.1	51.4	322	437	35.7
Total	**247.2**	**430.0**	**74.0**	**888**	**1,135**	**27.8**
(Of which: affiliates in the United States)	159.9	223.4	39.7	553	599	8.3

Source: Statistics Canada: CANSIM Table No.: 376-0061.

Annex table 6. Canada: main M&A deals, by outward investing firm, 2007-2009

Year	Acquiror	Target	Target industry	Target destination	Share acquired (%)	Estimated / announced transaction value (US$ billion)
2009	Bank of Montreal	Diners Club North American franchise	Com. services and supplies	US	100	0.93
2009 2009	Ontario Teachers' Pension Plan Canada Pension Plan	Transurban Limited	Transportation	Australia	100	5.75
2009 2009	Brookfield Infrastructure Partners L.P. Brookfield Asset Management Inc.	Babcock & Brown Infrastructure Limited	Diversified financials	Australia	100	1.01
2009	Fairfax Financial Holdings Limited	Odyssey Re Holdings Corp.	Insurance	United States	27	0.99
2009	Eldorado Gold Corp.	Sino Gold Mining Limited	Gold	Australia	80	1.35
2009	Viterra Inc.	ABB Grain Ltd.	Food, bev. and tobacco	Australia	100	1.26
2009	Canada Pension Plan	Macquarie Communications Infrastructure Group	Media	Australia	100	5.83
2009	Agrium Inc.	CF Industries Holdings, Inc.	Chemicals	United States	100	5.60
2009	Precision Drilling Trust	Grey Wolf, Inc.	Energy equipment and services	United States	100	1.81
2008 2008 2008	AMP Capital Investors (Australia) Stichting Pensioenfonds Zorg en Welzijn (Netherlands) Public Sector Pension	Compañia Logistica de Hidrocarburos CLH, S.A.	Oil, gas and consumable fuels	Spain	25	1.26

2008	Investment Board (Canada) Deutsche Bank Aktiengesellschaft (Germany)					
2008	New Gold Inc.	Peak Gold Ltd. Metallica Resources Inc.	Gold	Canada United States	100	1.29
2008	TransCanada Corp.	KeySpan-Ravenswood, LLC	Utilities	United States	100	2.79
2008	Barrick Gold Corp.	Cortez joint venture	Gold	United States	40	1.61
2007	Agrium Inc.	UAP Holding Corp.	Chemicals	United States	100	2.47
2007	EnCana Corporation	Deep Bossier natural gas and land interests	Oil, gas and fuels	United States	100	2.21
2007	Royal Bank of Canada	RBTT Financial Holdings	Banks	Trinidad and Tobago	100	2.04
2007	The T-D Bank	Commerce Bancorp, Inc.	Banks	United States	100	7.89
2007	Provident Energy Trust	Oil and gas assets	Oil, gas and fuels	United States	n.a.	1.41
2007	Royal Bank of Canada	Alabama National Ban Corp.	Financials	United States	100	1.66
2007	Canadian Pacific Railway Limited	Dakota, Minnesota & Eastern Railroad Corp.	Transportation	United States	100	1.44

Source: **Financial Post Crosbie, Mergers & acquisitions database in Canada, 2009, available at: www.fpinfomart.ca.**

Annex table 7. Canada: main greenfield projects, by outward investing firm, 2007-2009
(US$ million)

Year	Investing company	Target economy	Industry	Investment value
2009	Bombardier	United Kingdom	Aerospace	860 .0
2009	Cirrus Energy	Netherlands	Coal, oil and natural gas	505.7[a]
2009	EnCana	United States	Coal, oil and natural gas	1,900.0
2009	Cirrus Energy	Netherlands	Coal, oil and natural gas	505.7[a]
2009	Nexen	United Kingdom	Coal, oil and natural gas	504.5[a]
2009	Enbridge Energy	United States	Coal, oil and natural gas	4,400.0
2009	Fei Cui International	China	Coal, oil and natural gas	732.0
2009	Quadra Mining	Chile	Metals	704.0[a]
2009	Talisman Energy	Vietnam	Coal, oil and natural gas	1,100.0
2009	Methanex	Vietnam	Chemicals	1,000.0
2009	Talisman Energy	Norway	Coal, oil and natural gas	526.2[a]
2009	Canasia Power	India	Coal, oil and natural gas	646.2[a]
2009	TransCanada	United States	Coal, oil and natural gas	2,000.0
2009	Ivanhoe Mines	Indonesia	Coal, oil and natural gas	495.0[a]
2009	Ithaca Energy	United Kingdom	Coal, oil and natural gas	542.8[a]
2008	Vermilion Energy Trust	Australia	Coal, oil and natural gas	480.7[a]
2008	Methanex	Chile	Coal, oil and natural gas	600.0
2008	Cantex Mine Development Corporation	Yemen	Minerals	800.0
2008	Enbridge Energy	United States	Coal, oil and natural gas	487.3[a]
2008	CIC Energy	Botswana	Coal, oil and natural gas	727.7[a]
2008	Canasia Power	India	Coal, oil and natural gas	646.2[a]
2008	Bridge Resources	United Kingdom	Coal, oil and natural gas	542.8[a]
2008	Kinross Gold	Brazil	Metals	550.0
2008	Sterling Resources	United Kingdom	Coal, oil and natural gas	542.8[a]
2008	Homeland Energy Group	South Africa	Coal, oil and natural gas	521.9[a]
2008	TransCanada	United States	Coal, oil and natural gas	30,000.0
2008	TransCanada	United States	Chemicals	7,000.0
2008	Calvalley	Yemen	Coal, oil and natural gas	401.6[a]
2008	Asian Coast Development	Vietnam	Real Estate	4,200.0
2008	Western Goldfields	Nigeria	Coal, oil and natural gas	15,000.0
2007	Brookfield Power Corporation	United States	Alternative/renewable energy	262.7[a]
2007	Fairmont Raffles Hotels International	China	Hotels and tourism	283.9[a]
2007	Lignol Energy Corporation	United States	Alternative/renewable energy	716.6
2007	Magna International	Russia	Automotive	500.0

2007	National Industries Inc. (National Steel Car)	United States	Non-automotive transport	350.0
2007	Stratic Energy	Turkey	Coal, oil and natural gas	293.6[a]
2007	Fairmont Raffles Hotels International	China	Hotels and tourism	283.9[a]
2007	Eastern Platinum (Eastplats)	South Africa	Metals	328.5[a]
2007	Ivanhoe Mines	Mongolia	Metals	203.5[a]
2007	El Niño Ventures	Congo, Democratic Republic of	Metals	242.3[a]
2007	First Calgary Petroleum	Algeria	Coal, oil and natural gas	1,586.6[a]
2007	Goldcorp	Mexico	Metals	1,500.0
2007	Vermilion Energy Trust	France	Coal, oil and natural gas	526.2[a]
2007	Corriente Resources	Ecuador	Metals	300.0
2007	Bombardier	Switzerland	Non-automotive transport	297.3

Source: fDi Intelligence, a service from the Financial Times Ltd.
[a] Estimated.

Chapter 4 – Chile

Inward FDI and its policy context, 2010

José Eduardo Alatorre and Carlos Razo

At the time when many countries were following inward looking economic policies in the 1970s, Chile turned outward and sought foreign direct investment (FDI) as a part of its development strategy. Today, the country has the third largest FDI stock in Latin America, only behind the region's two largest economies. Chile has undertaken various policy efforts to use FDI to promote export diversification, encourage technology transfer and upgrade the country's production capabilities. As a result, Chile has attracted firms operating in more knowledge intensive sectors.

Trends and developments

Chile has been a trailblazer of economic reform in Latin America, and this also applies to policies regarding FDI. The country was one of the first ones in the region actively to seek FDI as a part of its development strategy, at a time when many countries were mostly following inward looking policies.

Today, Chile is the third largest recipient of FDI, in terms of stocks, in Latin America, only behind the two largest Latin American economies, Brazil and Mexico. In 2009, the country was the region's second most important recipient of FDI inflows, just behind Brazil. What is even more remarkable, in terms of FDI as a share of GDP, the country ranked number one.[69] The country's IFDI stock has grown by 150% in less than a decade, outperforming other Latin American countries with larger economies and keeping up with other FDI magnets from either the developing world, such as Thailand, or the developed world, such as the Czech Republic (annex table 1).

Country-level developments

At the end of the 1960s and the beginning of the 1970s, a set of reforms significantly changed the economic landscape of Chile. Nationalizations and the role of the State in the economic activity of the country limited the presence of private firms. This, coupled with a severe political and economic crisis, resulted in a contraction of FDI inflows. At the end of 1973, a *coup d'état* overthrew the democratically elected Government of Salvador Allende; the new regime drastically changed the country's economic policy. As a part of its attempts to move toward a market based economy, the Government enacted a new law to promote and protect FDI (Law

[69] This ranking excludes the Caribbean countries, where many small open economies report high ratios of FDI to GDP. In 2009, Chile's ratio of FDI to GDP was almost 8% compared to a ratio of 1.7% in Brazil (Economic Commission for Latin America and the Caribbean (ECLAC), *Foreign Direct Investment in Latin America and the Caribbean 2009* (Santiago: ECLAC, 2010).

Decree 600).[70] This law, together with instruments for debt conversion, led to a gradual increase in IFDI flows through the second half of the 1970s and the 1980s.

However, it was not until the 1990s and the return of a democratic regime, sound macroeconomic performance, and the globalization wave that started sweeping the world that FDI flows to Chile began their steep upward trend. From 1990 to 1999, IFDI flows grew from nearly US$ 700 million to almost US$ 9 billion, a 1,200% increase.[71] This trend was interrupted from 2000 to 2002, as a result of the combination of several factors, in particular the bursting of the dot-com bubble, relatively low commodity prices and the Argentinean crisis, and the contagious affects that undermined foreign investors' confidence. After the contraction, IFDI growth soon returned to its upward track, reaching its highest point in 2008 (annex table 2). In 2009, IFDI flows recorded their second highest level, a remarkable result considering the global economic crisis and the effects that it had on the flows to other countries of similar economic size that are also globally integrated, such as the Czech Republic and Thailand.

An analysis of the evolution of the sectoral composition of IFDI is limited by the data. Official statistics report the distribution by economic sector and industry only for IFDI entering the country under the Law Decree 600. Between 1974 and 2000, 96% of FDI entered through this scheme, but this figure fell to 66% by 2009, leaving 34% of the IFDI stock unspecified (annex table 3). The services sector stands out as the main recipient of FDI, with financial services and retail industries as the most important ones. However, the main recipient industry by far is mining, as the country's vast copper reserves make it a very attractive target for foreign investors.

FDI statistics on countries of origin suffer from the same limitation as mentioned above, but it is still possible to deduce the main investor countries. The United States has been the main foreign investor in Chile, at least since 1974, with investments in a large variety of industries; Spain follows with important investments in the services sector such as telecommunications, banking and electricity; and Canada, which ranks third, has important investments in the mining sector. FDI from developing regions, such as Africa, Asia or Oceania, is still limited. Investments from Latin American countries have increased, but their amounts are still much smaller than those from the main investor countries (annex table 4).

The corporate players

The biggest investors in Chile are active mainly in the primary and services sectors (annex table 5). The country's natural resource endowments, especially copper, have made Chile an attractive destination for mining firms such as BHP Billiton, Rio Tinto, Xstrata, Anglo-American, and Antofagasta PLC. On the other hand, the country's good economic conditions prevailing during the past two decades have also encouraged very well known market-seeking investors. Financial services have been one of the main industries, with such globally known firms as Santander, BBVA, Scotia Bank, and ING Groep investing heavily in the local market. The utilities sector has also been the target of MNEs, with Spanish firms playing an important role; in particular

[70] Law Decree 600 was introduced in 1974 with the objective of providing a clear legal framework that ensured transparency and equal treatment to foreign investors.
[71] For an interesting and complete review of government policies and inward FDI in Chile during the second half of the 20th century, see chapter 2 in ECLAC (2010), op. cit.

Telefónica (telecommunications) and Endesa[72] (electricity generation and distribution) quickly became market leaders in the country. Other firms recently entering the Chilean market have been OTPPB (Canada) in the water utilities sector and AES (USA) in the electricity sector.

The importance of the services and primary sectors is also reinforced by analyzing the top M&As of the past three years (annex table 6). The largest M&A deal was by Wal-Mart (USA), which has succeeded in penetrating a market in which many MNEs previously failed. The second largest is Marubeni's (Japan) acquisition of 30% shares in two of Antofagasta PLC's (UK) mining projects, La Esperanza and El Tesoro. With this transaction, the Japanese firm made a significant step toward securing copper resources for producing a wide range of products.

The relevance of the mining industry for IFDI is also evidenced from the list of top greenfield investments (annex table 7). In addition, the list shows the growing importance of a relatively new industry: renewable energy. Wind conditions in some regions of the country, together with the proper policy framework and the global need for greener sources of energy, have unleashed the interest of foreign direct investors in wind farms.[73] Endesa (at the time Spanish), has been one of the pioneers, but other investors such as Enel (Italy), Mainstream Power (Ireland), Sowitec (Germany), and Statkraft (Norway) have followed. IFDI in this sector is likely to rise in the coming years.

It is important to note that the list of top greenfield investments does not adequately capture the growing importance of an industry with higher knowledge intensity than traditional sectors: the global services industry, i.e., business process outsourcing (BPO), IT outsourcing (ITO), knowledge process outsourcing (KPO), and innovation process outsourcing (IPO). At first, Chile started attracting firms in the BPO sector, such as Capgemini and Citigroup. However, more recently, the country has managed to attract more firms with higher levels of process sophistication and knowledge intensity. Now, Chile is the home of firms such as Accenture, Orion, GE, and JP Morgan in ITO; Bayer, ABB and Evalueserve in KPO; and, more recently, the country received investments of Pioneer and Monsanto ITO.

Effects of the current global crisis

In 2009, the global economic and financial crisis had a moderate impact on FDI flows to Chile, which fell by 16% compared to the record level of 2008. Despite this decrease, IFDI reached its second highest level in history which is remarkable, especially considering the prevailing global economic conditions and the severe contraction of FDI flows in other developing countries.

This result can be attributed to two factors. For one, Chile's relatively good economic performance in previous years put the country in a good position to face the crisis and helped the recovery process - which in turn provided incentives to market-seeking investors. The second one is the fact that mining exploration or exploitation projects may not necessarily be correlated with the business cycle. Such projects require many years before they are ready to go on stream; thus, firms that still have the ability to invest do so even in recession periods, to be prepared for

[72] ENEL (Italy) acquired ENDESA at the beginning of 2009.
[73] For more details on the important role played by Chile's policy in unleashing such investments see UNCTAD, *World Investment Report 2010: Investing in a Low-Carbon Economy* (New York and Geneva: United Nations, 2010).

the boom years.[74] These two factors may have not only helped to cushion the effects of the economic crisis, but to keep FDI levels high.

The policy scene

For more than three decades, Chile has had a policy to promote and foster FDI. The combination of such a policy, economic and political stability and the country's natural resource endowments rendered positive results, as evidenced in the FDI statistics.[75] Chile's efforts to integrate into the global economy continue, and it has signed a number of FTAs and investment protection agreements with its main trading partners and other countries whose economies offer growth prospects.[76] In 2009, Chile's FTAs with Australia, Colombia and Peru came into force; Chile signed a FTAs with Turkey and initiated conversations with Malaysia and Vietnam. These agreements and the country's accession adherence to the OECD in January 2010 have been important for the development of exports, and may also have a positive impact on FDI flows.

In 2000, CORFO, Chile's economic development agency, launched *InvestChile*, a program to attract investment with a high technological content. The program started providing subsidies to foreign firms that produce goods or services in ICT or that make intense use of these technologies in order to build a critical mass of human capital in such sectors. Despite some resource limitations, the program has been successful, as evidenced by the number of firms attracted in the target sectors.[77] Since 2007, *InvestChile* has undertaken some changes aimed at broadening the type of investment it seeks to promote and to be more in line with the objectives of the country's National Council of Innovation for Competitiveness (NCIC). Today, besides promoting FDI in ICT, *InvestChile* actively seeks to attract investment in other industries, such as biotechnology, agribusiness, alternative energy, and the production of high-tech equipment for the mining and salmon clusters.[78] Since the launch of *InvestChile*, an important number of firms in the target sectors (e.g. IT, renewable energy, agricultural R&D) have arrived, and the country has managed to position itself as an attractive destination in the growing industry of global services.[79]

Conclusions and Outlook

Chile has become one of the main recipients of foreign direct investments of Latin America, keeping up with other FDI magnets from emerging markets of similar size in other regions of the world, such as the Czech Republic and Thailand. Chile's IFDI has had an outstanding performance in the past decade. In 2009, despite the global crisis, the country recorded its second

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[74] In fact, in Chile reinvested earnings in 2009 where much higher than in 2008.
[75] For a quantitative evaluation of FDI determinants in Chile, see for instance Miguel Ramirez, "Foreign direct investment and its determinants in the Chilean case: unit roots, structural breaks, and cointegration analysis," (Dublin: Trinity College, Department of Economics, September 2010) and Miguel Ramirez, "Economic and institutional determinants of foreign direct investment in Chile: a time-series analysis, 1960-2001," *Contemporary Economic Policy*, vol. 24, no. 3, 2006.
[76] The list of Chile's FTAs is available at: http://rc.direcon.cl/pagina/1897.
[77] For an economic evaluation of *InvestChile* and the list of firms it attracted see Manuel Agosin and Juan José Price, in Oscar Muñoz, ed., *Productive Development in Chile: CORFO Experience Between 1990 and 2009* (Santiago: CORFO, FLACSO, CATALONIA, 2009).
[78] For more details about *InvestChile*, see www.investchile.com/
[79] According to rankings from AT Kearney, Global Services, KMPG, Gartner, and the Black book of outsourcing, Chile is among the top destinations for offshoring services.

highest inflow of FDI in its history, becoming the year's second most important FDI recipient in the region, just behind Brazil. What is even more remarkable, in terms of FDI as a share of GDP, the country ranked number one in the region.

Chile was one of the first countries in Latin-American to include FDI in its development strategy. Against the trends of the 1970s, the country enacted laws to promote the arrival of FDI, which started flowing gradually. However, it was not until the 1990s and the return of a democratic regime that economic and political stability and the globalization winds from the north caused a boom in IFDI. In the past decade, besides the high inflows received, Chile's FDI policy has made various efforts to use foreign direct investment not just as a mere capital flow, but as a means to promote export diversification, technology transfer and the upgrading of production capacities. As growth prospects for 2010 improve, domestically and internationally, it is very likely that IFDI in Chile will resume its upward trend.

Additional readings

Economic Commission for Latin America and the Caribbean (ECLAC), "Chile: foreign direct investment and corporate strategies," chapter II, in ECLAC, *Foreign Direct Investment in Latin America and the Caribbean 2000* (Santiago: ECLAC, 2001).

Economic Commission for Latin America and the Caribbean (ECLAC), *Foreign Direct Investment in Latin America and the Caribbean 2009* (Santiago: ECLAC, 2010).

Muñoz, Oscar, *Productive Development in Chile: CORFO Experience between 1990 and 2009* (Santiago: CORFO, FLACSO, CATALONIA, 2009).

Useful websites:
FDI data:
Chile's Central Bank: http://si2.bcentral.cl/Basededatoseconomicos/951_portada.asp?idioma=E
http://www.cinver.cl/english/estadisticas/estadisticas.asp
Markets and trade agreements
http://www.investchile.com/the_chilean_advantage/markets_and_trade_agreements
http://www.cinver.cl/english/regulaciones/acuerdos.asp

Statistical annex

Annex table 1. Chile: inward FDI stock, 2000, 2008, 2009 (US$ billion)

Economy	**2000**	**2008**	**2009**
Chile	46	101	122
Memorandum: comparator economies			
Argentina	68	76	81
Colombia	11	67	74
Ecuador	6	11	12
Peru	11	30	37
Czech Republic	22	114	116
Philippines	18	21	24
Thailand	30	105	99

Source: UNCTAD's FDI/TNC database, available at: http://stats.unctad.org/fdi/.

Annex table 2. Chile: inward FDI flows, 2000-2009 (US$ million)

Economy	**2000**	**2001**	**2002**	**2003**	**2004**	**2005**	**2006**	**2007**	**2008**	**2009**
Chile	4,860	4,200	2,550	4,307	7,173	6,984	7,298	12,534	15,181	12,702
Memorandum: comparator economies										
Argentina	10,418	2,166	2,149	1,652	4,125	5,265	5,537	6,473	9,726	4,895
Colombia	2,436	2,542	2,134	1,720	3,016	10,252	6,656	9,049	10,583	7,201
Ecuador	720	1,330	783	872	837	493	271	194	1,001	312
Peru	810	1,144	2,156	1,335	1,599	2,579	3,467	5,491	6,924	4,760
Czech Republic	4,984	5,639	8,493	2,022	4,979	11,603	5,459	10,437	10,731	2,725
Philippines	2,240	195	1,542	491	688	1,854	2,921	2,916	1,520	1,948
Thailand	3,349	5,061	3,335	5,235	5,862	8,048	9,460	11,330	8,570	5,949

Source: The authors on the basis of official figures of the Central Banks of each country, UNCTAD, *op. cit*. and ECLAC, *Foreign Direct Investment in Latin America and the Caribbean 2009* (Santiago: ECLAC, 2010).

Annex table 3. Chile: distribution of inward FDI stock, by economic sector and industry, 2000, 2009[a] (US$ million)

Sector / industry	2000	2009
All sectors / industries	45,753	113,691
Primary	16,041	25,622
Agriculture, forestry, and fishing	770	1,073
Mining, quarrying and petroleum	15,272	24,549
Secondary	5,901	8,560
Services	22,098	40,800
Retailing	1,054	4,267
Financial services	5,873	7,255
Others	15,171	29,278
Unspecified other sectors/industries	1,712	38,709

Source: The authors on the basis of official figures of the Chilean Central Bank.

[a] The stock figures presented are the sum of net inward FDI flows since 1974.

Annex table 4. Chile: geographical distribution of inward FDI stock, 2000, 2009 [a]

(US$ million)

Region/economy	**2000**	**2009**
World	45,753	113,691
Developed economies	41,067	69,537
Europe	18,260	30,530
Spain	8,962	14,555
Netherlands	1,322	1,831
France	1,232	1,590
Others	6,744	12,554
North America	19,776	32,807
Canada	6,881	13,015
United States	12,894	19,793
Other developed economies	3,032	6,200
Australia	1,392	3,526
Japan	1,487	2,515
Others	153	159
Developing economies	2,769	5,088
Africa	360	431
Asia and Oceania	137	180
China	83	85
Others	54	95
Latin America and Caribbean	2,264	4,463
Mexico	131	1,341
Panama	198	322
Brazil	249	456
Argentina	523	534
Others	1,163	1,810
International organizations	204	358
Unspecified destination	1,712	38,709

Source: The authors on the basis of official figures of the Chilean Central Bank.

[a] The stock figures presented are the sum of net inward FDI flows since 1974.

Table 5. Chile: principal foreign affiliates in Chile, ranked by sales, 2009 (US$ thousand)

	Name	Home economy	Industry	Sales
1	Enersis	Spain	Electricity	6,076,108
2	Minera Escondida (BHP Billiton, Rio Tinto)	Australia/ United Kingdom	Mining	3,585,729
3	D&S (Wal-Mart)	USA	Retail	2,299,639
4	Telefónica Móvil	Spain	Telecommunications	1,474,672
5	Banco Santander	Spain	Financial services	977,170
6	AES Gener	USA	Electricity	838,499
7	Farmacias Ahumada	Mexico	Drugstores	831,955
8	BBVA	Spain	Financial services	446,691
9	Coca Cola Embonor	USA	Beverages	270,980
10	Metlife (Life Insurance)	USA	Financial services	237,961
11	Embotelladora Coca Cola	USA	Beverages	216,599
12	Scotiabank	Canada	Financial services	211,162
13	Chilena ConsolidadaSeguros de Vida (Zurich)	Switzerland	Financial services	187,429
14	Transelec (Hydro-Quebec)	Canada	Electricity	184,710
15	Compañía Chilenade Tabacos (British AmericanTobacco Chile)	United Kingdom	Tobacco	163,645
16	Votorantim Andina	Brazil	Financial services	160,574
17	ING Seguros de Vida	Netherlands	Financial services	159,406
18	Santander Seguros de Vida	Spain	Financial services	135,320
19	AFP Capital	Netherlands	Financial services	134,797
20	Banco Itaú	Brazil	Financial services	123,294
21	Esval	Canada	Water	109,307
22	Telmex	Mexico	Telecommunications	96,642

Source: The authors on the basis of *Capital Magazine*, no. 275, pp. 58 – 61.

Annex table 6. Chile: main M&A deals, by inward investing firm, 2007-2009

Year	Acquiring company	Target company	Target industry	Source economy	Estimated/ announced transaction value (US$ million)
2009	Wal-Mart Stores Inc	Distribucion y Servicio SA	Grocery stores	United States	1,551
2009	Wal-Mart Stores Inc	D&S	Grocery stores	United States	433
2009	Inversiones Breca SA	Lafarge Chile SA	Ready-mixed concrete	Peru	404
2009	Petrobras	Esso Chile Petrolera Ltda	Petroleum refining	Brazil	400
2009	Mitsubishi Corp	CAP SA	Cold-rolled steel sheet, strip and bars	Japan	171
2008	Marubeni Corp	Antofagasta PLC-Esperanza & El	Copper ores	Japan	1,310
2008	MorganStanley Infrastructure and the Ontario Teachers' Pension Plan	Saesa	Electric services	Canada	1,287
2008	Telefonica SA	Compania de Telecomunicacione s	Telephone communications, except radiotelephone	Spain	869
2008	Nexans SA	Madeco SA-Cable Business	Drawing and insulating of nonferrous wire	France	794
2008	Global Via Infraestructuras SA	Autopista del Aconcagua SA	Inspection and fixed facilities for motor vehicles	Spain	710
2008	ING Groep NV	AFP Bansander	Pension, health, and welfare funds	Netherlands	654
2008	Kinross Gold Corp	Minera Santa Rosa SCM	Gold ores	Canada	242
2008	Fonterra Coop Grp Ltd	Soprole SA	Dry, condensed and evaporated dairy products	New Zealand	202
2008	Brookfield Infrastructure	Nueva Transelec SA	Electric services	Bermuda	111
2007	Bank of Nova Scotia,Toronto	Banco Del Desarrollo	Banks	Canada	829
2007	AEI	Chilquinta Energia SA	Electric services	United States	685
2007	Ontario Teachers' Pension Plan	Esval	Water supply	Canada	579
2007	Grupo Financiero	Securitizadora La Construccion	Personal credit institutions	El Salvador	550
2007	Ontario Teachers'	Essbio	Water supply	Canada	342

	Pension Plan				
2007	Organizacion Terpel SA	Repsol YPF SA-Petrol Service	Petroleum bulk stations and terminals	Colombia	210
2007	Inversiones y Desarrollo	Indura SA	Industrial gases	Peru	195
2007	Citigroup Venture Capital Intl	Moller y Perez Cotapos Ltda	Residential construction	Cayman Islands	100

Source: Thomson ONE Banker, Thomson Reuters.

Table 7. Chile: main greenfield projects, by inward investing firm, 2007-2009

Year	Investing company	Target industry	Source economy	Estimated/ announced transaction value (US$ million)
2009	Antofagasta	Metals	UK	2,300
2009	Enhol	Alternative/renewable energy	Spain	1,000
2009	Mainstream Renewable Power	Alternative/renewable energy	Ireland	1,000
2009	Quadra Mining	Metals	Canada	704
2009	Enel	Alternative/renewable energy	Italy	322
2009	Sowitec	Alternative/renewable energy	Germany	322
2009	Abertis	Transportation	Spain	300
2009	GeoPark Holdings Limited	Coal, oil and natural gas	Bermuda	299
2009	Xstrata PLC	Metals	Switzerland	293
2009	Sowitec	Alternative/renewable energy	Germany	289
2009	Sowitec	Alternative/renewable energy	Germany	289
2009	Agbar	Industrial Machinery, Equipment & Tools	Spain	285
2009	Element Power	Alternative/renewable energy	USA	235
2009	Acciona	Alternative/renewable energy	Spain	230
2009	Enel	Coal, oil and natural gas	Italy	229
2008	Endesa	Alternative/renewable energy	Spain	3,000
2008	Nippon Mining Holdings	Metals	Japan	1,700
2008	Endesa	Alternative/renewable energy	Spain	710
2008	Methanex	Coal, oil and natural gas	Canada	600
2008	Endesa	Coal, oil and natural gas	Spain	525
2008	Goodyear	Rubber	USA	400
2008	Apache	Coal, oil and natural gas	USA	277
2008	Endesa	Alternative/renewable energy	Spain	225
2008	Endesa	Alternative/renewable energy	Spain	192
2008	Experian	Financial services	Ireland	181
2008	Ritrama	Paper, printing and packaging	Italy	161
2008	Statkraft	Alternative/renewable energy	Norway	140
2008	Investika	Metals	Australia	130
2008	Jindal Organization	Warehousing and storage	India	107
2008	Kimco Realty	Real estate	USA	60
2007	Anglo American	Metals	UK	1,700
2007	Agbar	Industrial machinery, Equipment and tools	Spain	342

2007	Abertis	Transportation	Spain	254
2007	McCain Foods	Food and tobacco	Canada	200
2007	Relacom	Communications	Sweden	85
2007	Xstrata PLC	Metals	Switzerland	70
2007	Alfa Romeo	Automotive OEM	Italy	44
2007	Munchis	Food and tobacco	Argentina	41
2007	Den Norske Bank (DnB NOR)	Financial services	Norway	31
2007	Goodyear	Rubber	USA	30
2007	Oracle	Software and IT services	USA	23
2007	Lanix	Business machines and equipment	Mexico	16
2007	Teléfonos de México (Telmex)	Communications	Mexico	15
2007	Worley Parsons	Business services	Australia	9
2007	Baby's Dream	Consumer products	USA	6

Source: fDi Intelligence, a service from the Financial Times Ltd.

Outward FDI and its policy context, 2010

Carlos Razo and Álvaro Calderón

Despite the recent financial and economic crisis, Chile's OFDI in 2009 surpassed the record level of 2008, reflecting the strength of Chilean firms and the country's continuous commitment to integrate into the world economy. Two decades ago, Chile was an unlikely foreign direct investor. Today, even with no explicit policies to promote outward investment or the creation of national champions, Chile stands out as the third biggest investor of Latin America in absolute terms and as the first one in proportion to its GDP, even outperforming other emerging economies of similar size in other regions of the world.

Trends and developments

In the middle of the 1980s, Chile underwent important market reforms that reshaped its private sector. At the time, the country ranked seventh as a foreign direct investor of Latin America and the Caribbean, based on its stock of assets held abroad. However, privatization, deregulation and trade and financial liberalization increased competition in local markets and pushed local firms to raise efficiency. The increased competitiveness of some domestic firms at the beginning of the 1990s led to the emergence of Chilean firms as global players.[80]

Today, Chile is the third largest foreign direct investor of the region, only behind Brazil and Mexico. What is even more remarkable, in terms of its GDP, the country ranked number one in the past two years.[81] Despite the worldwide financial and economic crisis, Chilean firms continued their expansion and, in 2009, Chile's OFDI amounted to US$ 8 billion, a 16% increase compared to 2008. Chile's OFDI stock has almost tripled in less than a decade, underlining the remarkable upward trend in the internationalization of Chilean MNEs (annex table 1).

Country-level developments

The emergence of Chilean firms in the 1990s resulted in a gradual increase of OFDI flows until 2000, followed by a sharp contraction in 2001- 2002 (annex table 2). The fall resulted from two factors: one was the economic crisis in Argentina, the main recipient of Chilean OFDI, accounting for 20% of it between 1998 and 2000; the other one was the acquisition of Enersis and AES Gener, the main Chilean electricity firms that had managed to grow abroad, but were acquired by bigger global players such as the Spanish Endesa.[82]

After the contraction in the years 2001 and 2002, Chilean OFDI has steadily grown, reaching almost US$ 8 billion in 2009, a historical record. Chile does not only stand out as the first foreign direct investor in proportion to its GDP in Latin-American, but it has also performed

[80] ECLAC, *Foreign Direct Investment in Latin America and the Caribbean 2005* (Santiago: ECLAC, 2006).

[81] ECLAC, *Foreign Direct Investment in Latin America and the Caribbean 2008* (Santiago: ECLAC, 2009).

[82] Calderón, Álvaro, "Outward foreign direct investment by enterprises from Chile," in UNCTAD, *Global Players from Emerging Markets: Strengthening Enterprise Competitiveness through Outward Investment* (New York and Geneva: United Nations, 2007), Chapter IV.

remarkably well in comparison with countries of similar economic size from other regions, which are also globally integrated, such as the Philippines, Thailand and the Czech Republic (annex table 2).

The growth of Chilean OFDI flows was accompanied by a fast process of regional diversification, mainly in North and Latin America. Certainly, Latin America remains the main recipient of Chilean OFDI in the past decade (40%). However, if at the end of the 1990s the main target of Chilean firms was Argentina, the accumulated flows from 2000-2008 show that Brazil, Peru and Uruguay have become the main target countries in recent years. In addition, Mexico and Colombia became more important for Chilean companies. Likewise, OFDI flows toward North America have risen significantly, from almost nothing to 11% of total flows in this decade, with the United States as the main target country. OFDI to Europe did not follow a continuous pattern; on average, they represented 11% of total flows in the period analyzed (annex table 4).[83]

The sectoral composition of Chilean OFDI during the period 2000-2008 is dominated by three sectors that together accounted for more than 50% of all direct investment abroad during this period: financial services, insurance and real estate and services (32%), mining (11%), and retail (10%). It is worth mentioning that almost 20% of Chilean OFDI in the past decade was directed to the Cayman Islands and Panama, i.e., to financial centers, thus overestimating the share of OFDI flows in financial services (annex table 3); it can be assumed that most of these funds are channeled via these offshore centers to other locations. A caveat of these statistics is that an important share of Chile's OFDI corresponds to net reinvestments where neither a sectoral nor a geographical destination is specified.

The corporate players

The biggest Chilean outward investors during the past decade (annex table 5), have been mainly concentrated in the primary and service sectors, with a small group of firms in the manufacturing sector:

1) Firms engaged in primary sector activities, producing natural-resource based manufactures and supplying basic inputs to the industrial sector, such as Empresa Nacional de Petróleo (ENAP), Arauco, Empresas CMPC, Molibdenos y Metales (Molymet), Madeco, and Masisa. These companies invested mainly in Latin America in their search for natural resources and markets and are primarily involved in hydrocarbons, mining and metal processing, as well as pulp and paper.

2) Firms in the service sector, previously owned by the state and local enterprises, that responded to the new competitive environment created by the reforms of the 1990s, such as Lan Chile, Compañía General de Electricidad (CGE), Compañía Sudamericana de Vapores (CSAV), and firms engaged in real estate, consumer products and retail, such as Fallabella, Ripley, Mall Plaza, and Cencosu

[83] Balance of payments data on outward FDI flows recorded by Chile's Central Bank do not show the ultimate host country of FDI outflows. Net reinvestments account for 37% of these flows, but their geographical and sectoral destination is not available in official statistics.

3) Firms engaged in manufacturing sector activities, such as Compañía Cerveceras Unidas (CCU), Embotelladora Andina, and Empresas Carozzi.

Three industries stand out from among the top merger and acquisitions (M&As) and greenfield investment projects of the past three years (annex tables 6 and 7). The first one is the pulp and cellulose industry in which Arauco and Empresas CMPC invested heavily in Brazil and Uruguay. On the real estate, consumer products and retail side, the Chilean champions Cencosud, Ripley, Fallabela and, until this year, D&S (now owned by Wall Mart), expanded their presence in Latin America. D&S's expansion strategy may well become more aggressive as Wall-Mart seeks to penetrate the South American market from its Chilean base.[84] The other industry worth mentioning is transportation, where Empresas Navieras y Compañía Sudamericana de Vapores (CSAV) invested in Malaysia and Hong Kong (China). Although this may be the firm's initial investment in Asia, it might indicate its interest in the Asian market. Likewise, Molymet recently invested in China, making it the biggest Chilean investment in that country.[85]

After Brazil and Mexico, Chile is the country that headquarters the largest number of the so called "trans-latin" MNEs in Latin America and the Caribbean.[86]

Effects of the current global crisis

In 2009, OFDI from Chile registered its fifth year of consecutive growth and reached a new historical record. In other words, the global financial and economic crisis did not stop Chilean firms' expansion, especially the ones operating in the natural resources sector that managed to accumulate capital during the boom years. In addition, some industries (like retail or pulp and paper) were not hit hard by the crisis as the demand for their products has a low income elasticity of demand, which enabled firms in that industry to continue to expand despite the economic slowdown.

[84] Wal-Mart spokesperson, Kevin Gardner, in "Wal-Mart traerá a Chile su estrategia mundial de precios bajos y planea mantener marcas de D&S," *La Tercera*, December 21, 2008.
[85] "Chilean Molymnet makes the biggest investment in China," *La Tercera*, December 4, 2009.
[86] Boston Consulting Group (BCG), "The 2009 BCG multilatinas: a fresh look at Latin America and how a new breed of competitors are reshaping the business landscape," available at http://www.bcg.com/documents/file27236.pdf.

The policy scene

In the past few years, Chile has pursued an ambitious strategy to foster the internationalization of the country. It has signed a number of FTAs and investment protection agreements with its main trading partners and other countries whose economies offer growth prospects. In 2009, Chile's FTAs with Australia, Colombia and Peru came into force, and Chile signed a FTAs with Turkey and initiated conversations with Malaysia and Vietnam. In January 2010, Chile joined the OECD. Although these initiatives have been important for the development of exports, their impact on Chilean OFDI is yet unclear. In the past, Chilean firms have preferred to operate in close and well-known environments and have used trade to exploit more distant markets.[87] Nevertheless, OFDI to other destinations, such as East-Asia, has increased in the past five years.

Since the restoration of democracy in 1990, Chile has enjoyed the political and economic stability that has created a solid base from which its firms can pursue new business strategies outside the country's borders, even during the recent economic crisis. In January 2010, after twenty years of a centre-left government, the centre right coalition won the presidential election. This political change is not expected to alter Chile's strategy to integrate further into the global economy, and thus on the behavior of Chilean firms toward international expansion.

Conclusions and Outlook

Chile has slowly become one of the main foreign direct investors of Latin America and the Caribbean, even outperforming emerging markets of similar size in other regions of the world, such as the Czech Republic, the Philippines and Thailand. Chile's OFDI has had an outstanding performance, even during the recent economic crisis. In 2009, Chilean OFDI reached a new record level, surpassing 2008 outflows.

Unlike other countries, Chile has not followed an explicit policy to promote OFDI or to create national champions.[88] The Chilean government has provided stable economic conditions in the domestic market, which has served Chilean firms as a platform to expand their business abroad. This shows that the best policy to support OFDI is perhaps a sound policy to promote stability and competition in national markets. Chilean firms have shown that they can compete successfully outside their borders. As growth prospects for 2010 improve,[89] domestically and internationally, it is very likely that Chilean MNEs will continue to expand abroad.

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[87] Calderon *op.cit.*, p. 47.
[88] In the case of ENAP, Chile's state owned oil company, the Government has promoted investment abroad. However, the goal, more than creating a national champion, is to ensure the availability of oil resources, which are very limited in Chile.
[89] Latin America and the Caribbean, the main recipient of Chile's OFDI, is expected to grow by 4.1% in 2010, after a contraction of -1.8% in 2009. Chile's real GDP is expected to grow by 4.5% in 2010 (ECLAC, *"Preliminary overview of the economies of Latin America and the Caribbean 2009,"* (LC/G.2424-P), Santiago, Chile, 2009.

Additional readings

Calderón, Alvaro, "Outward foreign direct investment by enterprises from Chile," in UNCTAD, *Global Players from Emerging Markets: Strengthening Enterprise Competitiveness through Outward Investment* (New York and Geneva: United Nations, 2007), chapter IV.

Dirección General de Relaciones Económicas Internacionales (DIRECON), *Chile: 20 Años de Negociaciones Comerciales* (Santiago: Chile, 2009), available at: http://rc.direcon.cl/pagina/1970.

Economic Commission for Latin America and the Caribbean (ECLAC), *Foreign Direct Investment in Latin America and the Caribbean 2005* (Santiago: ECLAC, 2006).

Economic Commission for Latin America and the Caribbean (ECLAC), *Foreign Direct Investment in Latin America and the Caribbean 2008* (Santiago: ECLAC, 2009).

Boston Consulting Group (BCG), "The 2009 BCG multilatinas: a fresh look at Latin America and how a new breed of competitors are reshaping the business landscape," available at: http://www.bcg.com/documents/file27236.pdf.

Statistical annex

Annex table 1. Chile: outward FDI stock, 2000, 2008 (US$ million)

Economy	**2000**	**2008**
Chile	11,154	31,728
Memorandum: comparator countries		
Argentina	21,141	28,749
Colombia	2,989	13,084
Peru	505	2,270
Venezuela	7,676	16,619
Czech Republic	738	9,913
Philippines	2,044	5,810
Thailand	2,203	10,857

Source: Based on UNCTAD, *World Investment Report 2009: Transnational Corporations, Agricultural Production and Development* (New York and Geneva: United Nations, 2009).

Annex table 2. Chile: net outward FDI flows, 2000-2009 (US$ million)

Economy	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
Chile	3,987	1,610	343	1,606	1,563	2,183	2,742	3,009	6,891	7,976
Memorandum: comparator countries										
Argentina	901	161	-627	774	676	1,311	2,439	1,504	1,391	
Colombia	325	16	857	938	142	4,662	1,098	913	2,254	
Peru	-146	74	18	60	59	174	428	66	729	
Venezuela	521	204	1,026	1,318	619	1,167	1,524	30	1,273	
Czech Republic	43	165	207	206	1014	-19	1467	1619	1900	
Philippines	125	-140	65	303	579	189	103	3,536	237	
Thailand	-22	430	171	621	76	503	972	1,857	2,835	

Source: Based on data from the Central Bank of Chile as of February 8, 2010*;* Instituto Nacional de Estadística y Censos (INDEC, Argentina); Central Bank of Colombia; Central Bank of Venezuela; and UNCTAD, *World Investment Report 2009,* op. cit.

Annex table 3. Chile: sectoral distribution of net outward FDI flows, 2000-2008
(US$ million)

Sector / industry	2000	2001	2002	2003	2004	2005	2006	2007	2008
All sectors / industries	3,986.4	1,609.7	343.1	1,606.3	1,563.1	2,182.6	2,742.4	3,009.0	6,891.3
Primary	175.8	212.2	44.1	128.0	-167.1	55.4	758.1	1,149.1	808.6
Agriculture, farming, fishing and forestry	131.5	235.2	29.0	116.1	8.0	52.3	13.9	10.5	10.7
Mining	44.3	-23.0	15.1	11.9	-175.1	3.1	744.2	1,138.6	797.9
Secondary	445.4	-110.8	-99.2	-6.7	29.8	252.2	-87.0	115.1	379.9
Manufacturing	166.4	-124.0	-79.3	-25.9	68.4	214.3	120.5	75.0	362.3
Construction	15.9	49.4	13.9	-72.4	-5.0	-9.9	1.7	28.4	0.9
Electricity, gas and water	263.1	-36.2	-33.8	91.6	-33.6	47.8	-209.2	11.7	16.7
Services	2,980.7	1,178.3	195.5	1,005.4	874.9	922.1	1,073.1	-649.6	3,476.8
Retail	227.6	110.9	113.3	190.9	394.8	104.7	255.9	277.1	806.8
Financial services, insurance, real estate and services.	2,637.9	932.6	86.7	807.6	439.0	749.2	705.0	-1,160.8	2,372.4
Communal, social and personal services	1.4	22.0	-3.4	1.2	44.4	19.0	26.5	10.8	82.8
Transport, storage and communications	113.8	112.8	-1.1	5.7	-3.3	49.2	85.7	223.3	214.8
Unspecified other sectors/industries	-0.4	-0.6	-28.6	-67.4	1.3	7.2	0.0	0.0	0.1
Net reinvestment	384.9	330.6	231.3	546.9	824.3	945.7	998.2	2,394.4	2,225.9

Source: Based on data from the Central Bank of Chile, "Financial account, balance of payments, outward foreign direct investment by destination sector," available at: http://www.bcentral.cl/estadisticas-economicas/series-indicadores/xls/inversion_en_el_exterior.xls.

Annex table 4. Chile: geographical distribution of net outward FDI flows, 2000–2008 (US$ million)

Country / region	2000	2001	2002	2003	2004	2005	2006	2007	2008
World	3,986.5	1,609.8	343.0	1,606.4	1,563.0	2,182.9	2,742.7	3,009.0	6,891.4
Developed economies	1,116.8	-95.9	255.3	303.3	96.4	744.1	1,148.5	-432.9	1,540.8
Europe	171.8	24.9	510.7	115.9	-4.4	246.9	1,053.7	516.1	56.6
European Union	182.0	8.2	513.9	85.2	-3.3	233.4	1,031.8	499.6	53.8
Austria	0.0	4.1	1.5	5.6	0.0	0.0	0.2	0.1	0.0
Belgium	10.2	0.1	-0.9	-0.5	0.0	0.1	118.0	-47.3	0.0
France	1.6	0.5	-9.8	7.1	1.0	-16.9	-0.7	6.1	-10.3
Germany	4.0	23.1	1.7	0.8	64.6	8.3	-0.8	21.3	8.1
Ireland	8.1	0.0	9.0	0.0	1.0	0.0	1.1	-1.0	-6.6
Luxembourg	6.8	1.9	-0.1	34.9	-17.7	7.7	279.4	0.0	-2.3
Netherlands	58.6	2.4	2.9	4.7	9.4	19.5	172.2	75.1	-245.3
Spain	74.5	-26.4	492.7	9.8	19.5	59.7	-15.5	82.5	38.8
Sweden	0.0	0.0	0.0	5.9	10.1	3.0	2.7	11.0	9.2
United Kingdom	18.2	2.5	16.9	16.9	-91.2	152.0	475.2	351.8	262.2
Other developed Europe	-10.2	16.7	-3.2	30.7	-1.1	13.5	21.9	16.5	2.8
North America	-105.5	-131.5	-255.4	119.8	100.8	502.3	94.4	999.4	1,373.2
Canada	6.4	2.6	1.0	0.5	2.0	0.5	8.8	-25.5	52.4
United States	-111.9	-134.1	-256.4	119.3	98.8	501.8	85.6	1,024.9	1,320.8
Other developed countries	1,050.5	10.7	0.0	67.6	0.0	-5.1	0.4	-1,948.4	111.0
Bermuda	0.5	0.0	0.0	67.6	0.0	-5.4	0.0	399.6	111.0
New Zealand	1,050.0	10.7	0.0	0.0	0.0	0.3	0.4	-2,348.0	0.0
Developing economies	2,481.1	1,367.4	-115.4	815.9	647.0	471.8	590.5	1,040.2	3,119.5
Africa	0.0	0.0	0.0	0.1	0.0	5.8	2.3	0.0	-19.2
Latin America and the Caribbean	2,474.9	1,367.3	-115.5	815.5	638.0	439.9	70.3	885.4	3,107.2
South and Central America	991.8	155.1	236.8	138.2	462.7	389.3	284.8	1,038.7	3,156.2
South America	488.3	26.5	160.3	104.5	437.0	311.5	233.3	1,001.3	1,637.7
Argentina	253.1	-86.4	-425.1	-16.1	322.6	104.6	41.3	147.5	234.6
Bolivia	-16.2	-1.5	-13.8	-8.4	3.7	-8.7	-11.4	-0.7	-9.8
Brazil	138.0	7.7	62.6	18.6	12.7	103.2	39.0	685.0	459.6
Colombia	20.0	23.9	5.2	1.3	0.8	16.3	14.8	30.4	31.2
Ecuador	-0.5	9.6	-12.6	2.5	-0.1	-16.0	22.2	-1.9	8.3
Paraguay	2.2	6.6	-8.2	-0.7	30.2	0.0	0.0	0.2	2.5
Peru	11.3	6.4	-42.9	-24.4	71.2	42.2	107.6	55.5	809.5

Uruguay	47.8	26.4	528.8	75.9	-13.9	68.3	8.9	71.1	83.8
Venezuela	32.6	33.8	66.3	55.8	9.8	1.6	10.9	14.2	18.0
Central America	503.5	128.6	76.5	33.7	25.7	77.8	51.5	37.4	1,518.5
Costa Rica	0.8	0.0	-0.5	0.4	-0.2	12.1	2.3	4.0	0.2
El Salvador	-0.1	0.3	-1.2	0.0	0.0	20.0	-27.1	0.0	0.0
Mexico	65.2	-19.8	84.9	60.4	2.2	52.6	28.5	11.7	146.4
Panama	437.6	148.1	-6.7	-27.1	23.7	-6.9	47.8	21.7	1,371.9
Caribbean	1,483.1	1,212.2	-352.3	677.3	175.3	50.6	-214.5	-153.3	-49.0
Asia and Oceania	6.2	0.1	0.1	0.3	9.0	26.1	517.9	154.8	31.5
Asia	6.2	0.1	0.1	0.3	9.0	26.1	517.9	154.8	31.5
West Asia	0.0	0.0	0.0	0.0	0.0	12.7	502.5	146.5	23.3
South, East and South-East Asia	6.2	0.1	0.1	0.3	9.0	13.4	15.4	8.3	8.2
East Asia	6.2	0.1	0.1	0.3	9.0	3.9	11.2	8.0	8.0
China	6.2	0.1	0.0	0.3	7.2	1.7	2.4	1.9	0.2
Hong Kong, China	0.0	0.0	0.1	0.0	1.8	2.2	8.8	6.1	7.8
South Asia	0.0	0.0	0.0	0.0	0.0	9.5	4.2	0.3	0.2
Rest	4.1	8.3	0.4	7.6	-5.9	14.1	5.5	7.3	5.1
Unspecified destination	-0.4	-0.6	-28.6	-67.4	1.3	7.2	0.0	0.0	0.1
Net reinvestment	384.9	330.6	231.3	546.9	824.3	945.7	998.2	2,394.4	2,225.9

Source: Based on data from The Central Bank of Chile, "Financial account, balance of payments, outward foreign direct investment by destination sector," available at: http://www.bcentral.cl/estadisticas-economicas/series-indicadores/xls/inversion_en_el_exterior.xls.

Annex table 5. Chile: principal MNEs, ranked by total sales, [a] 2008 [b] (US$ billion)

Rank	Name	Industry	Sales
1	Enap	Oil & gas	12.0
2	Cencosud	Retail	9.5
3	Falabella	Retail	5.8
4	CSAV	Industrial, transport and mining	4.8
5	Lan Airlines	Transport	4.5
6	Arauco	Industrial, transport and mining	3.6
7	Antofagasta PLC	Industrial, transport and mining	3.3
8	D&S	Retail	3.3
9	CMPC	Industrial, transport and mining	2.9
10	CGE	Utilities and telecommunication	2.8
11	Molymet	Industrial, transport and mining	2.4
12	SQM	Industrial, transport and mining	1.7
13	Ripley	Retail	1.6
14	Farmacias Ahumada	Retail	1.4
15	Embotelladora Andina	Food and beverages	1.3
16	Empresas Navieras	Transport	1.3
17	CCU	Food and beverages	1.2
18	Madeco	Industrial, transport and mining	1.1
19	Masisa	Industrial, transport and mining	1.0
20	Salfacorp	Industrial, transport and mining	0.9

Source: Based on "Top 100, las mayores compañías por ventas," *Capital*, Chile, May 15, 2009.

[a] World-wide sales.
[b] Data on foreign assets are not available.

Annex table 6. Chile: major cross-border M&As deals, by outward investing firm, 2007-2009. (US$ million)

Year	Acquiring company	Target company	Target industry	Target country (OFDI)	Announced value
Completed					
2009	Arauco and Stoda Enso (Finland)	ENCE	Pulp and paper	Uruguay	340.0
2009	Cencosud	Easy Colombia SA	Grocery stores	Colombia	60.0
2009	Corporacion Farmaceutica	Laboratorios Synthesis Ltda-	Pharmaceutical preparations	Colombia	18.0
2009	Sixtra Chile SA	Nekotec Tecnologia SA de CV	Computer integrated systems design	Mexico	6.0
2009	Antofagasta Minerals SA	Sunridge Gold Corp	Gold ores	Canada	5.1
2009	Gasco SA	Gasoducto del Pacifico Argenti	Natural gas transmission and distribution	Argentina	3.9
2009	ENAP	Gasoducto del Pacifico Cayman	Natural gas transmission and distribution	Cayman Islands	2.7
2009	Sociedad Punta del Cobre SA	Explorator Resources Inc	Copper ores	Canada	1.4
2009	Max Alberto Oemick	Fortune Valley Resources Inc	Gold ores	Canada	0.2
Announced					
2009	CMPC	Aracruz Cellulose SA-Guaiba	Pulp mills	Brazil	1,430
2009	CMPC	Cia Melhoramentos de Sao Paulo	Sanitary paper products	Brazil	202.6
2009	Antofagasta Minerals SA	Almaden Minerals Ltd-Tuligtic	Gold ores	Mexico	7.0
2009	Quintec SA	Qbase SA	Computer facilities management services	Argentina	1.2
Completed					
2008	Masisa SA	Tafibras Participaciones SA	Reconstituted wood products	Brazil	70.0
2008	Investor Group	HARVEST SA	Wines, brandy, and brandy spirits	Argentina	3.3
Announced					
2008	Investor Group	Bavaria SA-Agua Brisa Bottled	Bottled & canned soft drinks & carbonated waters	Colombia	92.0
Completed					
2007	Cencosud	Grupo Wong	Grocery stores	Peru	500.0
2007	Cencosud	G Barbosa	Grocery stores	Brazil	430.0
2007	Cencosud	Mercantil Rodrigues Comercial	Grocery stores	Brazil	21.0

2007	CMPC	Drypers Andina SA	Sanitary paper products	Colombia	5.6
2007	Madeco SA	CEDSA SA	Miscellaneous fabricated wire products	Colombia	3.7
2007	Forus SA	Pasqualini	Women's footwear, except athletic	Uruguay	2.4
2007	Forus SA	Maravilla SA	Women's footwear, except athletic	Colombia	1.9
2007	Laboratorios Andromaco SA	Iprofasa	Drugs, drug proprietaries, and druggists' sundries	Guatemala	1.6

Source: ECLAC, on the basis of data from *Thomson ONE Banker, Thomson Reuters* (http://thomsonreuters.com).

Chapter 5 – Germany

Inward FDI and its policy context, 2010

Thomas Jost

With a stable economic and political system, open capital markets, the largest domestic market in Europe, and European Union (EU) membership, Germany has attracted competitive and export-oriented MNEs since the 1960s. In the 1990s —after German unification and the opening up of Eastern Europe— IFDI grew more slowly than expected despite the increased market potential. In recent years, the German economy strengthened and the wage and cost gap against its main competitors narrowed, contributing to higher IFDI. With the financial and economic crisis, German IFDI declined considerably in 2008 but started to rise again in 2009. At the end of 2008, Germany ranked among the top four developed countries as host for IFDI. Germany's open investment regime was tightened in 2009, in reaction to the emergence of SWFs.

Trends and developments

Country-level developments

The successful reintegration of Germany into the world economy after the Second World War, as well as the European unification process, stimulated IFDI in Germany. Already in the 1960s, many of the largest MNEs worldwide (like General Motors or IBM) had established affiliates in Germany. In 1990, the year of the German reunification, the consolidated primary and secondary IFDI stock amounted to US$ 111 billion.[90] Since then, it has risen six-fold, to reach US$ 666 billion at the end of 2008 (annex table 1). The primary IFDI stock at the end of 2008 amounted to US$ 911 billion, Germany therefore ranked on the 4th place among the G-5 countries listed in annex table 1. Foreign MNEs were attracted by the size of the German market (the largest market in Europe, producing 20% of the EU-27 GDP), the competitiveness of the German corporate sector with its efficient suppliers, high quality infrastructures, a skilled labor force, the country's strong trade ties and low financing costs on German capital markets.[91]

At the end of 2008, the value of the German IFDI stock reached 50% of the value of the country's OFDI stock. From time to time, the gap between IFDI and OFDI has

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[90] The German inward FDI stock figures that are used most for analysis in this article are consolidated primary and secondary direct investment stock figures. This is a very special calculation done by Deutsche Bundesbank, looking through dependent (majority foreign owned) holding companies in Germany and including their direct investment enterprises in Germany. These figures are not comparable with the figures of most other countries, taking only primary FDI into account. The primary FDI stock in Germany is much higher than the consolidated primary and secondary one, because FDI in the dependent holding companies is much higher than the FDI stock in their direct investment enterprises, which replace the dependent holding companies by the consolidation. The reason for this is that the holding companies receive more money from their foreign investors to buy the secondary foreign direct investment enterprises than these secondary FDI enterprises show in their balance sheets. FDI stocks are calculated by own funds at book value of the direct investment enterprises.

[91] Axel Jochem, "International financial competitiveness," Deutsche Bundesbank, *Discussion Paper Series 1: Economic Studies,* No. 29/2008 (Frankfurt: Deutsche Bundesbank, 2008), available at: www.bundesbank.de/download/volkswirtschaft/dkp/2008/200829dkp.pdf

given rise to criticism about the quality of Germany as a business location.[92] In particular, high wages, a relatively inflexible and overregulated labor market and high marginal tax rates were seen as detrimental to investing in Germany.[93] In addition, low foreign investments in the Eastern part of Germany after reunification were criticized. The IFDI stock in East Germany amounted to US$ 22 billion at the end of 2008, only 5% of the total IFDI stock in Germany, whereas the East German GDP accounted for 12% of the total German GDP.[94] IFDI in East Germany has remained low since the mid 1990s.[95] It can be partially explained by the rapid adjustment of East German wages to the West German level after reunification, despite low labor productivity, as well as by the deindustrialization process that induced MNEs to supply the East German economy via their West German affiliates.

At the end of 2008, foreign companies employed 2.6 million workers in their affiliates in Germany. This employment was therefore much lower than employment of German MNEs in their affiliates abroad (5.9 million), reflecting the gap between OFDI and IFDI. However, foreign companies are very important for the German economy. In 2007, majority-owned foreign affiliates in the non-financial sectors produced 28% of the total value-added and employed 13% of the total workforce in these sectors.[96] The value-added of all foreign affiliates in Germany amounted to US$ 1.9 trillion in 2008.

Like in many other developed countries, IFDI flows in Germany evolved more irregularly than IFDI stocks and were influenced by single large transactions or tax changes (annex table 2). During the new technology boom at the turn of the century, the acquisition of Mannesmann by British Vodafone for US$ 202 billion led to a record IFDI flow of roughly US$ 200 billion in 2000.[97] In 2004, foreign MNEs withdrew US$ 10 billion on balance from Germany. This was mainly attributable to large net repayments of cross-border, intra-company loans by foreign affiliates, partly due to a revision of the German Corporation Tax Act, intended to encourage foreign companies to transform corporate loans to their foreign affiliates into equity capital.[98] In the second half of the past decade (2005-2009), IFDI flows increased to a relatively high annual average of US$ 60 billion in 2005-2007, and they only fell by 50% to an

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[92] Thomas Jost, "Direct investment and Germany as a business location," *Discussion Paper 2/1997*, Economic Research Group of the Deutsche Bundesbank (Frankfurt: Deutsche Bundesbank, 1997).
[93] Maik Dietrich and Dirk Kiesewetter, "Schwedische Direktinvestitionen in Deutschland und in Österreich: Eine empirische Untersuchung der gefühlten Steuerbelastung", *Perspektiven der Wirtschaftspolitik*, Vol. 9 (2008), pp. 62-82.
[94] The regional FDI figures should be taken with care as they are classified to that Federal State where the legal place of the enterprise is and possibly not to that Federal State where production and economic activity takes place. In Deutsche Bundesbank's figures for East Germany East Berlin is not included.
[95] The stock statistics of the Deutsche Bundesbank classified by the 16 German Federal States ("Bundesländer") are not published but are available on request.
[96] These figures are the first results of the new FATS-statistics of the German Federal Statistics Office (Statistisches Bundesamt). The FATS-statistics include only majority-owned enterprises whereas FDI figures include all participating interests above a 10%-threshold. Some big enterprises in Germany with a large number of employees are minority-owned by foreign investors. See Jörg Feuerhake, Alexander Schulze and Kirsten Untz, "Inward FATS: Auslandskontrollierte Unternehmen in Deutschland 2007", *Wirtschaft und Statistik*, Statistisches Bundesamt 5/2010, available at: www.destatis.de. The Federal Statistics Office is responsible for the EU-wide "Foreign affiliates atatistics" (FATS) for foreign-controlled companies in Germany, whereas Deutsche Bundesbank is responsible for the statistics on foreign affiliates of German companies abroad.
[97] UNCTAD, *World Investment Report 2001: Promoting Linkages* (New York and Geneva: United Nations, 2001), p. 244. In the year 2000, the other investments and divestments of foreign companies in Germany (the Vodafone-Mannesmann deal excluded) were nearly in equilibrium.
[98] Deutsche Bundesbank, "German balance of payments for the year 2004," *Monthly Report* (March 2004), p. 39.

average of US$ 30 billion in 2008-2009, despite the economic and financial market crisis.

FDI in Germany is concentrated in the services sector, with a stable share of around 65% of the total IFDI stock during the past decade (annex table 3). Privatization and liberalization in the telecommunication sector as well as in the electricity, gas and water supply sectors drove up inward investment in the past decade (2000-2009). Manufacturing accounted for roughly one third of IFDI in Germany, whereby the mere nominal investment figures fail to show the real importance of foreign affiliates for the German economy in manufacturing. In order to compete successfully with domestic German companies, these firms are often highly competitive and world market leaders.[99]

Developed economies contributed more than 96% of the IFDI stock in Germany at the end of 2008 (annex table 4). The EU partner countries alone were responsible for more than three quarters of these investments. Geographic proximity, the single European market, strong trade ties, and a common currency among sixteen EU countries are the main factors explaining the dominance of the EU. The Netherlands and Luxembourg, both important locations for holding companies, were the two countries with the largest IFDI stock in Germany (US$ 152 billion and US$ 97 billion, respectively) in 2008. Other important investors in Germany were the United States (U.S.) (US$ 67 billion) and France (US$ 62 billion). Emerging markets' FDI in Germany plays only a marginal role. It is only in recent years that MNEs from these markets, from Russia and West Asian countries, have been able to increase their FDI in the country. Investments from SOEs and SWFs triggered policy reactions especially from the German Government (see below).

The corporate players

Early after World War II, many big MNEs (foremost from the U.S.) had begun to build production facilities and distribution and service centers in Germany. Foreign MNEs therefore contributed to the rebuilding and reintegration of Germany into the world economy by transferring capital and technology. In 2008, there were 12,659 foreign direct investment enterprises in Germany with participating interests of foreign investors of 10% or more.[100] Foreign-controlled companies in Germany that belong to the top 125 companies of the non-financial sector in Germany are listed in annex table 5. In the financial sector, more than 200 foreign banks and other financial institutions operate in Germany.[101]

In recent years, foreign MNEs have continued to enhance their presence in Germany by undertaking cross-border M&As (annex table 6). In 2007 and 2008, a large number of mega-deals, valued US$1 billion and more, were concluded in many industries and were the main driver of IFDI. In 2009, due to the economic and financial crisis, the

[99] According to a study of Eurostat, six German regions are amongst the top 20 high-tech regions in the EU. Eurostat, "Regional employment in high-tech sectors," *Statistics in Focus*, 102/2007.
[100] Deutsche Bundesbank, "Bestandserhebung über Direktinvestitionen," *Statistische Sonderveröffentlichung 10* (April 20100, available at: www.bundesbank.de.
[101] In Spring 2010, the Association of Foreign Banks in Germany had more than 210 member institutions. Verband der Auslandsbanken e.V., "Pressemitteilung 1/2010," March 23, 2010, available at: http://213.83.8.9/owcms/frontend/downloads/ Presse/2010/Pressemeldung%201-2010_end.pdf

number of mega-deals sharply declined, like in most other developed countries. Indeed, there were only two. The most eye-catching transaction was the investment of Qatar Investment Authority in Volkswagen AG for US$ 9.6 billion, raising its capital stake to 17%.[102] The largest greenfield investments that were announced in the past three years are listed in annex table 7. Most investors are well-known MNEs from developed countries. In recent years MNEs from Russia and the United Arab Emirates have been emerging as important investors in Germany. Profiting from high incomes from the export of oil and other natural resources Russian and Arabian SOEs and SWFs increased their investments in Germany. Several large greenfield investments of Russia's energy giant Gazprom motivated by a strategy to expand its downstream activities to supply gas to final consumers drove Russia's FDI stock in Germany from US$ 1 billion in 2005 to US$ 6.3 billion at the end of 2008.

Effects of the current global crisis

In reaction to the global economic and financial crisis, IFDI flows to Germany sharply declined in 2008, by 68%, from US$ 77 billion to US$ 25 billion. Net equity capital investments halved to US$ 23 billion, reinvested earnings turned negative and net lending of foreign MNEs to their affiliates in Germany heavily declined to a mere US$ 1.5 billion, which could point to increased financial needs of parent companies abroad. In contrast to most other developed economies (and comparable economies listed in annex table 2), IFDI in Germany already started to rise again in 2009, despite the sharp recession of the German economy (with a 5% decline of real GDP).[103] Germany profited from a general improvement of the business climate, starting in the second quarter of 2009.

Despite the strong decline in output in 2009, Germany has weathered the financial and economic crisis better than many other countries and is regarded as a new "engine" in Europe.[104] Some survey results point in the same direction. UNCTAD's World Investment Prospects Survey 2009-11 ranks Germany among the most attractive business locations among developed countries.[105] The Global Competitiveness Report (GCR) of the World Economic Forum ranks Germany on 7th place worldwide as a preferred investment destination.[106] Recent studies of the American Chamber of Commerce and the Boston Consulting Group, as well as of Ernst&Young, underline the increased attractiveness of Germany as a business location.[107]

The policy scene

Already in the 1950s, Germany had a very open investment regime and no barriers against IFDI. Like in several other developed countries, the rise of SWFs in recent years initiated a public debate in Germany that led to a tightening of the German

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[102] Volkswagen AG, "Geschäftsbericht 2009", available at: http://geschaeftsbericht2009.volkswagenag.com/anhang/sonstigeerlaeuterungen/mitteilungennachwertpapierhandelsgesetz.html
[103] Deutsche Bundesbank, "German balance of payments in 2009," *Monthly Report*, March 2010, pp. 17-31.
[104] The Economist, "Germany – Europe's engine," March 11, 2010.
[105] UNCTAD, "World Investment Prospects Survey 2009-2011" (New York and Geneva: United Nations, 2009), p. 55 f.
[106] World Economic Forum, *Global Competitiveness Report* 2009-2010 (Geneva: WEF, 2009).
[107] American Chamber of Commerce and Boston Consulting Group, op. cit., and Ernst&Young, "Waking up to the new economy: Ernst&Youngs 2010 European attractiveness survey", available at: www.ey.com/GL/en/Issues/Business-environment/2010-European-attractiveness-survey.

investment law.[108] In April 2009, Germany's Government amended the German Foreign Trade and Payments Act and its implementing regulations. According to the new law, the Federal Ministry of Economics and Technology can review a planned acquisition of an existing German company by non-EU or non-European Free Trade Area purchasers and suspend or prohibit a transaction if it threatens national security or public order.

Only in very limited cases of a potential threat of national security or public order the Federal Ministry can initiate a review process. The procedure must also be in accordance with the requirements of the European Union treaties. In an explanatory memorandum on the new law,[109] the Government refers to the European Community Treaty (EC Treaty, articles 46 and 58(1), now articles 52 and 65 of the "Treaty on the Functioning of the European Union" that is part of the Lisbon Treaty) and to the case law of the European Court of Justice.[110] A screening of foreign investments in Germany is applicable to investors from outside the EU and the European Free Trade Association who seek to acquire 25% or more voting rights of a German company.[111] It is not limited to specific sectors or size of the target company. The new law does not explicitly distinguish between private and public foreign investors, but it was clearly motivated by the emergence of SWFs as important international investors.

According to the Federal Ministry of Economics and Technology, as of May 2010, 34 foreign companies had applied for a certificate of non-objection since the new law entered into force in April 2009. All companies received the certificate within on average two weeks. From April 2009 to May 2010, there was not a single review process initiated by the Government. Despite the rather positive experiences with the new law so far, this more restrictive investment law could send a wrong signal to potential foreign investors and was therefore heavily criticized by the German Council of Economic Advisors and the German Industry Federation.[112]

Notwithstanding the change in the investment law, the German Government has repeatedly emphasized that it welcomes foreign investors.[113] The Government has taken several measures to attract IFDI. Germany has concluded a large number of double taxation treaties (DTTs). As of May 2010, DTTs are in effect with 108 countries.[114] In January 2009, "Germany Trade and Invest", the foreign trade and

[108] Thomas Jost, "Sovereign wealth funds: size, economic effects and policy reactions," *Weidener Diskussionspapiere No. 13*, January 2009, available at: www.haw-w.de/fileadmin/user_upload/Aktuelles/Veroeffentlichungen/wen_diskussionspapier13.pdf.
[109] Federal Ministry of Economics and Technology, "Explanatory memorandum," available at: www.bmwi.de.
[110] Thomas Jost, "Sovereign wealth funds and the German policy reaction," in Karl P. Sauvant, Lisa Sachs and Wouter P.F. Schmit Jongbloed, eds, *Sovereign Investment: Concerns and Policy Reactions* (New York, forthcoming 2010).
[111] An investment by a European Union resident company of which a Community-non-resident holds at least 25% of the voting rights can also be reviewed.
[112] Sachverständigenrat, "Jahresgutachten 2007/08: Das Erreichte nicht verspielen," (Wiesbaden: 2007); Bundesverband der Deutschen Industrie, "BDI kritisiert geplante Änderungen im Außenwirtschaftsgesetz," *Pressemitteilung* 81, August 4, 2008, available at: www.bdi.eu.
[113] Federal Ministry of Economics and Technology, "Investitionsfreiheit und Prüfung ausländischer Investitionen: kein Widerspruch," *Schlaglichter der Wirtschaftspolitik*, Monatsbericht März 2008, pp. 7-10, available at: www.bmwi.de.
[114] The most recent official list of German DDTs is published by the Bundesministerium der Finanzen, "Stand der Doppelbesteuerungsabkommen und der Doppelbesteuerungsverhandlungen am 1. Januar 2010," available at: www.bundes-finanzministerium.de/nn_318/DE/BMF__Startseite/Aktuelles/BMF__Schreiben/Internationales__Steuerrecht/009.html.

inward investment agency of the Federal Republic of Germany, was formed after the merger of the "German Office for Foreign Trade" and "Invest in Germany". Its mission is to promote Germany as a location for industrial and technological investments and to identify investors for the German market. The organization advises foreign companies looking to expand their business activities on the German market and provides comprehensive and client-oriented economic and industry data as well as information about calls for proposals in foreign countries, investment and development projects and legal and customs regulations. The promotion of economic activity in Germany's new federal states, including Berlin, also forms an integral part of the agency's external trade and business location marketing remit. Last but not least, the German corporate sector (e.g., the Federation of German Industries) favors an open investment climate.[115]

Conclusions and Outlook

With the renewed uncertainty in the wake of the debt crisis in several EU countries, it is too early to forecast the medium-term investment behavior of MNEs in general and in Germany in particular. But the German economy has made some strong progress to improve business conditions in the past few years and, in combination with a sound economic growth, this could pave the way for new IFDI.

Additional readings

Deutsche Bundesbank, "German foreign direct investment (FDI) relationships: recent trends and macroeconomic effects," *Deutsche Bundesbank, Monthly Report* (September 2006), pp. 43-58, available at: www.bundesbank.de/download/volkswirtschaft/mba/2006/200609mba_en_foreign.pdf.

Deutsche Bundesbank, "German balance of payments in 2009," *Deutsche Bundesbank, Monthly Report* (March 2010), pp. 17-32, available at: www.bundesbank.de/download/volkswirtschaft/mba/2010/201003mba_en_german.pdf.

Jörg Feuerhake, Alexander Schulze and Kirsten Untz, "Inward FATS: Auslandskontrollierte Unternehmen in Deutschland 2007“, *Wirtschaft und Statistik*, Statistisches Bundesamt, 5/2010, available at: www.destatis.de.

Jost, Thomas, "Sovereign wealth funds and the German policy reaction," in Karl P. Sauvant, Lisa Sachs, and Wouter P.F. Schmit Jongbloed, eds., *Sovereign Investment: Concerns and Policy Reactions* (New York, forthcoming 2010).

Jochem, Axel, "International financial competitiveness, " Deutsche Bundesbank, *Discussion Paper Series 1: Economic Studies,* No. 29/2008, available at: www.bundesbank.de/download/volkswirtschaft/dkp/2008/200829dkp.pdf

[115] Bundesverband der Deutschen Industrie, op.cit.

Useful websites

Deutsche Bundesbank, “Special statistical publication 10: foreign direct investment stock statistics,” available at:

www.bundesbank.de/download/statistik/stat_soner/statso10_en.pdf.
www.bundesbank.de/statistik/statistik_zeitreihen.en.php

Statistical annex

Annex table 1. Germany: inward FDI stock, 1990-2008 (US$ billion)

Economy	1990	1995	2000	2005	2007	2008
Germany: consolidated primary and secondary inward FDI stock	111	166	272	476	696	666[b]
Germany: primary inward FDI stock[a]	120	193	471	640	952	911[b]
Memorandum: comparator economies						
United States	395	536	1,257	1,634	2,110	2,279
United Kingdom	204	200	439	841	1,264	983
France	98	191	260	628	950	991
Japan	10	34	50	101	133	203

Sources: For Germany, Deutsche Bundesbank, "Special statistical publication 10: foreign direct investment stock statistics," available at: www.bundesbank.de/download/statistik/stat_sonder/statso10_en.pdf (data converted from Euro in US-Dollar using end of year exchange rates from the International Monetary Fund, available at: http://www.imf.org/external/np/fin/data/param_rms_mth.aspx). For comparator economies, UNCTAD's FDI/TNC database, available at: http://stats.unctad.org/fdi/.

[a] For international comparisons the German primary inward FDI stock should be used (see the explanation in footnote 1 of the text).

[b] The decline of the inward FDI stock in 2008 is only due to the depreciation of the Euro against the US-Dollar. Measured in Euro the inward FDI stock increased slightly.

Annex table 2. Germany: inward FDI flows, 2000-2009 (US$ billion)

Economy	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
Germany	199	26	54	33	-10	47	56	77	25	37
Memorandum: comparator economies										
United States	314	160	75	53	136	105	237	271	328	136
United Kingdom	119	53	24	17	56	176	156	183	92	47
France	43	51	49	43	33	85	78	158	98	64
Japan	8	6	9	6	8	3	-7	23	25	12

Sources: For Germany, Deutsche Bundesbank, "Zahlungsbilanzstatistik, Statistisches Beiheft 3," March 2010, available at: www.bundesbank.de/volkswirtschaft/zahlungsbilanzstatistik/2010/zahlungsbilanzstatistik032010.pdf. For comparator economies, UNCTAD's FDI/TNC database, available at: http://stats.unctad.org/fdi/; US Department of Commerce, Bureau of Economic Analysis, "Balance of Payments Statistics," available at: www.bea.gov/international/xls/table1.xls; Office for National Statistics, "Statistical Bulletin, Balance of payments, 4th quarter of 2009," available at: www.statistics.gov.uk/pdfdir/bop0310.pdf; Banque de France, "Bulletin de la Banque de France No. 178, 4éme trimester 2009," available at: www.banque-france.fr/fr/publications/telechar/
bulletin/cahier-statistiques-03-2010.pdf; JETRO (Japan External Trade Organization), "Japanese Trade and Investment Statistics," www.jetro.go.jp/en/reports/statistics/data/bpfdi02_e_1004.xls. Data converted from national currencies in US-Dollar using annual average exchange rates from the International Monetary Fund, available at: http://www.imf.org/external/np/fin/data/param_rms_mth.aspx).

Annex table 3. Germany: distribution of inward FDI stock by economic sector and industry, [a] **2000, 2008** (US$ billion)

Sector/industry	2000	2008
All sectors/industries	**271.6**	**666.1**
Primary	**1.4**	**5.3**
Agriculture, hunting, forestry, and fishing	0.2	0.3
Mining, quarrying and petroleum	1.2	5.0
Secondary	**86.4**	**231.6**
Food, beverages and tobacco	5.1	20.9
Chemicals and chemical products	18.4	54.8
Rubber and plastic products	4.0	8.4
Other non-metallic mineral products	3.3	9.5
Basic metals	3.4	11.6
Fabricated metal products, except machinery and equipment	3.2	7.5
Machinery and equipment	8.9	26.7
Electrical machinery and apparatus	4.6	8.2
Radio, television and communication equipment	8.3	20.2
Medical, precision and optical instruments	3.3	14.3
Motor vehicles, trailers and semi-trailers	11.3	18.6
Services	**183.8**	**429.2**
Electricity, gas, and water supply	2.3	13.8
Trade, repair of motor vehicles, motorcycles and personal and household goods	35.7	74.6
Transport and communication	6.5	60.3
Finance and insurance	41.9	101.5
of which: Monetary Intermediation	14.2	54.3
Other monetary intermediation	22.2	18.0
Insurance and pension funding (except compulsory social security)	5.1	29.2
Real estate, renting and business activities	93.6	169.0
of which: Holding companies	75.2	101.2

Source: Deutsche Bundesbank, "Bestandserhebung über Direktinvestitionen," *Statistische Sonderveröffentlichung*, April 10, 2010, available at: www.bundesbank.de.

[a] Primary and secondary (i.e., through dependent domestic holding companies) foreign direct investment in Germany (consolidated), by economic activity of the investment enterprise in Germany. Data converted from Euro in US-Dollar using end of year exchange rates from the International Monetary Fund (available at: http://www.imf.org/external/np/fin/data/param_rms_mth.aspx).

Annex table 4. Germany: geographical distribution of inward FDI stock,[a] 2000, 2008
(US$ billion)

Region/economy	2000	2008
World	**271.6**	**666.1**
Developed economies	**264.8**	**643.0**
Europe	**.**	**557.2**
Austria	6.8	23.0
Belgium	6.0	9.6
Denmark	3.7	5.7
Finland	1.9	7.1
France	26.9	61.9
Norway	1.6	2.9
Ireland	0.9	4.2
Italy	3.9	47.3
Luxembourg	41.8	97.3
Netherlands	57.0	151.8
Spain	1.7	10.7
Sweden	7.7	19.9
Switzerland	21.6	43.1
United Kingdom	18.2	57.9
Memorandum item:		
European Union	*176.7*	*500.2*
European Monetary Union	*146.9*	*416.1*
North America	**41.5**	**71.0**
Canada	2.3	3.8
United States	39.2	67.2
Other developed economies	**.**	
Australia	0.1	1.3
Japan	9.5	19.5
Developing economies	**7.1**	**23.1**
Africa	**0.9**	**1.8**
South-Africa	0.8	1.7
Asia and Oceania	**4.5**	**10.7**
China	.	0.8
India	0.1	0.4
Iran	0.7	1.8
Korea, Rep. of	1.7	5.1
Latin America and the Carribean	**1.7**	**4.6**
Bermuda	0.4	1.7
Brazil	0.1	0.3
South-East Europe and CIS	**.**	
Russia	0.7	6.0

Source: Deutsche Bundesbank, "Bestandserhebung über Direktinvestitionen," *Statistische Sonderveröffentlichung*, April 10, 2010, available at: www.bundesbank.de.
[a] Primary and secondary (i.e, through dependent domestic holding companies) foreign direct investment in Germany (consolidated). Data converted from Euro in US-Dollar using end of year exchange rates from the International Monetary Fund (available at: http://www.imf.org/external/np/fin/data/param_rms_mth.aspx).

Annex table 5. Germany: Main non-financial foreign affiliates, ranked by foreign assets, 2008 (US$ million)

Rank	Name	Industry	Value added (US$ million)	Employees
1	Shell Deutschland	Mineral oil	44,906	4,300
2	Deutsche BP AG	Mineral oil	43,892	5,800
3	Ford Werke GmbH	Automobiles	28,944	29,800
4	Adam Opel GmbH	Automobiles	21,597	20,300
5	Vattenfall Europe AG	Energy	19,800	21,200
6	Total Deutschland	Mineral oil	18,020	4,000
7	Exxon Mobil	Mineral oil	17,800	3,400
8	Vodafone D2	Telecommunications	13,843	15,000
9	OMV Deutschland	Mineral oil	9,293	610
10	C&A	Warehouses	9,266	34,000
11	Airbus Deutschland GmbH	Aeroplanes	8,589	22,000
12	Hewlett-Packard Deutschland	Computer and electronics	7,376	8,600
13	Kion Group	Material handling	6,698	21,000
14	Sanofi-Aventis	Pharmaceutics	5,883	10,000
15	Procter & Gamble	Consumer goods	5,516	15,000
16	Telefonica O2	Telecommunications	5,286	4,700
17	Nestlé	Food	5,274	12,400

Sources: *Frankfurter Allgemeine Zeitung*, “Deutschlands größte Unternehmen in Zahlen,” July 8, 2009, available at: FAZ.net, and companies’ websites.

Annex table 6. Germany: main M&A deals, by inward investing firm, 2007-2009 (US$ million)

Year	Acquiring company	Investor economy	Target company	Target industry	Shares owned after transaction (%)	Transaction value (US$ million)
2009	Qatar Investment Authority	Qatar	Volkswagen AG	Motor vehicles	17.0	9,569.5
2009	Verbund	Austria	E On AG Hydro	Electrity	100.0	1,931.6
2009	IPIC	Unitad Arab Emirates	MAN Ferrostahl AG	Machinery and equipment	70.0	951.4
2009	Electrabel SA-Coal &Electricity	Belgium	E On AG Farge und Zolling	Electricity	100.0	686.1
2009	Investor Group	Czech Republic	Mibrag	Coal mining and energy	100.0	513.9
2009	Thermo Fisher Scientific Inc	United States	Brahms AG	Medical and biotechnology	100.0	470.6
2009	Honeywell International Inc	United States	RMG Regel- und Messtechnik GmbH	Electrical machinery and apparatus	100.0	400.0
2008	Banque Federative du Credit Mutuel	France	Citibank Privatkunden AG&Co KGaA	Banking	100.0	6,617.5
2008	Whitehall Street Fund	United States	LEG Landesentwicklungs-gesellschaft NRW GmbH	Real estate	100.0	5,255.0
2008	CVC Capital Partners Ltd	Luxembourg	Evonik Industries AG	Electricity	25.0	3,705.4
2008	Cie de Saint Gobain SA	France	Maxit Holding GmbH	Building materials	100.0	3,270.8
2008	Xella International SPV	France	Xella International GmbH	Building materials	100.0	3,183.7
2008	Eaton Corp	United States	Moeller Holding GmbH	Electrical	100.0	2,220.0

			& Co KG	machinery		
2008	Unicredito Italiano SpA	Italy	Bayerische Hypo- und Vereinsbank	Finance	100.0	1,891.5
2008	HRE Investment Holdings LP	Cayman Islands	Hypo Real Estate Holding AG	Finance	24.9	1,796.4
2007	Mylan Laboratories Inc	United States	Merck KGaA-Generic Drugs	Pharmaceuticals	100.0	6,627.9
2007	Nycomed A/S	Denmark	Altana AG-pharmaceutical business	Pharmaceuticals	100.0	5,753.2
2007	UCB SA	Belgium	Schwarz Pharma AG	Biological products	87.6	4,772.7
2007	Lavena Holding 4 GmbH	United States	ProSiebenSat.1 Media AG	Media	50.5	4,100.0
2007	Red & Black Lux Sarl	Italy	Hugo Boss AG	Clothing	88.0	2,842.8
2007	Sapardis SA	France	Puma AG	Sports wear	62.1	2,500.9
2007	Investor Group	United Kingdom	Aurealis Real Estate GmbH	Real estate	100.0	2,231.3

Source: Thomson ONE Banker, Thomson Reuters.

Annex table 7. Germany: main announced greenfield projects, by inward investing firm, 2007-2009 (US$ million)

Year	Company name	Source economy	Investment	Industry	Business activity
2009	ConocoPhillips	United States	2,500.0	Coal, oil and natural gas	Manufacturing
2009	Texas Instruments	United States	1,039.0[a]	Semiconductors	Manufacturing
2009	Gazprom	Russia	986.1	Coal, oil and natural gas	Logistics, distribution and transportation
2009	Nord Stream AG	Switzerland	599.6[a]	Coal, oil and natural gas	Logistics, distribution and transportation
2009	Multi Development	Netherlands	599.6	Real estate	Construction
2009	Green Wind Energy	Denmark	568.7[a]	Alternative/renewable energy	Electricity
2009	GDF SUEZ	France	526.2[a]	Coal, oil and natural gas	Extraction
2008	Vattenfall	Sweden	1557.0	Coal, oil and natural gas	Manufacturing
2008	Blackstone Group	United States	1544.0	Alternative/renewable energy	Electricity
2008	Bulberry Properties	Ireland	1240.0	Real estate	Construction
2008	Econcern	Netherlands	1078.0	Alternative/renewable energy	Electricity
2008	Advanced Technology Investment Company	United Arab Emirates	1,039.0[a]	Semiconductors	Manufacturing
2008	Minera S.A.	United States	993.5	Metals	Extraction
2008	Intico solar	Austria	954.5	Electronic components	Manufacturing
2007	Suez	France	1,463.0	Coal, oil and natural gas	Electricity
2007	ING Group	Netherlands	1,262.9	Real estate	Construction
2007	Sirenza Microdevices	United States	1,039.2[a]	Semiconductors	Manufacturing
2007	Morgan Stanley	United States	872.7	Real Estate	Construction
2007	Gazprom	Russia	616.5	Coal, oil and natural gas	Logistics, distribution and transportation
2007	Gazprom	Russia	542.7	Coal, oil and natural gas	Electricity
2007	Abengoa	Spain	525.0	Alternative/renewable energy	Manufacturing

Source: fDi Intelligence, a service from the Financial Times Ltd.

[a] Estimated.

Outward FDI and its policy context, 2010

Ralph Hirdina and Thomas Jost

German companies started early to internationalize their operations. They ranked among the top three of foreign investors measured by the value of their OFDI stock by the end of 2008.[116] *German FDI abroad increased in close connection with the rise of German exports, and received a new stimulus through the further integration of European markets and the opening up of Eastern Europe in the 1990s. After record FDI outflows in the boom years 2006 to 2008, German OFDI dropped markedly in 2009 - but less than in the previous downturn between 2002 and 2003. In recent years, the German Government has continued to provide a sound legal framework for German companies going abroad by creating a wide network of bilateral treaties and offering support as well as information services as the internationalization of the German corporate sector improves the competitiveness of the country's economy and promotes exports.*

Trends and developments

Country-level developments

In search of new markets and to support export growth, market-seeking German companies started expanding abroad early in the 1960s and 1970s. In times of strong real appreciations of the German currency and an accompanying loss of price competitiveness, efficiency-seeking FDI in countries with lower wage costs gained importance.[117] At the end of the 1980s and during the early 1990s, OFDI of German MNEs received a new stimulus from the EU Single Market Program and the opening up of the Eastern European economies.[118] The European Monetary Union and the introduction of the Euro in 1999 further raised German OFDI. It grew nearly tenfold since 1990, to reach a stock of US$ 1,450 billion at the end of 2008, making Germany the third largest investor in the world (annex table 1).

In the boom years from 2006 to 2008, annual German OFDI flows climbed to record values of up to US$ 163 billion in 2007 (annex table 2). The worldwide financial and economic crisis started to dampen this growth in the beginning of the fourth quarter in 2008. In 2009, OFDI fell by 61% (compared to 2007), reaching a total of US$ 63 billion. The decline in FDI was in line with the worldwide downward trend and paralleled the fall of domestic investments of the corporate sector. Compared to the previous bust in 2002 and 2003, OFDI decreased much less in relative terms, and the 2009 level of outflows was still the seventh highest on record.

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[116] UNCTAD, *World Investment Report 2009: Transnational Corporations, Agricultural Production and Development* (New York and Geneva, United Nations, 2009).
[117] Thomas Jost and Horst Rottmann, "Umfang und Motive deutscher Direktinvestitionen in den Industrieländern," *LIST-Forum für Wirtschafts- und Finanzpolitik*, vol. 30 (2004), pp. 153-166.
[118] Nigel Pain, "Fiscal policies, European integration and structural changes in the location of German foreign direct investment," in Heinz Herrmann and Robert Lipsey, eds., *Foreign Direct Investment in the Real and Financial Sector of Industrial Countries* (Berlin: Springer, 2003), pp. 96-136.

In the past, German companies heavily invested abroad in the services sector: it accounted for nearly three quarters of the value of Germany's OFDI stock at the end of 2007, followed by the manufacturing sector (26%) (annex table 3).[119] Foreign investments in the primary sector (of less than 1%) play only a minor role. In the services sector, the major investments by value (46%) were made in the finance and insurance sector, reflecting the strength of several German banks and insurance companies (which belong to the major players in world financial markets).[120] The success of Germany in the export of automobiles, machinery and equipment led to strong investments abroad in the sector of trade and repair of motor vehicles and personal as well as consumer goods; these accounted for 17% of the German OFDI stock in the services sector at the end of 2007.[121]

In recent years, German OFDI grew strongly in the electricity, gas and water supply as well as in the transport and telecommunications sectors (annex table 3). The liberalization and privatization process in the European Union network industries led to a wave of large-scale cross-border investments of German MNEs. In the energy and water supply sectors, the OFDI stock grew 15-fold, starting out from a low level of US$ 4 billion in 2000, to reach US$ 58 billion in 2007. In the same period, FDI abroad in the transport and telecommunications sectors increased tenfold, from $7 billion to $67 billion.[122]

Manufacturing accounts for a quarter of the value of German OFDI. Within the manufacturing sector, German companies heavily invest in chemicals/chemical products, motor vehicles, trailers and semi-trailers, as well as machinery and equipment; they account for 30%, 20% and 10% of all German OFDI in the secondary sector, respectively. Foreign affiliates of German MNEs of the manufacturing sector employ 2.8 million workers - more than half of all people employed in all German foreign affiliates. The strong growth of employment in foreign affiliates of German firms in the 1990s – mainly resulting from investments in production facilities in new EU member countries (especially in the Czech Republic, Hungary, Poland, and Slovakia) - slowed down in the past decade. But from time to time, criticism arises in the German public as regards possible detrimental effects of German FDI abroad, especially concerning job relocations. In contrast to these fears, the strong increase in German OFDI was only partially motivated by lower wage costs abroad. It was mainly driven by the search for new markets as well as by marketing, distribution and customer service motives.[123] Overall, German OFDI has strengthened the competitiveness of the German corporate sector and has contributed to investment and employment growth at home.[124]

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[119] FDI stock data of the Deutsche Bundesbank based on a compulsory annual survey of German companies show FDI of German firms according to the sector of the final investment object. These data are published with a time lag of one-and-a-half year. Therefore, detailed stock data are only available as of end of 2007.

[120] Claudia Buch and Alexander Lipponer, "FDI versus exports: evidence from German banks," *Journal of Banking and Finance,* 31 (2007), pp. 805-826.

[121] Sebastian Krautheim, "Export-supporting FDI," *Discussion Paper Series 1: Economic Studies*, No 20/2009, Economic Research Centre, Deutsche Bundesbank.

[122] Part of the increase in the dollar value of the German outward FDI stock is due to the strong appreciation of the Euro against the US dollar (of 48%) in the period 2000 to 2007.

[123] In various surveys of the German Industry Federation, German MNEs ranked the market-seeking motive as the most important driver of foreign investments. See e.g. DIHK, "Auslandsinvestitionen in der Industrie: Frühjahr 2010," *Ergebnisse der DIHK-Umfrage bei den Industrie- und Handelskammern* (2010), available at www.dihk.de.

[124] Deutsche Bundesbank, "German foreign direct investment (FDI) relationships: recent trends and macroeconomic effects," *Deutsche Bundesbank Monthly Report*, September 2006, p. 43-58.

Foreign investments of German firms are mainly concentrated in developed countries that are also the main target regions for German exports and that offer the factor inputs that German MNEs need for production (especially a highly qualified workforce). Developed countries account for 87% of the value of the OFDI stock (annex table 4). In the past decade, investments of companies abroad grew fastest in the new EU member countries and in certain other countries in Europe (notably the United Kingdom and Switzerland). The EU accounted for more than 57% of the German OFDI stock in 2007. In 2008 and 2009, German FDI in the European neighbor countries continued to be strong. This came partially at the cost of outward investment in North America and other developed countries outside Europe. Whereas OFDI in developing countries grew in line with the growth of total OFDI,[125] FDI outflows to Russia and Ukraine increased considerably during the past decade. The German OFDI stock in both countries grew 17-fold since 2000, to reach roughly US$ 30 billion in 2007. German investments in this region were mainly driven by several large-scale investments in the energy and gas sectors. Well-equipped with large profits generated in past years, German energy MNEs went east to increase the security of energy supply and to capture new markets.

The corporate players

German MNEs have successfully internationalized their production facilities and operations abroad. Most of the large companies in the chemical, motor vehicle, machinery and equipment, telecommunications, and energy sectors, as well as the major banks and insurance companies, are now operating worldwide (annex table 5). The 30 largest German companies listed at the German stock exchange (the DAX-30) are highly internationalized. They employ more than half of their workforce abroad (in 2008: 57%).[126] The largest outward M&As in recent years (annex table 6) were made by well-known global players like Volkswagen AG, RWE AG, Siemens AG, Deutsche Telekom AG, and Allianz AG. Not only large German MNEs, but also a growing number of small and medium-sized companies expanded their operations abroad. The total number of foreign affiliates of German companies reached 28,929 and the number of parent companies 6115 at the end of 2007.[127]

Effects of the current global crisis

The global financial crisis and recession seriously affected the German economy. German companies suffered from a sharp decline of exports and falling profits. In 2009, German OFDI fell by 53% against 2008, to reach US$ 63 billion. The decline in German OFDI in 2009 was mainly due to increased long-term credits of financing affiliates of German companies located in the Netherlands to their parents in Germany that were financed by the emission of securities abroad. These intra-firm financial transactions resulted in net disinvestments abroad via intra-company loans that explained three quarters of the decline in German OFDI abroad.[128] Despite the

[125] On the determinants of German FDI in developing countries, see Thomas Jost and Peter Nunnenkamp, “Bestimmungsgründe deutscher Direktinvestitionen in Entwicklungs- und Schwellenländern,” *Kieler Arbeitspapier* 1124, Kiel Institute for World Economics, 2002.
[126] Ernst&Young, “Entwicklung der Dax-30-Unternehmen 2007/08: Eine Analyse wichtiger Bilanzkennzahlen,” available at: www.ey.com.
[127] In the German FDI stock statistics, the reporting threshold was changed several times. Therefore, a consistent time series of the development of the number of foreign affiliates is not available.
[128] Deutsche Bundesbank, “Die deutsche Zahlungsbilanz für das Jahr 2009,” *Monatsbericht* (März 2010), p. 30.

difficult economic situation, German equity capital investments abroad remained remarkably strong, declining by only 27% against the record value of 2008 and amounting to US$ 66 billion in 2009. Especially German energy providers like RWE AG and E.on AG were very active in cross-border M&As and greenfield investments to expand their market share and to improve their competitive position in foreign markets (annex tables 6 and 7).

The policy scene

There are three main international legal frameworks for German FDI: the European Treaty, Treaties concluded by the European Union and national BITs. German MNEs have concentrated a large part of their OFDI in the EU member states. Therefore, the European treaties are a very important framework for Germany FDI activities. The EU guarantees free trade of goods and services for all members of the European Union and the free movement of capital among EU member states and with third states. In case of violations of these rights, the European Commission can bring a case before the European Court of Justice.[129] The EU has concluded several FTAs that contain declarations of supporting FDI flows between the EU and its partner states.[130] Since the Lisbon treaty took effect on December 1, 2009, the EU has gained new competences concerning FDI.[131] However, the practical implications of the Lisbon Treaty for Europe's FDI-policy remain uncertain (e.g. the Lisbon Treaty fails to clarify the exact definition of FDI).[132]

The EU and the United States have the most important bilateral trade and investment relations in the world. The United States is the single most important target country for German OFDI. Among the triad of North America, the EU and Japan, FDI flows are not restricted in any way and are not governed by BITs.[133]

Already in the 1950s, Germany fully liberalized its capital exports and the German Government recognized the need for a reliable legal framework for OFDI.[134] In 1959, Germany signed its first BIT with Pakistan (renewed on December 1, 2009), also became the first BIT worldwide.[135] Until March 2010, Germany had signed 138 BITs; it was the leading position in the world - along with Switzerland (116 BITs) and China (123 BITs).[136] Most of Germany's BITs were concluded in the 1990s, corresponding to the worldwide increase in the number of BITs after the collapse of

[129] The Treaty of Lisbon, December 1, 2009: Article 34 TEU (ex-Art. 28 TEU), article 56 TEU (ex-Art. 49 TEU), article 63 TEU (ex-Art. 56 TEU), article 258 TEU (ex-Art. 226 TEU) EU; available at: http://eur-lex.europa.eu/en/treaties/index.htm.

[130] Jan Ceyssens and Nicola Sekler, "Bilateral investment treaties (BITs) of Germany: effects on economic, social and ecological regulation in host countries and models to implement the responsibility of transnational corporations," *Forschungsprojekt der Hans-Böckler-Stiftung an der Universität Potsdam* (2005), p. 7, available at: www.opus.kobv.de/ubp/volltexte/2005/612/pdf/BITSStudie.pdf

[131] The Treaty of Lisbon, op. cit.

[132] Daman Vis-Dumbar, "The Lisbon Treaty: implications for Europe's international investment agreements," *Trade Negotiations Insights*, vol. 8, no. 9, November 2009, available at: http://ictsd.org/i/news/tni/59585/; José Guimón, "It's time for an EU investment promotion agency," *Columbia FDI Perspectives*, No. 20, March 4, 2010, available at: www.vcc.columbia.edu.

[133] Ceyssens and Sekler, op. cit., p. 24.

[134] Ceyssens and Sekler, op. cit., p. 25.

[135] Karl P. Sauvant and Lisa E. Sachs, eds., *The Effect of Treaties on Foreign Direct Investment: Bilateral Investment Treaties, Double Taxation Treaties, and Investment Flows* (New York : Oxford University Press, 2009).

[136] UNCTAD, "Total number of bilateral investment treaties concluded," available at: www.unctad.org/sections/dite_pcbb/docs/bits; Bundesministerium für Wirtschaft und Technologie, "Bilaterale Investitionsförderungs- und Schutzverträge," available at: www.bmwi.de.

the former Soviet Unions and its partner states.[137] To date, 127 of the 138 signed BITs have been ratified.[138] For German companies, BITs are an important tool for protecting their investment interests abroad. For example, after the terrorist bombing of Mumbai in November 2008, German companies asked for higher security standards in India. The basis for such claims was the BIT with India that came into force in 1998. Volkswagen, a big German car producer, emphasized that its planned investment in India would need high legal investment and security standards.[139] In 2009, the new Volkswagen group plant in India started its operation with a production capacity of 110,000 cars per year, the largest greenfield investment of a German company in India ever.

Within these legal frameworks, the German Government offers companies many services and support for FDI in developing countries. The German Government for example gives guarantees for FDI that may fail because of political risks. But those guarantees are only granted in case of a minimum of legal protection for FDI by the host countries - either in form of BITs or a stable legal system.[140] The state-owned German bank group "Kreditanstalt für Wiederaufbau" (KfW) and the "Deutsche Investitions- und Entwicklungs mbH" (DEG) offer credits for FDI and corresponding advisory services.[141] In 2009, the German Government granted investment guarantees for 76 FDI projects in 24 developing countries, with a total value of US$ 4.2 billion.[142] Beyond that, the German system of foreign chambers of commerce (Deutsche Auslandshandelskammern) helps to make German FDI successful by offering advisory services.[143] German foreign chambers of commerce can be found in 120 cities in 80 countries worldwide.[144]

Conclusions and Outlook

As a highly export-oriented country, Germany will continue to expand its presence in foreign markets via FDI. The pace of recovery of OFDI flows to pre-crisis levels will depend largely on the future development of the economies of Germany's major partner countries in the European Union and North America. East and South-East Asian markets are also expected to play a greater role as destinations for German OFDI in the future. According to a recent survey of the German Industry Federation (DIHK) German companies plan to step up investments in international sales and distribution networks as well as production facilities in key foreign markets in 2010.[145]

[137] Ceyssens and Sekler, op. cit., p. 23.
[138] Bundesministerium für Wirtschaft und Technologie, op. cit.
[139] Volker Müller, "Deutsche Firmen fordern mehr Sicherheit in Indien", *Welt Online*, November 28, 2008, available at: www.welt.de/politik/article2799353/Deutsche-Firmen-fordern-mehr-Sicherheit-in-Indien.html.
[140] Bundesministerium für Wirtschaft und Technologie, "Ratgeber für kleine und mittlere Unternehmen", 30.10.2007, available at: www.bmwi.de/BMWi/Navigation/Service.html.
[141] Bundesministerium für Wirtschaft und Technologie, op. cit.
[142] Bundesministerium für Wirtschaft und Technologie, "Investitionsgarantien 2009: Starke Nachfrage auch in der Wirtschaftskrise," Pressemitteilung, January 7, 2010, available at: www.bmwi.de.
[143] Deutscher Industrie und Handelskammertag e.v., "Deutsche Außenhandelskammern, Aufgaben," available at: http://ahk.de/ueber-ahk/ahk-aufgaben/.
[144] Deutscher Industrie und Handelskammertag e.V., "Deutsche Außenhandelskammern, Standorte," availabe at: http://ahk.de/ahk-standorte/.
[145] DIHK, op. cit.

Additional readings

Ceyssens, Jan and Nicola Sekler, "Bilateral investment treaties (BITs) of Germany : effects on economic, social and ecological regulation in host countries and models to implement the responsibility of transnational corporations," *Forschungsprojekt der Hans-Böckler-Stiftung an der Universität Potsdam*, 2005, available at: http://opus.kobv.de/ubp/volltexte/2005/612/pdf/BITSStudie.pdf.

Deutsche Bundesbank, "German foreign direct investment (FDI) relationships: recent trends and macroeconomic effects," *Deutsche Bundesbank Monthly Report* (September 2006), pp. 43-58, available at: www.bundesbank.de/download/volkswirtschaft/mba/2006/200609mba_en_foreign.pdf.

Deutsche Bundesbank, "Special statistical publication 10: foreign direct investment stock statistics," available at: www.bundesbank.de/download/statistik/stat_soner/statso10_en.pdf.

Deutsche Bundesbank, "Die deutsche Zahlungsbilanz für das Jahr 2009," *Deutsche Bundesbank Monatsbericht* (März 2009), pp. 17-32, available at: www.bundesbank.de/download/volkswirtschaft/monatsberichte/2010/201003mb_bbk.pdf.

Jost, Thomas and Horst Rottmann, "Umfang und Motive deutscher Direktinvestitionen in den Industrieländern," *LIST-Forum für Wirtschafts- und Finanzpolitik* (30) (2004), pp. 153-166.

Useful website for FDI flows and stocks statistics
www.bundesbank.de/statistik/statistik_zeitreihen.en.php

Statistical annex

Annex table 1. Germany: outward FDI stock,[a] 1990-2008 (US$ billion)

Economy	1990	1995	2000	2005	2007	2008
Germany	151.6	268.4	537.8	978.1	1205.1	1450.9 [b]
Memorandum: comparator economies						
United States	430.5	699.0	1,316.2	2,241.7	2,916.9	3,162.0
United Kingdom	229.3	304.9	897.8	1,198.6	1,841.0	1,510.6
France	112.4	204.4	445.1	868.5	1,291.6	1,397.0
Japan	201.4	238.5	278.4	386.6	542.6	680.3

Sources: For Germany, Deutsche Bundesbank, "Special statistical publication 10: foreign direct investment stock statistics," available at: www.bundesbank.de/download/statistik/stat_soner/statso10_en.pdf. For comparator countries, UNCTAD's FDI/TNC database, available at: http://stats.unctad.org/fdi/.

[a] Due to different statistical recording, the data for the selected economies are not fully comparable.
[b] UNCTAD estimate.

Annex table 2. Germany: outward FDI flows, 2000-2009 (US$ billion)

Economy	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
Germany	56.7	39.7	19.0	5.9	20.5	75.9	118.8	162.7	135.2	62.9
Memorandum: comparator economies										
United States	142.6	124.9	134.9	129.4	294.9	15.4	224.2	378.4	311.8	
United Kingdom	233.4	58.9	50.3	62.2	91.0	80.8	86.3	275.5	111.4	
France	177.4	86.8	50.4	53.1	56.7	115.0	121.4	224.7	220.0	
Japan	31.6	38.3	32.8	28.8	31.0	45.8	50.3	73.5	128.0	

Sources: For Germany, Deutsche Bundesbank, "Zahlungsbilanzstatistik, Statistisches Beiheft 3," March 2010, available at: www.bundesbank.de/volkswirtschaft/zahlungsbilanzstatistik/2010/zahlungsbilanzstatistik032010.pdf. For comparator countries, UNCTAD's FDI/TNC database, available at: http://stats.unctad.org/fdi/.

Annex table 3. Germany: distribution of outward FDI stock by economic sector and industry,[a] **2000, 2007** (US$ billion)

Sector/industry	2000	2007
All sectors/industries	**537.8**	**1205.1**
Primary	**4.8**	**9.3**
Agriculture, hunting, forestry, and fishing	0.6	1.2
Mining, quarrying and petroleum	4.2	8.1
Secondary	**165.4**	**312.3**
Food, beverages and tobacco	3.7	7.9
Chemicals and chemical products	49.0	93.7
Rubber and plastic products	5.4	14.4
Other non-metallic mineral products	7.2	19.2
Basic metals	2.3	11.0
Fabricated metal products, except machinery and equipment	4.5	12.7
Machinery and equipment	15.1	32.3
Electrical machinery and apparatus	16.4	21.1

Radio, television and communication equipment	5.7	10.1
Medical, precision and optical instruments	6.5	10.6
Motor vehicles, trailers and semi-trailers	38.8	61.5
Services	**367.6**	**883.4**
Electricity, gas, and water supply	3.9	57.7
Trade, repair of motor vehicles, motorcycles and personal and household goods	65.3	152.9
Transport and communication	7.3	66.9
Finance and insurance	215.8	410.5
of which: Monetary Intermediation	56.2	101.7
Other monetary intermediation	126.3	230.7
Insurance and pension funding (except compulsory social security)	24.0	54.1
Real estate, renting and business activities	69.2	182.3
of which: Holding companies	41.6	102.7

Source: Deutsche Bundesbank, "Bestandserhebung über Direktinvestitionen," Statistische Sonderveröffentlichung 10, April 2009, available at: www.bundesbank.de.

[a] Primary and secondary (i.e. through dependent holding companies abroad) German direct investment abroad (consolidated), by economic activity of the foreign investment enterprise.

Annex table 4. Germany: geographical distribution of outward FDI stock, [a] **2000, 2007** (US$ billion)

Region/economy	**2000**	**2007**
World	**537.8**	**1205.1**
Developed economies	**479.6**	**1043.2**
Europe	**262.4**	**740.6**
Austria	17.1	37.1
Belgium	22.1	50.8
Czech Republic	6.7	29.6
Finland	1.0	7.4
France	30.5	59.9
Hungary	6.6	23.6
Ireland	7.6	17.1
Italy	17.4	38.8
Luxembourg	18.5	57.0
Malta		33.6
Netherlands	33.7	58.4
Poland	7.3	25.9
Spain	12.5	28.1
Sweden	6.1	15.2
Switzerland	15.8	40.8
United Kingdom	50.1	169.0
North America	**203.1**	**277.8**
Canada	6.0	12.1
United States	197.1	265.7
Other developed economies	**14.1**	**24.8**
Australia	5.0	12.1
Japan	8.9	12.1
Developing economies	**54.9**	**127.0**
Africa	**4.4**	**8.8**
South-Africa	2.8	6.4
Asia and Oceania	**17.5**	**70.0**
China	5.2	20.8
India	1.4	6.0
Singapur	4.5	10.3
Korea, Rep. of	2.8	7.1
Latin America and the Carribean	**24.4**	**48.2**
Cayman Islands	3.1	14.1
Brazil	7.9	16.6
South-East Europe and CIS	**3.3**	**34.8**
Russia	1.4	23.3
Ukraine	0.3	6.2

Source: Deutsche Bundesbank, "Bestandserhebung über Direktinvestitionen," *Statistische Sonderveröffentlichung* 10, April 2009, available at: www.bundesbank.de.

[a] Primary and secondary (i.e. through dependent holding companies abroad) German direct investment abroad (consolidated), by economic activity of the foreign investment enterprise.

Annex table 5. Germany: Top MNEs, ranked by foreign assets, 2008 (US$ million)

Rank	Name	Industry	Foreign assets	Transnationality Index (2007)[a]
	Non-financial MNEs			
1	E.ON AG	Electricity, gas and water	141,168	53.6
2	Volkswagen Group	Motor vehicles	123,677	56.9
3	Siemens AG	Electrical and electronic equipment	110,018	72.0
4	Daimler AG	Motor vehicles	87,927	55.5
5	Deutsche Telekom AG	Telecommunications	95,019	47.8
6	BMW AG	Motor vehicles	63,201	56.2
7	Deutsche Post AG	Transport and storage	72,135	46.4
8	RWE Group	Electricity, gas and water	53,557	42.3
9	BASF AG	Chemicals	43,020	57.9
10	Linde AG	Chemicals	29,847	89.5
11	Metro AG	Retail	24,983	57.8
12	Thyssenkrupp AG	Metal and metal products	30,578	54.5
13	Bayer AG	Pharmaceuticals	26,317	43.8
	Financial MNEs			**Internationalization Index (2007)[b]**
1	Deutsche Bank AG		3,150,820	74
2	Allianz SE		1,367,062	76
3	Hypo Real Estate Holding		600,363	37
4	Muenchener Rueckversicherung AG		308,179	65

Sources: UNCTAD's FDI/TNC database, available at: http://stats.unctad.org/fdi/.

[a] UNCTAD's Transnationality Index is the average of the following three ratios: foreign assets to total assets, foreign sales to total sales and foreign employment to total employment.
[b] UNCTAD's Internationalization Index is calculated as the number of foreign affiliates divided by the number of all affiliates.

Annex table 6. Germany: main M&A deals, by outward investing firm, 2007-2009 (US$ million)

Year	Acquiring company	Target company	Target industry	Target economy	Shares acquired (%)	Transaction value (US$ million)
2009	RWE AG	Essent NV	Electricity, energy	Netherlands	100.0	10,410.7
2009	E.on AG	Severneftegazprom	Coal, oil, natural gas	Russia	25.0	3,958.7
2009	BASF AG	Ciba Specialty Chemicals	Chemicals	Switzerland	82.9	2,576.3
2009	K+S AG	Morton International Inc	Mining	United States	100.0	1,675.0
2009	Deutsche Telekom AG	OTE SA	Telecommunications	Greece	5.0	1,043.6
2009	Nordzucker AG	Danisco Sugar	Consumer goods	Denmark	100.0	938.6
2009	Munich Re	HSB Group Inc.	Insurance	United States	100.0	739.0
2008	Fresenius SE	APP Pharmaceuticals Inc	Pharmaceutics	United States	100.0	5,628.0
2008	SAP AG	Business Objects SA	Software	United States	78.0	5,511.0
2008	Henkel AG & Co. KGaA	Natl Starch& Chem Co-Adh.	Consumer goods	United States	100.0	5,506.9
2008	Volkswagen AG	Scania AB	Motor vehicles, trucks	Sweden	16.8	4,377.5
2008	Deutsche Telekom AG	OTE SA	Telecommunications	Greece	20.0	4,009.3
2008	Allianz SE	Hartford Fin Svcs Group Inc	Insurance	United States	23.7	2,500.0
2008	Heinrich Bauer Verlag KG	EMAP Consumer Media	Media	United Kingdom	100.0	1,435.1
2007	Allianz SE	AGF	Insurance	France	35.4	11,106.6
2007	Merck KGaA	Serono	Pharmaceutics	Switzerland	66.0	8,560.1
2007	Hypo Real Estate	DEPFA Bk PLC	Banking	Ireland	100.0	7,847.1
2007	E.on AG	OGK-4	Coal, oil, natural gas	Russia	47.4	3,947.3
2007	Siemens Automation	UGS Corp	Electronics	United States	100.0	3,500.0
2007	Tui Travel	First Choice Holidays PLC	Travel industry	United Kingdom	100.0	3,366.9
2007	Eurex AG	Intl Sec Exchange	Financial services	United States	100.0	2,821.4

Source: Thomson ONE Banker, Thomson Reuters.

Annex table 7. Chile: top 10 greenfield projects, by outward investing firm, 2007-2009 (US$ million)

Year	Investing company	Target industry	Target country	Investment
2009	Sigdo Koppers Group	Chemicals	Peru	650
2009	Falabella	Textiles	Peru	350
2009	Ripley	Real estate	Peru	157[a]
2009	Empresas Navieras SA	Transportation	Hong Kong (China)	129[a]
2009	Empresas Navieras SA	Transportation	Hong Kong (China)	67[a]
2009	Mardones Propiedades	Real estate	USA	41[a]
2009	Empresas Navieras SA	Transportation	Uruguay	33[a]
2009	Sociedad Quimicay Minera (SQM)	Chemicals	India	25[a]
2009	Bess Mobile	Communications	Venezuela	25
2009	Wines of Chile	Beverages	USA	22[a]
2008	Parque Arauco	Real estate	Colombia	160
2008	CSAV Norasia	Transportation	Malaysia	129[a]
2008	Masisa	Wood products	Brazil	91
2008	Distribucion y Servicio (D&S)	Food & tobacco	Peru	42[a]
2008	Credito Continental	Financial services	Colombia	32[a]
2008	Tesacom	Communications	Panama	24[a]
2008	Tesacom	Communications	Mexico	24[a]
2008	Wisetrack	Communications	Peru	24[a]
2008	e-Contact	Communications	Ecuador	24[a]
2008	Azurian	Software & IT services	Peru	23[a]
2007	Enap	Coal, oil and natural gas	Venezuela	800
2007	Ripley	Real estate	Mexico	400
2007	Paulmann Group	Consumer products	Colombia	200
2007	Sigdo Koppers Group	Chemicals	Peru	200
2007	Recycla	Alternative/renewable energy	Colombia	64[a]
2007	Iansa	Alternative/renewable energy	Colombia	60
2007	Salfacorp	Real estate	Peru	41[a]
2007	Ripley	Real estate	Peru	31
2007	Salfacorp	Real estate	Argentina	26[a]
2007	Cencosud	Consumer products	Colombia	15[a]

Source: ECLAC, based on information from the *fDi Intelligence*, a service from the *Financial Times Ltd* (www.fDimarkets.com).

[a] Estimate made by *fDi Intelligence*.

Chapter 6 – Hungary

Outward FDI and its policy context, 2010

Magdolna Sass and Kalman Kalotay

OFDI from Hungary has weathered the current crisis relatively well, although its volume is still moderate for a country classified as "high income" – but not necessarily if compared with other new European Union (EU) members. The Hungarian OFDI stock is highly concentrated in five big companies. Government policy has so far focused more on a vigorous promotion of IFDI than on helping outward investors. However, it sometimes protects strategic Hungarian OFDI firms from hostile takeovers. The main question for the future of Hungarian OFDI is how its sustainability can be assured, especially by way of broadening the company base of capital exporters.

Trends and developments

In terms of the volume of its OFDI stock, Hungary is the second largest source of outbound investment among the new EU member countries, not far behind Poland, whose population is four times larger (annex table 1). Hungary was among the countries that, during the early stage of transition, based their strategy of development and reinsertion into the world economy on IFDI.[146] Nevertheless, as early as 1997, a handful of Hungarian firms had overcome the difficulties of transition, had managed to keep their management in local hands (although some of them have accumulated large amounts of foreign *portfolio* investment in their shareholding) and had started expanding abroad, especially in neighboring countries.[147] Hungarian affiliates of foreign MNEs also invested abroad. However, up till today, IFDI flows and stocks have exceeded OFDI flows and stocks.

Country-level developments

The growth of Hungary's OFDI accelerated after 2000, making Hungary a relatively important outward investor among the new EU members, both in terms of volume and of relative importance of OFDI for the country's economy. Compared to GDP, Hungary is clearly ahead of the Czech Republic and Poland in its OFDI stock, although the difference has diminished since 2005. Between 2000 and 2005, Hungary's OFDI stock increased more than sixfold, and doubled again between 2005 and 2007 (annex table 1). Therefore, the ratio of outward to inward FDI, which reached a historical low as a result of massive FDI inflows in 1995 (2.5%), rose steadily, reaching 18% in 2007 and 22% in 2008 (annex table 1a). However, this ratio is higher both in certain small new EU member countries (Estonia, Slovenia) and in

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[146] Magdolna Sass, "The effectiveness of host country policy measures in attracting FDI: the case of Hungary," in Americo Beviglia Zampetti and Torbjörn Fredriksson, eds., *The Development Dimension of FDI: Policy and Rule-Making Perspectives* (New York and Geneva: United Nations, 2003), pp. 49–58.

[147] UNCTAD, *World Investment Report 1997: Transnational Corporations, Market Structure and Competition Policy* (New York and Geneva: United Nations, 1997), pp. 98–99.

the Russian Federation (with the exception of the crisis year 2009). Russia follows a different development strategy based on OFDI, while Estonia is used as a platform for OFDI by Scandinavian firms for investing in other Baltic countries and the Commonwealth of Independent States, and Slovenia is capitalizing on its inherited connections with former Yugoslav republics. Hungary's position is similar when making a regional comparison of OFDI flows: for example, in 2005–2007 and in 2009, it was in third position, behind the Russian Federation and Poland, although in 2008 both Poland and Hungary were surpassed exceptionally by the Czech Republic (annex table 2).

The sectoral composition of Hungary's OFDI changed markedly in the 2000s. In 2000, services (including financial services and trade) represented almost four-fifths of the total OFDI stock (annex table 3). Manufacturing gradually gained importance, accounting for almost 40% of the total OFDI stock in 2008. There was also a marked increase in the share of mining and quarrying, reaching almost 7% in 2008. Other industries playing an important role in Hungarian OFDI include coke and refined petroleum, financial intermediation, chemicals (including pharmaceuticals), electrical and optical equipment, and business services.

The geographical distribution of Hungary's OFDI follows – on the one hand - the same patterns as the OFDI of other emerging markets:[148] Hungarian MNEs target mainly neighboring countries at a similar or lower level of development (annex table 4). Eleven geographically close countries, including Slovakia (20%), Croatia (8%) and Bulgaria (6%), host almost 55% of the total Hungarian OFDI stock.[149] On the other hand, speculative investments, sometimes aimed at tax optimization, explain the relatively important shares of Cyprus, Luxembourg, the Netherlands, and Switzerland. One-off large transactions result in (temporary) surges of shares for certain countries. Such is the case for the Republic of Korea in 2006 or, more recently, for Central America (one deal in the Netherlands Antilles).

The corporate players

One of the most important features of Hungarian OFDI is its concentrated nature in terms of investing companies. Altogether, the estimated number of Hungarian MNEs is 7,000, including many SMEs. However, according to our estimates, the country's five largest MNEs (MOL, OTP Bank, Magyar Telekom, MKB Bank, Gedeon Richter) accounted for at least 65% of the total OFDI stock in 2008 (annex table 5).

This concentration explains the volatility of annual OFDI flows, as well as the sectoral and geographical distribution of OFDI. This is the reason, for example, for the high share of mining and quarrying (MOL), coke and refined petroleum (MOL), financial intermediation (mainly OTP and MKB Bank), and pharmaceuticals and chemicals (Richter Gedeon, BorsodChem and TVK) in Hungarian OFDI. The manufacturing of electrical and optical equipment is the second most important

[148] Dilek Aykut and Andrea Goldstein, "Developing country multinationals: south-south investment comes of age," *OECD Development Centre Working Paper* No. 257 (Paris: OECD, 2006), mimeo.

[149] This is in line with the findings of gravity models on bilateral FDI in the region. See, for example, Christina Borrmann, Rolf Jungnickel and Dietmar Keller, "What gravity models can tell us about the position of German FDI in Central and Eastern Europe," HWWA Discussion Paper No. 328 (Hamburg: Hamburg Institute of International Economics, 2005), mimeo.

industry within manufacturing, which may be connected to the foreign activities of Samsung[150] and Videoton. The largest cross-border acquisitions are also carried out by these few dominating firms, mainly in neighboring or geographically close countries, and often related to privatization deals (annex table 6), in which Hungarian MNEs benefit from first mover advantages. By the time privatization had started in neighboring countries, some Hungarian firms such as MOL and OTP had already become private firms, ready to invest abroad. The same large Hungarian MNEs, as well as the real estate firm TriGránit, are also the most active ones in key foreign greenfield projects (annex table 7). Hungarian companies invest abroad predominantly with a market-seeking motive. There are a few efficiency-seeking MNEs, such as the electronics firm Videoton, which has acquired a company in Bulgaria with the aim of transferring there its most labor intensive activities.

At the other extreme, there are also SMEs investing abroad, some of them in faraway places (they could be called "born globals").[151] They establish offices on more developed markets (for example in Western Europe or in the United States) in order to be closer to their main customers – and competitors. In Hungary, such companies operate mainly in high-technology industries, such as information technology, software or medical instruments. For example, the 3DHistech company, a medical instruments producer, set up small affiliates in Germany and in the United States. Thales Nanotechnologies, a biotechnology firm, established offices in the United Kingdom and in the United States. However, this type of OFDI represents only a minor share of the total.[152]

Similarly to MNEs from other new EU member countries, Hungarian MNEs can be categorized into four main groups: "genuine", "foreign-controlled", "virtually foreign-controlled", and "formally headquartered elsewhere":

- "Genuine" MNEs' ownership is mostly local and their management is Hungarian. Examples include Jászplasztik, a first tier supplier of Samsung and Electrolux, which established an affiliate in Galanta, Slovakia, following Samsung's investment there.
- "Foreign-controlled" MNEs[153] are foreign affiliates located in Hungary that, for various reasons, have invested abroad from their Hungarian base. Examples include Magyar Telekom (majority-owned by Deutsche Telekom) or the Dunapack paper mill (controlled by Austria's Mosburger). The FDI carried out by these firms can be called "indirect investment."[154]
- In "virtually foreign-controlled" Hungarian MNEs, foreign *portfolio* investors hold the majority of shares, but do not have a controlling stake. As a result, the

[150] Samsung (Republic of Korea) realized its Slovakian investment partly through its Hungarian affiliate.

[151] Tage Koed Madsen and Per Servais, "The internationalization of born globals: an evolutionary process?," *International Business Review,* vol. 6, no. 6 (1997), pp. 561–83.

[152] Katalin Antalóczy and Andrea Éltető, "Outward foreign direct investment from Hungary: trends, motivations and effects," in Marjan Svetlicic and Matija Rojec, eds., *Facilitating Transition by Internalization: Outward Direct Investment from Central European Economics in Transition* (Aldershot: Ashgate, 2003), pp. 155–74.

[153] Eric Rugraff, "Strengths and weaknesses of the outward FDI paths of the central European countries," *Post-Communist Economies,* vol. 22, no.1 (2010), pp. 1–17.

[154] Wilfried Altzinger, Christian Bellak, Andrea Jaklic, and Matija Rojec, "Direct versus indirect foreign investment from transition economies: Is there a difference in parent company/home country impact?," in Svetlicic and Rojec, *op cit.*, pp. 91–110; Wladimir Andreff, "The new multinational corporations from transition countries," *Economic Systems*, vol. 26, no. 4 (2002), pp. 371–79.

management is Hungarian, and all decisions are taken in Hungary. This group of MNEs deserves particular attention because, in the literature, it is assumed to be part of the foreign-controlled group, while, in substance, it is closer to genuine MNEs. We call FDI realized abroad by these firms "virtual" indirect investment, as opposed to the real indirect investment of firms such as Magyar Telekom. Out of the list of the most important investor companies, MOL, OTP and Richter (annex table 5), as well as Synergon (not in the table), belong to this category. The dispersion of ownership is a result of the fact that these firms were privatized through the Budapest Stock Exchange. As one example, the majority (more than 65%) of OTP Bank's shares were owned by foreigners in 2009, although none of them alone controlled more than 10%, and only three of them (Artio Global Management of United States, 9%; three Russian private persons, 8%; and Groupama, France, 8%) exceeded 5%. Domestic investors owned together 22%, the Government 0.5%, and the management 11%.[155] Decisions of strategic importance, including those about foreign acquisitions, are taken by the Hungarian management.

- The most salient example of Hungarian MNEs whose formal headquarters are located elsewhere but whose management is mostly Hungarian, and whose decisions are taken in the Hungarian base, is the real estate firm TriGránit (registered officially in Budapest but majority-owned by a Cyprus-based parent company owned by a Hungarian private person). For analytical purposes, these companies have to be considered Hungarian MNEs, although it is nearly impossible to include them in the statistics, given methodological difficulties such as the accounting of domestic versus foreign activities.

Effects of the current global crisis

The global crisis affected Hungarian OFDI relatively quickly, given the structural weaknesses of the Hungarian economy. In 2008, OFDI flows declined by 56%, followed by a modest recovery (5%) in 2009 (annex table 2).

The drop in 2008 was related to a halt in large cross-border M&A deals that year. In most other countries of the region (except Estonia), the decline in FDI outflows did not start before 2009. However, the decline in Hungarian OFDI was not exceptional by global standards. In 2008, the decline in outflows was larger than the world average (-13%), but its recovery in 2009 was going against a global decline of about 39%. As for OFDI stock, it grew till 2008 (annex table 1), and declined by 3% in 2009 as Hungarian assets abroad devalued. This depreciation of the OFDI stock was relatively mild in international comparison (annex table 1).

The relative resilience of OFDI is surprising given the sharp drop in Hungarian GDP (-6.3% in 2009, caused mostly by a 17.7% drop in manufacturing production)[156] and the contraction in the market value of Hungarian firms. In 2008, the index of the Budapest Stock Exchange (BUX), where most of the large Hungarian companies are quoted, contracted by 53%, although it recovered to 82% of the January 2008 value in 2009.[157] The decrease in home-country revenues reduced the scope of equity and

[155] https://www.otpbank.hu/portal/en/IR_Ownership_structure.
[156] According to data from the Central Statistical Office (www.ksh.hu).
[157] According to data from the Budapest Stock Exchanges (www.bse.hu).

other investments by Hungarian MNEs, while lower host-country revenues were translated into smaller reinvested earnings.

Anecdotal evidence shows that certain Hungarian MNEs had to postpone or reduce projects due to difficulties of financing, as was the case with TriGránit in Zagreb, Croatia. The crisis and the drying-up of financial resources also revealed the vulnerability of Hungarian MNEs to takeovers or take-over attempts by MNEs from other countries. To date, the most important attempt has been undertaken by Russia's oil firm Surgutneftegaz, which acquired 26% of the shares of MOL from Austria's OMV in March 2009. So far, MOL has prevented a take-over by invoking a company rule according to which no shareholder can have more than 10% voting rights, irrespective of the amount of shares it owns, and administrative difficulties in properly registering the new Russian shareholder for the company's general assembly.[158] However, the case is still abeyance at the moment of writing this analysis.

The policy scene

Being a EU member, Hungary's policies are framed by the Lisbon Treaty and the treaties concluded by the EU, as well as by the BITs signed by the Hungarian government (57 in force in 2009).[159] These cover all major target economies of Hungarian OFDI. There are also government agencies and institutes offering assistance to OFDI. The institutional framework has undergone changes over time; however, the three main areas of support (subsidized information and consultancy services; investment finance and insurance; lobbying abroad) have remained the same. Information and consultancy services are provided (and business meetings are organized) by the Hungarian Investment and Trade Development Agency ITDH (an integrated agency, promoting IFDI and OFDI, exports and SMEs), and some chambers of commerce (national, regional, bilateral). Finance and insurance is provided by the state-owned Corvinus Group and by the Hungarian Development Bank. Both of these agencies support mostly OFDI by Hungarian SMEs. Corvinus also maintains an information system on investment opportunities in Hungary and abroad, in and outside the EU. In addition, Hungarian MNEs and government agencies carry out some lobbying abroad, especially related to privatization deals, although no formal institution exists in that area.

According to company interviews, the first two services, namely subsidized information and consultancy services and investment finance and insurance, are mainly used by SME foreign investors, while large investors are more likely to rely on lobbying. The latter consider that the lobbying activity of the Hungarian Government and its foreign representatives is weaker than that of countries with a longer history of OFDI. This is especially problematic in the case of large privatization deals, which are particularly important as a mode of entry for large Hungarian investors abroad.[160]

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[158] Kalman Kalotay, "The political aspect of foreign direct investment: The case of the Hungarian oil firm MOL," *The Journal of World Investment & Trade,* vol. 11, no. 1 (2010), pp. 79–90.

[159] See www1.pm.gov.hu/web/home.nsf/portalarticles/16E5406F25E730F2C1256E1A004373A4?OpenDocument.

[160] ICEG European Centre, "Background studies for the update of Hungarian External Economic Strategy" (2007) (www.icegec.hu/publications).

Conclusions and Outlook

So far, Hungary's strategy of international competitiveness has been based on IFDI rather than on OFDI. However, over time, the latter has gained in importance, despite the financial crisis that has hit Hungary hard. The future of Hungarian OFDI is difficult to predict as the era of uncertainty is far from being over at the time of writing this *Profile* (June 2010). In addition, with a change in government (and potentially government policies) in Hungary, approaches toward Hungarian MNEs may change. One of the lessons drawn from Hungarian OFDI strategies is that foreign acquisitions are an imperative to prevent hostile takeovers by competitors. Thus, Hungarian MNEs will most probably continue to increase their presence in geographically close countries, reaping especially the benefits from privatization. Moreover, some indigenous firms, those that weathered the crisis well and are increasingly sensitive to wage costs, are expected to transfer in the future their most labor-intensive activities to nearby countries. These can be mainly SMEs in the labor-cost sensitive metal, plastic and machinery industries. High-technology SMEs could also be important sources for potential OFDI, though the volume of their transactions is expected to remain small.

Additional readings

Antalóczy, Katalin and Andrea Éltető, "Outward foreign direct investment from Hungary: trends, motivations and effects," in Marjan Svetlicic and Matija Rojec, eds., *Facilitating Transition by Internalization. Outward Direct Investment from Central European Economics in Transition* (Aldershot: Ashgate, 2003), pp. 155–174.

Antalóczy, Katalin and Magdolna Sass, "Emerging multinationals: the case of Hungary," Conference on emerging multinationals: Outward Foreign Direct Investment from Emerging and Developing Economies, Copenhagen Business School, Copenhagen, Denmark, October 9–10, 2008 (available at: http://gdex.dk/ofdi/7%20Antaloczy%20Katalin.pdf).

Kalotay, Kalman, "The political aspect of foreign direct investment: the case of the Hungarian oil firm MOL," *The Journal of World Investment & Trade,* vol. 11, no. 1 (2010), pp. 79–90.

Rugraff, Eric, "Strengths and weaknesses of the outward FDI paths of the Central European countries," *Post-Communist Economies,* vol. 11, no. 1 (2010), pp. 1–17.

Sass, Magdolna, "FDI in Hungary: the first mover's advantage and disadvantage," *European Investment Bank Papers,* vol. 9, no. 2 (2003), pp. 62–90.

Statistical annex

Annex table 1. Hungary: outward FDI stock, selected years

Economy	Outward FDI stock (US$ million)						Ratio of outward FDI stock to GDP (Percentage)				
	1995	2000	2005	2007	2008	2009	1995	2000	2005	2007	2008
Hungary	278	1 280	7 810	17 596	19 979	19 451	0.6	2.7	7.1	12.7	13.0
Memorandum: comparator economies											
Czech Republic	345	738	3 610	8 557	12 531	14 348	0.6	1.3	2.9	4.9	5.8
Estonia	68	259	1 940	6 174	6 657	6 534	1.8	4.6	14.1	29.5	28.7
Poland	539	1 018	6 277	21 201	22 560	26 211	0.4	0.6	2.1	5.0	4.3
Russian Federation	3 346	20 141	146 679	370 161	202 837	…	0.8	7.8	19.2	28.9	12.0
Slovenia	727	768	3 290	7 197	8 650	…	3.5	4.5	9.2	15.3	15.9

Source: Authors' calculation, based on UNCTAD's FDI/TNC database (available at: http//stats.unctad.org/fdi/) and national statistics.

Annex table 1a. Hungary: inward and outward FDI stock, selected years

Item	1990	1995	2000	2005	2007	2008	2009
Inward FDI stock (US$ million)	570	11 304	22 870	61 970	100 335	89 717	92 432
Outward FDI stock (US$ million)	159	278	1 280	7 810	17 596	19 979	19 451
Ratio of outward to inward FDI stock (%)	27.9	2.5	5.6	12.6	17.5	22.3	21.0

Source: Authors' calculation, based on UNCTAD's FDI/TNC database (available at: http://stats.unctad.org/fdi/) and national statistics.

Annex table 2. Hungary: outward FDI flows, 2000–2009 (US$ million)

Economy	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009[a]
Hungary	620	368	278	1 643	1 119	2 178	3 874	3 737	1 661	1 740
Memorandum: comparator economies										
Czech Republic	43	165	207	206	1014	-19	1 467	1 619	4 332	1 340
Estonia	63	200	132	156	268	688	1 112	1 737	1 071	1 487
Poland	16	-90	230	305	955	3 358	9 149	5 664	3 102	2 924
Russian Federation	3 177	2 533	3 533	9 727	13 782	12 767	23 151	45 916	56 091	46 057
Slovenia	66	144	156	475	548	641	862	1 805	1 440	871

Source: Authors' calculation, based on the UNCTAD FDI/TNC database (available at: http://stats.unctad.org/fdi/) and national statistics.

[a] Preliminary estimates.

Annex table 3. Hungary: sectoral distribution of outward FDI stock, 2000 and 2008 (Percent of total)

Sector/industry	2000	2008	Sector/industry	2000	2008
Agriculture, forestry and fishing	0.00	0.03	**Electricity, gas and water**	0.16	0.06
Mining and quarrying	1.89	6.88	**Construction**	0.28	0.31
Manufacturing	12.99	37.54	**Services**	79.98	52.70
Food, beverages and tobacco	1.50	0.15	Wholesale, retail and repair	19.57	6.48
Textile and leather	1.12	0.09	Hotels and restaurants	1.55	0.98
Wood, pulp, paper and publishing	1.13	0.53	Transport and telecom	1.29	0.97
Coke, refined petroleum and nuclear fuel	0.00	17.42	Financial intermediation	45.65	23.26
Chemicals	2.46	2.05	Real estate	0.31	0.20
Rubber and plastic	1.43	0.28	Computer services	0.04	0.04
Other non-metallic minerals	2.27	1.39	Business services	8.95	20.30
Metals	0.01	0.06	Other services	0.01	0.32
Machinery and equipment n.e.c.	0.02	0.03	**Acquisition of real estate and OFDI by households**	3.51	2.44
Electrical and optical equipment	0.18	14.57			
Transport equipment	2.84	0.84	**Not identified**	1.18	0.05
Furniture and manufacturing n.e.c.	0.01	0.12	**Total**	100.00	100.00

Source: Authors' calculation, based on data from the National Bank of Hungary.

Annex table 4. Hungary: geographical distribution of outward FDI stock, 2000 and 2008 (Percent of total)

	2000	2008	Region/economy	2000	2008
Total	100.00	100.00	***Other Europe***	3.40	29.15
Europe	87.61	74.56	Croatia	1.33	8.31
European Union	83.66	45.16	Montenegro	..	1.35
Austria	6.73	0.38	Russian Federation	0.50	1.76
Bulgaria	0.31	6.16	Serbia	..	3.15
Cyprus	6.95	3.78	Switzerland	0.35	6.93
Czech Republic	5.42	1.58	TFYR of Macedonia	0.00	3.94
Denmark	10.24	0.03	Turkey	0.00	0.81
France	0.11	0.06	Ukraine	1.22	2.90
Germany	2.90	0.39	**North America**	4.84	1.36
Ireland	2.80	0.01	Canada	0.01	1.03
Italy	0.10	0.78	United States	4.83	0.33
Luxemburg	0.11	4.29	**Central America**	0.10	7.20
Netherlands	32.01	1.53	**Asia**	0.26	14.61
Poland	1.08	1.34	Republic of Korea	0.00	14.33
Romania	4.96	4.11	China	0.10	0.02
Slovakia	8.73	20.25	India	0.07	0.05
Slovenia	0.37	0.26	Japan	0.03	0.01
Spain	0.04	0.13	**Africa**	0.13	0.00
United Kingdom	0.80	0.08	**Not identified**	7.00	2.36

Source: Authors' calculation, based on data from the National Bank of Hungary.

Annex table 5. Hungary: the top 10 MNEs, ranked by foreign assets, 2008
(US$ million)

Rank	Company	Industry	Host economies of OFDI	Foreign assets[a]
1	MOL	Oil and gas	Austria, Bosnia-Herzegovina, Croatia, Cyprus, Czech Republic, Germany, Italy, Jersey, Kazakhstan, Oman, Poland, Romania, Russian Federation, Serbia, Slovakia, Slovenia, Syria, The Netherlands, Ukraine, United Kingdom, Yemen	4 800
2	OTP Bank	Banking	Austria, Bulgaria, Croatia, Cyprus, Luxemburg, Montenegro, Romania, Russian Federation, Serbia, Slovakia, The Netherlands, Ukraine, United Kingdom	2 500
3	Magyar Telekom (Deutsche Telekom Group)	Telecom	Bulgaria, TFYR of Macedonia, Montenegro, Romania, Ukraine	1 200
4	MKB Bank (Bayern LB Group)	Banking	Bulgaria, Romania	250
5	Gedeon Richter	Pharmaceuticals	Armenia, Germany, India, Italy, Japan, Republic of Moldova, Poland, Romania, Russian Federation, Ukraine	192
6	Danubius Hotels	Hotels	Czech Republic, Romania, Slovakia	171
7	BorsodChem	Chemicals	Czech Republic, Italy, Poland	100
8	Dunapack (Prinzhorn Holding)	Paper	Bulgaria, Croatia, Lithuania, Poland, Romania, Slovakia, Ukraine	75
9	Samsung Hungary	Electronics	Slovakia	30
10	Videoton	Electronics	Bulgaria	25

Source: Authors' estimates based on balance sheets of the companies and values of individual M&A transactions.
[a] Estimated values.
Note: TriGránit is not included.

Annex table 6. Hungary: main M&A deals, by outward investing firm, 1998–2009 (US$ million)

Acquiring company	Target company	Target industry	Target economy	Year	Transaction value (US$ million)	Shares acquired (%)
MOL	Italiana Energia e Servizi SpA	Oil and gas	Italy	2007	1 097.0	100.0
OTP Bank	Raiffeisenbank Ukraine	Banking	Ukraine	2006	832.7	100.0
MOL	INA Industrija Nafte	Oil and gas	Croatia	2003	508.1	25.0
OTP Bank	Investsberbank	Banking	Russian Federation	2006	477.0	96.4
OTP Bank	DSK Bank	Banking	Bulgaria	2003	358.6	100.0
MOL	Slovnaft	Oil and gas	Slovakia	2003	329.7	31.6
Magyar Telekom (Deutsche Telekom Group)	Macedonian Telecom (Maktel)	Telecom	TFYR of Macedonia	2001	323.5	51.0
OTP Bank	Nova Banka	Banking	Croatia	2005	316.7	95.6
MOL	Slovnaft	Oil and gas	Slovakia	2000	262.0	36.2
MOL	Slovnaft	Oil and gas	Slovakia	2004	242.3	28.5
OTP Bank	Kulska Banka	Banking	Serbia	2006	151.8	67.0
Magyar Telekom (Deutsche	Telecom Montenegro	Telecom	Montenegro	2005	150.7	51.0
Wizz Air	Wizzair Ukraine	Airlines	Ukraine	2007	137.0	100.0
OTP Bank	Crnogorska Komercijalna Banka	Banking	Montenegro	2006	132.0	100.0
Danubius Hotels	Ramada Plaza Regents Park Hotel	Hotels	United Kingdom	2005	112.2	100.0
MKB Bank (Bayern LB Group)	Unionbank	Bank	Bulgaria	2006	85.5	..
BorsodChem	Moravské Chemické Závody	Chemicals	Czech Republic	2000	54.9	97.5
MOL	Pearl Petroleum Company Ltd.	Oil and gas	Iraq	2009	54.1	10.0
OTP Bank	Banca Comerciala Robank	Banking	Romania	2004	47.5	100.0
Gedeon Richter	Polfa Grodzisk	Pharmaceuticals	Poland	2008	43.0	36.8
OTP Bank	Zepter Banka	Banking	Serbia	2006	41.3	75.1
OTP Bank	Donskoy Narodny Bank	Banking	Russian Federation	2008	41.0	100.0
Gedeon Richter	Polfa Grodzisk	Pharmaceuticals	Poland	2002	30.1	51.0

Magyar Telekom (Deutsche Telekom Group)	Telecom Montenegro	Telecom	Montenegro	2005	29.6	21.9
Waberer	Somitco Trans	Transport	Romania	2008	29.5	100.0
Danubius Hotels	Health Spa Piestany	Hotels	Slovakia	2002	27.0	..
TVK (MOL Group)	Hamburger Unterland	Chemicals	Austria	1998	27.0	74.0
OTP Bank	Niska Banka AD	Banking	Serbia	2006	16.9	89.4
Danubius Hotels	Lécebné Lázne Márianské Lázne	Hotels	Czech Republic	2000	15.5	65.0
OTP Bank	Investicni a Rozvojova Banka	Banking	Slovakia	2002	14.6	92.6

Source: Authors' collection and estimation, based on company reports and Thomson ONE Banker, Thomson Reuters.

Annex table 7. Hungary: the top 10 greenfield projects, by outward investing firm, in 2007–2009 (US$ million)

Year	Investing company	Target industry	Target economy	Investment
2009	TriGránit	Real estate	Slovakia	2 230
2009	MOL	Oil and gas	Croatia	524 [a]
2009	WIZZ Air	Air transport	Czech Republic	128 [a]
2009	Omninvest	Biotechnology	Uzbekistan	70 [a]
2009	WIZZ Air	Air transport	Switzerland	61 [a]
2009	Genesis Energy Befektetési Nyrt.	Electronics / renewable energy	Spain	58 [a]
2009	MOL	Oil and gas	Pakistan	40
2009	CIG Central European Insurance	Financial services	Romania	23 [a]
2009	DKG East	Machinery	Qatar	18 [a]
2009	Domoinvest	Pharmaceuticals	Serbia	14 [a]
2008	TriGránit	Real estate	Romania	1 573
2008	TriGránit	Real estate	Poland	782
2008	MOL	Oil and gas	Slovakia	450 [a]
2008	TriGránit	Real estate	Croatia	311
2008	TriGránit	Real estate	Russian Federation	289 [a]
2008	TriGránit	Real estate	Russian Federation	289 [a]
2008	Brixxon	Automotive	Austria	236 [a]
2008	System Consulting Zrt.	Renewable energy	Russian Federation	197 [a]
2008	WIZZ Air	Air transport	Romania	150
2008	TriGránit	Real estate	Slovenia	145 [a]
2007	TriGránit	Real estate	Russian Federation	1 000
2007	Libri	Bookshops	Romania	194
2007	TriGránit	Real estate	Romania	188
2007	TriGránit	Real estate	Poland	130 [a]
2007	TriGránit	Entertainment	Russian Federation	40 [a]
2007	MOL	Oil and gas	Serbia	39 [a]
2007	OTP Bank	Banking	Ukraine	36 [a]
2007	OTP Bank	Banking	Russian Federation	36 [a]
2007	OTP Bank	Banking	Netherlands	25 [a]
2007	Cerbona	Food	Romania	24 [a]

Source: Authors' collection and estimation, based on information from the *fDi Intelligence*, a service from the *Financial Times Ltd*.
[a] Estimate made by *fDi Intelligence*.

Annex table 7. Germany: main greenfield projects, by outward investing firm, 2007-2009 (US$ million)

Year	Company name	Destination economy	Investment	Sector	Business activity
2009	RWE	Netherlands	2,857.6	Coal, oil and natural gas	Electricity
2009	E.on	Equatorial Guinea	1586.0 [a]	Coal, oil and natural gas	Manufacturing
2009	Volkswagen	Spain	1068.7 [a]	Automotive OEM	Manufacturing
2009	Daimler AG	India	1,014.0	Automotive OEM	Manufacturing
2009	Wacker	USA	1,000.0	Chemicals	Manufacturing
2009	Mühlbauer	USA	986.1 [a]	Semiconductors	Manufacturing
2009	BASF	Quatar	899.9 [a]	Chemicals	Manufacturing
2008	ThyssenKrupp (TK)	Brazil	5,200.0	Metals	Manufacturing
2008	Q-Cells AG	Mexico	3,500.0	Electronic components	Manufacturing
2008	RWE	Poland	2,320.0	Coal, oil and natural gas	Electricity
2008	MAN	Russia	2,058.0	Wood products	Manufacturing
2008	Marquard & Bahls	USA	1,800.0	Coal, oil and natural gas	Logistics & distribution
2008	Daimler AG	Hungary	1,239.6	Automotive OEM	Manufacturing
2008	WPD	France	1,200.0	Alternative/renewable energy	Electricity
2007	E.on	Turkey	3,167.7	Coal, oil and natural gas	Manufacturing
2007	Infineon Technologies	Singapore	2,703.0	Semiconductors	Manufacturing
2007	E.On	Belgium	2,197.0	Coal, oil and natural gas	Electricity
2007	Conergy	Australia	1,800.0	Alternative/renewable energy	Electricity
2007	ECE Projekt Management	Romania	1,469.0	Real Estate	Construction
2007	Volkswagen	USA	1,000.0	Automotive OEM	Manufacturing
2007	E.On	Russia	1,000.0	Coal, oil and natural gas	Electricity
2007	Wacker	Singapore	1,000.0	Electronic components	Manufacturing

Source: fDi Intelligence, a service from the Financial Times Ltd.

[a] Estimated.

Chapter 7 – Ireland

Inward FDI and its policy context, 2010

Louis Brennan and Rakhi Verma

Ireland has one of the highest ratios of IFDI stock to GDP among the OECD countries. The surge in IFDI from the 1990s onwards is regarded as one of the factors that contributed to the "Celtic Tiger" era of rapid economic growth, rising living standards and full employment. However, stocks of IFDI fell in four of the six years from 2004 to 2009, largely due to outflows of capital from foreign affiliates in Ireland to their parent companies abroad. More recent data show an increase in IFDI stock in 2009, which continued into the first quarter of 2010. This rise is in large part due to the scale of reinvested earnings on the part of foreign affiliates in Ireland and the growing success in attracting knowledge intensive investment, while the lowering of the cost base since the advent of the crisis in Ireland has enhanced its attractiveness as an investment location. Changes in business taxation that have taken effect in 2010 have been designed to improve Ireland's attractiveness to knowledge intensive industries and as a location for company regional headquarters. The Irish Government is committed to maintaining the low rate of corporate taxation of 12.5%. While the current crisis has had the paradoxical effect of increasing Ireland's attractiveness as a location for FDI, future FDI prospects will also be enhanced by Ireland demonstrating a capacity to overcome its present difficulties.

Trends and developments

Country-level developments

Since the opening up of Ireland's economy in the 1960s, Ireland has embraced FDI as an integral part of its strategy of economic development. Its efforts to attract such investment have been highly successful. According to the OECD Factbook 2010, the country has the fifth highest ratio of IFDI stock to GDP among the OECD countries, and the highest ratio of employment in foreign affiliates in the manufacturing and services sectors.[161] The impact of IFDI on Ireland's economy is highly significant, with foreign owned firms accounting for just under 90% of the country's exports in 2008 and 73% of business expenditures on R&D in 2007.[162]

The country's IFDI stock grew by just over 50% between 2000 and 2009 (annex table 1). Ireland's ratio of IFDI stock to GDP increased sharply in the later years of the 1990s and into the early years of the past decade, peaking in 2002 at 149%. Since 2003, the ratio has turned downward, with the exceptions of 2007 and 2009, when it rose again. For 2009, the ratio stood at 85% (annex table 1).[163]

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[161] OECD, **OECD Factbook 2010: Economic, Environmental and Social Statistics** (Paris: OECD, 2010), pp. 79 and 83, available at: www.oecd.org.

[162] Forfas Annual Competitiveness Report, available at: www.forfas.ie/media/NCC100723-acr_bip_2010.pdf.

[163] UNCTAD's FDI/TNC database, available at: http://stats.unctad.org/fdi/.

Over the period 1997-1999, the average value of annual FDI inflows was US$ 9.7 billion, while over the period 2007-2009, it was US$ 9.9 billion (annex table 2).[3] A notable feature of Ireland's IFDI position is that, over the time period 2004-2009, net inflows were negative in four out of that six-year period. This indicates that inter-affiliate loan advances and repayments from Ireland-based foreign affiliates exceeded inward equity flows and reinvested earnings. This phenomenon may be partly explained by changes in the US tax code reducing taxes on repatriated profits from affiliates abroad. Following the American Jobs Creation Act of 2004 that taxed foreign profits at a rate of 5.25% compared to the regular rate of 35%, over 800 US corporations repatriated US$ 362 billion in foreign profits.[164] These were paid by their foreign affiliates as dividends. Of that amount, US$ 312 billion were deemed to be eligible for the tax break, giving those companies total tax deductions of US$ 265 billion claimed from 2004 through 2006. Almost a third of the amount repatriated was accounted for by companies in the pharmaceutical and medical manufacturing sectors, both heavily invested in Ireland. In the case of Ireland's chemicals sector (which includes pharmaceuticals at the level of secondary data aggregation considered), the IFDI stock fell from US$ 66 billion in 2003 to US$ 16 billion in 2006 (annex table 3). Given that Ireland was found to be world's most profitable foreign location for US companies in 2002,[165] it would be surprising if payment of dividends by US affiliates to their parent firms did not play a role in the reduction in Ireland's IFDI stock over the period 2004 to 2006. The rate of return on investment for US FDI in Ireland continues to be one of the highest in the world, exceeded only by that in Hungary in 2009.[166] It is also important to note that Irish data on FDI usually differentiate between FDI coming into Dublin's International Financial Services Centre (IFSC) and non-IFSC FDI. IFSC FDI is associated with financial intermediation by international banks, and is very different in terms of the effect on the local economy than traditional FDI; it is also volatile in its year-to-year movements (annex table 3). This volatility contributes to the fluctuations in Ireland's overall IFDI position.

As a result of these negative flows, Ireland's IFDI stock fell from a high of US$ 223 billion in 2003 to a level of US$ 193 billion in 2009. A further notable feature of the country's FDI flows is the extent to which these have benefited from reinvested earnings in recent years. Ireland continues to perform very well in terms of attracting IFDI. Ireland was ranked eleventh out of 141 countries in UNCTAD's 2009 IFDI performance index.[167] The National Irish Bank/fDi Intelligence Inward Investment Performance Monitor reported that Ireland attracted 0.7% of global FDI flows (based on the number of projects won, capital investment and the number of jobs created) in 2009 – a proportion larger than its 0.3% share of global GDP.[168] Likewise, Ireland's share of IFDI among the EU-27 was almost 6.9% – well in excess of its 1% share of the EU economy.[169] The Irish Industrial Development Authority (IDA) - the state agency responsible for attracting FDI to Ireland - had already in the first half of 2010 secured 63 new investments, of which 20 were from companies setting up operations in Ireland for the first time, 22 were expansion investments from existing client

[164] *New York Times*, June 24, 2008.
[165] Martin Sullivan, "Data show dramatic shift of profits to tax havens," *Tax Notes*, September 13, 2004, pp. 1190–1200.
[166] Forfas Annual Competitiveness Report, op. cit.
[167] UNCTAD, *World Investment Report 2010: Investing in a Low-Carbon Economy* (Geneva: United Nations, 2010), Country Fact Sheet: Ireland, p. 2.
[168] National Irish Bank, *Press release*, February 24, 2010.
[169] UNCTAD, op. cit., p. 167, annex table 1.

companies and 21 of the investments were in R&D.[170] IDA attributes this success to a number of factors, both external and internal. These include the growth in the US technology sector, growing trends in clean technology, an improvement in Ireland's competitiveness, currency movements, and the overall global FDI recovery, combined with Ireland's excellent corporate tax regime, 171 talent, track record, 172 and technology capability.

Unlike in the 1980s and 1990s, Ireland is no longer a low-cost location. This was starkly demonstrated in early 2009 with the decision by Dell to close its manufacturing operations in Ireland while retaining its higher value functions. With its educated and flexible labor force, Ireland has increasingly attracted higher value-added, knowledge-intensive activities that are in many cases research and development and innovation (R&D&I)-driven.[173] For example, in 2008, 43% of FDI investments supported by the IDA were in R&D. This shift in the nature of FDI from being lower-value, employment-intensive to being more higher-value knowledge-intensive is the result of a deliberately evolving strategy on the part of the Government and its agencies that involves the scanning of the horizons of enterprise and the focusing on, and securing FDI in, new technologies, innovative business models and new markets. These developments are mirrored in the data for FDI stock: the share of manufacturing in the FDI stock has fallen from 45% in 2003 to 39% in 2008, while that of the services sector rose from 56% to 61% (annex table 3). Within the services sector, the finance and insurance industries and other business activities have tended to account for the bulk of IFDI stock. Along with the availability of an educated workforce, low taxation, light touch regulation, and ease and speed of doing business have been major factors in attracting IFDI in the financial sector. Such investment has mostly encompassed such activities as funds administration, treasury management, asset financing, and shared services and other back-office activities that have largely been unscathed by the crisis. However, since Ireland also served as a center for "shadow banking" a number of players have exited since the onset of the crisis. The other impact of the crisis on the financial sector from the perspective of IFDI has been the recent exit of some foreign players from the domestic banking sector, such as HBOS and BNP Paribas Fortis.

To date, virtually all of Ireland's IFDI stock has emanated from the developed world, with the major economies of the European Union (Netherlands, UK, Germany, Italy, France), along with Luxembourg and Switzerland, accounting for the total emanating from Europe (83% in 2008); the United States and Canada (and to a much lesser extent Japan) accounted for most of the remainder (16% in 2008) (annex table 4).

[170] Revealed by the Minister for Enterprise, Trade and Innovation, Batt O'Keeffe, TD, Ireland, at a media briefing at IDA headquarters in Dublin, on July 14, 2010. *Irish Examiner*, July 15, 2010.

[171] Ireland is committed to maintaining its 12.5% corporation tax rate; the corporation tax system is simple and transparent, and income taxes are relatively low. More information on taxes is available at: www.revenue.ie.

[172] Ireland is ranked third in Europe (seventh in the world) by the World Bank in terms of ease of doing business (World Bank, *Doing Business 2010*, available at: www.doingbusiness.org). Ease of paying taxes and starting a business, as well as investor protection, are some areas in which Ireland scores especially high.

[173] R&D&I is defined to include the setting up of a dedicated center to support either corporate research or an innovation agenda, through a stand-alone facility in Ireland, an investment in R&D&I that is co-dependent on a substantial collaborative engagement with an Irish or international academic institution and/or with a MNE or indigenous Irish company, R&D&I done at a manufacturing or service delivery site that improves the manufacturing or service delivery process, or R&D&I investments through which the outputs will be developed and produced in Ireland for export markets.

However, it should be noted that the data in annex table 4 only correspond with the immediate investment source country; it does not necessarily equate to the ultimate investment source country. Some 1,000 MNEs,[174] of which some 60% are from the US,[175] have chosen Ireland as their European base. A key issue that arises in relation to IFDI is its sustainability. One indicator of FDI sustainability of foreign affiliates is the extent to which they are successful in attracting further investment in the form of new mandates. In a recent survey[176] of MNEs in Ireland, three out of four foreign affiliates stated that they had tried (or were currently trying) to secure new mandates. Sixty percent of those affiliates that had vied for new mandates had secured them.

The corporate players

Ireland has been successful in attracting investment in information and communications technology (ICT), life sciences, financial services, and globally traded business, including digital media, engineering, consumer brands, and international services. This is the result of a strategy that has focused on the three key areas of high-value manufacturing, global business services and R&D&I.[177] Ireland now hosts affiliates from many of the leading global companies (annex table 5) and hosts operations from 8 out of the top 10 ICT companies, 8 out of the top 10 pharmaceutical companies and 15 of the top 20 medical devices companies.[178]

The number of M&A sales peaked at 76 in 2007, declining to 41 in 2009.[179] However, the value of such sales peaked in 2001.[180] Even in 2008, which recorded the highest sales value since 2001, they were only about a third of the 2001 value. The largest deal in 2009 was the acquisition of a 18.46% share by Johnson and Johnson in Elan in the pharmaceutical sector, valued at US$ 0.8 billion, while in 2008 the largest deal was the acquisition of Airtricity by Scottish and Southern Energy for US$ 2 billion in the renewable energy sector (annex table 6). After a reduction in the number of greenfield FDI projects from 192 in 2005, the number rose again during the past two years, with 176 such projects in 2009.[181] The evidence to date suggests that a high level of activity will be sustained in 2010. Major corporate players in such industries as renewable energy, software and information technology, pharmaceuticals, and medical devices invested in greenfield projects in recent years (annex table 7).

Effects of the current global crisis

After falling sharply in 2008 and 2009, the Irish real GDP returned to growth in the first quarter of 2010, due to an impressive export performance. Ireland's GDP expanded by 2.2% relative to that of the fourth quarter of 2009, while exports grew by 6.9%. However, although exports continued their impressive growth in the second quarter, GDP declined by 1.2%. Paradoxically, Ireland's economic decline has had the effect of making it more attractive as a location for FDI. The European

[174] IDA Ireland, *Guide to Tax in Ireland, 2010*, available at: www.idaireland.com/news-media/publications/library-publications/ida-ireland-publications/IDA%20Tax%20Brochure%202010.pdf.
[175] US Government, Department of Commerce, "Doing business in Ireland, 2010", available at: www.buyusa.gov/ireland/en/irelandcountrycommercialguide2010.pdf
[176] Irish Management Institute, *Survey of MNCs in Ireland* (Dublin: Irish Management Institute, 2009).
[177] IDA Ireland, *Horizon 2020 IDA Ireland Strategy* (Dublin: IDA, 2010).
[178] IDA Ireland, available at: www.idaireland.com/news-media/press-releases/tanaiste-launches-ida-ire/.
[179] UNCTAD, *World Investment Report 2010*, op. cit., annex table 10.
[180] UNCTAD, *World Investment Report 2010*, op. cit., annex table 9.
[181] UNCTAD, *World Investment Report 2010*, op. cit., annex table 18.

Commission forecasts that the cumulative fall in Irish unit labor costs will be 9% in the period 2008-2011.[182] Relative to the EU average, this represents an improvement of 13 percentage points. While Ireland's economy contracted sharply in the past two years, it still retains many of the gains that it attained from the Celtic Tiger era, such as infrastructure and human capital. For example, Ireland has advanced from twenty-ninth on the UN Human Development Index in 1990 to fifth position, ahead of countries such as The Netherlands, Sweden, France, Switzerland, and the US in 2009. These gains taken together with the greatly reduced cost of operating in Ireland as a result of the recession should continue to ensure Ireland's attractiveness as a destination for FDI. However, given the openness of the Irish economy and the extent of its integration into the world economy, future prospects for IFDI will also be tempered by the outlook for the global economy. While tax increases are likely as a means of reducing the increased government budget deficit arising from the current crisis, there is a consensus among political parties and policy makers that Ireland's current rate of low corporate taxation must be maintained regardless of the current fiscal pressures.

The policy scene

Ireland has long used its tax system as a means of attracting FDI. Some recent changes in the business taxation system have been designed to enhance the country's attractiveness as a location for a range of knowledge-based activities and as a location for regional headquarters, by offering a scheme of tax relief for capital expenditure on intangible assets.[183] Irish tax legislation contains important measures to drive the development of Ireland as a hub for companies engaged in the ownership and development of intellectual property (IP)[184] assets.[185] Other recent changes include an increase in the R&D tax credit and the introduction of a payable credit and improvement in the tax benefits offered to senior executives and highly skilled workers who relocate to Ireland to work there for a period of time.[186]

Ireland is among the world's most competitive locations for R&D investment, according to a recent study[187] that evaluated the cost of global R&D initiatives after tax and other cost incentives in 20 countries. Ireland had an effective tax rate of 1%, making it the second most competitive of the countries evaluated. Grant aid and R&D credit can reduce the cost of investment by up to 60% of the investment costs for firms that chose to set up and establish in Ireland to carry out R&D&I.[188]

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[182] European Economy Forecast - Spring 2010 (Luxembourg, European Economy 2/2010), p. 87, available at: http://ec.europa.eu/economy_finance/publications/european_economy/2010/pdf/ee-2010-2_en.pdf.
[183] Department of Finance, Ireland, *Budget 2010: Financial Statement*, published 9th December 2009, available at: www.budget.gov.ie.
[184] IP is broadly defined and includes the acquisition of, or the license to use, patents, designs, inventions, trademarks, brands, copyrights, know how, and goodwill directly attributable to such IP.
[185] Ireland was ranked seventh out of 24 in the Global Intellectual Property Index in 2009 (Taylor Wessing Global Intellectual Property Index 2009, available at: www.taylorwessing.com/ipindex/). This was the first year Ireland was included in the index which assesses 24 leading economies for protection and enforcement of patents, trademarks, copyright and domain names.
[186] Department of Finance, Ireland, op.cit.
[187] Mazars, **Review** of **Global R&D Tax Incentives (Dublin:** Mazars, **2010)**, available at: www.mazars.ie.
[188] Deloitte & Touche, *Ireland as a Knowledge Economy* (Dublin: Deloitte and Touche, 2010), available at: www.deloitte.com/ie.

Recent legislation has been designed to enable Ireland to compete as a location with other established European holding company locations.[189] As a result, Ireland has started to emerge as an onshore location for MNEs establishing regional or global headquarters to manage the profits, functions and shareholdings associated with their international businesses. While the country offers tax advantages for holding companies, it is not, unlike some other destinations, seen as a tax haven, thus increasing the attractiveness of Ireland as a sustainable location.

Ireland has introduced new rules about transfer pricing to fall in line with OECD regulations, for both domestic and cross border transactions that will be in effect from January 1, 2011.[190] It is expected that these rules will align Ireland with best international practices, position Ireland better in intervening on behalf of companies where other jurisdictions adopt transfer pricing positions that do not accord with the arm's length principle and also enhance Ireland's capacity to influence the direction of future developments in relation to transfer pricing in international taxation.

Ireland has signed comprehensive double taxation agreements (DTTs) with 56 countries, of which 48 are in effect and the remainder awaits ratification.[191] These agreements allow for the elimination or mitigation of double taxation. Two new tax agreements with Macedonia and Malta came into effect January 1, 2010. Ireland has only one BIT; it was signed in 1997 with the Czech Republic. With the Lisbon Treaty having entered into force on December 1, 2009, the EU, rather than individual member states like Ireland is now responsible for the negotiating of international investment treaties.[192]

Conclusions and Outlook

Ireland's IFDI strategy is based on its position as one of the most innovative economies in the world - a hub of innovation, R&D and high-end manufacturing and intellectual property opportunities. Recent trends suggest that Ireland should continue to attract R&D investments. In 2009, there was a 10% increase in the number of R&D&I investments compared to 2008. R&D&I investments accounted for 49% of all investments in 2009.[193] The PricewaterhouseCoopers (PwC) 2010 CEO Pulse Survey of Ireland-based CEOs of foreign affiliates conducted at the end of May 2010 found that a quarter more of MNE CEOs are considering additional investment in Ireland compared to last year.[194] In addition, Ireland is making a concerted effort to attract IFDI from the fast growing emerging markets, to benefit from the rapidly growing levels of outward FDI from these economies.

[189] Originally signaled in Department of Enterprise, Trade and Employment submission to Commission on Taxation, available at: www.commissionontaxation.ie/submissions/Government%20Depts%20-%20Political%20Parties//F01%20-%20Dept.%20Enterprise,%20Trade%20&%20Employment.doc,May 23, 2008.
[190] Revenue Commissioners, Ireland, available at: www.revenue.ie/en/practitioner/law/finance-bill-2010/transfer-pricing.pdf.
[191] IDA Ireland*, 2010 Guide to Tax in Ireland* (Dublin: IDA, 2010).
[192] Selen Sarisoy Guerin, *Do the European Union's bilateral investment treaties matter? The way forward after Lisbon*,,CEPS Working Document No. 333, July 2010.
[193] IDA Ireland, available at: www.idaireland.com
[194] PwC, *PwC Pulse 2010: What CEOs are Saying* (Dublin: PricewaterhouseCoopers, July 2010).

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Statistical annex

Annex table 1. Ireland: Inward FDI stock 2000, 2008, 2009 (US$ billion)

Economy	2000	2008	2009
Ireland	127	168	193
IFDI stock as a percentage of GDP	132	62	85
Memorandum: comparator economies			
Belgium	n.a.	671	830
Netherlands	243	638	596
Singapore	110	326	343
UK	438	980	1125

Source: UNCTAD's FDI/TNC database, available at: http://stats.unctad.org/fdi.

Annex table 2. Ireland: Inward FDI flows, 2000-2009 (US$ billion)

Economy	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
Ireland	25	9	29	22	-10	-31	-5	24	-20	24
Memorandum: comparator economies										
Belgium	n.a.	n.a.	16	33	43	34	58	118	109	33
Netherlands	63	51	25	21	4	47	7	115	-7	26
Singapore	16	15	6	11	21	15	29	35	10	16
UK	118	52	24	16	55	176	156	186	91	45

Source: UNCTAD's FDI/TNC database, available at: http://stats.unctad.org/fdi.

Annex table 3. Ireland: distribution of inward FDI stock, by economic sector and industry, 2003-2008 (US$ billion)

Sector/industry	**2003**	**2004**	**2005**	**2006**	**2007**	**2008**
All sectors/industries	222	207	163	156	193	163
Primary						
Agriculture, farming, fishing and forestry	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Mining	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Secondary						
Manufacturing	98	89	82	45	65	63
Textiles, wearing apparel, wood, publishing and printing	14	7	8	7	12	10
Food products	5	6	5	5	6	4
Chemical products	66	60	54	16	n.a.	1
Office machinery and computers	4	4	4	4	3	4
Metal and mechanical products	0.6	0.7	1	0.4	1.2	1.2
Motor vehicles and other transport equipments	0.1	0.2	0.2	0.3	0.4	0.4
Radio, TV, communication equipments	3	4	4 .8	5	4	3.9
Services						
Total services	124	117	80	110	127	99
Transports, storage and communication	2	2	1	3	4	2
Financial intermediation	110	104	64	88	108	62
Financial intermediation, except insurance and pension funding	87	76	38	53	67	33
Monetary intermediation	24	29	31	38	55	49
Activities auxiliary to financial intermediation	3	4	3	3	1	1
Other financial intermediation	63	46	6	14	12	-15
Insurance	20	24	21	31	38	26
Computer activities	1	1	1	1	5	4
Business and management consultancies	0.2	0.7	1	1	1	3
Other business activities	n.a.	n.a.	4	5	n.a.	20

Source: OECD.*Stat Extracts*, available at: http//:stats.oecd.org.

Annex table 4. Ireland: geographical distribution of inward FDI stock, 2003-2008 (US$ billion)

Region/economy	2003	2004	2005	2006	2007	2008
World	222	207	163	156	193	163
Developed economies						
Europe	170	171	131	128	128	136
European Union	149	154	129	122	117	128
Austria	0.1	0.6	0.2	0.2	0.4	0.5
Belgium	-0.1	2.4	-0.1	-0.6	-1.3	6.6
Cyprus	n.a.	0.8	1.4	0.5	0.4	0.6
Czech Republic	-0.0	-0.1	-0.6	n.a.	-0.9	-0.7
Denmark	0.1	-0.4	-1	-0.5	-1	-0.1
Finland	0.1	.-8	-1	n.a.	-1	0.2
France	2	3	6	8	6	3
Germany	10	7	1	4	4	6
Italy	6	6	6	7	8	8
Luxembourg	21	33	34	46	42	35
Netherlands	71	70	65	37	48	42
Poland	-0.2	-0.2	n.a.	0.0	-0.2	-0.2
Portugal	0.5	0.8	1.6	1.9	1.7	1.3
Slovakia	-0.0	-0.0	-0.1	n.a.	n.a.	-0.1
Spain	-0.9	-0.9	-2	-2	-6	-0.2
Sweden	3.8	-0.6	-0.2	5.2	3.5	6.9
UK	34	31	20	15	11	16
Other European economies						
Isle of Man	0.4	-0.6	-2.1	2.7	1.3	n.a.
Jersey	n.a.	6.8	-0.2	-0.8	0.8	-1
Norway	0.1	0.7	0.2	0.1	0.4	-0.1
Switzerland	6	7	4	5	7	7
Turkey	0.1	0.1	-0.0	0.1	n.a.	n.a.
Other developed economies						
Australia	-0.7	-0.5	-0.7	0.2	-0.0	-0.2
Canada	8.7	n.a.	6.1	10.9	17	12
Japan	-0.4	1.8	3.6	3.5	1.5	1.1
New Zealand	0.0	-0.0	0.0	0.1	-0.2	-0.1
USA	30.2	14.5	13.8	7.6	29	12.3
Developing and transition economies						
China	-0.2	0.3	0.1	0.2	0.3	0.2
Hong Kong (China)	0.2	n.a	n.a.	-0.9	-0.9	-0.4
India	0.0	-	-0.1	-0.1	-0.1	-0.1
Indonesia	-0.0	-0.0	n.a.	n.a	0.0	0.0
Mexico	-1	-0.5	0.2	-0.2	-0.1	-0.3
Republic of Korea	-0.1	-0.7	-1	-2	-2	n.a.
Russian Federation	-0.0	-0.0	-0.0	-0.1	0.6	0.1
Singapore	1	1	-0.2	-0.2	0.1	0.5
Unspecified destination	-2	-2	-0.5	-3	-0.4	-10

Source: OECD.*Stat Extracts*, available at: http//:stats.oecd.org.

Annex table 5. Ireland: Principal foreign affiliates in Ireland, ranked by turnover, 2009 (US$ billion)

Rank	Name	Turnover	Industry
1	Dell	15	Manufacturer and sales of computer systems
2	Microsoft Ireland operations	13	Software manufacturer/distributions
3	Google Ireland	8	Internet search operator
4	BSC Int. Holdings Ltd (Boston Scientific)	5	Manufacturer of medical devices/ healthcare
5	Oracle Emea Ltd	5	Software manufacturer/sales
6	Tesco Ireland	3 [a]	Supermarket retail and petrol stations
7	Aryzta	4	Bakery products
8	ConocoPhillips Ireland Ltd	3	Mineral oil refining
9	Western Union International	2	Money transfer
10	Pfizer Global Supply	2	Wholesale of pharmaceutical goods
11	Forest Laboratories Holdings Ltd	2	Manufacture of basic pharmaceutical products
12	Apple Computer	2 [a, b]	Computer supply/R&D Centre
13	Diageo Ireland	2.2-2.5 [a]	Alcoholic beverages production/sales/distribution
14	Adobe Software Trading Co. Ltd	2	Software consultancy and supply

Source: *The Irish Times* Top 1000 Companies Magazine, June 30, 2010.
[a] Estimated accounts.
[b] Estimated based on global turnover divided by global employees multiplied by Irish employees.

Annex table 6. Ireland: main M&A deals, by inward investing firm, 2007-2009

Year	Acquiring company	Home economy	Target Company	Target industry	Transaction value (US$ billion)	Shares acquired (%)
2009	Johnson & Johnson	USA	Elan Corp PLC	Pharmaceuticals	0.8	18.46
2009	Endesa SA	Spain	Electricity Supply Board-Power	Energy Supply	0.7	20
2009	Biovail Corp	Canada	Cambridge Laboratories	Chemicals	0.2	100
2009	Carbon Acquisition Co	UK	EcoSecurities Group PLC	Financial services	0.1	100
2009	Star Energy Group PLC	UK	Marathon Oil Ireland Ltd	Oil &gas	0.1	100
2009	MasterCard Inc	USA	Orbiscom Ltd	Business support	0.1	n.a.
2009	Popolare Vita SpA	Italy	The Lawrence Life Assurance Co	Financial services	0.03	100
2009	OASiS Group PLC SPV	USA	OASiS Group PLC	Business services	0.03	60
2009	Celsa Steel (UK) Ltd	UK	BRC McMahon Reinforcements Ltd	Building & construction	0.014	50
2009	Capita Group PLC	UK	Capmark Services Ireland Ltd	Financial services	0.013	100
2009	ISS Holding A/S	Denmark	Chubb Sec Personnel Ireland	Security services	0.005	100
2009	Genetix Group PLC	UK	SlidePath Ltd	Data management	0.004	100
2009	Corneal Laser Centre Ltd	UK	Eye Laser Ireland	Medical technology	0.004	100
2009	Norsat International Inc	Canada	Bluemoon 4G Ltd	Telecommunica tion services	0.003	100
2009	Sagem Securite SA	France	CardBASE Technologies Ltd	Business support	0.003	100
2008	Scottish & Southern Energy PLC	UK	Airtricity Holdings Ltd	Renewable energy	2	100
2008	Capital Research & Mgmt Co Ltd	USA	Kingspan Group PLC	Building & construction	0.1	6
2008	EAG Inc	USA	EAG Ltd	surface and materials analysis	0.1	100
2008	Investor Group	UK	Noonan Services Group Ltd	Facility services	0.1	100
2008	Dreamport Ltd	UK	NTR PLC	Renewable energy	0.1	39.6
2008	Investor Group	UK	Glanbia Meats Ireland	Food market	0.05	100
2008	Investor Group	Libya	Circle Oil Plc	Oil &gas	0.05	45.27
2008	Oxford Aviation Academy Ltd	UK	Parc Aviation Ltd	Personnel solutions & technical support	0.04	100
2008	DiaSorin SpA	Italy	Biotrin International	Diagnostics	0.03	100
2008	Amdocs Ltd	Guernsey	Changing Worlds Ltd	Digital service provider	0.03	100
2008	QUALCOMM Inc	USA	Xiam Technologies Ltd	Software development	0.03	100
2008	Barclays Capital	UK	Mainstream Renewable Power Ltd	Renewable energy	0.02	14.6
2008	Penninn hf	Iceland	Insomnia Coffee Co	Food & beverages	0.02	100

2008	Intersnack Knabbergebaeck	Germany	Largo Food Exports Ltd	Food	0.02	15
2008	Charles Taylor Consulting PLC	UK	Santam Europe Ltd	Financial services	0.018	100
2007	Hypo Real Estate Holding AG	Germany	DEPFA Bk PLC	Banking services	7	100
2007	Britvic PLC	UK	C&C Group-Soft Drinks Business	Beverage	0.3	100
2007	Cardpoint PLC	UK	Alphyra Group PLC	Electronic solution services	0.3	100
2007	Telekom Austria AG	Austria	e Tel Group Ltd-6 Subsidiaries	Telecom	0.1	100
2007	Munich Re	Germany	Allfinanz	Business Processing Solution	0.06	100
2007	Credit Suisse Group	Switzerland	EcoSecurities Group PLC	Carbon finance expertise	0.05	9.9
2007	Level 3 Communications Inc	USA	Servecast	Internet broadcasting	0.04	100
2007	White Young Green PLC	UK	PH McCarthy Consulting	Building & construction	0.03	100
2007	Societa Cattolica di Assicurazioni SCRL	Italy	Vicenza Life Ltd	Financial services	0.03	50
2007	WeDo Consulting-Sistemas	Portugal	CAPE Technologies Ltd	Telecom software	0.02	100
2007	DataCash Group PLC	UK	EuroCommerce Call Centre	Business support	0.01	100
2007	G4S PLC	UK	Omada Fire & Security Group	Security services	0.01	100
2007	Computershare Ltd	Australia	Datacare Software Group Ltd	Business support	0.01	100
2007	SmartConnect Holdings PTE Ltd	Philippines	Blue Ocean Wireless Ltd	Mobile communication	0.01	30
2007	Crompton Greaves Ltd	India	Microsol Holdings Ltd	Automation	0.01	100

Source: Thomson ONE Banker, Thomson Reuters.

Annex table 7. Ireland: main greenfield projects, by inward investing firm, 2007-2009

Year	Company name	Home economy	Industry	Investment/ estimated investment (US$ billion)
2009	Covanta	USA	Alternative/renewable energy	0.5
2009	Enel	Italy	Coal, oil and natural gas	0.3
2009	Green Wind Energy	Denmark	Alternative/renewable energy	0.2
2009	Scottish & Southern Energy	UK	Alternative/renewable energy	0.2
2009	Interxion	Netherlands	Communications	0.1
2009	Cable & Wireless	UK	Communications	0.1
2009	Boston Scientific	USA	Medical devices	0.1
2009	Activision Blizzard	USA	Software and IT services	0.1
2009	Takeda Pharmaceutical	Japan	Pharmaceuticals	0.1
2009	Leo Pharma	Denmark	Pharmaceuticals	0.1
2009	Hovione	Portugal	Pharmaceuticals	0.07
2009	Groupe de Recherche Servier	France	Pharmaceuticals	0.06
2009	Euro Construction Corp Ltd	UK	Real estate	0.06
2009	Intel	USA	Semiconductors	0.06
2009	Marks & Spencer	UK	Textiles	0.06
2008	Diageo	UK	Beverages	1
2008	Sosina	UK	Coal, oil and natural gas	0.5
2008	Houghton Mifflin	USA	Business services	0 .4
2008	Aldi Group	Germany	Food and tobacco	0.4
2008	Microsemi	USA	Semiconductors	0.33
2008	Coca-Cola	USA	Beverages	0.3
2008	Pfizer	USA	Biotechnology	0.2
2008	Intel	USA	Semiconductors	0.2
2008	Genzyme	USA	Pharmaceuticals	0.2
2008	Johnson & Johnson	USA	Consumer products	0.1
2008	EMC	USA	Communications	0.1
2008	Royal BAM Group	Netherlands	Real estate	0.1
2008	Millipore	USA	Medical devices	0.1
2008	Teva Pharmaceutical Industries	Israel	Pharmaceuticals	0.09
2008	EMC Instytut Medyczny	Poland	Healthcare	0.07
2008	Optical Express Group	UK	Healthcare	0.07
2007	Microsoft	USA	Software and IT services	0.05
2007	GlaxoSmithKline (GSK)	UK	Pharmaceuticals	0.03
2007	Merck & Co	USA	Pharmaceuticals	0.02
2007	Quinn Group	UK	Financial services	0.02
2007	Aldi group	Germany	Food and tobacco	0.01
2007	UCB SA	Belgium	Pharmaceuticals	0.01
2007	Baxter	USA	Medical devices	0.01
2007	Deutsche Post	Germany	Transportation	0.01
2007	Etex	Belgium	Building and construction materials	0.01
2007	New York Residence	USA	Real estate	0.008
2007	Gilead Sciences	USA	Biotechnology	0.008
2007	Equifax	USA	Financial services	0.007
2007	Regus	UK	Real estate	0.006
2007	Balcas	UK	Wood products	0.005
2007	Marks & Spencer	UK	Textiles	0.005

Source: fDi Intelligence, a service from the Financial Times Ltd.

Chapter 8 – Israel

Inward FDI in Israel and its policy context

Yair Aharoni

In the first four decades of its existence, Israel was not successful in attracting inward foreign direct investment (IFDI) despite attempts to do so. In the past two decades, Israel have become a haven for multinational enterprises (MNEs) that have taken advantage of its unique assets – among them a skilled, educated workforce and cutting-edge research-and-development (R&D) capabilities – by establishing production lines or R&D centers and acquiring dozens of successful start ups. Israel's IFDI stock sharply increased from US$ 4.5 billion in 1990 to US$ 71.3 billion in 2009. It is expected that IFDI will further accelerate following Israel's accession to the OECD in May 2010 and as more firms from emerging market economies, including China and India, will come to appreciate its characteristics as an ideal locational choice. Israel also weathered the global economic crisis well, even though IFDI declined sharply. Israel actively encourages IFDI, mainly in high technology areas. In 2010, the Government also created special incentives to attract research centers of financial institutions.

Trends and developments

Country level developments

Israel is a tiny parliamentary republic. Government intervention was very high until the mid-1980s, mainly in the form of an absolute control of the capital market and a high level of import protection. Since July 1985, ***responsible fiscal and monetary policies have accompanied reforms that have liberalized the economy*****,** freed the capital markets from government's shackles, abolished foreign exchange controls, reduced the size of the public sector ***and public debt, accelerated the process of privatization*****,** liberalized foreign exchange rules, ***and made the economy more competitive.***

The high quality of human capital has become a great advantage to Israel in seeking a place in the world. Its R&D investment as a percentage of its gross national product (GNP) of 4.7% in 2008 is the highest in the world. So is the number of researchers in R&D per million inhabitants.[195] Since the 1980s, the Office of the Chief Scientist (OST) in the Ministry of Industry, Trade and Labor has been operating a variety of programs to support R&D. The Bi-national Industrial Research and Development Foundation (BIRD F) was founded in 1977 and a venture capital industry emerged. Indeed, over the past two decades, Israel has become famous for its capacity for innovation and its highly educated, skilled workforce. Israel's high-tech industry accounted for about 15% of the country's GDP in 2009 (of US$ 195 billion) and more than 75% of its industrial exports. In addition, exports of R&D and software amounted to 29% of services exports and nearly 48% of business services exports in

[195] In 2005-2006, there were 4.5 researchers per one million inhabitants in Israel, compared to 2.6 in the United States and 1.3 in China. See UNCTAD, *World Investment Report 2007: Transnational Corporations, Extractive Industries and Development* (Geneva: United Nations, 2007), table A7.

that year. As a result, many high-tech MNEs have established R&D centers and production facilities in Israel. Today, the country's market economy can be characterized as resilient, globally-oriented and advanced-technology-based. The 2010-2011 World Competitiveness Yearbook ranked Israel in 24th place among 139 economies.[196]

Almost since it became an independent state, Israel tried to attract foreign investors. There were, however, at least four reasons why it was not very successful until the 1990s. First, the Arab countries rejected Israel's right to exist and boycotted firms doing business with Israel.[4] Many perceived Israel as synonymous with conflict and geopolitical instability. Second, Israel was not well developed, and its infrastructure was not at par with that of more developed nations. Telephone services were woefully inadequate and were allocated by the Government on the basis of a priority list. Road construction was inadequate, growing much less than the growth in the number of cars, resulting in congestion and many road accidents. Railways were very few. Even though the economy grew by leaps and bounds up to 1973,[198] by 1988 GNP per capita was only US$ 8,100.[199] Third, the tiny size of its domestic market was not very attractive for large MNEs. Finally, the leaders of the country believed in socialist ideology, and the Government intervened in all aspects of business.

Most foreign investments were small in size and seem to have been motivated by solidarity of businesspeople in the Jewish diaspora. By the end of 1980, the IFDI stock was US$ 3.2 billion. Annual IFDI flows during the 1970s were only a few US$ million – the highest being US$ 149 million in 1973. Even as late as 1990, Israel's IFDI stock as a percentage of GDP was 7.9%, compared to 9.0% for developed countries. In 2009, it was 36.6% compared to 31.5% in the developed world.[200] During the past two decades, major changes in Israel's economic policy, the liberalization of the economy and the encouragement of high technology firms and R&D were noticed by foreign MNEs. As a result, the IFDI stock zoomed up to US$ 22.6 billion in 2000 and US$ 71.3 billion in 2009 (annex table 1). Since 2000, annual IFDI flows have been more than US$ 1 billion (annex table 2). Their magnitude fluctuated considerably, with a peak value of US$ 15.3 billion (10.5% of GDP) reached in 2006 – largely because of two major transactions worth about US$ 4 billion each. The decline in IFDI flows in 2009 to US$ 3.9 billion seems to have been more the result of the crisis in the home countries of MNEs and much less of an economic recession in Israel.

The sectoral distribution of IFDI is slanted toward high-tech investments - more than half of foreign investments were made in high technology firms and the building up of

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[196] World Economic Forum, *Global Competitiveness Report 2010-2011* (Lausanne: WEF, 2010).
[197] On the Arab boycott see Aaron J. Sarna, ed., *Boycott and Blacklist: A History of Arab Economic Warfare against Israel* (Totowa N.J.: Rowman and Littlefield, 1986); Chaim Fershtman and Neil Gandal, "The effect of the Arab boycott on Israel: the automobile market," *Rand Journal of Economics*, vol. 29, no. 1 (1998), pp. 193-214; Dan S. Chill, *The Arab Boycott of Israel: Economic Aggression and World Reaction* (New York: Praeger, 1976).
[198] Israel's GDP per capita in relation to the United States increased from 25% in 1950 to 60% in 1970. See Dan Senor and Saul Singer, *Start-up Nation: The Story of Israel's Economic Miracle* (New York and Boston: Council of Foreign Relations, 2009), p. 115.
[199] For more information on Israel until 1990 see Yair Aharoni, *The Israel Economy: Dreams and R*ealities (London and New York: Routledge, 1991).

[200] UNCTAD's FDI/TNC database, available at: http://unctad.stats.org/fdi.

research centers. The Israeli Central Bureau of Statistics is responsible for the collection of statistical data, including on IFDI. Unfortunately, it does not publish Israel's IFDI stock in a sectoral breakdown nor does it publish the geographical distribution of home countries. The latest figures available are on output and employment in foreign affiliates in different sectors in 2005 (annex table 3). In that year, foreign affiliates comprised 17% of total manufacturing output (by employing 13% of the total workforce in this sector) and produced 19% of the total output of the services sector (with only 4% of the sectoral workforce). The economic importance of foreign affiliates is very high in the R&D sector (60% of total output and 43% of employees), in computer and related services (38% of output and 23% of employees). IFDI output was also very high in electronic components (54% of output and 32% of employees) and electronic communication equipment (56% of output, 49% of employees). Foreign firms produce half of the value added of high technology firms in Israel.[201] Firms such as Intel, Google or Microsoft rely on their affiliates in Israel for major innovations of new products and processes. As Bill Gates observed "innovation going on in Israel is critical to the future of the technology business." [202]

In practice, Israel allows access to foreigners in all economic branches. The main driver for IFDI was the desire to take advantage of innovative entrepreneurs and researchers in Israel and to profit from the institutional arrangements that support them (for details see the policy section). Other drivers have been opportunities to acquire vital components for the value chain. A total of 60% of Israel's exports is done by MNEs – 40% by affiliates of foreign MNEs in Israel and 20% by Israeli MNEs. Most of the exports of these MNEs are directed to affiliated firms. 70% of the service exports of these firms are composed of computer and R&D services.[203] The annual average value of IFDI flows in the past decade was 5% of GDP and 28% of gross fixed capital formation in the past three years.[204] *The high-tech sector accounts for three quarters of all industrial exports.*

[201] Bank of Israel, *Annual Report 2009*, p. 285.
[202] Senor and Singer, op. cit., p. 151. For similar observations by Warren Buffett, see the website of the Israeli Ministry of Trade, available at: www.moital.gov.il.
[203] Bank of Israel, *Annual Report 2009*, p. 272.
[204] UNCTAD's FDI/TNC database, available at: http://stats.unctad.org.

In terms of geographic distribution, official figures are not available. However, virtually all IFDI transactions are reported in the daily press and are also accumulated in a data bank of the Israel Venture Capital Association. In addition, cross-border M&As are published on the *Invest in Israel* website. One can therefore report that the largest number of parent companies is from the United States, followed by investors from the European Union.[205] Two of the largest food MNEs in Europe – Unilever and Nestlé – have invested in Israel, as has Siemens. Recently, Indian and Chinese MNEs have started to do the same. The first investment by a Chinese firm was made in January 2010 when the Sanhua group invested US$ 9.3 million in Helio Focus – a developer of solar heat systems using air. In late 2010, ChemChina was reported to have acquired a part of Machteshim-Agan, a producer of pesticides. This acquisition raised fears that the new owner would move production from Israel, thus reducing employment.

The corporate players

By the end of 2008, 489 foreign affiliates operated in Israel, compared to 278 in 2007, and only 37 in 2005.[206] The majority of them are in high technology industries. Practically every large MNE has opened or acquired a development center in Israel. The Israel Venture Capital Research Center's data base lists 286 foreign R&D centers, including those owned by Alcatel-Lucent, Applied Materials, Cisco, EMC, General Electric, Google, Hewlett Packard, IBM, Intel, Microsoft, and Siemens. Intel also invested in production facilities and has the largest foreign affiliate in Israel. Most foreign investments in Israel are relatively small in value. Only a handful of cross-border acquisitions were valued at US$ 1 billion or more.[207] The 15 principal foreign affiliates are listed in annex table 4. With the exception of Intel, the majority of IFDI are acquisitions of existing firms – many of them successful start-ups.

In 2009, M&A proceeds involving Israeli companies that were either acquired or merged, totaled US$ 2.5 billion, 7% lower compared to 2008, and 33% lower than in 2007. The top ten deals in 2009 yielded roughly US$ 2 billion, 80% of the total for the year. Four deals exceeded the US$ 200 million mark and five exceeded the US$ 100 million mark. Annex table 5 lists the largest cross-border M&As in 2007-2009.

According to the Israel Venture Capital Research data base, 63 Israeli companies were acquired or merged in 2009, a 28% drop from an average of 87 companies in the previous three years. However, the average deal size in 2009 was US$ 40 million, an increase of 21% from US$ 33 million in 2008. Venture capital backed deals (28) totaled US$ 1.6 billion, an increase of 3% compared to 35 transactions valued at US$ 1.5 billion in 2008. The most noteworthy M&As of 2009 were Siemens' US$ 418 million acquisition of Solel, Medtronic's acquisition of Ventor, estimated at

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[205] Official figures of the exact geographical distribution are not available. Given the small size of the population of foreign investors, the number of the different foreign investors was counted.

[206] Figures are from UNCTAD's FDI/TNC database, op. cit.

[207] Cross-border acquisitions valued more than US$1 billion since 1999 were: Lucent technology's acquisition of Chromatis for US$ 4.8 billion in 2000, HP's acquisition of Mercury in 2006 for US$ 4.5 billion, Berkshire Hathaway's acquisition of 80% of Iscar – a producer of metal cutting tools – for US$ 4 billion in 2006, Broadcom's acquisition of Galileo for US$ 2.7 billion in 2000, Intel's acquisition of DSPG for US$ 1.6 billion in 1999, Sandisk acquisition of M Systems for US$ 1.6 billion in 2006, and ECI's acquisition of Swarth for US$ 1.2 billion in 2007. In addition, Perrigo acquired Agis for US$ 0.9 billion, and Kodak acquired Creo for US$ 1 billion.

US$ 325 million, and IBM's US$ 225 million acquisition of Guardium. In the period from January to October 2010, there were 50 cross-border acquisitions; only two of them – by 3M (US$ 230 million for Attenti) and by Roche (US$ 160 million for Medingo) - were valued at more than US$ 85 million.[208]

As to greenfield investments, there were about 20 of those every year, with a maximum of 41 in 2008.[209] Large greenfield investments have been undertaken by Intel and Marriott in recent years (annex table 6).

Effects of the current global crisis

The global economic and financial crisis occurred after five years of economic growth of Israel at the end of which the unemployment rate was 5.9% - the lowest level in 20 years. The financial system and the mortgage markets were managed conservatively and were not affected by the crisis, and the country accumulated a surplus on the current account. Thanks to its sound macroeconomic and structural fundamentals, the Israeli economy recovered quickly. Following a reduction of GDP of 1.5% in the first quarter of 2009, economic growth resumed: real GDP increased by 3.6% and 4.9% in the third and fourth quarters, respectively. For 2010 and 2011, a 4% annual growth rate of real GDP is forecast. Unemployment in the second quarter of 2010 fell to 5.9% (though it rose back up to 7.2% in the third quarter). Yet exports were 12.5% lower than in the same period of the previous year.

IFDI plummeted by 64% in 2009, to only US$ 3.9 billion, down from US$ 10.9 billion in 2008 – compared to a 37% decline in global IFDI flows. Israel fell from the 54th place in 2008 to the 80th in 2009 in terms of IFDI. The increased uncertainty large high-tech MNEs felt during the crisis explains much of the decline in inward FDI. Indeed, cross-border investment in Israel in the high-tech sectors plunged to just US$ 1.4 billion in 2009, compared with US$ 3.2 billion in 2008.[210]

The policy scene

Since the 1990s, Israel has implemented a thorough unilateral trade liberalization program, exposing its domestic industry to foreign competition. The country made great efforts to attract IFDI to all economic sectors, with the possible exception of the military industry.

Investment incentives – which are the same for domestic and foreign investors - are outlined in the Law for the Encouragement of Capital Investment that was first enacted in 1950, and revised in 1959. Since 1959 there have been 60 amendments to the law; the most recent were made two years ago.[211] Under the Law, the country is geographically divided into three National Preference Zones: A, B and C. The most preferential benefits accrue to businesses located in Zone A - areas far from central Israel that are relatively weak economically. The Law allows an enterprise to choose the type of its benefit from two alternatives: grants plus tax benefits. It is coordinated

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[208] The figures are from the data base of Israel Venture Capital Research.
[209] UNCTAD's FDI/TNC database, op. cit..
[210] Note, however that the data are skewed. Volatility is affected by the impact of large transactions. As an extreme example, in 2006 two individual acquisitions amounted to 50% of total IFDI.
[211] Details can be found at: www.investinisrael.gov.il. The new law differs from the previous one by adding a new path for incentives – an Automatic Tax Program.

by the Israel Investment Center (IIC). Israel offers a wide range of incentives and benefits to investors in industry, tourism, real estate, film production,[212] and (since August 2010) financial services. Special emphasis is given to high-tech companies and R&D activities.[213]

The Office of the Chief Scientist (OCS) of the Ministry of Industry and Trade is responsible for implementing the Government's policy of encouraging and supporting industrial R&D in Israel. The OCS provides a variety of support programs that have helped make Israel a major center of high-tech entrepreneurship.[214]

Israeli trade policy is aimed at maintaining the expansion of its network of bilateral trade agreements. Its network of international trade and economic cooperation agreements includes free trade area agreements (FTAs) with NAFTA member countries (the United States, Canada, Mexico) and an association agreement with the European Union. The FTA provides for import-duties exemptions for most Israeli-made products arriving in the EU. Israel has also signed FTAs with the EFTA countries, as well as with Turkey. Recently, Israel signed an FTA with Mercosur (comprising Brazil, Argentina, Uruguay, Paraguay). Israel has also signed an Agreement on Trade and Economic Cooperation with Jordan; it includes significant tariff reductions for bilateral trade. Israel is also negotiating an FTA with India.

Israel has also signed bilateral investment treaties (BITs) with more than 30 countries, including Argentina, China, Germany, India, Kazakhstan, Poland, Romania, the Republic of Korea, South Africa and Turkey. Treaties for the avoidance of double taxation (DTTs) were concluded with 40 countries, including the United States, Brazil, Canada, China, France, Germany, Italy, Japan, the Netherlands, and Russia. According to UNCTAD, as of May 2010 Israel had signed 86 international investment agreements (IIAs), of which 37 were BITs, 45 DTTs and 4 others.[215]

Israel has also developed an extensive network of international R&D accords that foster industrial and technological cooperation with many countries. These include bilateral R&D funds with the United States, the United Kingdom, Canada, Singapore, and the Republic of Korea, as well as with the Province of Ontario in Canada and the State of Victoria in Australia. Israel has also concluded bilateral R&D agreements with 13 countries, including France, Germany, Italy, India, and China. Israel is the only non-European Associated State participating as an equal member in the EU Sixth Framework Program.[216]

In May 2010, OECD countries unanimously agreed to extend membership to Israel, following three years of accession negotiations and careful review of its compliance with OECD standards and benchmarks. In August 2010, the Government of Israel launched a special program to encourage research centers of financial institutions, and several foreign banks are understood to be interested.

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[212] The *Law for the Encouragement of the Production of Films* was approved by the Israeli Knesset on October 28, 2008. Its main aim is to encourage the production of foreign films in Israel. To this end, the law offers generous tax benefits that reduce the cost of production by up to 20%.
[213] For details see www.investinisrael.gov.il
[214] See www.investinisrael.gov.il.
[215] UNCTAD, *World Investment Report 2010: Investing in a Low Carbon Economy* (Geneva: United Nations, 2010).

The many acquisitions of successful Israeli start-ups initiated a heated debate on appropriate national policies. Clearly, because the country is small, dependence on the very few Israeli-based large MNEs could make such firms "too large to fail", and also strong political players. Ideally, the country would nurture dozens of home-based MNEs out of the 3,800 start-ups that would increase value-added and employment in Israel, not confining them to research centers and development work. Israel boasts the most high-tech start-ups per capita in the world. Its entrepreneurs and perhaps more so venture capitalists prefer to exit by selling their firms to large (foreign) MNEs instead of turning them into large independent firms that can provide local jobs. In the public debate about what is best for the country and what policies the government should pursue, many argue that Israel does not have enough experts in marketing, nor does it have managers able to direct large firms. There is also a shortage of later stage financing. A *Wall Street Journal* article[217] has pointed out that short-term thinking is ingrained in Israel, so it is unable to turn its high-tech start-ups into mature companies that stay in the country**.** If this is so, the best policy is to encourage R&D and then exit. Yet it is inconceivable to assume that a large number of entrepreneurs would be able to make a series of innovations, creating one start up after another and exiting from all of them. It is more plausible to assert that Israel is losing much potentially highly-paid employment by selling off its new technologies.

Conclusions and Outlook

Though Israel is a small country with limited resources, responsible fiscal and monetary policies and a host of reforms aimed at liberalizing the economy have allowed it to stand out as one of the world's most competitive economies. Despite continuing tension in the region, Israel has evolved in just 20 years from an emerging to an industrialized economy. Israel's market economy is resilient, globally-oriented and technologically advanced. Over the past two decades, Israel has become well-known for its high-tech capacity, particularly in telecommunications, information technology, electronics, and life sciences. Its capacity for innovation, coupled with a highly-educated, skilled workforce, has played a key role in attracting IFDI.

Additional readings

Aharoni, Yair, *The Israel Economy: Dreams and Realities* (London and New York: Routledge, 1991).

Senor, Dan and Saul Singer, *Start-Up Nation: The Story of Israel's Economic Miracle* (New York and Boston: Council of Foreign Relations Book, 2009).

Useful websites

Israel Ministry of Industry Trade and Labor, available at: **www.moital.gov.il.**

[217] **See http://online.wsj.com/article/SB10001424052748703632304575451211403181030.html?KEYWORDS=israel+high+tech#ixzz11smMk84W.**

Israel Ministry of Industry Trade and Labor Investment Promotion Center, available at: **www.investinisrael.gov.il**.

Bank of Israel, available at: www.bankisrael.gov.il.

Israel Central Bureau of Statistics, available at: http://www.cbs.gov.il.

Israel Venture Capital Research Center with data base on foreign investors, available at: **www.ivc-online.com/**.

Israel Central Bureau of Statistics, available at: www.cbs.gov.il/www/hodaot2008n /09_08_223t20.pdf.

Statistical Annex

Annex table 1. Israel: inward FDI stock, 2000-2009 (US$ billion)

Economy	**2000**	**2005**	**2008**	**2009**
Israel	23	38	64	71
Memorandum: comparator economies				
Finland	24	55	83	88
Ireland	127	164	168	193
Sweden	94	172	272	305
Switzerland	87	170	439	464

Source: UNCTAD's FDI/TNC database, available at: http://stats.unctad.org/fdi.

Annex table 2. Israel: inward FDI flows, 2000-2009 (US$ billion)

Economy	**2000**	**2001**	**2002**	**2003**	**2004**	**2005**	**2006**	**2007**	**2008**	**2009**
Israel	7.0	1.8	1.6	3.3	2.9	4.8	15.3	8.8	10.9	3.9
Memorandum: comparator economies										
Finland	8.8	3.7	8.0	3.3	2.8	4.8	7.7	12.4	-2.0	2.6
Ireland	25.8	9.7	29.3	22.8	-10.6	-31.7	-5.5	24.7	-20.0	25.0
Sweden	23.4	10.9	12.3	5.0	11.0	9.9	27.3	27.2	33.7	10.9
Switzerland	19.3	8.9	6.3	16.5	0.9	-1.0	31.2	51.7	5.1	9.7

Source: UNCTAD's FDI/TNC database, available at: http://stats.unctad.org/fdi.

Annex table 3. Israel: Output and employment of foreign affiliates in Israel in different sectors in relation to total output and employment, 2005

Sector	Output of foreign affiliates to total economy (in %)	Employment of foreign affiliates to total economy (in %)
Manufacturing	**17**	**13**
Food, beverages and tobacco products	12	13
Textiles and wearing apparel	7	6
Paper, publishing and printing products	14	10
Chemicals and chemical products	11	31
Plastic and rubber products	6	6
Non-metallic mineral products	19	15
Basic metall	29	29
Metal products and machinery and equipment	11	8
Electric motors and electric distribution apparatus	15	10
Electronic components	54	32
Electronic communication equipment	56	49
Industrial equipment for control and supervision	26	16
Transport equipment	15	7
Other manufactures	2	1
Services	**19**	**4**
Construction	2	1
Wholesale trade, retail trade and maintenance of vehicles	5	3
Hotels and accomodation services	20	4
Transport, storage and communications	5	1
Computer and related services	38	23
Research and development	60	43
Other industries	**2**	**0**

Source: Israel Central Bureau of Statistics

Annex table 4. Israel: 15 principal foreign affiliates, listed among Israel top 100 industrial and service companies in Dun's 100, 2009

Rank	Name	Industry	Number of Employees	Export (US$ mil lion)	Turnover (US$ million)
1	Intel electronic Israel Intel Israel 74	Electronic devices	5,951	3,422	3,433
2	Berkshire Hathaway (Iscar)	Metal cutting devices	1,500	1,495*	1,531
3	Vishay Israel	Electronic devices	12,000	n.a.	1,148
4	Hewlett Packard Software Development Israel	Computers	880	n.a.	995
5	Sandisk IL	Electronic devices	500	865	913
6	Osem (Nestlé)	Food	4,720	166	867
7	Comverse	Software	5,000	n.a.	765
8	NDS (News Corp.)	Communication equipment	3,700	n.a.	765
9	Motorola	Electronic devices	2,589	304	686
10	IBM Israel	Computers	1,800	n.a.	548
11	Emblaze	Other		106	552
12	Formula systems	Software	4,200	n.a.	471
13	Perrigo Israel	Pharmaceuticals and cosmetics	1,700	n.a.	459
14	Kimberly Clark	Paper and cardboard	1,515	129	440
15	Unilever Israel	Food	1,800	n.a.	370

Source: Calculated by the author from Dun's 100.
* Estimated.

Annex table 5. Israel: main M&A deals, by inward investing firm, 2007-2009

Year	Target company	Acquiring company	Investor economy	Percent of shares acquired	Transaction value (US$ million)
2009	Levantine Basin	Bontan Corp Inc	Canada	71.6	2.7
2009	AiPoint Ltd-Workforce	ClickSoftware Ltd	United States	100.0	1.5
2009	CopperGate Communications Ltd	Sigma Designs Inc	United States	100.0	164.5
2009	Arava Power Co	Siemens Project Ventures GmbH	Germany	40.0	57.2
2009	Dblur Technologies Ltd-Assets	Tessera Technologies Inc	United States	100.0	5.0
2009	Ventor Technologies Ltd	Medtronic Inc	United States	100.0	325.0
2009	Dmatek Ltd	Investor Group	United States	100.0	70.3
2009	Scopus Video Networks Ltd	Harmonic Inc	United States	100.0	78.9
2009	CMT Medical Technologies Ltd	Thales SA	France	87.4	26.4
2009	ABIC Biological Laboratories	Phibro Animal Health Corp	United States	100.0	46.0
2009	Aladdin Knowledge Systems Ltd	Investor Group	United States	86.0	137.1
2008	MediGuide Inc	St Jude Medical Inc	United States	100.0	300.0
2008	Ex Libris Group	Leeds Equity Partners LLC	United States	100.0	200.0
2008	Ness Tech Inc-SAP Sales	SAP AG	Germany	100.0	30.0
2008	Plastro Irrigation Systems Ltd	Deere & Co	United States	100.0	66.0
2008	Halman Aldubi Ltd	Capernaum Finance	Canada	49.9	35.6
2008	Avenue Israel Ltd-License	TomCo Energy PLC	United Kingdom	50.0	51.9
2008	BeInSync Ltd	Phoenix Technologies Ltd	United States	100.0	22.1
2008	Ness Technologies Inc	Citigroup Private Equity	United States	9.6	33.5
2008	Orca Interactive Ltd	Viaccess SA	France	100.0	21.4
2008	NUR Macroprinters Ltd	Hewlett-Packard Co	United States	100.0	117.5
2008	Taro Pharmaceutical Industries	Sun Pharmaceuticals Inds Ltd	India	9.4	38.1
2008	Dorot Water Technologies Ltd	Miya Luxemburg Holdings Sarl	Luxembourg	96.0	29.6
2008	Saifun Semiconductors Ltd	Spansion Inc	United States	100.0	421.1
2008	Fraud Sciences Ltd	Paypal Inc	United States	100.0	169.0

2008	Solel Solar Systems Ltd	Ecofin Ltd	United Kingdom	40.0	105.0
2007	Bank Hapoalim BM	Lazard Asset Management LLC	United States	5.0	323.2
2007	Maccabi Tel Aviv	Alex Shnaider	Canada	80.0	17.0
2007	Ester Neurosciences Ltd	Amarin Corp PLC	Ireland-Rep	100.0	32.1
2007	Clal Ind & Invest-Startup Co	Newbury Partners LLC	United States	-	20.0
2007	Golden Pages Ltd	Babcock & Brown Capital Ltd	Australia	100.0	212.3
2007	Bonei Arim Ltd	Undisclosed Acquiror	Unknown	-	63.0
2007	NaanDan Irrigation Sys CS Ltd	Jain Irrigation Systems Ltd	India	50.0	21.5
2007	SPL Software Ltd	Software AG	Germany	80.0	61.6
2007	Inolase Ltd	Candela Corp	United States	100.0	16.5
2007	Eyesquad	Tessera Technologies Inc	United States	100.0	18.0
2007	SigValue Technologies Inc	Amdocs Ltd	Guernsey	86.0	54.0
2007	Disc-O-Tech-Spine -Related Ast	Kyphon Inc	United States	100.0	220.0
2007	PowerDsine Ltd	Microsemi Corp	United States	100.0	275.1
2007	Alliance Tire Co(1992)Ltd	Warburg Pincus LLC	United States	100.0	150.0
2007	Delta Galil Industries Ltd	GMM Capital LLC	United States	21.3	27.7

Source: Thomson ONE Banker, Thomson Reuters.

Annex table 6. Israel: top 15 greenfield projects, by inward investing firm, 2007-2009 (US$ million)

Date	Company name	Source economy	Estimated Investment	Industry	Business activity
2009	Marriott International	USA	160.0[a]	Hotels & tourism	Construction
2009	Hewlett-Packard (HP)	USA	22.7	Software & IT services	Research & development
2009	ToLuna	UK	11.5	Business Services	Research & Development
2009	Intel	USA	120.2	Semiconductors	Manufacturing
2009	Dolphin Integration	France	19.1	Electronic components	Design, development & testing
2009	Phoenix Corporate Finance Partners	UK	15.1	Financial services	Business services
2009	France Telecom	France	26.0	Communications	Design, development & Testing
2009	Bank of Georgia (Sakartvelos Banki)	Georgia	15.1	Financial services	Business services
2009	Merchant Diamond Group	Cyprus	12.2	Minerals	Sales, marketing & support
2009	SunGard	USA	82.6	Software & IT services	ICT & internet infrastructure
2009	Thuasne	France	30.2	Textiles	Logistics, distribution & transportation
2009	Covance	USA	33.3	Pharmaceuticals	Research & development
2009	TANTK im. G.M. Beriyeva (Beriev Aircraft Company JSC)	Russia	15.2	Aerospace	Sales, marketing & support
2009	Namakwa Diamond	South Africa	12.7	Minerals	Sales, marketing & support
2009	HCL Group	India	8.7	Software & IT services	Sales, marketing & Support
2008	Software AG	Germany	15.3	Software & IT services	Design, development & testing
2008	Hennes & Mauritz (H&M)	Sweden	15.9	Textiles	Retail
2008	Intel	USA	20.0[a]	Industrial machinery, equipment & tools	Recycling
2008	Inditex	Spain	17.3	Textiles	Retail
2008	Skunkfunk	Spain	17.3	Textiles	Retail

2008	SAP	Germany	15.0	Software & IT services	Design, development & testing
2008	General Dynamics	USA	86.4	Aerospace	Manufacturing
2008	Inventure Chemical	USA	107.2	Alternative/renewable energy	Manufacturing
2008	Cognate BioServices	USA	87.5	Biotechnology	Manufacturing
2008	Microsoft	USA	18.5	Software & IT services	Design, development & testing
2008	GL Trade	France	121.2	Software & IT services	ICT & internet infrastructure
2008	IBM	USA	20.0	Software & IT services	Research & development
2008	Tata Group	India	61.6	Software & IT services	Design, development & testing
2008	Air Logistics Group	France	32.6	Transportation	Sales, marketing & support
2008	Yahoo	USA	20.0	Software & IT services	Research & development
2007	eBay	USA	15.3	Software & IT services	Design, development & testing
2007	Sunshine Makers, Inc.	USA	40.7[a]	Consumer products	Manufacturing
2007	Dai-Ichi Kogyo Seiyaku	Japan	8.0[a]	Chemicals	Manufacturing
2007	Pfizer	USA	31.9	Pharmaceuticals	Research & development
2007	Continuity Software	USA	15.3	Software & IT services	Design, development & testing
2007	Sigma-Aldrich	USA	29. 0[a]	Biotechnology	Manufacturing
2007	General Motors (GM)	USA	103.0	Automotive OEM	Research & development
2007	Credit Suisse Group	Switzerland	15.1	Financial services	Business services
2007	Criterium	USA	8.8	Pharmaceuticals	Sales, marketing & support
2007	Johnson & Johnson	USA	23.3	Medical devices	Research & development
2007	Babcock & Brown	Australia	15.1	Financial services	Business services
2007	Motorola	USA	41.6	Communications	Design, development & testing
2007	Netineo	France	27.1	Communications	Design, development & testing
2007	Smart Energy Solutions	USA	28.0	Automotive components	Manufacturing
2007	Hewlett-Packard (HP)	USA	18.5	Software & IT services	Design, development & testing

Source: fDi Intelligence, a service from the Financial Times Ltd.

[a] Actual investment (not estimated).

Chapter 9 – Italy

Outward FDI and its policy context, 2010

Marco Mutinelli and Lucia Piscitello

Italian companies started to invest abroad in the 1960s in search of new markets. However, Italy's OFDI performance is quite modest compared with that of other European Union (EU) countries, mainly due to structural characteristics like the low number of large firms, the specialization in traditional low- and medium-technology manufacturing industries and the almost negligible activity in advanced services. The global economic and financial crisis seriously affected the Italian economy. However, the positive trend of Italian OFDI was not interrupted, and in 2009 OFDI flows remained stable compared to 2008. Habitually silent on this policy area in earlier decades, the Italian Government has recently shown a more favorable stance toward OFDI, introducing specific policy measures addressed to SMEs, which have started to expand strongly abroad – these now constitute almost 90% of Italian MNEs.

Trends and developments

Country-level developments

Italy's OFDI performance is quite modest compared with that ofmost other EU countries. In 2009, the total OFDI stock reached US$ 578 billion (annex table 1). The ratio of its OFDI stock to GDP amounted to 27%, which is much smaller than the corresponding ratio for the whole EU (55%) or comparable economies like France (65%), Germany (41%), Spain (44%) and the United Kingdom (76%).[218] Several structural characteristics of the Italian economy play a role in explaining these figures, including the low number of large firms, specialization in "traditional", low- and medium-technology manufacturing industries and the almost negligible activity in advanced service sectors.

Italian companies started to invest abroad in the 1960s in search of new markets and/or export growth. Nevertheless, until the first half of the 1980s, the internationalization of Italian companies remained far lower than that of other large European countries. Outflows started to rise noticeably only in the second half of the 1980s, stimulated by the EU Single Market Program. In this phase, the international growth of Italian firms was also favored by the recovery of competitiveness of large Italian companies and the strengthening of the Italian Lira, whose weakness had previously favored internationalization strategies of Italian firms based on exports rather than OFDI. In addition, protectionist policies previously used to tackle the growing deficit of the balance of payments were relaxed. In addition, policies mainly aimed at the financial support of Southern Italy which had required heavy investments especially by State-owned firms, ended. Thus, the latter could initiate strategies for undertaking multinational expansion

[218] UNCTAD, *World Investment Report 2010*: Investing in a Low-carbon Economy (Geneva: United Nations, 2010).

and international strategic alliances.[219] This favorable period, during which the significant growth of Italian OFDI was led by market-seeking M&As of the largest Italian manufacturing firms (Fiat, Pirelli, Montedison, ENI, IRI, Olivetti), was abruptly interrupted by the sharp depreciation of the Italian Lira in September 1992, when the currency fell nearly 30% against the US dollar and the stronger European currencies.

In subsequent years, the decline in cross-border M&As of large Italian companies was counterbalanced by increasing outward investment by SMEs. The internationalization of Italian SMEs combined both market-seeking strategies, mainly in EU-15 countries, and offshoring strategies, aimed at regaining cost competitiveness. The latter prevailed in low-technology manufacturing industries, such as textiles and apparel, shoes and leather products, furniture and other household products, which together constitute the bulk of "Made in Italy".[220]

Italian OFDI stock increased strongly during the 2000s, from US$ 180 billion in 2000 to US$ 578 billion at the end of 2009. In particular, OFDI flows rose considerably after 2004, driven by a new wave of M&As made by a limited number of large Italian firms (annex table 2). Italian OFDI flows jumped from an average value of US$ 15.6 billion per year in 2000-2004 to US$ 52.6 billion in 2005-2009, peaking at US$ 91 billion in 2007. As a result, the Italian OFDI stock grew by 221% between 2000 and 2009, less than the Spanish OFDI stock (+400%) but much stronger than that of the EU-27 countries (+158%), Germany (+154%), France (+86%), and the United Kingdom (+ 84%).

In 2009, services accounted for 44% of Italian OFDI stock (annex table 3).[221] Industrial products maintained a significant weight (29.5%), while energy products (petroleum, electricity, gas and water supply) accounted for 26.1% of the total, mainly reflecting OFDI by ENI in the oil and gas industry and by ENEL in the electricity sector. Finally, agricultural, forestry and fishing products accounted for only 0.4% of total OFDI stock.

However, the sectoral breakdown changes significantly when considering the number of employees in foreign affiliates.[222] At the end of 2007, majority-owned foreign affiliates of Italian firms employed nearly 1,421,000 workers. Nearly 806,100 workers (56.7%) were employed in the secondary sector, compared with 583,300 (41%) in the tertiary sector and 31.600 (2.2%) in the primary sector. More than 752,300 workers (52.9% of the

[219] R&P-Ricerche e Progetti (a cura di), *Italia Multinazionale. L'internazionalizzazione dell'industria italiana* (Milano: Edizioni del Sole 24 Ore, 1986).
[220] Marco Mutinelli and Lucia Piscitello, "Differences in the strategic orientation of Italian MNEs in Central and Eastern Europe", *International Business Review*, vol. 6, no. 2 (1997), pp. 185-205; Marco Mutinelli and Lucia Piscitello, "The influence of firm's size and international experience on the entry mode choice: Evidence from the internationalization of the Italian industry", *Small Business Economics*, vol. 11 (1998), pp. 43–56; and Sergio Mariotti and Lucia Piscitello, "Localised capabilities and internationalization of manufacturing activities by SMEs," *Entrepreneurship and Regional Development*, vol. 13 (2001), pp. 65-80.
[221] The banking sector is not included.
[222] Data on foreign majority-owned affiliates of Italian companies are gathered by the Italian National Institute of Statistics (ISTAT) as a result of compulsory surveys. More recent data refer to 2007. See ISTAT, *Le imprese a controllo nazionale residenti all'ester, Anno 2007* (Rome, May 31, 2010).

total) were employed in the manufacturing sector, where the textile and apparel industry (124,200) and the machinery industry (111,600) employed the largest shares.

OFDI by Italian firms is mainly concentrated in Europe (80% of total OFDI stock in 2009). In the past decade, Italian OFDI has grown faster in the EU-15 countries than in other regions. Italian OFDI remained low in North America (7.5% of OFDI stock in 2009, compared to 11.7% in 2000) and in developing countries (12%). BRIC countries (Brazil, Russia, India, China) accounted for less than 2%. The small average size of the Italian firms crucially hinders expansion toward the fastest growing regions (in particular, China), owing to the severe managerial and financial constraints that SMEs face when expanding abroad, especially into geographically and culturally distant countries.

FDI statistics collected by the Bank of Italy record direct or primary investments undertaken by Italian firms and not indirect investments made via holding companies established abroad. Thus, the distribution of OFDI data does not properly reflect the geographical breakdown of Italian firms' foreign activities. Some Italian firms manage their foreign activities through financial holdings established in the Netherlands and in Luxembourg, which together account for about 36% of total Italian OFDI stock, while their weight measured by the total number of employees in foreign affiliates, gathered by the Italian National Institute of Statistics (ISTAT) as a result of compulsory surveys, is less than 1%.

Data on the employment of foreign affiliates of Italian firms give a more valid representation of the geographical breakdown of their foreign activities. According to ISTAT, foreign majority-owned affiliates of Italian firms in the EU-27 countries employ nearly 655,000 workers, accounting for 46% of the total. The role of countries outside the EU is particularly important for manufacturing activities, which are mainly located in Central and Eastern European countries, as well as in the United States, Brazil and China. A significant presence of manufacturing activities controlled by Italian firms is also recorded in Russia, Argentina, India, Mexico, and Tunisia. The United States ranked first by the number of employees in foreign affiliates of Italian firms in 2007 (147,803), followed by Romania (147,542), Germany (116,875), France (100,719), Brazil (94,048), China (85,439), Poland (82,673), Spain (67,661), and the United Kingdom (55,810).

The corporate players

It is assumed that about 8.000 Italian enterprise groups have at least one foreign affiliate (either majority-owned or 50-50 or minority joint ventures). However, in 2009, only two Italian firms ranked in the top 100 non-financial MNEs in the world (compared with 18 from the United States, 15 both from France and from the UK, 12 from Germany, nine from Japan, five from Switzerland, and three from Sweden). ENI, the largest Italian non-financial MNE, ranked only 17th in the world's top 100 by foreign assets in 2009, while the Fiat Group ranked 52nd. Three Italian firms ranked in world's top 50 financial MNEs: Generali (rank 4), Unicredit (rank 7), and Intesa SanPaolo (rank 28).

The market-seeking motive is the most important driver of foreign investments for the few large Italian firms, combined with the resource-seeking motive in the case of ENI, in the oil industry. Efficiency-seeking strategies are often an important motivation of FDI by SMEs.[223] A recent survey of 15,000 European MNEs confirms that less than 40% of Italian firms which have undertaken foreign investment are pursuing strategies explicitly aimed at selling their own products in the host country or at using the investment as an export platform, the most important motive being exporting back to Italy. By contrast, market-seeking strategies are prominent for about 65% of German investors, while export-platform FDI is used by some 45% of French investors.[224]

The breakdown of Italian MNEs by region reflects the long-term structural imbalances of the Italian economy. Nearly 80% of Italy's MNEs are located in the Northern regions; Central Italy hosts less than 15% of Italian MNEs, while the South ("Mezzogiorno") plays a negligible role.

Effects of the current global crisis

The global financial and economic crisis seriously affected the Italian economy similar to other European economies, causing a sharp decline in 2009 of 25% in exports and 5% in real GDP, as well as a fall in profits of Italian companies.

Nevertheless, despite the difficult economic situation of the country, the positive trend of Italian OFDI was not interrupted, and in 2009 OFDI flows remained stable compared with 2008 and divestments abroad[225] did not grow significantly in 2009 compared to previous years. In contrast, most of the other large EU countries, with the exception of France (-8.6%), experienced a sharp decline of OFDI flows (Germany -53.4%, Spain -78.1%, UK -88.5%). It is also worth observing that in 2009 Italian OFDI flows (US$ 43.9 billion) were higher than OFDI flows of the UK (US$ 18.5 billion) and Spain (US$ 16.3 billion) combined, two countries that in the past were among the main foreign investors worldwide.

The policy scene

Until the start of the first stage of the European Monetary Union (EMU) in July 1990, the foreign expansion of Italian firms was hampered by barriers to capital outflows. However, since the late 1980s, the Italian government has introduced specific policy measures aimed at supporting OFDI, particularly addressed to SMEs, which had started expanding abroad although facing severe managerial and financial constraints.

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[223] See Mutinelli and Piscitello,op. cit.

[224] See Giorgio Barba Navaretti et al., *The Global Operations of European Firms. The second Efige Policy Report* (Bruegel, 2010); see, in particular table 4.6., p. 28.

[225] For a study of Italian firms' divestments, see Sergio Mariotti and Lucia Piscitello, "Is divestment a failure or part of a restructuring strategy? The case of Italian transnational corporations", *Transnational Corporations*, vol. 8(3) (1999), pp. 25-54.

Launched by Act 49/87, Italian OFDI policy rests on four State-controlled agencies: SIMEST (Società italiana per le Imprese Miste all'ESTero – Italian Company for Foreign Joint-Ventures), FINEST (Finanziaria per gli Imprenditori del Nord-EST – Financial Company for North-Eastern Entrepreneurs), ICE (Istituto italiano per il Commercio Estero – Italian Institute for Foreign Trade, also known as Italian Trade Commission) and SACE (Società di Assicurazione e Credito alle Esportazioni – Company of Insurance and Credit to Exports). SIMEST[226] and FINEST[227] can acquire shares of up to 49% in the capital stock of joint ventures set up abroad by Italian firms. These shares must be transferred to third parties within eight years of their first intervention. They also grant soft loans[228] for the creation of joint ventures outside the EU and provide professional consultancy and technical support services, such as scouting activities (seeking out opportunities abroad), matchmaking initiatives (locating partners), pre-feasibility/feasibility studies, and financial, legal and corporate assistance related to foreign investment projects in which their subsequent involvement is foreseen. So far, SIMEST has approved more than 1,000 FDI projects, investing more than Euro 1 billion. Moreover, SIMEST has set up a venture capital fund that may be added to its shares in the joint ventures set up in Central and Eastern Europe (excluding EU countries), Asia, Africa and Latin America. Support for 44 FDI projects was approved in 2009.

Advisory services to Italian firms are also offered by ICE, a government agency entrusted with promoting trade, business opportunities and industrial co-operation between Italian and foreign companies. ICE operates through 115 branch offices in 86 countries in the world and through the network of Italian foreign chambers of commerce, which can be found in 75 cities in 40 countries worldwide.[229]

By June 2010, Italy had signed 92 BITs, 71 of which had been ratified. The first BIT was signed with Chad in 1969, but most BITs were concluded in the 1990s (50) and in the first decade of the 2000s (28). The most recent BIT was signed with Turkmenistan in November 2009.[230] Italy has also entered into double taxation treaties (DTTs) with 86 countries, within and outside the EU, to avoid double taxation on income and property.[231] Draft agreements with additional countries are at the discussion stage. Furthermore, there are forms drawn up unilaterally by the foreign tax authorities that can equally be used to facilitate operations.

Conclusions and Oulook

Italian OFDI surged in recent years after having stagnated in 2000-2004. It is worth highlighting that this increase continued in the crisis year of 2009. Notwithstanding the

[226] Founded in 1990 and in operation since 1991, SIMEST is controlled by the Ministry for International Trade and Commerce, along with private share-holders which include major Italian banks and industrial companies. For more information see http://www.simest.it.
[227] The main shareholders of FINEST, founded in 1991, are local administrations of the North-Eastern Italian regions, SIMEST and several banks. For more information see http:\\www.finest.it.
[228] A soft loan is a loan with a below-market interest rate.
[229] For more information see http://www.ice.gov.it and http://www.assocamerestero.it.
[230] For the list of BITs signed by Italy, see http://www.unctad.org/sections/dite_pcbb/docs/bits_Italy.pdf.
[231] For more information see http://www.finanze.it/export/finanze/Per_conoscere_il_fisco/fiscalita_Comunitaria_Internazionale/convenzioni_e_accordi/convenzioni_stipulate.htm

crisis, Italian companies have not divested abroad on a larger scale; on the contrary, they continue to grow. The recent trend of Italian OFDI can be characterized by a renewed leading role of larger companies, by an increasing amount of foreign investment in services sectors and by an increasing presence of Italian companies in countries outside the EU, especially in the United States and the newly emerging economies. However, the role of SMEs is also worth emphasizing; they operate independently from large MNEs and hold competitive advantages in high valued added market niches, and carry out M&As abroad as a vehicle to strengthen their position in international value chains, including knowledge sourcing strategies. This specific phenomenon, sometimes called by the press "Pocket MNEs", is possibly the most valuable and original contribution of Italy to global OFDI trends.

Italian OFDI abroad is expected, at least in the medium term, to evolve in a more similar fashion (both in quantity and in quality) to that of its main international partner and competitor countries.

Additional readings

Banca d'Italia, *Local Economies and Internationalization in Italy*, available at: http://www.bancaditalia.it/studiricerche/convegni/atti/econ_loc;internal&action=_setlanguage.action?LANGUAGE=en.

ICE, *Rapporto ICE 2009-2010. L'Italia nell'economia industriale* (Roma, 2010) (http://www.ice.it/statistiche/rapporto_ICE.htm).

ISTAT, *Le imprese a controllo nazionale residenti all'estero*, Statistiche in breve, 31 maggio 2010, Rome

(http://www.istat.it/salastampa/comunicati/non_calendario/20100531_00/).
Mariotti, Sergio and Marco Mutinelli, *Italia Multinazionale 2010* (Rubbettino Editore, 2011).

Useful websites

For FDI policy: www.ice.it/statistiche/pdf/Rapporto_ICE_2010_cap9.pdf

For FDI statistics: www.istat.it; www.bancaditalia.it

For information on Italian MNEs:

www.ice.it/statistiche/pdf/Rapporto_ICE_2010_cap9.pdf;

http://www.ice.gov.it/statistiche/pdf/Sintesi_Italia_Multinazionale_2008.pdf

Statistical annex

Annex table 1. Italy: outward FDI stock, 2000, 2009 (US$ billion)

Economy	2000	2009
Italy	180	578
Memorandum: comparator economies		
France	926	1 720
Germany	542	1 378
Spain	129	646
United Kingdom	898	1 652

Source: UNCTAD's FDI/TNC database, available at: http://stats.unctad.org/fdi/.

Annex table 2. Italy: outward FDI flows, 2000-2009 (US$ billion)

Economy	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
Italy	12	21	17	9	19	42	42	91	44	44
Memorandum: comparator economies										
France	177	87	50	53	57	115	111	164	161	147
Germany	57	40	19	6	21	76	119	162	135	63
Spain	58	33	33	29	61	42	104	137	75	16
UK	233	59	50	62	91	81	87	318	161	18

Source: UNCTAD's FDI/TNC database, available at: http://stats.unctad.org/fdi/.

Annex table 3. Italy: distribution of outward FDI stock, by economic sector and industry, 2000, 2009[a] (Percentage shares)

Sector/industry	**2000**	**2009**
All sectors/industries (excluding banking services)	100.0	100.0
Agricultural, forestry and fishing products	0.3	0.4
Energetic products (petroleum; electricity, gas and water supply)	8.0	26.1
Industrial products	32.3	29.5
Minerals and metals	4.1	2.7
Chemical products	4.7	5.9
Machinery	8.0	9.0
Transport equipment	4.4	2.9
Food products	2.9	2.2
Textiles and wearing apparel	1.8	1.4
Services	59.5	44.0
Trade and repairs	4.5	3.8
Transports, storage and communication	3.0	0.8
Financial intermediation[a]	35.9	27.2

Source: Banca d'Italia, *Relazione Annuale sul 2009* (Roma, May 31, 2010); Banca d'Italia, *Relazione Annuale sul 2000* (Roma, May 31, 2001) (available at: http://www.bancaditalia.it/pubblicazioni/relann).

a Classified according to the activity of the foreign operator. FDI in the real estate sector and by the Italian banking sector are not included.

b The banking sector is not included.

Annex table 4. Italy: geographical distribution of outward FDI stock, 2000, 2009
(Percentage shares)

	2000	2009
World	100.0	100.0
Developed countries	n.a.	88.0
Europe	n.a.	80.0
EU-27	n.a.	76.9
EU-15	n.a.	75.3
Belgium	1.8	3.2
France	10.0	7.9
Germany	6.7	4.7
Luxembourg	12.6	5.5
Netherlands	14.9	30.7
Spain	4.1	13.1
Sweden	0.4	0.2
United Kingdom	8.7	5.7
Liechtenstein	0.1	0.1
Switzerland	6.3	3.0
North America	11.7	7.5
Canada	0.6	0.4
United States	11.1	7.1
Other developed countries	n.a.	n.a.
Japan	0.9	0.4
Developing countries	n.a.	12.0
Africa	n.a.	n.a.
Asia and Oceania	n.a.	n.a.
Latin America and Caribbean	n.a.	n.a.
Argentina	1.5	0.5
Brazil	2.6	1.4
Transition economies	n.a.	n.a.
Unallocated	n.a.	n.a.

Source: Banca d'Italia, *Relazione Annuale sul 2009*, Roma, May 31, 2010; Banca d'Italia, *Relazione Annuale sul 2000* (Roma, May 31, 2001) (available at: http://www.bancaditalia.it/pubblicazioni/relann).

Annex table 5. Italy: principal non-financial MNEs, ranked by foreign sales, 2009

Rank	Company	Industry	Foreign sales (US$ million)	% of total sales
1	ENI	Oil & gas (ENI), engineering (Saipem)	77,016	66.4
2	Exor/FIAT	Motor vehicles and related components (Fiat, Iveco, Magneti Marelli); agricultural and construction machinery (CNH)	53,784	73.5
3	ENEL	Electricity and gas	43,793	50.6
4	Finmeccanica	Aeronautics, helicopters, space, defence electronics and systems, energy and transportation	19,786	78.1
5	Telecom Italia	Telecommunication services	9,189	24.6
6	Edizione (Benetton Group)	Wearing apparel (Benetton); food & beverage and retail services for travellers (Autogrill)	7,752	49.4
7	Luxottica Group	Eyewear	6,841	96.4
8	Italcementi	Cement, ready mixed concrete	5,668	81.3
9	Pirelli & C.	Tyres	5,162	83.0
10	Prysmian	Cables	4,176	80.3
11	Parmalat	Dairy products	4,141	75.0
12	Saras	Petroleum refining	3,836	52.6
13	Indesit Company	Electric domestic appliances	3,000	82.4
14	De Agostini	Publishing, media	2,813	56.2
15	Buzzi Unicem	Cement, ready mixed concrete	2,754	74.0

Source: Politecnico di Milano, *Reprint database.*
1 US$ = 0.737717 euro.

Annex table 5a. Italy: principal MNEs, ranked by foreign employees, 2009

Rank	Company	Industry	Foreign employees	% of total employees
1	FIAT	Motor vehicles and related components (Fiat, Iveco, Magneti Marelli); agricultural and construction machinery (CNH)	109,580	57.7
2	Unicredit	Banking and financial services	109,300	66.2
3	Generali	Insurance	69,366	81.3
4	Edizione	Wearing apparel and textiles (Benetton Group); food & beverage and retail services for travellers (Autogrill)	54,245	75.9
5	Luxottica Group	Eyewear	52,967	87.2
6	ENEL	Electricity and gas	43,087	53,1
7	ENI	Oil & gas (ENI), engineering (Saipem)	40,118	51.2
8	Intesa SanPaolo	Banking and financial services	32,914	31.7
9	Finmeccanica	Aeronautics, helicopters, space, defence electronics and systems, energy and transportation	29,953	41.0
10	Pirelli & C.	Tyres	25,116	84.9
11	Italcementi	Cement, ready mixed concrete	17,179	81.2
12	Parmalat	Dairy products	11,555	83.8
13	Indesit Company	Electric domestic appliances	11,257	69.1
14	Telecom Italia	Telecommunication services	10,285	14,7
15	Prysmian	Cables	10,054	85.9

Source: Politecnico di Milano, *Reprint database.*

Annex table 6. Italy: main M&A deals, by outward investing firm, 2007-2009
(US$ billion)

Year	Acquiring company	Target company	Target industry	Target economy	Shares acquired (%)	Estimated/ announced transaction value
2007	ENEL SpA	Endesa SA	Electric services	Spain	45.6	26.4
2009	ENEL SpA	Endesa SA	Electric services	Spain	25.0	13.5
2007	ENEL SpA	Endesa SA	Electric services	Spain	11.6	6.3
2007	EniNeftegaz (ENI SpA 60%, ENEL SpA 40%)	OAO Arctic Gas Company ZAO Urengoil OAO Neftegaztechnologia OAO Gazprom Neft	Oil and gas field exploration services	Russian Fed	100.0 100.0 100.0 20.0	5.8
2008	Finmeccanica SpA	DRS Technologies Inc	Defense electronics	United States	100.0	5.5
2007	ENEL SpA	Endesa SA	Electric services	Spain	9.99	5.5
2008	Generali SpA-Central & Eastern	PPF Group-Central & Eastern	Insurance	Czech Republic	100.0	4.9
2007	ENI SpA	Dominion Resources-Exploration Assets	Oil and gas field exploration services	United States	100.0	4.8
2009	ENI SpA	Distrigaz	Distribution of natural gas	Belgium	100.0	4.5
2007	Mediaset-Telecinco (with Cyrte Fund e Goldman Sachs Private Equity)	Endemol	Broadcasting	Netherlands	33.0	3.6
2007	ENI SpA	Burren Energy	Extraction of petroleoum	United Kingdom	100.0	3.3
2007	Luxottica Group SpA	Oakley Inc	Sunglasses	United States	100.0	2.3
2007	Pirelli & C. Real Estate	Baubecon	Real estate	Germany	100.0	2.2
2007	Unicredit (via Bank Austria)	Ukrsotbank (USB)	Banking	Ukraine	94.2	2.2
2008	Unicredito Italiano SpA	Bayerische Hypo- und Vereins	Banks	Germany	4.5	1.9
2007	ENEL SpA	OGK-5	Electricity	Russian Federation	12.2	1.5
2007	ENI SpA	Maurel & Prom SCA-Congo	Crude petroleum and natural gas	Rep of Congo	100.0	1.4
2009	Edison SpA	EGPC-Abu Qir Concession	Crude petroleum and natural gas	Egypt	100.0	1.4
2008	Unicredito	Bank Austria	Banks	Austria	3.7	1.3

	Italiano SpA	Creditanstalt AG				
2008	ENI SpA	First Calgary Petroleums Ltd	Crude petroleum and natural gas	Canada	100.0	1.2
2008	Autogrill SpA	World Duty Free Europe Ltd	Liquor stores	United Kingdom	100.0	1.1
2007	ENEL SpA	Electrica Muntenia Sud SA	Electric services	Romania	67.5	1.1

Source: Thomson ONE Banker, Thomson Reuters.

Note : M&A by Italian companies controlled by foreign MNEs are excluded.

Annex table 7. Italy: main greenfield projects, by outward investing firm, 2007-2009
(US$ billion)

Year	Investing company	Joint venture partner (if any)	Industry	Target economy	Shares owned (%)	Estimated/ announced investment value
2009	Telecom Italia SpA		ICT (internet broadband services)	Brazil	100.0	4.3
2009	ENI SpA	Calik Energy	Oil & gas (pipeline)	Turkey	n.a.	4.0
2007	Fiat SpA		Automotive OEM (motor vehicles)	Brazil	100.0	2.8
2008	Techint SpA		Metals (Iron)	Mexico	100.0	2.7
2007	ENEL SpA		Electrical energy (coal-powered energy plant)	Portugal	100.0	2.7
2008	Moncada Energy Group		Electrical energy (wind farm)	Tunisia	100.0	2.4
2007	ENI SpA		Oil & gas (oil extraction)	Angola	100.0	2.3*
2007	ENEL SpA		Electrical energy (thermoelectric power plant)	Albania	100.0	2.2
2008	Techint SpA		Metals (iron)	Mexico	100.0	1.6
2008	ENEL SpA	E.On (Germany)	Electrical energy (thermoelectric power plant)	Romania	n.a.	1.5
2008	Falcione Group		Oil & gas (liquified natural gas regasifier terminal)	Albania	100.0	1,5
2008	ENI SpA		Oil & gas (oil extraction)	United States	100.0	1,5
2009	ENI SpA	Allied Energy	Oil & gas (oil extraction)	Nigeria	40.0	1.3*
2007	ENI SpA		Oil & gas (oil extraction)	Algeria	100.0	1.2
2008	IT Holding		Real Estate	UAE	100.0	1.2
2008	Techint SpA		Metals	Argentina	100.0	1.2
2008	Fiat SpA		Automotive OEM (motor vehicles)	Serbia	100.0	1.1
2009	Finmeccanica SpA		Coal, oil and natural Gas	Syria	100.0	0.9
2009	Todini Finanziaria SpA		Hotels & tourism	Russia	100.0	0.9
2009	Moncada Energy Group		Electrical energy (wind farm)	Tunisia	100.0	0.8*

Source: fDi Intelligence, a service from the Financial Times Ltd.
* Estimated.

Chapter 10 – Norway

Outward FDI and its policy context, 2010

Gabriel R.G. Benito

Norwegian OFDI has increased substantially since the turn of the millennium: the country's stock of US$ 30 billion in 2000 had grown to US$121 billion in 2008, i.e. a 300% increase. That represents a notable average annual growth rate of 19%. But the development of Norwegian OFDI has been rather uneven, with stable periods punctuated by boom years. 2008 ended at the same level as the preceding year, reflecting the cooling down of the world economy as a result of the international financial crisis and recession. The latest available data indicate that OFDI remained in a slump in 2009. As a country with liberal policies regarding companies' foreign activities, the composition of Norwegian OFDI largely follows the structure of Norway's private sector economy, with a striking dominance of the manufacturing, oil and gas and shipping sectors.

Trends and developments

Norwegian OFDI has increased considerably since the turn of the millennium. The stock of Norwegian OFDI amounted to US$ 121 billion at the end of 2008 (annex table 1), the same figure as the preceding year.[232] That puts Norway between its – in terms of population – very comparable Nordic neighbors Denmark (US$ 150 billion) and Finland (US$ 88 billion), but considerably lower than its somewhat larger neighbor Sweden, whose OFDI stock in 2008 was US$ 253 billion.[233] All Nordic countries have highly internationalized and open economies. However, relatively speaking, i.e. compared with the size of their national economies, it is actually Norway that is the "laggard" amongst the Nordic countries in terms of FDI. In 2008, the value of Norwegian OFDI stock amounted to 44% of its GDP, whereas the 2008 OFDI-stock/GDP ratios in Denmark and Sweden were 75% and 74%, respectively. In Finland, the OFDI stock amounted to 47% of its GDP in 2008.[234]

[232] This report deals with FDI made by companies. As is well-known, a considerable amount of Norwegian investment is managed by the country's sovereign wealth fund the *Government Pension Fund – Global* (www.regjeringen.no/en/dep/fin). The fund invests in both financial instruments and equity; the market value of its holdings amounted to more than US$ 400 billion at the end of 2009 (www.norges-bank.no/templates/report76238.aspx). However, the guidelines for the fund specifically state that equity holdings are limited to less than ten percent of the equity of any given company. Hence, the fund does not engage in FDI.

[233] Figures taken from UNCTAD's, foreign direct investment database, available at: http://stats.unctad.org/fdi/. The original data are compiled by Statistics Norway, available at: www.ssb.no.

[234] Calculated on the basis of OFDI figures taken from UNCTAD's foreign direct investment database, op. cit. and figures from the World Bank, available at: www.worldbank.org.

Country-level developments

The year-by-year pattern shows a rather uneven development of Norwegian OFDI. Stable periods punctuated boom years (annex tables 1 and 2). To some extent, this is due to general developments in the world economy, especially the boom period from 2003 to 2007. After a slow start at the turn of the millennium due to, above all, the burst of the IT bubble, a couple of years followed characterized by a somewhat uneasy international political situation. However, the pattern also reveals some unique and rather enduring characteristics of Norwegian OFDI,[235] of which the bulk stems from investments made by a rather small set of relatively large Norwegian companies such as Statoil, Aker, Kvaerner (now part of Aker), Norsk Hydro (which was split into Yara International, Hydro and StatoilHydro – which was recently renamed Statoil again), Norske Skog and Telenor.[236]

The combination of a small number of companies and the sometimes very large investments made by these companies typically results in a pattern where FDI flows may vary considerably from one year to the next. For manufacturing companies like Aker, Hydro and Yara International, increasing one's global or regional manufacturing capacity by acquiring an existing plant somewhere else typically entails a large investment for the company, but such investments are seldom done every year. Likewise, oil companies like Statoil strive to expand their production base by obtaining licenses to explore, develop and operate new fields, but new ventures tend to come in a lumpy way, both because the availability of attractive new projects is limited and considerable time and effort is needed to succeed in getting them, and because the capital requirements for taking on each new venture are formidable for even the largest oil companies. Finally, Telenor is a telecommunications company that has successfully expanded internationally during the past decade: but since each entry into a new country requires considerable capital investments and resource commitments – often over a period of some years after the initial entry – the company has to find a balance between its strategic ambitions and its means to carry them out; hence, it cannot enter into major new markets on an annual basis.

Aggregate returns on OFDI rose from US$ 5 billion in 2004 to US$ 11 billion in 2007, indicating that returns to OFDI slightly improved over that period, with returns on stock ratios moving from 6 in 2004 to 9 in 2007.[237] The bulk of returns are typically repatriated dividends. In 2007, 75% of total returns were dividends, 15% were reinvested earnings and 10% were net interest income.

[235] See G.R.G. Benito, J. Larimo, R. Narula, and T. Pedersen, "Multinational enterprises from small economies: internationalization patterns of large companies from Denmark, Finland and Norway," *International Studies of Management and Organization* (32) (2002), pp. 57-78.

[236] According to Grünfeld (2005) about 70 % of all Norwegian OFDI is done by its five largest MNEs, and the twenty largest MNEs represent approximately 85% of total OFDI; see L.A. Grünfeld, "Kapitalens utvandrere: Norske investeringer og aktiviteter i utlandet (Capital emigrants: Norwegian investments and activities abroad)," *Økonomisk Forum*, 59 (2005), pp. 7-19.

[237] Figures provided by Statistics Norway, op. cit. Returns (US$ at current prices and exchange rates) were 5 billion in 2004, 12 billion in 2005, 9 billion in 2006, and 11 billion in 2007.

The composition of Norwegian OFDI largely emulates the structure of the private sector in the Norwegian economy: close to half of the Norwegian OFDI stock is in manufacturing and in oil and natural gas exploration and extraction (annex table 3). The OFDI shares of these two sectors have been fairly stable over the past decade – the two sectors together represented 48% of the Norwegian OFDI stock in 2000 and 47% in 2008 – but there is a discernible trend toward a slightly lower importance of manufacturing over time. Conversely, the importance of the oil and natural gas sector has increased somewhat during the first decade of this millennium. The sectoral distribution of the Norwegian OFDI stock also shows that the shipping industry, which has traditionally been very important in Norway, [238] is highly international: together with telecommunications (i.e. mainly Telenor), the shipping industry counts for almost 17% of Norwegian OFDI in 2008.

At the turn of the millennium, the lion's share of OFDI went to other developed countries (annex table 4). The European Union (EU) in particular was the main recipient, with almost two-thirds of Norwegian OFDI, followed by Sweden and the UK (19% each) and the US (13%). Other major host countries were The Netherlands and Denmark. Thus, as late as in 2000, the geographical composition clearly retained much of its historical structure, with a heavy emphasis on countries that are geographically and culturally close to Norway.[239]

In just a few years, however, the picture had changed considerably. In 2006, the EU share of total OFDI stock had dropped to just 55%; even within the EU, there has been a small but evident shift from the traditional host countries (the Nordic countries, UK, France, Germany) to countries in Southern and Central Europe. Nevertheless, the most noticeable change is the increasing importance of countries outside the EU and US, i.e. countries such as Canada, Singapore and Brazil, and perhaps most dramatic, the influx of Norwegian investments into Algeria, Angola and Azerbaijan. The bulk of these investments were made by oil and gas companies looking for opportunities outside their traditional domain of North Sea exploration and production. In the case of Singapore, much of the investment has traditionally been shipping related, but in recent years it has also been in alternative and renewable energy technologies such as solar energy.

The corporate players

While the Norwegian economy is very open – international trade (imports plus exports) as percent of GDP has hovered at between 80 and 86 in the past decade – and there are quite many export firms and companies that have foreign affiliates of various sorts, there are very few truly large Norwegian MNEs; but, being a small country with slightly fewer than 5 million inhabitants, that is of course not surprising. Among Norwegian MNEs, only Statoil and Telenor are included in the *World Investment Report*'s 2007 top 100 list of non-financial MNEs, on places 62 and 99, respectively. The list of the twenty largest

[238] G.R.G. Benito, E. Berger, M. de la Forest, and J. Shum, "A cluster analysis of the maritime sector in Norway," *International Journal of Transport Management* (1) (2003), pp. 203-215.
[239] R.P. Amdam, "The internationalisation process theory and the internationalisation of Norwegian firms, 1945 to 1980," *Business History* (51) (2009), pp. 445-461.

Norwegian MNEs (annex table 5),[240] comprises companies in a variety of industries. It is noteworthy that the four largest MNEs are partly state-owned, and six more companies on the list are also wholly or partially owned by either the Norwegian State or a public authority (e.g. municipalities): Aker Solutions (40%-owned by Aker Holding, where the state has a 30% share), DnBNor, KLP, Posten, Statkraft, and Hafslund.

Foreign direct investments are usually classified into four main types, based on the primary motivations behind them: (*i*) resource-seeking, (*ii*) market-seeking, (*iii*) efficiency-seeking, and (*iv*) asset-seeking.[241] Although Norwegian companies' OFDI can be grouped into all four categories, the three first mentioned motives are by far the most common:

- First, resource-seeking investments are typically made by oil and gas companies into exploration and production activities. Norwegian oil companies had operated mainly in the North Sea until about a decade ago, but have increasingly ventured into field exploration, development and production projects elsewhere -- lately in Africa and South America. The fish farming industry is another example – even though the total volume of investment is much lower – of resource-seeking investment, with significant projects in Chile, Canada and the UK (Scotland).
- Second, internationalization motivated by market-seeking is exemplified by Telenor's expansion since the mid-1990s into numerous European and Asian markets, with entries into Pakistan (2005) and India (2009) being the most recent. Telenor's entry into India in 2009, which involved greenfield investments as well as the acquisition of an equity stake in Unitech Wireless, was by far that year's largest foreign entry made by a Norwegian company (annex tables 6 and 7).
- Third, Norway's generally high-cost position has led to considerable efficiency-seeking OFDI activity by manufacturing companies, in recent times even affecting "high value-added" manufacturing activities in sectors such as energy generation and infrastructure, ship building and offshore facilities. A consistently strong currency (Norwegian kroner) throughout most of the decade, partly fuelled by a comparatively high interest rate level, has provided a steady impetus to move manufacturing activities offshore.

While asset-seeking investments are perhaps less conspicuous in the broader picture of Norwegian OFDI, asset-seeking motives have been strong drivers for some companies. The development of three companies in the solar energy area – REC, Scatec, Vetro Solar – is illustrative. Expanding by acquisitions as well as greenfield investments (annex tables 6 and 7), these companies have recently moved into selected locations in Germany (Vetro Solar; glass production and processing), Singapore (Scatec; silicone wafer

[240] Only Norwegian MNEs are listed in annex table 5. Hence, companies without foreign operations are excluded, as are foreign-owned Norwegian affiliates, some of which are quite large (for example in terms of revenues), especially in the oil and gas sector.
[241] J.H. Dunning and S.M. Lundan, *Multinational Enterprises and the Global Economy* (Cheltenham: Edward Elgar, 2008).

production; REC, integrated production) and US (REC: R&D lab in Silicon Valley, CA, and silicon technology and production center in Moses Lake, WA).

For some companies, the motives are obviously more mixed, such as Statkraft's (SN Power) various electricity production projects using hydro, gas, wind, and solar technologies in numerous European countries, and recently in Peru (annex tables 6 and 7). FDI in (renewable) energy production and supply typically takes into account resource availability (waterfalls, wind, sun etc.) as well as market conditions (current and future electricity demand).

Effects of the current global crisis

As shown in annex tables 1 and 2, the latest available data reveal that the recent global economic crisis barely had a slowing down effect on aggregate FDI flows in 2008, with 2008 ending on about the same level as the preceding year; hence, Norwegian OFDI has been less affected than, for example, that of its neighbor Finland. However, the decline in OFDI may have begun late in 2008, with FDI outflows dropping more sharply in 2009.[242]

An apparent dip in investment can be seen when the values of major M&A deals completed in 2009 are compared to deals completed in the two preceding years (annex table 6): the three largest deals in each of the years 2008 and 2007 are far larger than the single top deal of 2009.[243]

Apart from Telenor's very substantial investment into the Indian market in 2009, a similar pattern emerges when comparing greenfield investments across the years 2007 to 2009 (annex table 7). The average value for the ten largest greenfield projects in 2009 was US$ 659 million, down from US$ 893 million in 2008 and US$ 1,286 million in 2007.

It must be noted however that it may not be straightforward to compare asset prices before the crisis with those during and after it. Economic crises typically lead to lower prices for property, equity and various investment assets, which in turn will affect the values of M&A transactions and greenfield investments. Also, although an economic crisis *per se* might increase the risks associated with foreign investments, the strong Norwegian currency combined with lower asset prices abroad currently makes it relatively more attractive to pursue foreign investment opportunities. Nevertheless, a more marked downturn is likely to have happened in 2009. The most recently available balance-of-payments data from Statistics Norway show a large drop in foreign invested equity capital in 2009 (down 90% from 2008), but an equivalent increase in OFDI in the form of loans.[244]

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[242] For example, a sharp drop in OFDI was revealed for 2009 in the case of Germany; see R. Hirdina and T. Jost, "Outward FDI of Germany and its policy context," **Columbia FDI Profiles,** April 9, 2010**.**

[243] The average value for the top 10 M&A deals dropped dramatically from US$ 867 million in 2007 and US$ 791 million in 2008, to only US$ 97 million in 2009.

[244] Statistics Norway, available at: www.ssb.no/ur_en/tab-fin-aar-en.html.

The policy scene

Regulations – both in terms of concession laws regulating inward foreign investments and takeovers, and in terms of capital and foreign exchange permits needed to make outward investments – were loosened considerably in the early 1980s on both OFDI and IFDI.[245] Norway has been part of the European Economic Area agreement since 1994, which governs much of its economic relations with Europe. Beyond Europe, Norway generally favors multilateralism with the UN and WTO as key institutions.

Norwegian authorities have generally taken a *laissez faire* approach to Norwegian companies' foreign investments. The official policy is that such investments should be made on the basis of business interests and benefits, as long as due concern is taken of taxation, corruption and security issues.[246] A variety of assistance measures for internationalizing firms are available through the governmental agency Innovation Norway. The Norwegian Government also actively promotes and assists investments in less developed countries. An investment fund, NORFUND, dedicated to such investments has been operating since 1997, and GIEK, the state-owned Norwegian Guarantee Institute for Export Credits, provides an insurance scheme against political risk concerning foreign investments.

Despite the dominant position of the Norwegian State as an owner of several large commercial companies and businesses, national authorities tend to take a hands-off approach to their management, including their internationalization strategies.[247] Although concerns are sometimes raised about a possible "exporting of jobs" due to investments abroad, it is widely accepted that competitiveness is the only way to sustain domestic employment in the private sector.

Conclusions and Outlook

Norway was a relative latecomer to the OFDI scene, and it is only during the past few decades that it has become a home country for significant MNEs. Norwegian OFDI has increased considerably since the turn of the millennium, and the composition of that investment has undergone some noticeable changes during a relatively short period of time. Traditional efficiency-seeking and market-seeking OFDI remain important for most Norwegian MNEs, but, alongside them, resource-seeking investments have also risen appreciably in recent years. Norway's large energy companies – oil and gas as well as renewable energy – have become front runners in this millennium's wave of FDI, which has led them to countries that previously were seldom hosts to Norwegian companies.

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245 OECD, *Reviews of Foreign Direct Investment: Norway* (Paris: OECD, 1995).

246 There are tight guidelines on ethical, environmental and social responsibility issues for investments made by the country's sovereign wealth fund, the *Government Pension Fund – Global* (available at: www.regjeringen.no/en/dep/fin), but private investments are generally left to the discretion of the companies and their owners.

247 H. Hveem, "Norwegian foreign policy and investment abroad: confusing conditions?" *Internasjonal Politik,* (67) (2009), pp.380-411.

Additional readings

Benito, Gabriel R.G, and Rajneesh Narula, eds., *Multinationals on the Periphery* (London: Palgrave, 2007).

Hodne, Fritz, "The multinational companies of Norway," in Geoffrey G. Jones and Harm Schröter, eds., *The Rise of Multinationals in Continental Europe* (Cheltenham: Edward Elgar, 1993), pp. 128-151 .

Lunde, Leiv, Henrik Thune, Eiler Fleischer, Leo A. Grünfeld, and Ole Jacob Sending, *National Interest: Foreign Policy for a Globalised World. The Case of Norway* (Oslo: Norwegian Ministry of Foreign Affairs 2008).

OECD, *OECD Economic Surveys: Norway 2010* (Paris: Organisation for Economic Co-operation and Development, 2010), available at: www.oecd.org/norway.

Van den Bulcke, Daniel, Alain Verbeke and Wenlong Yuan, eds., *Handbook of Small Nations in the Global Economy: The Contribution of Multinational Enterprises to National Economic Success* (Cheltenham: Edward Elgar, 2009).

Useful websites

For statistical material about Norway, see Statistics Norway, *Focus on: External Economy,* available at: www.ssb.no/ur_okonomi_en/.

For trade policy issues, regulations and international relations, the web portal www.government.no provides many useful links. The web pages of the Ministry of Foreign Affairs (www.regjeringen.no/en/dep/ud) and the Ministry of Trade and Industry (www.regjeringen.no/en/dep/nhd) are particularly relevant.

Statistical annex

Annex table 1. Norway: outward FDI stock, [a] **2000 to 2008** (US$ billion)

Economy	**2000**	**2001**	**2002**	**2003**	**2004**	**2005**	**2006**	**2007**	**2008**
Norway	30.3	32.7	42.8	49.0	79.4	76.3	95.7	121.6	121.5
Memorandum: comparator economies									
Denmark	45.9	43.5	53.1	65.8	82.5	94.0	108.0	120.5	150.5
Finland	24.3	24.1	34.0	50.3	57.4	54.8	70.6	92.1	87.9
Sweden	94.0	91.9	119.4	158.9	196.2	171.8	227.5	290.0	253.5

Source: UNCTAD's FDI/TNC database, available at: http://stats.unctad.org/fdi/. Data for Norway are originally compiled by Statistics Norway, available at: www.ssb.no.

[a] All figures in US$ at current prices and current exchange rates.

Annex table 2. Norway: outward FDI flows, 2000 to 2008 [a] (US$ billion)

Economy	2000	2001	2002	2003	2004	2005	2006	2007	2008
Norway	7.1	2.1	0.8	3.5	2.5	5.4	6.4	4.4	-0.1
Memorandum: comparator economies									
Denmark	16.5	5.8	5.8	2.4	-0.9	8.9	8.2	9.4	10.9
Finland	8.8	3.7	8.0	3.3	2.8	4.8	7.6	12.4	-4.2
Sweden	23.4	10.9	12.3	5.0	11.0	10.1	27.2	22.1	43.7

Source: UNCTAD's FDI/TNC database, available at: http://stats.unctad.org/fdi/. Data for Norway are originally compiled by Statistics Norway, available at: www.ssb.no.

[a] All figures in US$ at current prices and current exchange rates.

Annex table 3. Norway: distribution of outward FDI stock, by economic sector and industry, 2000 and 2008[a, b]

Sector / industry	2000	2008
All sectors / industries	US$ 30 billion	US$ 121 billion
Distribution across sectors (*in percent*)	*100*	*100*
Primary		
Mining, quarrying and petroleum	*22*	*23*
Secondary		
Manufacturing, of which:	*26*	*24*
• Chemicals	*8*	*4*
• Paper and pulp	*2*	*4*
• Basic metals	*1*	*4*
• Food and beverages	*2*	*2*
• Automotive	*5*	*3*
Services		
Transport and communication	*16*	*17*
Banking, finance, and real estate	*16*	*12*
Wholesale and retail, incl. hotels and restaurants	*4*	*3*
Unspecified other sectors/industries	*17*	*21*

Source: Statistics Norway, available at: www.ssb.no.

[a] Figures in US$ at current prices and current exchange rates.
[b] Percentages may not add up to hundred due to rounding.

Annex table 4. Norway: geographical distribution of outward FDI stock, 2000 and 2006.[a, b]

Economy / region	2000	2006
World (US$ billion)	US$ 30 billion	US$ 97 billion
Distribution across economies (*in percent*)	*100*	*100*
Europe	***70***	**58**
European Union	*68*	*55*
Denmark	*9*	*4*
Finland	*2*	*2*
France	*2*	*2*
Germany	*3*	*4*
Netherlands	*6*	*8*
Sweden	*19*	*21*
UK	*19*	*4*
Other EU countries	*9*	*11*
Other European countries	*3*	*3*
North America	***14***	***15***
United States	*13*	*10*
Canada	*1*	*5*
Other developed countries	*0*	***2***
Australia	*0*	*1*
Japan	*0*	*0*
Other countries	***16***	***26***
Algeria	*0*	*2*
Angola	*1*	*2*
Azerbaijan	*0*	*3*
Brazil	*2*	*2*
Singapore	*3*	*8*
Other	*10*	*9*

Source: Statistics Norway, available at: www.ssb.no.

[a] Figures in US$ at current prices and current exchange rates.
[b] Percentages may not add up to hundred due to rounding.

Table 5. Norway: twenty largest MNEs headquartered in the country, ranked by total sales in 2008 [a] (US$ billion)

Rank	Name	Industry	Total sales (US$ billion)
1	StatoilHydro ASA	Oil and gas operations	112.4
2	Telenor ASA	Telecommunications	16.8
3	Yara International ASA	Chemicals	15.3
4	Hydro ASA	Metals	15.3
5	Orkla ASA	Conglomerate	11.3
6	Aker Solutions ASA	Ship yards	10.0
7	Reitangruppen AS	Retailing	9.8
8	DnB Nor	Banking, insurance and finance	5.9
9	KLP	Banking, insurance and finance	5.0
10	Posten Norge AS	Postal services	4.9
11	Storebrand ASA	Banking, insurance and finance	4.8
12	Norske Skog ASA	Paper and pulp	4.4
13	Statkraft	Electricity and renewable energy	4.3
14	Veidekke ASA	Construction	3.3
15	Tine Gruppen	Food products	3.2
16	Gjensidige	Banking, insurance and finance	3.0
17	Nortura SA	Food products	2.9
18	Atea ASA	Business services	2.7
19	Schibsted ASA	Media	2.3
20	Hafslund	Electricity and renewable energy	1.9

Source: Dagens Næringsliv "DN 500" and the Amadeus Database.

[a] List only includes companies that are Norwegian (fully or partly) owned. Norwegian subsidiaries of foreign groups are excluded.

Table 6. Norway: the 10 most important completed M&A deals, by outward investing firm, 2007-2009

Year	Acquiring company	Target company	Target industry	Target economy	Equity share (%)	Transaction value (US$ million)
2009	Telenor ASA	Unitech Wireless Ltd	Telecommunication	India	49.0	477
2009	StatoilHydro ASA	World Point Terminals	Oil and natural gas	Bahamas	100.0	258
2009	Statktaft SA	Yesil Enerji	Renewable energy	Turkey	95.0	137
2009	Schibsted ASA	InfoJobs SA	Media	Spain	98.5	49
2009	Telenor ASA	BiBoB AS	Telecommunication	Denmark	100.0	17
2009	Tilway Oil	Toreador Turkiye Ltd	Oil and natural gas	Turkey	100.0	11
2009	Cecon ASA	Davie Yards Inc	Ship yards	Canada	39.3	7
2009	Statkraft SA	Atlantis Resources Corp Pte	Renewable energy	Singapore	…	7
2009	Rocksource Geotech AS	TechnoImaging LLC	Oil and natural gas	USA	36.0	5
2009	Offshore Holding AS	Davie Yards Inc	Ship yards	Canada	28.5	5
2008	StatoilHydro ASA	Chesapeake Energy-Marcellus	Oil and natural gas	USA	32.5	3375
2008	StatoilHydro ASA	Anadarko Petroleo Ltda	Oil and natural gas	Brazil	100.0	1800
2008	Yara International ASA	Saskferco Products Inc	Chemicals	Canada	100.0	1590
2008	Revus Energy ASA	Palace Exploration	Oil and natural gas	UK	100.0	258
2008	Aker Solutions ASA	Qserv Ltd	Oil and natural gas	UK	100.0	197
2008	Herkules PEF	Gothia-AFS Business	Business services	Sweden	100.0	163
2008	Investor Group	Stena Fastigheter AB	Real estate	Sweden	100.0	142
2008	Imarex ASA	Spectron Group Ltd	Oil and natural gas	UK	100.0	138
2008	SeaDrill Ltd	Scorpion Offshore Ltd	Oil and natural gas	Bermuda	36.0	127
2008	Norsk Hydro ASA	Alumafel SA	Metals	Spain	100.0	119
2007	Storebrand ASA	SPP Livsförsäkring AB	Insurance	Sweden	100.0	2761
2007	Statoil ASA	North American Oil Sands Corp	Oil and natural gas	Canada	100.0	1961
2007	Investor Group	Aibel	Oil and natural gas	UK	100.0	900
2007	Acta Holding ASA	Property Portfolio	Real estate	Germany	100.0	693
2007	Kongsberg Automotive ASA	Teleflex Inc – Global Automotive	Automotive	USA	100.0	560
2007	Acta ASA	Kuwait Finance House - Malon	Real estate	Sweden	100.0	553
2007	Statkraft Norfund	Electroandes SA	Renewable energy	Peru	100.0	390

	Power					
2007	PGS ASA	MTEM Ltd	Oil and natural gas	UK	100.0	276
2007	Block Watne AS	Prevesta AB	Construction	Sweden	100.0	272
2007	Tandberg ASA	Codian Ltd	Electronics	UK	100.0	270

Source: Thomson One Banker, Thomson Reuters.

Table 7. Norway: top 10 greenfield projects per year, by outward investing firm, 2007-2009 [a]

Year	Investing company	Target industry	Target economy	Investment (US$ million)
2009	Telenor ASA	Telecommunication	India	3200
2009	KLP	Real estate	Denmark	804
2009	Statkraft	Renewable energy	UK	651
2009	StatoilHydro ASA	Oil and natural gas	Indonesia	525[a]
2009	Umoe Group	Renewable energy	Canada	480
2009	Bonheur ASA	Renewable energy	Sweden	216[a]
2009	StatoilHydro ASA	Oil and natural gas	Brazil	213[a]
2009	Norse Energy Corp ASA	Oil and natural gas	Brazil	200[a]
2009	InterOil E&P ASA	Oil and natural gas	Peru	160[a]
2009	InterOil E&P ASA	Oil and natural gas	Colombia	140[a]
2008	Intex Resources ASA	Metals	Philippines	2900
2008	StatoilHydro ASA	Oil and natural gas	Greece	1500
2008	REC Group	Electronics	Canada	1200
2008	StatoilHydro ASA	Oil and natural gas	Canada	820[a]
2008	Vetro Solar AS	Ceramics & glass	Germany	579
2008	Staur Holding AS	Real estate	Latvia	537
2008	TGS-NOPEC ASA	Business services	Nigeria	378[a]
2008	StatoilHydro ASA	Oil and natural gas	USA	356[a]
2008	Norse Energy Corp ASA	Oil and natural gas	USA	356[a]
2008	Scatec AS	Renewable energy	Singapore	300
2007	REC Group	Renewable energy	Singapore	4354
2007	Norsk Hydro ASA	Metals	Russia	4000
2007	Norsk Hydro ASA	Metals	Brazil	2200
2007	Larvik Cell AS	Paper and packaging	Russia	1086
2007	Yara International ASA	Chemicals	Netherlands	426
2007	Pronova BioPharma ASA	Pharmaceuticals	Denmark	264
2007	Norwegian Air Shuttle ASA	Aerospace	Denmark	194[a]
2007	Global Green One	Renewable energy	Hungary	140
2007	Odfjell	Oil and natural gas	China	107
2007	Norsk Hydro ASA	Metals	Tajikistan	90

Source: Based on information from fDi Intelligence, a service from Financial Times Ltd.

[a] Estimated investment.

Chapter 11 – Poland

Inward FDI and its policy context, 2010

Zbigniew Zimny

By 2009, Poland had attracted the highest IFDI stock (US$ 182 billion) among the new members of the European Union (EU) from Central and Eastern Europe. Its FDI inflows increased considerably after the country's accession to the EU. They fell during the crisis, but rather modestly, remaining at higher levels than in other countries of the region. The combination of a competitive and constantly improving policy framework for FDI and investment in general, the best GDP growth performance among the Organisation for Economic Co-operation and Development (OECD) countries in 2009 and favorable projections for 2010 and 2011 augurs well for the recovery of IFDI in Poland. In fact, there are signs of strong recovery already in the first quarter of 2010, with FDI inflows over two times higher than during the same period of the previous year.

Trends and developments

Country-level developments

With an IFDI stock of US$ 182 billion in 2009 (annex table 1), Poland is, in absolute terms, by far the largest host country among new EU member countries from Central and Eastern Europe.[248] The Czech Republic comes next with a stock of US$ 122 billion and Hungary third (US$ 100 billion). During 2000–2009, Poland received the largest FDI inflows in the region in all years but two, reaching a record of US$ 23 billion in 2007 (annex table 2). After the accession to the EU, annual average inflows into Poland nearly tripled from US$ 6 billion during 2000–2003 to over US$ 16 billion during 2004–2008. Having reached a peak in 2007, IFDI flows declined during the subsequent crisis, to US$ 17 billion in 2008 and US$ 12 billion in 2009 (annex table 2).

During 2000–2008, the composition of Polish IFDI flows improved, reflecting the growing attractiveness of Poland as a business location. During 2000–2003, inflows consisted predominantly of equity capital, with some loans of parent corporations to their Polish affiliates and negative reinvested earnings. Since 2004, in every year but 2008, reinvested earnings were strongly positive, accounting for 30% of total FDI inflows while the share of equity capital fell to 45%. Foreign investors started reaping increasing benefits, as indicated by the surge in dividends transferred from affiliates to parent companies, which amounted to nearly US$ 12 billion in 2008.[249]

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[248] These countries include, apart from Poland, Bulgaria, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Romania, Slovakia, and Slovenia. They compete for FDI, especially export-oriented FDI, benefiting from free access to the EU market.

[249] The ratio of transfers from affiliates (including dividends and income on credit) to FDI inflows rose from 28% during 2000–2004 to 54% during 2005–2008. In 2008, transfers and FDI inflows were almost equal. See Narodowy Bank Polski (NBP), *Zagraniczne inwestycje bezpośrednie w Polsce w 2008 roku* (Warszawa: NBP, 2009) and for the

Services accounted for 68% of Poland's IFDI stock in 2008 (up from 60% in 2000), with trading and financial services as the largest industries, each accounting for 17–18% of the total stock, followed by other business services (9%) and real estate services (8%) (annex table 3). Telecommunications and power generation have also attracted significant foreign investments. IFDI in the primary sector is minimal. In manufacturing (accounting for 31% of IFDI stock in 2008), the largest industries for FDI include food, metal products and motor vehicles (each 7—8% of the total stock).

Nearly all IFDI in Poland originates from developed countries and, among them, predominantly from the EU-15, accounting for over 82% of the total stock in 2008 (annex table 4). The four largest home countries in 2008 (similarly to 2000, although in a different order) were the Netherlands (holding 19% of the stock), Germany (16%), France (11%), and the United States (6%).[250] Between 2000 and 2008, the top four increased their IFDI stock by 280%, but their share in the total stock fell from 65% to 52%, because firms from many other countries invested vigorously in Poland during the 2000s. These included several West European countries, each holding by 2008 a stock of FDI between US$ 3 billion and US$ 5 billion (Ireland, Switzerland, Denmark, Spain) and US$ 5–8 billion (Belgium, Austria, Italy, the UK, Sweden). Significant new home countries also include Japan, increasing its stock to US$ 1.3 billion in 2008.[251] More than 60% of the US$ 5 billion FDI stock from developing economies is registered in Caribbean tax heavens. Only the Republic of Korea (US$ 1 billion) and China (US$ 300 million) are visible as increasingly significant developing home countries, undertaking "genuine" FDI.

The corporate players

The list of the largest 20 foreign affiliates in Poland reflects the importance of the corresponding industries in FDI (annex table 5). Metro Group (Germany), dealing in retail trading and featuring several chains of supermarkets, home, electric and electronic appliances leads the list (with sales of nearly US$ 14 billion in 2008), followed by the largest telecommunication company Telekomunikacja Polska (Telecom France) (US$ 11 billion) and Fiat (Italy), with sales of US$ 7.6. The list also features three MNEs in the automotive industry (in addition to Fiat, Volkswagen, Toyota and Delphi), three banks and six trading companies (in addition to Metro Group).

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years 2000–2007. These are annual publications of the National Bank of Poland on FDI in Poland (in Polish, with English subtitles in the tables).

[250] Luxembourg emerged in 2008 as one of largest home countries, with a stock of US$ 14 billion, and a share in the total IFDI stock equal to 9%. But most of FDI registered in Luxembourg originates from MNEs of other countries, choosing to channel funds to their affiliates through Luxembourg for tax reasons. Since 2006, funds called "capital in transit" have flown through Poland (much of them from Luxembourg and the Netherlands). These funds are registered as inward FDI flows. But in the same year, they have been typically "invested" in other countries, giving rise to FDI outflows from Poland.

[251] Narodowy Bank Polski (NBP), *Zagraniczne inwestycje bezpośrednie w Polsce w 2008 roku* (Warszawa: NBP, 2009).

Cross-border acquisitions were quite important in the 1990s[252] when Poland implemented a large privatization program involving, among others, banks, a couple of power generating firms and manufacturing firms. During the 2000s, privatizations became less important, and cross-border purchases shifted toward Polish private companies that had emerged during the transition process and, sometimes, toward foreign affiliates changing hands among foreign investors (annex table 6). The revival of the privatization program by the current government has added momentum to cross-border M&As.

The growing stock of IFDI in Poland has been accompanied by a growing role of foreign affiliates in the Polish economy, from 16% in 1995, to 34% in 2000 and around 40% in recent years, according to a transnationalisation index that calculates averaged shares of foreign affiliates in all firms in Poland for the following measures: employment, total sales and export sales, investment in fixed assets, value of fixed and current assets and equity and liabilities.[253] With increasing weight, foreign affiliates have made several positive contributions to the Polish economy:[254]

- The labor and capital productivity of foreign affiliates are higher than that of domestic firms by, respectively, 80% and 40%,[255] raising the productivity of the entire economy.
- Foreign affiliates in tradable goods and services exhibit a much higher export orientation than domestic firms: the share of exports in the revenues of the former was 26% in 2008 versus 7% for the latter.[256] The export propensity of foreign affiliates is increasing (in 2000 it was 16%) while that of domestic firms remains stagnant. Consequently, FDI is a driving force of Polish exports, accounting for over 63% of goods exports in 2007 (up from 50% in 2000).
- Foreign affiliates have improved the composition of exports (and that of manufacturing), shifting it toward medium-high and high technology goods (mainly to the former).
- Foreign affiliates employed over 1.5 million people in 2008 (or 28% of the employment of all enterprises in Poland or 11% of the total employment), compared to over 0.9 million in 2000. Given that during this period most FDI consisted of greenfield projects,[257] most of this increase of over 600,000 can be attributed to job creation. In addition, foreign affiliates pay significantly higher wages. For example, in 2007 the average monthly gross salary in manufacturing foreign affiliates was over 55% higher than that in domestic companies.[258]

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[252] The ratio of M&A sales to FDI inflows was 35% during 1991–1995 and 46% during 1996–2000 (calculated from UNCTAD's FDI/TNC data base).

[253] Institute for Market, Consumption and Business Cycles Research (IMCBCR), *Foreign Investment in Poland: Annual Report* (Warszawa: IMCBCR, 2009), pp. 182-83.

[254] If not otherwise indicated, sources of data in this section include annual publications of the Central Statistical Office on *Economic Activity of Entities with Foreign Capital* and those of the Institute for Market, Consumption and Business Cycles Research (IMCBCR) on *Foreign Investment in Poland.*

[255] Labor productivity is measured as sales per employee and capital productivity as sales per unit of fixed assets.

[256] The export propensity of manufacturing affiliates is much higher, at 50%. Manufacturing generates over 80% of Polish exports.

[257] This is indicated by a very low ratio of cross-border acquisitions to total FDI inflows, 4% during 2006–2008 (compared to 17% during 2001–2005). See UNCTAD's FDI/TNC data base.

[258] It was, however, 15% lower than in state-owned companies. Central Statistical Office (CSO), *Statistical Yearbook of Industry* (Warszawa: CSO, 2008), p. 309.

- In the past few years, world renowned MNEs such as Bayer, IBM, Microsoft, LG Electronics, and Oracle, to name a few, have chosen Poland as a location for investment in corporate services, including in R&D. According to PAIiIZ,[259] the Polish investment promotion agency, the number of corporate service centers was nearing 50 in 2008, and that of R&D affiliates was close to 45, both with the tendency to grow. R&D affiliates already employ several thousand persons and conduct R&D in informatics, automotive, chemical, food, and aerospace industries.

Effects of the current global crisis

During the crisis, Poland, as other host countries, has experienced lower IFDI flows. However, FDI reductions have not been drastic. In 2009, the decline by about one third, compared to 2008, was less than in comparator countries (annex table 2). In addition, foreign affiliates did not postpone or suspend their investment plans, at least in the first year of the crisis. Their investment expenditures[260] in fixed assets grew by 19% in 2008 – much faster than their annual average growth during 2004–2007 (16%).[261] Given the significance of the aggregated value of the main greenfield projects announced in 2008–2009 (US$ 22 billion, annex table 7), which will be turned into actual investment expenditures in the near future, the strong investment performance of foreign affiliates is likely to continue in the coming years. Moreover, PAIiIZ did not register any significant weakening of investors' interest in new FDI projects. As of March 2010, the agency had been servicing 122 FDI projects worth € 4.5 billions (or roughly US$ 6 billion), potentially creating over 33,000 jobs.[262]

Moreover, FDI inflows seem to be recovering strongly already in 2010. In the first quarter of 2010, they amounted to US$ 4.5 billion, and were more than two times higher than inflows in the same period of 2009. Half of these inflows were reinvested earnings, signifying their strong recovery.[263] The revival of the privatization program, implemented during 2008–2011, should support FDI recovery.[264]

This relatively good FDI performance during the crisis can be attributed to the relatively good economic performance during the crisis. The crisis affected Poland relatively mildly. Without any significant stimulus package, Poland was the only OECD country to register GDP growth of 1.7% in 2009. Projections for 2010-2011 are favorable, much better than

[259] The Polish acronym for the Polish Agency for Information and Foreign Investment.
[260] In current prices and in national currency.
[261] Annual publications of the Central Statistical Office of Poland on *Economic Activity of Entities with Foreign Capital* (in Polish with English subtitles in the tables). The latest one, listed in the references, is: Central Statistical Office (CSO), *Economic Activity of Entities with Foreign Capital in 2008* (Warszawa: CSO, 2009).
[262] Communication from PAIiIZ.
[263] Communications from the National Bank of Poland on the balance of payments in January, February and March 2010; and Polish Information and Foreign Investment Agency, *Newsletter*, May 20, 2010, number 175.
[264] The government plans to privatize 802 firms for an estimated value of 30 billion of Polish zlotys (or close to US$ 10 billion). Privatization sales were over US$ 2 billion in 2009 and nearly US$ 2 billion in the first four months of 2010. The plan for 2010 is to reach US $ 8 billion of revenues (see the website of the Polish Ministry of Treasury www.msp.gov.pl). Of course, not all privatized firms have been or will be sold to foreign investors. But press reports indicate quite strong interest and participation of MNEs in the program, which will, most likely, add a few billions of dollars to FDI inflows into Poland.

for most other OECD countries, around 3% for each year.[265] So far, no bank or other financial institution in Poland has been threatened by the financial crisis. Polish public debt has been manageable. Amid the surrounding economic turmoil, Poland has been perceived by investors as an island of stability. As A.T. Kearney put it in its 2010 FDI Confidence Index, "the country's relatively strong performance during the crisis gives investors cause for confidence."[266]

The policy scene

With the beginning of the transition toward a market economy in the early 1990s, Poland declared IFDI as one of the key drivers of economic growth and development. Consequently, the country introduced FDI policies serving this purpose, and turned them into treaty commitments through BITs, OECD membership (1997), an association agreement with the EU during the 1990s, and full EU membership since 2004. As early as in 1990, Poland had signed a BIT with the United States, a country known for requiring partner countries to adopt above-average commitments regarding FDI policy. As a result, since the beginning of the transition, Poland's FDI policy has incorporated high international standards concerning the entry, treatment and protection of FDI. There are no restrictions on any types of FDI (including on M&As), privatization is generally open to foreign investors and the choice of buyers is based on non-discrimination and guided by economic considerations.

Since years, Poland has a viable Investment Promotion Agency, PAIiIZ. It also grants incentives (guided by the EU rules on state-subsidies) to greenfield investment projects in manufacturing and corporate services. Projects located in special economic zones are granted tax holidays or tax reductions. In addition, investment grants can be given to FDI projects in six industries of particular importance to the national economy[267] and to projects in other branches that exceed a certain size of employment or investment value. The total value of aid is capped at 15% of an investment's value for projects located in special economic zones and at 30% for others.[268] Real estate tax exemptions are also available to investors.

As of June 1, 2009, Poland had 59 BITs and 85 double taxation agreements.[269] As an EU member, it does not conclude bilateral trade or economic partnership agreements, but is a party to agreements concluded by the EU on behalf of member countries.

As in other countries, there have been investment disputes in Poland, though not too many, often involving SOEs. The most prominent dispute involved the largest state-

[265] *The Economist*, June 5 – 11, 2010, p. 97.
[266] A.T. Kearney, *Investing in a Rebound: The 2010 A.T. Kearney FDI Confidence Index* (Vienna, Virginia, USA: A.T. Kearney, 2010), p. 17.
[267] Including automobiles, aviation, biotechnology, IT and electronics, business process outsourcing, and R&D. See PAIiIZ and PricewaterhouseCoopers, *Why Poland?* (Warsaw: PAIiIZ, 2010), pp. 15–16.
[268] Ibid., p. 16. For example, Dell, which in 2009 started to expand its existing facility in Łódź into a computer assembly factory, has received a grant of 55 million Euro (or close to US$ 70 million), an equivalent to a quarter of the value of the investment. See *Rzeczpospolita*, September 24, 2009.
[269] UNCTAD data base on international investment agreements, available at: www.unctad.org/sections/dite_pcbb/docs/bits.

controlled insurance company (Polish Insurance Company), and Eureko (Netherlands); it was settled amicably in 2009, when the Polish Government paid compensation for a broken promise to sell the insurance company PZU's majority shares to Eureko.[270]

Having had since years high standards of entry, treatment and protection of foreign investors, Poland has focused its efforts on improving the general investment climate for all investors. In one notable change also affecting foreign investors, the corporate tax rate was lowered in 2004 to 19% (from 40% prior to 1997 and 30% later on). Other efforts aimed at improving overall conditions of doing business have been rather slow-moving. Poland occupies a rather low position in a 2010 World Bank's ranking[271] of countries in this regard, being 72nd among 183 countries. Among the new EU members from Central and Eastern Europe, only the Czech Republic had a lower rank (74th). Poland ranks especially low on construction permits (163rd position) and the general tax burden (151).

This low position, indicative of several bureaucratic and regulatory hurdles to investment, coupled with poor transportation infrastructure (and in particular slow progress in building highways connecting the country to the West European highway system), explains why Poland, although the largest host country in the region in terms of the absolute size of FDI stock and/or flows, does no perform so impressively when the size of FDI is related to the size of the country. In 2008, in terms of the FDI stock as a percentage of GDP, Poland was ninth among ten new member countries of the EU from the region, and it was eighth in terms of FDI stock per capita. Poland's ranking is similarly low when its record FDI inflows in 2007 are related to its GDP and the size of its population.[272] Needless to say, Poland still has a large room for improving its investment climate, including its FDI climate. If it does so vigorously, it may utilize better its FDI potential, which is much higher than its actual FDI performance.

Conclusions and Outlook

Poland, which opened to FDI only in the early 1990s, is rapidly climbing the ladder of the world's significant host countries, reaching the 21st position in 2008 as regards its IFDI stock.[273] FDI inflows reached the record of US$ 23 billion in 2007, but declined during the following crisis, though rather modestly. At the beginning of 2010, FDI inflows began to recover, owing, in addition to continued greenfield FDI and to the revival of the privatization program, to the country's good macroeconomic performance.

All in all, as foreign affiliates in Poland mature and their parent firms reap increasing financial returns on FDI in Poland, the country's benefits from FDI are shifting away from a contribution to net capital inflows toward contributions that include technology,

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[270] Other disputes concerned difficulties in obtaining required permits or government actions in heavily regulated sectors. See, US Department of State, *2009 Investment Climate Statement: Poland*, February 2009, http://www.state.gov/e/eeb/rls/othr/ics/2009.
[271] World Bank, *Doing Business*, http://www.doingbusiness.org/ExploreEconomies/?economyid=154.
[272] The ranking was calculated from the FDI/TNC data base of UNCTAD.
[273] UNCTAD, *World Investment Report 2009: Transnational Corporations, Agricultural Production and Development* (New York and Geneva: United Nations, 2009), pp. 251–54.

access to international markets, new, more productive and better paid jobs, and, in general, more advanced types of FDI.

Additional readings

Hagemajer, J. and M. Kolasa, "Internationalization and economic performance of enterprises: evidence from firm-level data," Working Paper no. 51 (Warszawa: National Bank of Poland, 2008).

Institute for Market, Consumption and Business Cycles Research (IMCBCR), *Foreign Investment in Poland: Annual Report* (Warszawa: IMCBCR, 2009).

Invest in Poland and JP Weber, *Investor's Guide: Poland. How to do Business* (Warszawa: PAIiIZ, 2009).

Karaszewski, W., *Bezpośrednie inwestycje zagraniczne. Polska na tle świata* (Toruń: Dom Organizatora, 2004).

Kolasa, M., "How does FDI inflow affect productivity of domestic firms? The role of horizontal and vertical spillovers, absorptive capacity and competition," Working Paper no. 42 (Warsaw: National Bank of Poland, 2007).

Michałków, I., *Bezpośrednie inwestycje zagraniczne w Polsce w dobie globalizacji* (Warszawa: Wyższa Szkoła Ekonomiczna, 2003).

PAIiIZ and PricewaterhouseCoopers, *Why Poland?* (Warsaw: PAIiIZ, 2010).

Zorska, A., *Korporacje międzynarodowe w Polsce. Wyzwania w dobie globalizacji i regionalizacji* (Warszawa: Difin, 2002).

Useful websites

Information on how to establish firms and do business in Poland, business guides and analytical reports: PAIiIZ (investment promotion agency) (http://www.paiz.gov.pl/pl)

For FDI statistics: National Bank of Poland (http://www.nbp.pl).

For statistics on the activities of foreign affiliates: Central Statistical Office (http://www.stat.gov.pl/gus/index_ENG_HTML.htm).

For the privatization program 2008–2011: Ministry of Treasury (http://www.msp.gov.pl/portal/en).

Statistical annex

Annex table 1. Poland: inward FDI stock, 2000, 2008 and 2009 (US$ billion)

Economy	2000	2008	2009
Poland	34	161	182
Memorandum: comparator economies			
Czech Republic	22	114	122
Hungary	23	64	100
Romania	7	72	74
Bulgaria	3	46	51
Slovakia	5	46	50[a]

Source: UNCTAD, World Investment Report 2009: Transnational Corporations, Agricultural Production and Development (New York and Geneva: United Nations, 2009), p. 251; and websites of the national banks for 2009.
[a] *End of third quarter 2009.*

Annex table 2. Poland: inward FDI flows, 2000-2009 (US$ billion)

Economy	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
Poland	9	6	4	5	13	10	20	23	17	12
Memorandum: comparator economies										
Czech Republic	5	6	8	2	5	12	5	10	11	3
Romania	1	1	1	2	6	6	11	10	13	6
Hungary	3	4	3	2	5	8	8	6	7	4
Bulgaria	1	1	1	2	3	4	8	12	9	5
Slovakia	2	2	4	2	3	2	5	3	3	0

Source: UNCTAD's FDI/TNC database for 2000-2008, available at: http://stats.unctad.org/fdi/ and websites of national banks for 2009.

Annex table 3. Poland: distribution of inward FDI stock, by economic sector and industry, 2000, 2008 (US$ billion)

Sector/industry	2000	2008
All sectors/industries	**34**	**163**
Primary	**0.3**	**1.1**
Secondary	**13.2**	**50.6**
Food	2.9	7.8
Metal products	0.7	7.4
Motor vehicles	2.1	6.7
Chemicals	1.4	5.1
Services	**20.5**	**111.3**
Financial	6.8	31.4
Trade	5.7	26.9
Business	1.3	15.1
Real estate	1.1	12.7
Telecommunications	2.3	7.9
Power	0.4	5.9

Source: *Zagraniczne inwestycje bezpośrednie w Polsce w 2008 roku* (Warszawa: National Bank of Poland, 2010); *Zagraniczne inwestycje bezpośrednie w Polsce w 2000 roku* (Warszawa: National Bank of Poland, 2001).

Annex table 4. Poland: geographical distribution of inward FDI stock, 2000, 2008
(US$ billion)

Region/economy	**2000**	**2008**
World	**34.2**	**163**
Developed economies	**33.5**	**157**
Europe	30.1	146
European Union - 15	27.1	134
Netherlands	8.4	31.1
Germany	6.5	21.6
France	4.2	17.6
Luxembourg	...	14.1
North America	3.3	10.2
United States	3.2	10
Other developed countries	0.2	0.9
Japan	0.1	1.3
Developing economies	**0.7**	**5.1**
Africa	0	0
Asia and Oceania	0.5	1.9
Rep. of Korea	0.5	1
China	0	0.3
Latin America and Car.	0.1	3.2

Source: *Zagraniczne inwestycje bezpośrednie w Polsce w 2008 roku* (Warszawa: National Bank of Poland, 2010); and *Zagraniczne inwestycje bezpośrednie w Polsce w 2000 roku* (Warszawa: National Bank of Poland, 2001).

Annex table 5. Poland: principal foreign affiliates, ranked by sales,[a] 2008 (US$ million)

Rank	Name of affiliate	Industry	Parent firm and home economy	Sales
1	Metro Group[b]	Trading	Metro Group, Germany	13,753
2	Telekomunikacja Polska[c]	Telecommunications	Telecom, France	10,920
3	Fiat[d]	Automotive	Fiat, Italy	7,634
4	Volkswagen[e]	Automotive	Volkswagen, Germany	5,217
5	Jeronimo Martins	Trading	Jeronimo Martins, Portugal	3,736
6	BP Polska	Trading	BP, United Kingdom	3,652
7	Tesco	Trading	Tesco, United Kingdom	3,362
8	Polska Telefonia Cyfrowa	Telecommunications	T-Mobile, Germany	3,082
9	Carrefour	Trading	Carrefour, France	3,030
10	Bank Pekao	Banking	UniCredit, Italy	2,962
11	Toyota[f]	Automotive and trading	Toyota, Japan	2,423
12	Bank BPH SA GK	Banking	General Electric, USA	2,099
13	Auchan	Trading	Auchan, France	1,992
14	Eurocash	Trading	Politra BV, Netherlands	1,963
15	Shell	Trading	Shell, United Kingdom	1,859
16	Vattenfall	Energy	Vattenfall, Sweden	1,661
17	Saint Gobain	Glass	Saint Gobain, France	1,619
18	Bank Zachodni	Banking	Allied Irish Bank, Ireland	1,613
19	Delphi Poland SA	Automotive	Delphi, USA	1,556
20	Philips Lighting	Lighting equipment	Royal Philips Electronics, Netherlands	1,523

Source: Author's compilation, based on: Rzeczpospolita, *Lista 500*, 29 April 2009; PAIiIZ, *List of Major Foreign Investors in Poland with Comment*, December 2008; and companies' websites.

[a] To the extent possible, foreign affiliates include a consolidated list of firms owned by individual MNEs, even if they are registered in Poland as separate companies. The list excludes affiliates, in which foreign shareholdings exceed 10%, when these affiliates are controlled by local investors. Sales of banks include revenues from interests, fees, commissions, shares, and other securities and gains from financial operations.

[b] Consolidated affiliates, including companies listed separately on the list of the top 500 largest firms: Makro Group, Makro Cash and Carry, Real, and Media Saturn Holding.

[c] Including also PTK Centertel, a mobile telephone affiliate owned by Telekomunkacja Polska.

[d] Including Fiat Auto Poland (an assembly plant) and two auto component plants: Fiat GM Powertrain (a joint venture of Fiat and General Motors) and Magneti Marelli.

[e] Includes an assembly plant in Poznan and an engine factory in Polkowice.

[f] Includes component factories in Walbrzych and Leg and a trading affiliate of Toyota, Toyota Motor Poland.

Annex table 6. Poland: main M&A deals, by inward investing firm, ranked by value (completed transactions), 2007-2009 (US$ million)

Year	Target company	Acquiring company	Home economy	Shares acquired (%)	Transaction value
2009	TC Debica	Goodyear Luxembourg Tires SA	Luxembourg	100	99
2009	Multimedia Polska SA	M2 Investments Ltd	United Kingdom	32	58
2009	Bukowa Gora SA	PCC SE	Germany	90	7
2009	Kredyt Bank SA	Investor Group	Belgium	5	61
2009	ICM Polska SP Zoo	Undisclosed Acquiror	Unknown	52	35
2009	Pol-Aqua SA	Dragados SA	Spain	66	165
2009	Poldrim Sp Zoo	Carpathian PLC	Isle of Man	100	9
2009	DT SPV15-Office Bldg	Deka Immobilien Invest GmbH	Germany	100	161
2009	Drumet SA	Penta Investments sro	Czech Republic	100	38
2009	Bankier.pl SA	MIH Allegro BV	Netherlands	83	20
2009	Sephora Polska Sp zoo	Sephora SA	France	24	16
2009	EMO-FARM Sp zoo	Valeant Pharm Intl Inc	United States	100	28
2009	Kakadu Sp zoo	Arx Equity Capital	Czech Republic	…	13
2009	Zara Polska Sp zoo	Industria de Diseno Textil SA	Spain	100	33
2009	The Polish Re	Fairfax Financial Holdings Ltd	Canada	100	72
2008	Grupa Energetyczna ENEA SA	Vattenfall AB	Sweden	19	608
2008	LC Corp Sky Tower Sp zoo	LC Corp BV	Netherlands	…	43
2008	Polkomtel SA	Vodafone Group PLC	United Kingdom	24	255
2008	GE Real Estate Central Europe-	Union Investment Real Estate	Germany	100	129
2008	Orbis SA	Accor SA	France	50	47
2008	Marynarska Business Park	DEGI	Germany	100	246
2008	Warsaw Office Tower	Wiener Stadtische	Austria	100	108
2008	Grodziskie Zaklady	Richter Gedeon Nyrt	Hungary	100	43
2008	Bioton SA	Polaris Finance	Netherlands	10	88
2008	Europa Eagle-Shopping Centers	Balmain European Property	United Kingdom	100	80
2008	Krakow hotel	Warimpex Finanz- und	Austria	100	46
2008	Conforama SA-Polish Operations	Leroy Merlin SA	France	100	67
2008	BPH-Branded Branches(200)	GE Money	United States	66	862
2008	Eolica Ceiplowody Sp zoo	Fersa Energias Renovables SA	Spain	100	338
2008	P4 Sp zoo	Investor Group	Cyprus	23	192
2007	Gadu-Gadu SA	Naspers Ltd	South Africa	96	150

2007	Stora Enso Poland SA	Stora Enso Oyj	Finland	94	88
2007	Forum Shopping Centre	Deka Immobilien Invest GmbH	Germany	100	176
2007	Zabka Polska SA	Penta Investments sro	Czech Republic	100	178
2007	Plaza Centers-Shopping Centers	Klepierre SA	France	100	122
2007	Zakopianka	Macquarie CountryWide Trust	Australia	100	83
2007	Turzyn Sp zoo	Macquarie CountryWide Trust	Australia	100	81
2007	PolCard SA	First Data International	United States	100	325
2007	Polmos Lublin SA	Oaktree Capital Management LLC	United States	40	80
2007	BA-CA Real Invest-Real Estate	TMW Pramerica Immobilien GmbH	Germany	100	256
2007	PZL-Mielec	Sikorsky Aircraft Corp	United States	100	84
2007	BOC Gazy Sp zoo-Industrial Gas	Air Products & Chemicals Inc	United States	100	485
2007	NCC Roads Polska Sp zoo	Strabag Oesterreich AG	Austria	100	146
2007	BISE Bank SA	Bank DnB NORD	Denmark	76	185
2007	Ahold Polska Sp zoo	Carrefour SA	France	100	500

Source: Thomson ONE Banker. Thomson Reuters.

Annex table 7. Poland: main greenfield projects, by inward investing firm (announced), 2007-2009
(US$ million)

Date	Investing company	Home economy	Sector	Announced value[a]
2009	IKEA	Sweden	Trading and construction	243
2009	American International Group	USA	Financial services	203
2009	Electricity Supply Board	Ireland	Energy	1400
2009	Asea Brown Boveri	Switzerland	Engines & turbines	221
2009	Dell Computer	USA	Business machines & equipment	277
2009	Mondi Group	UK	Paper, printing & packaging	505
2009	LM GlasFiber	Denmark	Industrial machinery, equipment	202
2009	FX Energy	USA	Energy	300
2009	IKEA	Sweden	Trading and construction	250
2009	Octapharma	Switzerland	Pharmaceuticals	188
2009	Fiat	Italy	Engines	506
2009	IKEA	Sweden	Wood products	522
2009	Cemex	Mexico	Building & construction materials	514
2009	Jeronimo Martins	Portugal	Retail trading, food & tobacco	330
2009	Vattenfall	Sweden	Energy	713
2008	Titan Group	Greece	Energy	449.5
2008	Vattenfall	Sweden	Energy	1090
2008	Toyota Motor	Japan	Automotive components	723
2008	Vattenfall	Sweden	Energy	3500
2008	Electricite de France (EDF)	France	Energy	713.2
2008	RWE	Germany	Energy	2320
2008	Electrolux	Sweden	Household appliances	464.6
2008	State Street	USA	Financial services	1494.5
2008	Lafarge	France	Building & construction materials	550.7
2008	TriGranit	Hungary	Real estate	781.8
2008	Auchan Group (Mulliez Group)	France	Retail trading	1134
2008	Stora Enso	Finland	Paper, printing & packaging	587.82
2008	EFG Group	Switzerland	Financial services	747.2
2008	Anglo American	UK	Paper, printing & packaging	437.66
2008	Prometheus Energy	USA	Energy	449.5
2007	Carlo Tassara	Italy	Financial services	586.84
2007	Fiat	Italy	Automotive OEM	400
2007	Suez	France	Alternative/renewable energy	735.31
2007	Euroglas	Germany	Ceramics & glass	283.55
2007	Suez	France	Energy	2942.3
2007	Schmack Biogas	Germany	Alternative/renewable energy	215.5
2007	Michelin	France	Rubber	342
2007	Anglo American	UK	Paper, printing & packaging	481.94
2007	LG	Korea, Rep. of	Electronic components	1080
2007	Electricity Supply Board (ESB)	Ireland	Energy	713.2

2007	Videocon Industries	India	Consumer electronics	1700
2007	Fiat	Italy	Automotive OEM	340
2007	Cemex	Mexico	Building & construction materials	260.3
2007	Ford	USA	Automotive components	276
2007	Nanette Real Estate Group	Netherlands	Real estate	251

Source: fdi Intelligence, a service from the Financial Times Ltd.

[a] Actual or estimated value of the investment project. Most are actual value.

Chapter 12 – Switzerland

Inward FDI and its policy context, 2010

Philippe Gugler and Xavier Tinguely

Switzerland has constantly sought to build an open economy in which foreign actors have been a crucial element of the economic growth process. The quality of the business environment, the central geographic location in Europe and the stability of the political, legal and social system have traditionally attracted a relatively high-level of IFDI to the country. However, this success should not be taken for granted. The current economic crisis and the globalization of the world economy are challenging the attractiveness of Switzerland as a FDI location. In a context of fierce competition among countries to attract FDI, Switzerland has constantly to improve the quality of its business environment in order to remain a competitive location for foreign investors.

Trends and developments

Country-level developments

Despite the current global financial and economic crisis, Switzerland remains an attractive location for foreign investors. The FDI stock in Switzerland constantly rose over the past years, to reach US$ 439 billion in 2008 (annex table 1); between 2007 and 2008 alone, it rose by 30%.[274] The decline in 2005 stands out as a special case. The "American Jobs Creation Act" passed in October 2004 by the US Government temporary allowed US companies to repatriate their reinvested earnings at a tax-privileged rate.[275] Nevertheless, Switzerland hosts a relatively high level of IFDI:[276] among selected comparable economies (annex table 1), Switzerland recorded the second largest stock of IFDI in 2008, behind the Netherlands. Moreover, the ratio of the country's IFDI stock as a percentage of GDP rose to 76%, while it amounted to 34% in Austria, 53% in Sweden, 64% in Ireland, and 74% in the Netherlands.[277]

While the IFDI stock in Switzerland grew steadily during the period 2000-2008, IFDI flows evolved more irregularly (annex table 2). The past years under review bore out this erratic trend. Whereas new acquisitions and increased reinvested earnings boosted IFDI flows to US$ 49.2 billion in 2007 (the highest flow ever recorded),[278] this unusually high figure did not last more than one year as FDI inflows sharply declined to US$ 5.1 billion in 2008.[279] Provisional data for 2009 seem to confirm a relatively low level of FDI flows.[280]

FDI in Switzerland is concentrated in the services sector, accounting for 84% of the total IFDI stock in 2008 (annex table 3). This share remained relatively stable between 2000 and 2008. Within services, finance and holding companies were responsible for nearly 70% of the total foreign investment in services. Manufacturing traditionally attracts less FDI (16%). More than half of the foreign FDI in manufacturing (55%) was in

[274] It is necessary to keep in mind that, although FDI flows influence FDI stocks, a change in FDI flows does not necessarily provide any direct indication about FDI stocks, and vice versa. Changes in FDI stocks can be due to various factors that do not result in FDI flows. For instance, changes in FDI stocks may also be due to exchange rate movements, the raising of investment capital in third or domestic markets, new valuation principles (e.g. adjustment to international accounting standards), etc. For more information, see Swiss National Bank, *Direct Investment 2008* (Bern and Zurich: SNB, 2009), p. 18.
[275] Swiss National Bank, *Development of Direct Investment in 2005* (Bern and Zurich: SNB, 2006).
[276] UNCTAD, *World Investment Report 2009: Transnational Corporations, Agricultural Production and Development* (Geneva: UNCTAD, 2009).
[277] UNCTAD, *World Investment Report 2009*, op. cit.
[278] Swiss National Bank, *Direct Investment 2007* (Bern and Zurich : SNB, 2008).
[279] Swiss National Bank, *Swiss Balance of Payment (Quarterly Estimates) 4th Quarter 2009* (Bern and Zurich: SNB, 2009).
[280] The fall in investments will be analyzed in the section devoted to the effects of the current global crisis.

chemicals and plastics, reflecting the attractiveness of the chemical and biopharmaceutical industry in Switzerland, mainly clustered in the Basle area.[281]

Developed economies contributed to more than 90% of the IFDI stock in Switzerland in 2008 (annex table 4). Among developed economies, inflows from the EU amounted to US$ 309 billion (70% of the total inward stock). Of this, nearly two-third came from the Netherlands (US$ 88 billion), Austria (US$ 57 billion) and Luxembourg (US$ 55 billion), three well-known holding company locations.[282] By owning a FDI stock of more than US$ 80 billion in Switzerland, the United States is one of the country's most important foreign investors. Developing economies accounted for 10% of the IFDI stock (US$ 42 billion), of which 93% originated from offshore financial centers in Central and South America (US$ 39 billion).

The sectoral and regional breakdown of the Swiss IFDI stock reflects the motivation of foreign companies to invest in Switzerland. On the one hand, the attractive corporate tax system attracts a high level of investment by holding companies. On the other hand, the quality of the business environment[283] makes Switzerland the appropriate location for high value-added functions and explains the large number of strategic-asset seeking investments in knowledge-intensive sectors by companies mainly from developed countries.[284]

In line with IFDI growth, foreign companies in Switzerland steadily increased their employment, from around 130,000 in 2000 to 395,000 in 2008.[285] This corresponded to around 10% of the total workforce in Switzerland (estimated at 4 million at the end of 2008).[286] In 2008, the number of staff employed by foreign investors in Switzerland rose by 16,000 individuals. The breakdown by investing country is relatively similar to the IFDI distribution: some 80% of the workforce of foreign investors was employed by European firms, 15% by North American companies and 5% by developing country ones.[287] Looking at the sectoral level, 38% was active in manufacturing and 62% in services. It is worth noting that, whereas finance and holding companies generated 58% of the total foreign investment in Switzerland, they accounted for only 4% of the total work force employed by foreign companies. This suggests that some holding companies are set up in Switzerland to avoid double taxation of income earned by foreign affiliates.[288]

The corporate players

For decades, MNEs from across the globe have chosen Switzerland as a location for their foreign operations.[289] In 2007, Switzerland recorded the second highest concentration of *Fortune 500* companies per million inhabitants (1.6), behind Luxembourg.[290] Furthermore, the *World Investment Report 2009* identified 6,852 foreign affiliates located in Switzerland in 2008.[291] By generating around 10% of the total Swiss GDP, foreign

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[281] P. Gugler and M. Keller, "The economic performance of Swiss regions," Center for Competitiveness, University of Fribourg, Switzerland (2009), available at: http://www.isc.hbs.edu/econ-natlcomp_resources.htm.

[282] The breakdown by ultimate beneficial owner gives a different picture as the share of these three countries in the total investment by EU countries dropped to only one-third. For more information about ultimate investors, see Swiss National Bank, *Direct Investment 2008*, op. cit., pp. 14-16.

[283] In particular the availability of skilled and multilingual labor, access to leading research and academic institutions, a stable macroeconomic, political, legal and social context, and high-quality infrastructure.

[284] For further information about the sectoral and regional breakdown of the IFDI stock in Switzerland, see The Swiss-American Chamber of Commerce and The Boston Consulting Group, *Multinational Companies on the Move: How Switzerland Will Win the Battle* (Zurich, 2007), and to R. J. Allen and P. R. Altenburger, *Switzerland: More than just Taxes*, Swiss-American Chamber of Commerce Yearbook 2009/2010 (Zurich: 2010).

[285] Swiss National Bank, *Development of Direct Investment in 2002* (Bern and Zurich: SNB, 2003), and Swiss National Bank, *Direct Investment 2008*, op. cit.

[286] Swiss National Bank, *Direct Investment 2008*, op. cit.

[287] Ibid.

[288] Although these firms are often depicted as "letter-box" companies, they undertake key activities that allow parent firms to maximize the effectiveness of their global business.

[289] Allen and Altenburger, op. cit.

[290] Swiss-American Chamber of Commerce and The Boston Consulting Group, op. cit.

[291] UNCTAD, *World Investment Report 2009*, op. cit.

MNEs play a pivotal role in the domestic economy.[292] Annex table 5 lists a sample of the main foreign affiliates established in Switzerland, ranked by number of employees in Switzerland. In order to illustrate the strong presence of foreign companies in Switzerland, a look at the structure of the banking industry is interesting. At the end of 2008, Switzerland hosted 154 foreign banks, representing 48% of all banks, 17% of gross profit of all banks, 15% of domestic employees of all banks, and 20% of taxes paid by all banks, and approximately 2% of the Swiss GDP.[293]

Foreign MNEs continued to strengthen their position in Switzerland by undertaking new investment. On the one hand, between 2000 and mid-2009, foreign MNEs concluded 946 M&As in Switzerland, worth more than US$ 100 billion.[294] Annex table 6 lists the ten largest M&As by foreign investors in Switzerland between 2007 and 2009. By acquiring 98% of the shares of the Swiss biotechnological firm Serono for some US$ 9 billion, the German pharmaceutical company Merck undertook the largest foreign investment in a Swiss company. It is interesting to note that M&As by foreign companies were principally oriented toward high-value added firms, highlighting thus the strategic asset-seeking nature of foreign investors. But foreign MNEs were also very active through greenfield investment. During the period 2004-March 2009, 611 greenfield FDI projects were established by foreign investors.[295] Annex table 7 shows the ten biggest greenfield transactions between 2007 and 2009: five projects were in the hospitality and tourism industry, two in the pharmaceutical industry, two in IT services and one in the food and tobacco industry.[296]

Effects of the current global crisis

As illustrated in the previous sections, despite the global financial and economic crisis, the IFDI stock in Switzerland continued to grow between 2007 and 2008. Furthermore, this trend was corroborated in 2009 as IFDI stock rose by US$ 25 billion, to US$ 464 billion. Whereas IFDI flows reached a new record peak of US$ 49 billion in 2007, they sharply decreased by US$ 44 billion to US$ 5 billion in 2008.[297] This impressive fall, more accentuated than the global trend and the slowdown of the economic activity, resulted from a strong decline in reinvested earnings, a drop in acquisitions and significant disinvestments. Investors from the EU withdrew more than US$ 4 billion from Switzerland in 2008, while they invested US$ 48 billion the previous year.[298] Looking at the sectoral level, FDI inflows in manufacturing and services dropped between 2007 and 2008 by 99%, to US$ 0.1 billion (compared to US$ 23 billion in 2007), and by 80% to US$ 5 billion (compared to US$ 28 billion).[299] Within manufacturing, chemicals and plastics recorded the largest decrease, shrinking from an investment of US$ 14 billion in 2007 to a disinvestment of US$ 0.4 billion in 2008. With regard to services, although finance and holding companies remained the largest foreign investors in the country, they recorded the highest decline, reducing their investment from US$ 15 billion in 2007 to US$ 6 billion in 2008.[300]

Provisional data for 2009 also indicate low inflows. Although inward flows of US$ 6.3 billion recorded in the first quarter hinted at a probable recovery (they exceeded total inflows of the previous year by US$ 1.2 billion),

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[292] M. Naville and P. Tischhauser, "Comment la Suisse peut gagner la course difficile aux faveurs des multinationales," *La Vie Economique*, (3) (2008), pp. 32-34.
[293] Association of Foreign Banks in Switzerland, *Foreign Banks in Switzerland and their Association: Who are they?* (Zurich, 2009).
[294] UNCTAD's FDI/TNC database, available at: http://stats.unctad.org/fdi, and UNCTAD, *World Investment Report 2009*, op. cit.
[295] UNCTAD, *World Investment Report 2009,* op. cit.
[296] Although it can be surprising that five of the ten biggest greenfield transactions in Switzerland between 2007 and 2009 were in the hospitality and tourism industry (instead of in traditional attractive and competitive Swiss sectors such as pharmaceuticals or financial services), the inherent characteristics of greenfield investment (i.e. investment to construct a project in basic components) make investments in hospitality and tourism a common phenomenon.
[297] It is important to keep in mind that the unusual high 2007 figure accentuated the extent of the fall.
[298] Swiss National Bank, *Direct Investment 2008*, op. cit.
[299] Swiss National Bank, *Direct Investment 2008*, op. cit.
[300] This fall was mainly due to lower profits retained.

IFDI flows dropped again during the second, third and fourth quarters, to, respectively, US$ 1.9 billion, US$ 2.2 billion and an outflow of US$ 0.7 billion.[301] Provisional data for 2009 show therefore total FDI inflows of US$ 9.7 billion. Although this figure was almost twice that of 2008 (US$ 5.1 billion), it remained 33% lower than the average of the nine previous years (US$ 14.5 billion).

The financial and economic crisis also triggered the emergence of SWFs as new investors in Switzerland.[302] Between 2007 and 2009, Asian and Middle East SWFs invested in six Swiss companies.[303] Three transactions were effectively classified as FDI: (i) Abar Investment (UAE) acquired 100% of AIG Private Bank, (ii) Mubadala Development Company (UAE) obtained 40% of the Swiss engineering firm SR Technics and (iii) Kuwait Investment Authority acquired 24% of the Swiss hotel group Victoria-Jungfrau Collection.[304] Furthermore, due to liquidity needs resulting from the financial crisis, SWFs also invested in the two largest Swiss banks, Credit Suisse and UBS. Qatar Investment Authority acquired 9.9% of Credit Suisse and the Government of Singapore Investment Corporation (GIC) injected almost US$ 10 billion in UBS.[305] Although SWFs flows into Switzerland triggered a debate about the need for legislative change and the possible strategic nature of these investments, the Government seems to have reached the conclusion that there is no justification to discriminate against SWFs and that protectionism could generate unnecessary negative trade-offs.[306]

The policy scene

Despite the competitiveness of the Swiss economy, the country has to tackle several challenges to maintain its leading position and strengthen the attractiveness of its business environment *vis-à-vis* a growing number of new players that are aggressively seeking to attract FDI, including with special tax schemes and better infrastructure. For example, whereas Switzerland used to be a major location for investment funds, a lack of flexibility in the regulatory framework and the tax regime has allowed Luxembourg and Ireland to outperform Switzerland in this area of business.[307] The financial industry is particularly illustrative of the fierce competition among countries to attract FDI, and the necessity to constantly reassess a country's institutional, regulatory and tax framework.

In order to safeguard the interests of the Swiss economy abroad and to improve Switzerland's attractiveness as a business location, the Swiss Government seeks to set up a strong network of FTAs and BITs.[308] In 2009, Switzerland signed 14 double taxation agreements (DTTs).[309] After having been placed by the OECD and the G-20 states on a "grey list" of "uncooperative tax havens" in April 2009, the Federal Council decided to extend administrative assistance in tax matters and to adopt Art.26 of the OECD Model Convention.[310] The signature

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[301] Swiss National Bank, *Swiss Balance of Payment (Quarterly Estimates) 4th quarter 2009*, op. cit.
[302] Although SWFs were traditionally more active in portfolio investment, they recently sharply increased their involvement in FDI and cross-border M&As by acquiring 10% or more of equity, with voting power, in enterprises abroad. Even though the amounts invested in FDI by SWFs remain relatively low proportionally to the size of these funds (estimated to be about US$ 4 trillion), they dramatically increased since 2005. In fact, cumulative FDI by SWFs over the past two decades reached US$ 65 billion in 2008, of which US$57 billion were invested in the past four years. For more information on SWFs, see UNCTAD, *World Investment Report 2008: Transnational Corporations and the Infrastructure Challenge* (Geneva: UNCTAD, 2008), UNCTAD, *World Investment Report 2009*, op. cit.; P. Gugler and M. Keller, "The Role of SWFs in shaping the neopolar world: the Asia-Europe perspective," in Lars Oxelheim, Eds., *The Repolarization of the Global Economic Area*, forthcoming.
[303] Information obtained from an internal database on SWFs, established by the Center for Competitiveness, University of Fribourg, Switzerland.
[304] Ibid.
[305] The third portfolio investment by SWFs in a Swiss company was in Glencore, a Swiss commodity trader firm.
[306] KPMG, *Sovereign Wealth Funds: The New Global Investors* (Zurich: KPMG, 2008).
[307] For more details about the Swiss financial industry, see the website of the Swiss Bankers Association, available at: http://www.swissbanking.org.
[308] For more information about the Swiss network of international agreements and treaties, see the website of the State Secretariat of Economic Affairs SECO available at: http://www.seco.admin.ch, and Philippe Gugler and Xavier Tinguely, "Swiss outward FDI and its policy context," *Columbia FDI Profiles*, April 29, 2010.
[309] Between March 2009 and May 2010, Switzerland signed DTTs (with OECD Art. 26) with Austria, Denmark, the Färöer Islands, Finland, France, Luxembourg, Mexico, the Netherlands, Norway, Poland, Qatar, Spain, the United Kingdom, and the United States.
[310] Federal Department of Finance, *International Double Taxation* (Bern: FDF, 2010). Detailed information is available at: http://www.efd.admin.ch.

of these DTTs is likely to facilitate the activities of the export sector, promote investment in Switzerland and contribute to prosperity of the country.[311]

Nevertheless, other reforms of the domestic economy are necessary to respond to the challenge of globalization. The *Global Competitiveness Report* (GCR) offers an overview of the main strengths and weaknesses of the Swiss business environment compared with those of 132 other countries.[312] Although Switzerland topped the overall ranking in 2009-2010, it performed relatively badly in certain categories that are important to foreign investors. For example, Switzerland ranked only 27th in the intensity of local competition, 30th in business impact of rules on FDI, 60th in time required to start a business, 93rd in the prevalence of trade barriers or 122th in strength of investor protection.[313] The Swiss Government wants to overcome these shortcomings. For instance, in the past years, the competencies of the competition authorities were reinforced, and the Swiss authorities started a liberalization process of traditionally protected sectors such as agriculture in which a FTA with the EU is under negotiation. Recognizing the crucial importance of foreign investors in Switzerland's international economy, the Swiss government also set up a special institution to promote Switzerland as a business location.[314] Moreover, in the framework of the OECD Code of Capital Movements, Switzerland is committed progressively to abolish restrictions on the movement of capital.[315] It is worth noting that, although reservations apply to certain sectors subject to special conditions (such as real estate or financial operations), Swiss investment laws do not establish a general screening mechanism for foreign investment in Switzerland.[316]

Conclusions and Outlook

Even if the global financial and economic crisis affected FDI inflows in 2008 and 2009, Switzerland continued to attract a relatively high level of FDI. However, even though the country ranks among the world's most competitive economies, this success is not set in stone. International competition has become stronger, and many countries are becoming more attractive and more active in approaching foreign investors. As foreign companies play a crucial role in the dynamism of the Swiss economy, the constant improvement of the business environment is an essential prerequisite to maintain Switzerland's attractiveness, competitiveness and prosperity in the future.

Additional readings

Gugler, Philippe and Lamia Ben Hamida, "Are there demonstration-related spillovers from FDI? Evidence from Switzerland," *International Business Review,* 18 (5) (2009), pp. 494-508.

Naville, Martin and Pia Tischhauser, "Comment la Suisse peut gagner la course difficile aux faveurs des multinationals," *La Vie Economique,* 3 (2008), pp. 32-34.

Swiss-American Chamber of Commerce and Boston Consulting Group, *Foreign Companies in Switzerland: The Forgotten Sector* (Zurich, 2006).

[311] For more information see OECD, Centre for Tax Policy and Administration, available at: http://www.oecd.org.
[312] World Economic Forum, *Global Competitiveness Report 2009-2010* (Geneva: WEF, 2009).
[313] The apparent lack of investor protection has to be seen in perspective, as Swiss law provides a high level of investor protection. Switzerland's low ranking is likely to be explained by the fact that the country lies outside the applicable scope of the markets in financial instruments directive (MiFID). For more information, see M. Hess and H.-L. Chou, *MiFID: Challenge for Swiss Investment Firms as well?* (Zurich: Wenger & Vieli, 2007).
[314] For more information, see OSEC Business Network Switzerland available at: www.osec.ch.
[315] OECD, *Code of Liberalisation of Capital Movements* (Paris: OECD, 2009).
[316] For more information, see ibid.

Swiss-American Chamber of Commerce and Boston Consulting Group, *Multinational Companies on the Move: How Switzerland Will Win the Battle!* (Zurich, 2007).

Swiss-American Chamber of Commerce and Boston Consulting Group, *Creative Switzerland? Fostering an Innovation Powerhouse!* (Zurich, 2008).

Useful websites

For FDI policy: Swiss Government, Federal Department of Economic Affairs, available at: www.evd.admin.ch.

For FDI statistics: Swiss National Bank, available at: www.snb.ch.

Statistical annex[317]

Annex table 1. Switzerland: inward FDI stock, 2000 – 2009 (US$ billion)

Economy	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
Switzerland	**86.8**	**89.3**	**125.1**	**161.8**	**195.9**	**169.0**	**218.0**	**337.5**	**439.1**	**463.8**[a]
Memorandum: comparator economies[b]										
Austria	31.2	35.0	44.9	57.6	70.7	82.6	111.1	163.4	139.3	-
Ireland	127.1	134.1	182.9	222.8	207.6	163.5	156.5	193.5	173.4	-
Netherlands	243.7	282.9	350.0	426.6	477.2	451.2	513.3	724.1	644.6	-
Sweden	94.0	91.9	119.4	158.9	196.2	171.8	227.3	290.0	253.5	-

Source: UNCTAD's FDI/TNC database, available at: http://stats.unctad.org/fdi and authors' calculations, based on SNB, *Development of direct investment 2001, 2002, 2003, 2004, 2005, 2006* (Zurich and Bern: SNB 2002-2007); *Direct Investment 2007, 2008* (Zurich and Bern: SNB 2008 - 2009).

[a] Provisional data from SNB, *Monthly Statistical Bulletin March 2010* (Zurich and Bern: SNB, 2010).
[b] Comparator economies have been chosen because of the comparable size of their population, GDP per capita and/or institutional framework.

Annex table 2. Switzerland: inward FDI flows, 2000-2009[a] (US$ billion)

Economy	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
Switzerland	**19.3**	**8.9**	**5.6**	**16.6**	**0.7**	**-1.3**	**26.3**	**49.2**	**5.1**	**9.7**[b]
Memorandum: comparator economies[c]										
Austria	8.8	5.9	0.4	7.1	3.9	10.8	7.9	29.6	13.6	-
Ireland	25.8	9.7	29.3	22.8	-10.6	-31.7	-5.5	24.7	-20.0	-
Netherlands	63.9	51.9	25.0	21.0	4.6	47.8	7.5	118.4	-3.5	-
Sweden	23.4	10.9	12.3	5.0	11.0	10.0	27.2	22.1	43.7	-

[317] As Swiss FDI data are published in Swiss Franc (CHF), they were converted in US$ using the official CHF/US$ conversion key provided by the Swiss National Bank and used by UNCTAD to harmonize data in US$. In the statistics on direct investment, the Principality of Liechtenstein is included in the Swiss domestic data.

Source: UNCTAD's FDI/TNC database, available at http://stats.unctad.org/fdi and authors calculations, based on SNB (2002-2007), "*Development of direct investment 2001, 2002, 2003, 2004, 2005, 2006*", Zurich/Bern and SNB (2008-2009), "*Direct Investment 2007, 2008*", Zurich/Bern.

[a] A minus sign (-) indicates an outflow of capital (disinvestment).
[b] Provisional data from SNB, *Swiss Balance of Payments (Quarterly Estimates) 4th Quarter 2009* (Bern and Zurich: SNB, 2010).
[c] Comparator economies have been chosen because of the comparable size of their population, GDP per capita and/or institutional framework.

Annex table 3. Switzerland: distribution of inward FDI stock, by economic sector and industry, 2000, 2008[a] (US$ billion)

Sector / industry	2000	2001	2002	2003	2004	2005	2006	2007	2008
Manufacturing	**15.4**	**14.9**	**17.9**	**26.6**	**35.3**	**30.3**	**39.1**	**55.9**	**67.9**
Chemicals and plastics	4.6	5.9	6.4	9.4	16.2	12.6	18.8	27.3	37.1
Metals and machinery	2.1	2.0	2.6	3.8	4.8	4.5	5.6	8.3	9.1
Electronics, energy, optical and watchmaking	5.7	4.3	5.9	7.9	8.8	8.4	10.2	14.8	13.8
Other manufacturing and construction	3.0	2.7	3.0	5.5	5.5	4.8	4.5	5.5	7.9
Services	**71.4**	**74.4**	**107.2**	**135.2**	**160.6**	**138.7**	**178.9**	**281.6**	**371.2**
Trade	12.2	11.5	14.0	16.6	25.0	24.2	28.7	38.2	39.3
Finance and holding companies[b]	38.7	37.8	67.1	85.5	95.9	77.4	98.8	179.8	253.8
Banks	13.0	13.8	17.4	21.1	24.1	22.0	26.3	31.8	36.1
Insurance companies	3.4	2.9	2.8	3.3	4.9	4.6	13.7	16.4	19.6
Transportation and communications	2.3	3.7	3.3	5.2	5.1	5.2	5.9	8.5	12.0
Other services	1.8	4.7	2.6	3.5	5.6	5.3	5.5	6.9	10.4
Total	**86.8**	**89.3**	**125.1**	**161.8**	**195.9**	**169.0**	**218.0**	**337.5**	**439.1**

Source: Authors' calculations, based on SNB (2002-2007), *Development of Direct Investment 2001, 2002, 2003, 2004, 2005, 2006* (Zurich and Bern: SNB 2008-2009), *Direct Investment 2007, 2008* (Zurich and Bern: SNB 2008-2009),

[a] Capital stock at year-end (book value); The breakdown by sector and economic activity refers to a company's core business in Switzerland. Until 2003, classification according to the General Classification of Economic Activities, ASWZ 1985 (*Allgemeine Systematik der Wirtschaftszweige*); from 2004 onwards, classification according to the General Classification of Economic Activities, NOGA 2002 (*Nomenclature générale des activités économiques*); Expansion of the reporting population in 2004.
[b] Expansion of the reporting population in 2006.

Annex table 4. Switzerland: geographical distribution of inward FDI stock, 2000, 2008[a] (US$ billion)

Economy / region	2000	2008
World	**86.8**	**439.1**
Developed economies	**85.5**	**397.0**
Europe	**51.7**	**312.7**
European Union [b]	51.6	309.6
Austria	0.4	57.5
Denmark	1.2	10.8
France [c]	8.3	32.5
Germany	12.4	35.8
Luxemburg	3.0	54.9
Netherlands	17.4	88.0
United Kingdom	3.1	9.1
Other European economies [d]	0.1	3.1
North America	**31.9**	**82.8**
Canada	1.4	1.5
United States	30.5	81.3
Other developed economies	**1.9**	**1.5**
Developing economies	**1.3**	**42.1**
Asia, Africa and Oceania	**0.4**	**2.0**
Central and South America	**0.9**	**40.1**
of which		
Offshore financial centers [e]	-	38.8

Source: Authors' calculations, based on SNB, *Development of Direct Investment 2001* (Zurich and Bern: SNB, 2002); *Direct Investment 2008* (Zurich and Bern: SNB, 2009).

[a] Capital stock at year-end (book value); Expansion of the reporting population in 2004; The definition of countries is based on the Eurostat geonomenclature.
[b] As of 2004, EU25; as of 2007, EU27.
[c] As of 2000, incl. Monaco, Réunion, French Guiana, Guadeloupe, and Martinique.
[d] As of 2000, incl. Guernsey, Jersey and the Isle of Man, excl. Monaco; until 2003, incl. Baltic countries, Malta, Poland, Slovakia, Slovenia, Czech Republic, Hungary, and Cyprus; until 2006, incl. Bulgaria and Romania.
[e] Virgin Island (US), Anguilla, Antigua and Barbuda, Bahamas, Barbados, Belize, Bermuda, Virgin Island (British), Dominica, Grenada, Jamaica, Cayman Islands, Montserrat, Netherlands Antilles, Panama, St Kitts and Nevis, Santa Lucia, St-Vincent and the Grenadines, Turks and Caicos Islands.

Annex table 5. Switzerland: some main foreign affiliates, ranked by number of employees in Switzerland, 2008-2009 (US$ millions)

Rank	Name	Economy	Industry	Number of employees
1	IBM	United States	Software and services	3,320
2	Johnson & Johnson	United States	Drugs and biotechnology	3,150
3	Procter & Gamble	United States	Household and personal products	2,700
4	HSBC Private Bank (Suisse) SA	United Kingdom	Banking	2,669
5	Hewlett-Packard	United States	Technology hardware and equipment	2,000
6	BSI SA	Italy	Banking	1,827
7	BNP Paribas (Suisse) SA	France	Banking	1,756
8	Sarasin & Cie AG	Netherlands	Banking	1,537

Source: Association of Foreign Banks in Switzerland, *Economic Figures 2008* (Zurich: AFBS, 2009); Bilan, *Les 20 Patrons Qui Font la Suisse* (Genève: Bilan, October, 18 - 21 2010).

Annex table 6. Switzerland: the ten largest M&A deals, by inward investing firm, 2007-2009 (US$ billion)

Year	Acquiring company	Target company	Target industry	Source economy (IFDI)	Shares acquired (%)	Estimated/ announced transaction value
2009	Mirror Lake Oil & Gas Co Ltd	Addax Petroleum Corp	Oil and gas operations	Canada	100	7.2
2009	BASF SE	Ciba Specialty Chemicals	Chemicals and biopharmaceuticals	Germany	96	2.6
2009	Berkshire Hathaway Inc	Swiss Reinsurance Co Ltd	Insurance	United States	23	2.6
2008	General Dynamics Corp	Jet Aviation International SA	Aviation services	United States	100	2.2
2008	BlackRock Inc	UBS AG - Mortgage Assets	Diversified financial	United States	100	1.5
2007	Merck KGaA	Serono International SA	Chemicals and biopharmaceuticals	Germany	98	8.6
2007	SCOR	Converium Holdong AG	Insurance	France	96	2.7
2007	Medi-Clinic Luxemburg Sarl	Klinik Hirslanden AG	Healthcare	Luxemburg	100	2.4
2007	Rank Group Ltd	SIG Holding	Packaging and filling machines	New Zealand	100	2.3
2007	Allianz Capital Partners GmbH	Selecta Group	Vending services	Germany	100	1.5

Source: UNCTAD, *World Investment Report 2009: Transnational Corporations, Agricultural Production and Development* (Geneva: UNCTAD, 2009); Thomson ONE Banker. Thomson Reuters.

Annex table 7. Switzerland: the ten largest greenfield projects, by inward investing firm, 2007-2009
(US$ million)

Year	Investing company	Target industry	Business activity	Source economy (IFDI)	Estimated/ announced transaction value
2009	Rezidor Hotel Group	Hotels and tourism	Construction	Belgium	92
2009	Starwood Hotels & Resorts	Hotels and tourism	Construction	United States	92
2008	Aldi Group	Food and tobacco	Headquarters	Germany	95
2008	Carlson Companies	Hotels and tourism	Construction	United States	92
2008	Orascom Group	Hotels and tourism	Construction	Egypt	92
2008	Accor	Hotels and tourism	Construction	France	92
2008	Merck & Co	Pharmaceuticals	Manufacturing	United States	80
2007	Cambridge Solutions	Software and IT services	ICT and internet infrastructure	United States	91
2007	Yahoo	Software and IT services	ICT and internet infrastructure	United States	91
2007	Baxter	Pharmaceuticals	Manufacturing	United States	80

Source: fDi Intelligence, a service from the *Financial Times Ltd.*

Outward FDI and its policy context, 2010

Philippe Gugler and Xavier Tinguely

Switzerland's OFDI has traditionally been relatively high. The small size of the country, a natural resources shortage and the geographical location at the heart of Europe induced Swiss firms constantly to expand their activities abroad. This exposure to global markets is reflected in its OFDI. Although the global financial and economic crisis pushed the country into a recession and triggered a sharp decrease of OFDI flows, the Swiss OFDI stock continued to grow in 2008 and 2009. Thanks to a well-balanced economic structure based on innovation and knowledge and coherent government policies, Switzerland weathered, at least in the short-term, the effects of the crisis and set the path for a sustainable growth of OFDI.

Trends and developments

Country-level developments

Despite the global financial and economic crisis, Swiss OFDI remained at a high level in 2008.[318] As illustrated by annex table 1, the stock of Swiss OFDI has continuously grown since 2000, to reach US$ 760 billion in 2008. This represented a 15% increase from the 2007 stock. Among comparable economies (selected in annex table 1), Switzerland recorded the second highest OFDI stock in 2008, behind the Netherlands. Furthermore, the ratio of its OFDI stock to GDP rose to 148% whereas it amounted to 37% for Austria, 59% for Ireland, 67% for Sweden, and 97% for the Netherlands.[319]

While the OFDI stock recorded a steady growth during 2000-2008, OFDI flows evolved more irregularly (annex table 2).[320] Although comparable economies have higher fluctuations (annex table 2), three distinctive phases characterize Switzerland's. First, FDI outflows sharply decreased from US$ 45 billion in 2000 to only US$ 8 billion in 2002 (the lowest level since 1993). This spectacular decline, in line with the global trend, was mainly attributable to a large drop of the number of M&As after the record year 2000 and a decrease in reinvested earnings reflecting the losses of banks, insurance and holding companies in the United States and the United Kingdom.[321] In a second phase, OFDI flows gradually soared to US$ 70 billion in 2006, a new peak. This recovery was principally due to a substantial increase in reinvested earnings and a rapid growth of acquisitions, favored by a flourishing international economy and a high level of liquid funds held by companies.[322] Finally, OFDI flows dropped again to US$ 57 billion in 2007 and US$ 51 billion in 2008. This new fall, parallel to the slowdown of the global economy, resulted from a combination of reduced expenditure on acquisitions abroad, a decline in reinvested earnings and a repatriation of foreign equity.[323] According to the quarterly estimates, this decline seems to be even more pronounced in 2009. After nine months, Swiss OFDI

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[318] Swiss National Bank, *Direct Investment 2008* (Bern and Zurich: SNB, 2009).
[319] UNCTAD, *World Investment Report 2009: Transnational Corporations, Agricultural Production and Development* (Geneva: UNCTAD, 2009).
[320] It is necessary to keep in mind that, although FDI flows influence FDI stocks, a change in FDI flows does not necessarily provide any direct indication about FDI stocks, and vice versa. Changes in FDI stocks can be due to various factors not related to FDI flows. For instance, changes in FDI stocks may be due to exchange rate movements, new valuation principles (e.g. adjustment to international accounting standards) or the raising of capital in domestic or international markets. For more information, please refer to Swiss National Bank, *Direct Investment 2008*, op. cit., p. 18.
[321] Swiss National Bank, *Development of Direct Investment in 2001* (Bern and Zurich: SNB, 2002) and Swiss National Bank, *Development of Direct Investment in 2002* (Bern and Zurich: SNB, 2003).
[322] Swiss National Bank, *Development of Direct Investment in 2003* (Bern and Zurich: SNB, 2004) and Swiss National Bank, *Direct Investment 2006* (Bern and Zurich: SNB, 2007).
[323] Swiss National Bank, *Direct Investment 2007* (Bern and Zurich: SNB, 2008) and Swiss National Bank, *Direct Investment 2008*, op. cit.

flows amounted to US$ 14 billion, constantly decreasing from US$ 6 billion in the first quarter to US$ 4 billion in the third quarter.[324]

At a more disaggregated level, annex table 3 shows that some 40% of the capital stock abroad emanated from the manufacturing industry in 2008 (US$ 305 billion). This share constantly rose after reaching its lowest level at 29% in 2001.[325] Within manufacturing, chemicals and plastics accounted for the largest amount (US$ 131 billion). Services however continued to hold the majority of OFDI stock, namely US$ 455 billion on a total of US$ 760 billion. Among services, financial activities (finance and holding companies, banks, insurance) contributed to nearly 90% of the services' stock abroad. The numbers in annex table 3 bear out the notion that Switzerland has a quite diversified base of FDI.

With regard to the geographical distribution of Swiss OFDI stock in 2008, 72% was still held in developed economies (annex table 4). This share however decreased by 8 percentage points since 2000. The EU held around 37% (US$ 284 billion), including 7% in Germany, 6% in the United Kingdom and 4% in France. The Swiss OFDI stock in North America rose from US$ 59 billion in 2000 to US$ 171 billion in 2008. It corresponded thus to 22% of the total stock abroad. Although the share of the Swiss OFDI stock in Canada rose from 5% in 2000 to 17% in 2008, the United States still gathered more of the Swiss OFDI stock in North America. Regarding developing economies, Africa accounted for 2%, Asia and Oceania for 6% and Latin America and the Caribbean for 19% of the Swiss OFDI stock, of which 74% stemmed from offshore financial centers. It is interesting to note that the share of the Swiss FDI stock in the BRIC countries rose from 2% to 6% between 2000 and 2008, in line with the global trend reflecting the higher share of BRICs in global FDI. The most impressive increase occurred in Brazil, where it jumped from US$ 3.5 billion in 2000 to US$ 31 billion in 2008. It is also worth observing that offshore financial centers, which serve almost exclusively as hubs for investments in other countries, hosted some 21% of the Swiss OFDI stock in 2008.

The sectoral and regional breakdown of the Swiss OFDI stock corroborates some of the major precepts of the theory of the MNE.[326] On the one hand, as the possession of some kinds of ownership-specific advantages *vis-à-vis* foreign competitors is necessary to engage in cross-border activities, Swiss OFDI stock is mainly distributed among sectors in which Swiss MNEs possess specific skills and knowledge, such as the financial sector or the chemical industry.[327] On the other hand, as Switzerland is a small innovation-driven country in which competitiveness and prosperity strongly depend on the use of the most sophisticated processes, Swiss OFDI stock is mainly dispersed within the most technologically advanced regions, namely Europe and North America. Swiss MNEs are therefore particularly prone to undertake strategic-asset seeking investment constantly to enhance their knowledge and technological assets.

As FDI data provided by the Swiss National Bank (SNB) allow for a relatively detailed analysis, it is possible to explore the evolution of the workforce employed by Swiss affiliates in foreign territories. In parallel to the observed OFDI growth, Swiss affiliates abroad increased their employment by 94,000 to 2.44 million in 2008, confirming thus the positive trend of the past six years.[328] Looking at the sectoral distribution, manufacturing accounted for 52% and services for 48% of employment abroad. Within manufacturing, the "chemicals and plastics", "metals and machinery" and "other manufacturing and construction" sectors employed 78% of the manufacturing labor abroad. Regarding services, 18% out of 48% were employed by Swiss-domiciled but

[324] Swiss National Bank, *Swiss Balance of Payment Q3 2009* (Bern and Zurich: SNB, 2009).
[325] Ibid.
[326] For an exhaustive overview of the theory of the multinational enterprise, see John H. Dunning and Sarianna M. Lundan, *Multinational Enterprises and the Global Economy* (Cheltenham: Edward Elgar, 2008).
[327] In terms of the motivations for investment, market access in services is likely to be relatively more important, whereas pharmaceutical investments are driven by knowledge acquiring motives. Either way, OFDI by Swiss MNEs is mainly oriented toward advanced economies.
[328] Swiss National Bank, *Direct Investment 2008*, op. cit.

foreign-controlled finance and holding companies. Whereas the share of staff employed by Swiss companies in Europe (around 50%) and in North America (around 16%) remained relatively stable between 2004 and 2008, Swiss-companies increased their share of employees in Asia from 16% in 2004 to 21% in 2008.

The corporate players

The *World Investment Report 2009* reported 2,616 parent corporations established in Switzerland in 2008.[329] Among these, 40 Swiss MNEs ranked among the Forbes 2000 list of the world's biggest companies.[330] By comparison, Ireland classed 9 companies, Austria 13, the Netherlands 22 and Sweden 22. Annex table 5 lists the twelve Swiss MNEs recording sales higher than US$ 20 billion worldwide in 2008. These flagship firms depict the strengths, international scope and structure of the Swiss economy. Moreover, Nestlé, Roche, Holcim, and Novartis also appeared on the list of the world's top 100 non-financial MNEs, and Zurich Financial Services, UBS, Credit Suisse, and Swiss Reinsurance Company on the list of the top 50 financial MNEs.[331]

Swiss MNEs continued to strengthen their international stake by undertaking new investment abroad. Between 2000 and mid-2009, Swiss MNEs concluded 1,327 cross-border M&As worth more than US$ 1,846 billion.[332] Annex table 6 lists the ten largest M&As undertaken by Swiss MNEs between 2007 and 2009. Six of the ten were conducted by enterprises mentioned in annex table 5. By acquiring the U.S. firm Genentech for US$ 46.7 billion in March 2009, the Swiss biopharmaceutical Roche concluded the largest M&A in terms of transaction value of the period.[333] It is worth noting that four M&As were carried out by chemical and biopharmaceutical companies and three by firms active in the resources seeking industry. Regarding geographical distribution, the United States were the most targeted economy, with five M&As. Swiss MNEs were also particularly active in greenfield investment. During the period 2004-2009, 1,670 greenfield FDI projects were conducted by Swiss MNEs. A record peak of 459 projects had even been reached in 2008.[334] Annex table 7 lists the ten biggest greenfield transactions concluded by Swiss investors. Interestingly, eight projects were conducted in emerging markets.

Effects of the current global crisis

Despite the weight of the financial sector in economic activity and massive losses of large Swiss banks in the US subprime mortgage market, Switzerland has weathered the financial and economic crisis better than many other countries – at least in the short term.[335] The diversification of the Swiss economy, the specialization in innovative niches, a proactive monetary policy and a coherent government blueprint helped Switzerland to respond quickly to one of the worst economic downturns of the past decades.[336] As illustrated above, Swiss direct investment abroad confirmed this analysis by remaining at a relatively high level in 2007 and 2008. In

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[329] UNCTAD, 2009, op. cit.
[330] "Forbes global 2000 lists of the world's biggest companies," *Forbes*, 2009.
[331] Both lists are published annually by the *World Investment Report* (Geneva: UNCTAD).
[332] UNCTAD, 2009, op. cit.; UNCTAD,FDI/TNC database, available at: http://stats.unctad.org/fdi.
[333] This impressive transaction contrasts with the provisional outflow figure for 2009 (annex table 2: US$ 14 billion). Because of confidentiality restriction, no comments on individual transactions are provided by the SNB. However, a general explanation can give an insight on why M&A figures do not always match FDI figures. Swiss FDI flows only include cross-border transactions (Switzerland-abroad). MNEs headquartered in Switzerland sometimes buy enterprises abroad via affiliates abroad. In other words, company "X" in Switzerland owns company "Y" in country "B", and this company "Y" buys company "Z" in country "C". In this case, the acquisition is included in the outward FDI figures of country "B" and not in the FDI outward figures of Switzerland. When it comes to Swiss FDI stocks and numbers of staff, a different methodology is applied. There, the SNB looks through intermediate companies and shows the ultimate owner abroad. In the previous example, the Swiss OFDI stock and the number of staff in country C will increase following the acquisition.
[334] UNCTAD, 2009, op. cit.
[335] OECD, *Economic Survey of Switzerland 2009 – Getting out of the Crisis* (Paris: OECD 2010).
[336] Ibid.

2009, the Swiss OFDI stock continued to grow.[337] In contrast, Swiss OFDI flows gradually decreased from nearly US$ 70 billion in 2006 to US$ 57 billion in 2007, US$ 51 billion in 2008 and US$ 14 billion in the first three quarters of 2009 (annex table 2). The first decline in 2007 was mainly attributable to a strong drop in cross-border M&As of Swiss manufacturing companies: capital outflows shrank by US$ 24 billion, to US$ 21 billion.[338] Furthermore, OFDI flows of banks fell by 42%, to US$ 10 billion.[339] This investment fall in the bank industry would have been even sharper if it had not been influenced by two reverse forces: on the one hand, losses contracted in the US real estate market generated negative (results in) reinvested earnings, while, on the other hand, banks injected new equity capital into their struggling foreign affiliates.[340] In other words, the downward pressure on OFDI flows generated by negative reinvested earnings was partially counterbalanced by the injection of fresh equity capital.[341]

Although new acquisitions led OFDI flows in manufacturing to rise to US$ 34 billion and additional fresh equity slightly enhanced OFDI flows by banks, direct investment flows abroad still diminished in 2008.[342] This trend seems to be confirmed in 2009 as OFDI flows amounted to only US$ 14 billion after the first three quarters.[343] The slowdown in Swiss OFDI flows has nevertheless to be considered in perspective. Indeed, Swiss direct investment flows abroad in 2007 and 2008 remained nearly 60% higher than the average of the preceding seven years. Second, the US$ 51 billion flow recorded in 2008 can be broken down into an outward flow of US$ 54 billion in equity capital, a withdrawal of US$ 24 billion in reinvested earnings and an outflow of US$ 21 billion in other capital.[344] Income from direct investment abroad plummeted from US$ 50.5 billion in 2007 to US$ 7.6 billion in 2008.[345] This collapse was mainly due to the massive losses realized by Swiss banks abroad. After recording losses reaching US$ 8 billion in 2007, banks suffered losses exceeding US$ 51 billion in 2008.[346] Finally, it seems that this weak income performance might last. Although the Swiss economy slowly regained momentum in 2009, OFDI flows are likely to remain at the 2007-2008 level throughout the period 2009-2010.[347]

The policy scene

Despite the gloomy performance of the world economy and the resulting protectionist pressure, the overall global policy trend continues to foster greater openness and FDI.[348] As prosperity increasingly depends on greater international cooperation, Swiss policy makers constantly seek to build an optimal environment conducive to the growth of the Swiss economy and the international expansion of Swiss companies. As an economy characterized by a pronounced outward orientation, Switzerland's competitiveness depends to a large extent on international trade and cross-border investment activities.[349] The improvement of access to foreign markets represents therefore a core objective of Swiss foreign economic policy.

Beside the multilateral approach (within the WTO framework), Switzerland aims to strengthen its economy by setting up a strong network of BITs and FTAs. At the beginning of 2010, Switzerland had 124 agreements on

[337] Swiss National Bank, *Monthly Statistical Bulletin February 2010* (Bern and Zurich: SNB, 2010).
[338] Swiss National Bank, *Direct Investment 2007*, op. cit.
[339] Ibid.
[340] Ibid.
[341] Swiss FDI flows can be broken down in equity capital, reinvested earnings and other capital.
[342] Swiss National Bank, *Direct Investment 2008*, op. cit.
[343] Swiss National Bank, *Swiss Balance of Payment Q3 2009*, op. cit.
[344] Swiss National Bank, *Direct Investment 2008*, op. cit.
[345] Ibid.
[346] Ibid.
[347] Swiss National Bank, *Quarterly Bulletin 4/2009* (Bern and Zurich: SNB, 2009).
[348] UNCTAD, 2009, op. cit.
[349] State Secretariat for Economic Affairs, *Free Trade Agreements* (FTAs), 2010, available at: http://www.seco.admin.ch/themen/00513/00515/01330/index.html?lang=en, also for the information in the following paragraph.

the promotion and reciprocal protection of investment with economies such as Argentina, China, Hong Kong (China), India, Indonesia, Japan, Russia, Saudi-Arabia, South Africa, and Singapore. Furthermore, in addition to the EFTA Convention and the FTA with the EU, Switzerland has concluded 22 FTAs with 31 partners outside the EU. Between 2008 and 2009, two new FTAs came into force, one with Canada and one with the South African Custom Union.[350] FTAs have also been signed with Albania, Serbia, the Cooperation Council of the Arab States of the Gulf, Columbia, and Peru. They will come into force in the course of 2010. Negotiations are currently being undertaken or will start soon with Algeria, China, Hong Kong (China), India, Indonesia, Russia, Thailand, Ukraine, and Vietnam. The foreign policy conducted by the Swiss Government seems to pay off as FTAs generated significant benefits for Swiss direct investors. In fact, the accumulated capital flows from Switzerland to its 31 partners outside the EU (FTAs) totaled more than US$ 19 billion from 1988 to 2007. They represented some 5% of Switzerland's accumulated total capital exports. Moreover, while total Swiss OFDI increased on average by 13% in the years 1988-2007, the growth of OFDI in the partner countries was on average 18% in the first four years after the respective FTAs came into force.

Conclusions and Outlook

Although the world economic recession curbed the growth of Swiss OFDI, the operations of Swiss companies abroad remained extensive in 2008. Despite a slowdown of economic activity in 2009 and unsure forecasts for 2010, foreign investments of Swiss firms are expected to be relatively stable compared to their 2007-2008 level.[351] The foreign policy pursued by the Swiss authorities, the diversification of the Swiss economy and the strong integration of Swiss firms into the world economy will continue to limit the impact of the current economic downturn by stimulating entrepreneurship and favoring the development of new partnerships abroad.

Additional readings

Abt, Marianne, "L'importance des accords de libre-échange avec des partenaires extérieurs à l'UE," *La Vie Economique,* 10 (2009),pp. 4-6.

Federal Department of Foreign Affairs, *Foreign Policy Report 2009* (Bern: FDFA, 2009).

Gugler, Philippe and Julie Michel, "***Foreign direct investment in R&D activities: location and motivations of Swiss foreign R&D." Paper*** presented at the 69th International Atlantic Economic Conference, Prague, March 24-27, 2010.

Michel, Julie, *Investissements Directs à l'étranger dans les Activités de Recherche et Développement: Fondements Théoriques et Application aux Entreprises Suisses* (Bern: Peter Lang Publishing Group, 2009).

Useful websites

For FDI policy: Swiss Government, Federal Department of Economic Affairs, available at: www.evd.admin.ch.

For FDI statistics: Swiss National Bank, available at: www.snb.ch.

[350] South Africa, Botswana, Lesotho, Namibia and Swaziland.
[351] Swiss National Bank, *Monthly Statistical Bulletin February 2010*, op. cit.; Swiss National Bank, *Swiss Balance of Payment Q3 2009*, op. cit.

Statistical annex [352, 353]

Annex table 1. Switzerland: outward FDI stock, 2000-2009 (US$ billion)

Economy	2000	2001	2002	2003	2004	2005	2006	2007	2008	2008 [a]	2009 [b]
Switzerland	**233**	**248**	**295**	**343**	**396**	**426**	**518**	**658**	**760**	**762**	**810**
Memorandum: comparator economies											
Austria	25	29	43	56	70	72	106	156	153	-	-
Ireland	28	41	59	73	107	104	121	146	159	-	-
Netherlands	306	332	397	523	587	616	758	877	844	-	-
Sweden	123	123	147	186	215	209	266	327	319	-	-

Source: Authors calculations, based on UNCTAD, FDI/TNC database; Swiss National Bank, *Development of Direct Investment* (2001-2006); Swiss National Bank, *Direct Investment* (2008-2009).

[a] Data at the end of the third quarter.
[b] Provisional data at the end of the third quarter. Authors calculation based on Swiss National Bank, *Monthly Statistical Bulletin February 2010* (Bern and Zurich: SNB, 2010).

Annex table 2. Switzerland: outward FDI flows, 2000-2009 (US$ billion)

Economy	2000	2001	2002	2003	2004	2005	2006	2007	2008	2008 [a]	2009 [b]
Switzerland	**45**	**17**	**8**	**15**	**27**	**54**	**70**	**57**	**51**	**30**	**14**
Memorandum: comparator economies											
Austria	6	3	6	7	8	11	14	33	28	-	-
Ireland	5	4	11	6	18	14	15	21	14	-	-
Netherlands	76	51	32	44	29	132	65	29	58	-	-
Sweden	41	7	11	21	21	27	24	38	37	-	-

Source: UNCTAD, *World Investment Report 2003: FDI Policies for Development. National and International Perspectives* (Geneva: UNCTAD, 2003); UNCTAD, *World Investment Report 2006: FDI from Developing and Transition Economies: Implications for Development* (Geneva: UNCTAD, 2006); UNCTAD, *World Investment Report 2009: Transnational Corporations, Agricultural Production and Development* (Geneva: UNCTAD, 2009).

[a] Data for the first three quarters of 2008.
[b] Provisional data for the first three quarters of 2009. Authors calculation based on Swiss National Bank, *Monthly Statistical Bulletin February 2010* (Bern and Zurich: SNB, 2010).

[352] As Swiss FDI data are published in Swiss Franc (CHF), they have been converted into US$ on the basis of the official CHF/US$ conversion key provided by the Swiss National Bank and used by UNCTAD to harmonize data in US$.
[353] In the statistics on direct investment, the Principality of Liechtenstein is included in the Swiss data.

Annex table 3. Switzerland: sectoral distribution of outward FDI stock, 2000 – 2008 (US$ billion) [a]

Sector / industry	2000	2001	2002	2003	2004	2005	2006	2007	2008
Manufacturing	**76.6**	**73.5**	**97.9**	**115.6**	**140.5**	**150.8**	**209.6**	**268.9**	**305.4**
Textiles and clothing [b]	1.4	0.9	1.0	7.7	8.7	6.2	13.0	19.1	17.4
Chemicals and plastics	34.3	33.4	44.9	50.3	64.6	73.3	98.7	113.5	130.7
Metals and machinery	10.9	11.1	14.9	16.3	18.8	18.1	29.3	42.0	47.2
Electronics, energy, optical and watchmaking	9.7	6.7	11.1	10.1	10.9	10.8	16.6	30.0	33.8
Other manufacturing and construction	20.3	21.4	26.0	31.2	37.5	42.4	52.0	64.3	76.3
Services	**156.8**	**174.3**	**197.5**	**227.0**	**255.9**	**275.4**	**308.5**	**389.0**	**454.7**
Trade	7.2	7.3	8.9	8.7	12.2	17.4	18.0	24.2	25.8
Finance and holding companies	55.3	59.9	82.2	93.9	106.6	121.0	122.9	186.3	229.0
of which									
Swiss-controlled [c]	12.6	11.2	15.4	20.8	26.7	23.1	26.7	30.4	37.5
Foreign-controlled [d, e]	42.7	48.7	66.8	73.1	79.9	97.9	96.2	155.9	191.5
Banks	33.1	33.2	39.1	48.1	48.7	53.3	73.3	77.1	87.2
Insurance companies	52.5	62.3	57.8	65.5	76.5	72.9	79.3	75.0	91.1
Transportation and communications	2.2	4.3	3.0	3.1	2.8	2.7	4.7	10.7	11.1
Other services	6.5	7.3	6.5	7.7	9.1	8.1	10.3	15.7	10.5
Total	**233.4**	**247.8**	**295.4**	**342.6**	**396.4**	**426.2**	**518.1**	**657.9**	**760.1**
Total excluding foreign-controlled finance and holding companies	190.7	199.1	228.6	269.5	316.5	328.3	421.9	502.0	568.6

Source: Authors calculations, based on Swiss National Bank, *Development of Direct Investment* (2001-2006); Swiss National Bank, *Direct Investment* (2007-2008).

[a] Capital stock at year-end (book value). The breakdown by sector and by economic activity refers to a company's core business in Switzerland. Until 2003, classification according to the General Classification of Economic Activities, ASWZ 1985 (Allgemeine Systematik der Wirtschaftszweige); from 2004 onwards, classification according to the General Classification of Economic Activities, NOGA 2002 (Nomenclature générale des activités économiques). Expansion of the reporting population in 2004.
[b] Expansion of the reporting population in 2003.
[c] A company is considered to be Swiss-controlled if a majority share of its capital is in Swiss hands.
[d] A company is considered to be foreign-controlled if a majority share of its capital is in foreign hands.
[e] Expansion of the reporting population in 2006.

Annex table 4. Switzerland: geographical distribution of outward FDI stock, 2000, 2008 (US$ billion) [a]

Economy / region	2000	2008
World	**233.4**	**760.1**
Developed economies	**185.9**	**553.6**
Europe	**121.5**	**352.1**
European Union [b]	113.9	284.1
France [c]	11.2	33.1
Germany	14.0	52.7
Luxemburg	10.2	23.9
Netherlands	12.3	32.8
United Kingdom	35.9[5]	47.7
Other European countries [d]	7.7	68.0
Russian Federation	0.4	5.1
Offshore financial centers [e]	…	54.3
North America	**58.6**	**170.8**
Canada	3.2	30.3
United States	55.4	140.5
Other developed economies	**4.9**	**30.7**
Australia	1.9	15.2
Japan	2.9	14.0
Developing economies	**47.6**	**206.5**
Africa	**2.0**	**12.6**
Egypt	0.4	1.6
South Africa	0.8	8.3
Asia and Oceania	**15.7**	**46.1**
China	1.0	6.4
Hong Kong (China)	1.6	4.3
India	0.2	2.2
Indonesia	0.3	5.6
Singapore	7.5	7.7
United Arab Emirates	0.1	8.0
Latin America and Caribbean	**29.9**	**147.8**
Brazil	3.5	31.0
Offshore financial centers [f]	19.3	106.2

Source: Authors calculations, based on Swiss National Bank, *Development of Direct Investment* 2001; Swiss National Bank, *Direct Investment* 2008.

[s] Capital stock at year-end (book value). Expansion of the reporting population in 2004. The definition of economies is based on the Eurostat geonomenclature.
[b] As of 2004, EU25; as of 2007, EU27.
[c] As of 2000, incl. Monaco, Réunion, French Guiana, Guadeloupe, and Martinique.
[d] As of 2000, incl. Guernsey, Jersey and the Isle of Man, excl. Monaco; until 2003, incl. Baltic countries, Malta, Poland, Slovakia, Slovenia, Czech Republic, Hungary, and Cyprus; until 2006, incl. Bulgaria and Romania.
[e] Gibraltar, Guernsey, Jersey, and the Isle of Man.
[f] Anguilla, Bahamas, Barbados, Bermuda, Virgin Island (British), Jamaica, Cayman Islands, Montserrat, Netherlands Antilles, Panama, and St Kitts and Nevis; as of 2000, incl. Virgin Islands (US), Antigua and Barbuda, Belize, Dominica, Grenada, Santa Lucia, St Vincent and the Grenadines, Turks, and Caicos Islands.

Annex table 5. Switzerland: principal MNEs headquartered in the country, ranked by world total sales, 2009 (US$ billion)

Rank	Name	Industry	Sales [a]	Profits [a]	Assets [a]
1	Nestlé	Food, drink and tobacco	103.01	16.91	97.12
2	UBS	Diversified financial	61.23	-18.52	1,894.85
3	Credit Suisse Group	Diversified financial	45.64	-7.70	1,089.61
4	Roche Holding	Drugs and biotechnology	42.75	8.41	69.77
5	Novartis	Drugs and biotechnology	42.01	8.30	73.22
6	ABB	Capital goods	34.91	3.12	31.99
7	Zurich Financial Services	Insurance	32.35	3.04	325.04
8	Swiss Re Group	Insurance	31.08	-0.81	214.16
9	Adecco	Business services and supplies	29.56	0.73	10.51
10	Petroplus Holdings	Oil and gas operations	28.26	-0.51	6.93
11	Xstrata	Materials	27.95	3.60	55.31
12	Holcim	Construction	23.58	1.67	42.21

Source: Authors elaboration, based on "Forbes global 2000 lists of the world's biggest companies," *Forbes*, 2009.

[a] Sales, profits and assets are world totals.

Annex table 6. Switzerland: the ten largest cross-border M&A deals, by outward investing firm, 2007-2009 (US$ billion)

Year	Acquiring company	Target company	Target industry	Target economy	Shares acquired (%)	Estimated/ announced transaction value
2009	Roche Holding AG	Genentech Inc	Chemicals and biopharmaceuticals	United States	100	46.7
2009	Holcim Ltd	Cemex SAB de CV-AU Assets	Construction	Australia	100	1.6
2008	Novartis AG	Alcon Inc	Chemicals and biopharmaceuticals	United States	77	10.5
2008	Roche Holding AG	Ventana Medical Systems Inc	Chemicals and biopharmaceuticals	United States	94	3.7
2008	Xstrata PLC	Jubilee Mines NL	Materials	Australia	100	2.8
2008	Glencore International AG	Century Aluminium Co	Coal, oil and natural gas	United States	38.9	1.8
2008	STMicroelectronics NV-Wireless	NXP Semiconductors-Wireless Op	Semiconductors	Netherlands	100	1.5
2007	Nestle SA	Gerber Products Co	Food, beverages and tobacco	United States	100	5.5
2007	Swisscom AG	Fastweb SpA	Telecommunications	Italy	82	5.5
2007	Givaudan SA	Quest InternationalBV	Chemicals and biopharmaceuticals	Netherlands	100	2.3

Source: UNCTAD, *World Investment Report 2009: Transnational Corporations, Agricultural Production and Development* (Geneva: UNCTAD, 2009); Thomson ONE Banker. Thomson Reuters.

Annex table 7. Switzerland: the ten largest greenfield transactions, by outward investing firm, 2007-2009
(US$ billion)

Year	Investing company	Target industry	Business activity	Host economy	Estimated/ announced transaction value
2009	Novartis	Chemicals and biopharmaceuticals	Research and development	China	1.0
2008	Glencore International	Coal, oil and natural gas	Manufacturing	Colombia	3.0
2008	Glencore International	Alternative and renewable energy	Electricity	Zambia	1.5
2008	STMicroelectronics	Semiconductors	Manufacturing	France	1.3
2008	Advanced Power AG	Coal, oil and natural gas	Electricity	Netherlands	1.2
2008	Holcim	Building and construction materials	Manufacturing	Brazil	0.7
2008	EFG Group	Financial services	Business services	Poland	0.7
2007	Xstrata PLC	Metals	Extraction	New Caledonia	3.8
2007	Vimetco	Metals	Manufacturing	Kyrgyzstan	3.2
2007	Jelmoli	Real estate	Construction	Algeria	1.3

Source: fDi Intelligence, a service from the Financial Times Ltd.

Chapter 13 – United States of America

Outward FDI and its policy context, 2009

Marilyn Ibarra-Caton and Raymond Mataloni Jr.

United States (U.S.) OFDI was $65 billion during the third quarter of 2009 (annex figure 1). The average flow during the seven quarters of the current recession (Q1:2008 to Q3:2009) decreased 17 percent, compared with the last seven quarters of the expansion that preceded it (Q2:2006 to Q4:2007; henceforth "expansionary period"). The pronounced decline in U.S. OFDI parallels the broader falloff in business investment worldwide in the current economic recession. Despite the slowdown in U.S. OFDI flows, they remained over 25 percent higher than the average for the preceding five years, which is partly attributable to the continuing attraction of big emerging markets.

A protracted recession

The current recession, which began in December 2007, could rank as the longest U.S. economic downturn since the Great Depression. In addition to the severe economic downturn of the U.S. economy, global economic indicators have registered sharper declines than in the previous two global recessions of 1981 and 1990.[354] Has the severity and duration of the current global recession corresponded with a severe and sustained reduction in flows of U.S. OFDI? During the current recession, these flows fell 17 percent in current dollars, to $483 billion, from $585 billion in the expansionary period. Over three-fourths of the decline occurred in net equity capital flows—largely payments to acquire or establish new foreign affiliates (annex figure 1). During the current recession, equity capital flows were $101 billion, or 50 percent lower than the $202 billion in the expansionary period. Changes in the two other components of FDI—reinvested earnings and intercompany debt—accounted for a small decline in flows of U.S. OFDI. Reinvested earnings—the parent firms' share of affiliates' earnings that are reinvested--declined 5 percent during the current recession. Intercompany debt flows—loans between parent firms and affiliates—are a very small component of U.S. OFDI and are extremely volatile; they change direction frequently because the loans, which are often for the purpose of providing short term financing for intra-firm trade, tend to be repaid soon after they are created.

Equity capital flows for new investments experienced a sharp decline (49 percent) during the current recession. The pronounced decline in equity capital flows for new investment coincided with a worldwide decline in global merger and acquisition activity. According to Thompson Reuters, global merger and acquisition activity fell by 40 percent during the current recession, from the expansionary period. In Europe, the value of merger and acquisition activity decreased 34 percent and, in Asia Pacific, it decreased 27 percent. A sharp decline also occurred in the average size of U.S. OFDI transactions which fell by 34% from $230 million in the expansionary period to $150 million in the current recession. This tracks the 34% decline that Thompson Reuters reports in the average size of global transactions between the two periods.

Long term trends in equity capital flows for new investments become more apparent when viewed in the context of a moving average because a single large transaction can dominate flows in any given period. A four-quarter moving average reveals that movements in equity capital flows for new investments have not always paralleled movements in the business cycle (annex figure 2). For example, the increase that began in the third quarter of 2003 peaked in the fourth quarter of 2004 and then began a decline that lasted until the second quarter

[354] M. Ayhan Kose, Prakash Loungani and Marco E. Terrones, "Out of the ballpark," 46 (2) *Finance & Development* (June 2009).

of 2006; this decline was not associated with a worldwide drop in economic activity, according to data from the United Nations, or with a drop in worldwide M&A activity, according to data from Thompson Reuters (annex figure 2).

The increase in equity capital flows for new investments that began in the third quarter of 2006 and continued through 2007 was propelled by acquisitions or establishments of affiliates in various industries, including finance (except banks) and insurance; oil and gas extraction; wholesale and retail trade; professional, scientific, and technical services; and several manufacturing industries, such as pharmaceuticals, transportation equipment, and machinery.

The decline in equity capital outflows for new investments has been accompanied by a decline in equity capital *in*flows, resulting from the sale of foreign affiliates. Selloffs declined by 48 percent during the current recession compared with the expansionary period; this decrease is similar to the 51 percent decline in outflows. The paucity of sell-offs and new investments may be related to difficulties in financing deals in the current risk-averse environment and to banks' reluctance or inability to renew and extend credit lines and insistence on tighter credit terms. These factors may have played a role in shrinking the pool of potential buyers.

During the current recession, U.S. parents firms chose to reinvest about the same share of their affiliates' earnings as they did in the expansionary period. Unlike equity capital flows which declined at the onset of the recession—in the first quarter of 2008—reinvested earnings and total earnings held up through the second quarter of 2008 as affiliates' earnings were boosted by the depreciation of the dollar against many foreign currencies and by growth in global economic activity through the first quarter of 2008. The share of earnings reinvested trended upward through 2008, indicating that parent firms were still choosing to invest in their foreign affiliates rather than remit their earnings to the United States (annex figure 3).

The attraction of emerging markets

Despite weak economic conditions, U.S. multinationals have continued to expand their investments in newly emerging markets at a more rapid rate than in advanced economies. Average quarterly U.S. OFDI decreased 14 percent for low-to-middle-income countries during the current recession, compared with 39 percent for high-income countries.[355] This pattern primarily reflects the attraction of new, rapidly growing consumer markets in emerging markets where foreign affiliates of U.S. multinationals typically sell most of their output to local customers. To illustrate the potential of one of these new markets, consider that there were only about 10 automobiles per 1,000 people in China in 2005, compared with 500 per 1,000 people in the United States.[356]

These burgeoning national markets present attractive business opportunities that are at least partially sheltered from the effects of business cycles elsewhere in the world. The rate of return for U.S. FDI abroad has remained significantly higher in the big emerging markets than in the more advanced economies during the current recession. In high income countries, it was roughly 10 percent, compared with nearly 20 percent in low-to middle-income countries.[357] U.S. multinationals have tended to reinvest their affiliates' profits to expand their business ventures abroad and to seek out new opportunities; this pattern has continued in the emerging markets.

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[355] These figures exclude investments in countries that tend to host a disproportionate number of holding companies. A significant portion of direct investment capital flows associated with these countries are ultimately destined for use by affiliates in other countries. See, for example, "Holding companies in the data on U.S. direct investment abroad," in Marilyn Ibarra and Jennifer Koncz, "Direct investment positions for 2008: country and industry detail," *Survey of Current Business,* 89 (July 2009), p.25.

[356] L. Alan Winters and Shahid Yusef (eds.), *Dancing with Giants: China, India, and the Global Economy* (Washington D.C.: World Bank, 2007).

[357] These rates of return were calculated as the ratio of direct investment income to the average of the beginning- and end-of-period direct investment positions. The imprecision of the resulting estimates is a result of the denominator being at historical cost, which, in

Many U.S. firms find that they must serve these foreign markets through direct investment rather than through exports from the United States. Having a local presence allows firms to be more responsive to customers and, in many cases, to offer a lower price. For large markets, like China, foreign affiliates are increasingly conducting their own R&D in order to tailor products to local tastes and to comply with local regulations. R&D expenditures by Chinese affiliates of U.S. companies, for example, increased from less than $50 million in 1997 to over $1.1 billion in 2007.[358] Production of goods in the host country also allows firms to avoid the shipping costs that would have to be incurred if they chose to serve these markets by exporting from the United States. Production of services in the host country is often necessary, either because proximity to the customer is necessary to deliver the service or because of restrictions on the provision of certain services by nonresidents. Nearly three-quarters of total sales by Chinese and Indian affiliates of U.S. companies were to local customers in 2007.[5] An additional attraction of emerging markets is that labor costs there are usually significantly lower than those in the United States, although finding workers with the necessary skills can be difficult.

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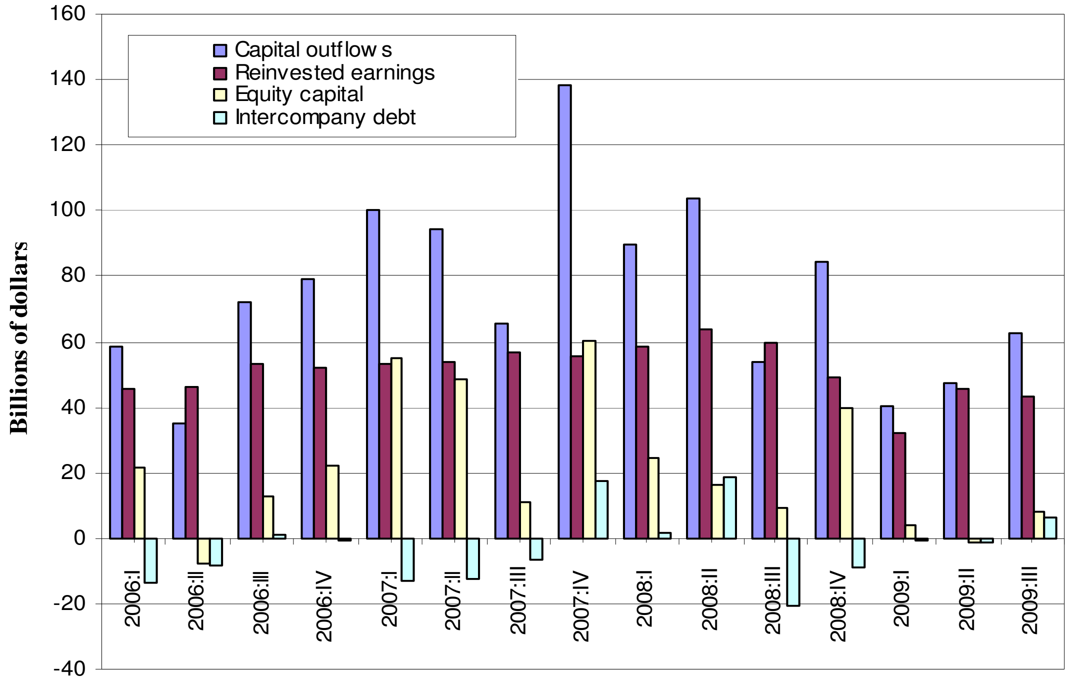
most cases, is the original cost of the investment. Under normal (inflationary) price conditions, older assets will be undervalued relative to newer assets and, thus, yield an overstated rate-of-return. For this reason, the estimates presented here are intended *only to give a rough impression* of the relative rates of return in highly developed economies and in emerging markets. For an exposition of the valuation issues involved, and for a description of methods to estimate rates of return in current-period prices, see Ned G. Howenstine and Ann M. Lawson, "Alternative measures of the rate of return on direct investment," *Survey of Current Business,* 71 (August 1991), pp. 44-45.

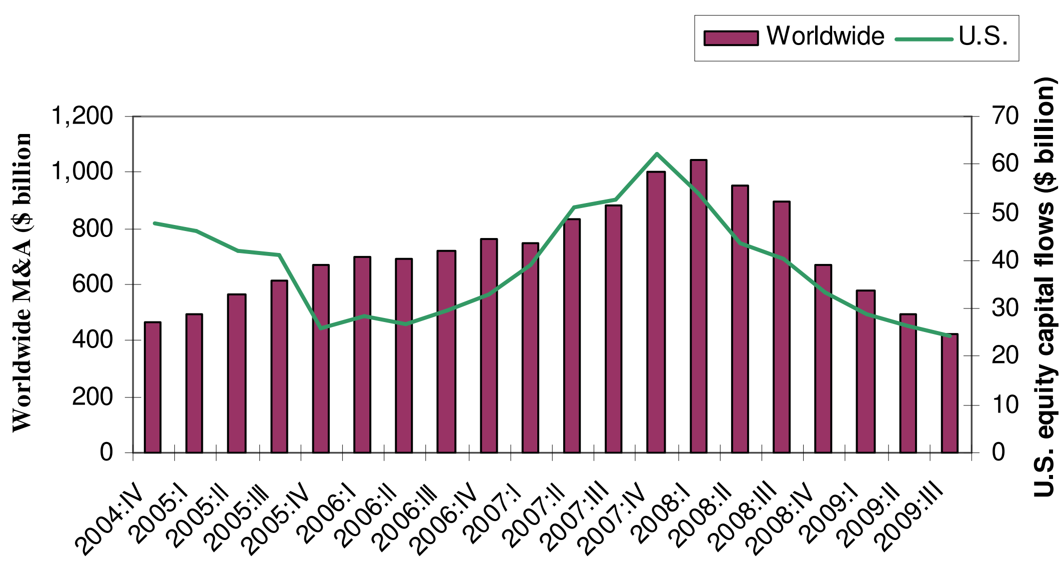
[358] U.S. Bureau of Economic Analysis, https://www.bea.gov.

Annex figure 1. Quarterly flows on U.S. outward foreign direct investment, by component, seasonally adjusted, 2006:Q1-2009:Q3



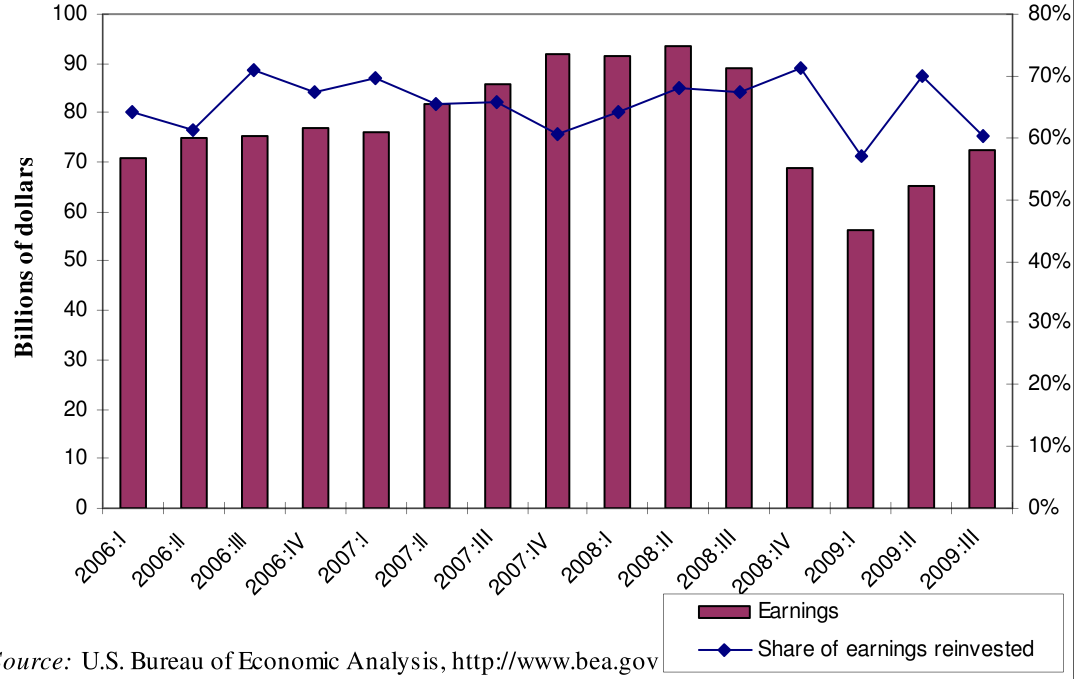
Source: U.S. Bureau of Economic Analysis, http://www.bea.gov

Annex figure 2. Equity capital flows for new U.S. investments abroad and value of worldwide mergers and acquisitions, four-quarter moving average, 1999:Q1 to 2009 Q3



Source: U.S.Bureau of Economic Analysis, http://www.bea.gov, and Thomson Reuters M&A

Annex figure 3. Seasonally adjusted quarterly earnings and the share of earnings reinvested, 2006:Q1 to 2009:Q3



Source: U.S. Bureau of Economic Analysis, http://www.bea.gov

PART II

EMERGING MARKETS

Chapter 14 – Argentina

Inward FDI and its policy context, 2010

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With a long-standing tradition of an international business presence, Argentina followed an open investment policy since its early stages of development. The most recent wave of foreign direct investment (FDI) growth took place between 2004 and 2008, with investments primarily in the manufacturing, natural resources and new technology sectors. In 2008, IFDI flows reached US$ 10 billion, positioning the country as a relevant investment destination worldwide. Moreover, with a 50% annual increase, Argentina was one of the ten fastest growing FDI destinations in the world.[359] *In 2009, IFDI contracted due to the global economic crisis in line with the rest of the world.*

Trends and developments

Country-level developments [360]

Beginning in the late 19th century, Argentina registered four distinct waves of IFDI, the first under the agro-export model of development and the following under import substitution industrialization. In the following wave in the 1990s, FDI was fuelled initially by a broad privatization process and later driven by a widespread series of M&As, both mainly targeting services, public utilities and the oil sector. The two trends were reflected in the high share of changes in ownership in FDI inflows in the period, which accounted for 57% of total flows. As a result, while FDI inflows reached an annual average of US$ 7 billion during the 1990-2000 period,[361] flows net of privatizations averaged US$ 5 billion,[362] and flows net of all changes in ownership recorded a lower annual average of US$ 4 billion for the same period. Growing foreign investments were reflected in an expanding FDI stock that reached US$ 80 billion in 2001 (annex table 1).

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[359] ProsperAr based on UNCTAD, *World Investment Report 2009: Transnational Corporations, Agricultural Production and Development* (New York and Geneva: United Nations, 2009). The ranking is based on all countries receiving more than US$ 5 billion in FDI inflows in 2008.

[360] FDI data cited in this section and in annex tables 1 through 4 come from the two main official sources responsible for recording FDI statistics in Argentina: the National Office for International Statistics at the National Institute of Statistics and Census (INDEC) and Argentina's Central Bank (BCRA). Both sources follow the methodology established in the International Monetary Fund's *Balance of Payments Manual* (fifth edition). Data on FDI flows are based on INDEC statistics, which are also the source for UNCTAD and IMF. FDI stock data from 2000 to 2003 are also cited from INDEC reports. Stock data from 2004 to 2008 are cited from BCRA reports, which offer more details for those years.

[361] This average figure includes the extraordinary FDI inflow received in 1999 (US$ 24 billion) mainly due to Repsol's purchase of the oil and gas company YPF, the country's largest company. This unique operation accounted for more than 60% of FDI flows that year and included the purchase of outstanding shares still held by the public sector and the associated purchase of YPF's publicly traded shares dispersed among minority shareholders.

[362] Figure corresponds to average annual inflows net of privatizations and net of Repsol's associated purchase in 1999 of YPF publicly traded shares. Figures net of privatizations are presented with the sole purpose of providing a homogeneous measure of comparison of FDI inflows over time. State-owned companies in Argentina (in the public utilities and energy sectors) were all sold during the wave of privatization of the 1990s, resulting in exceptional inflows of FDI. Given that privatizations are one-off events, a comparison of total FDI flows received during the 1990s with those corresponding to the period under analysis (2000-2008) could lead to inaccurate conclusions.

IFDI flows declined sharply in 2001 due to domestic and international developments. The effects of the global decline in FDI flows (41%) were magnified locally by the convertibility crisis in Argentina, severely impacting FDI inflows to the country: they dropped by 79% (annex table 2). Furthermore, the effect of the peso devaluation resulted in a sharp drop in the dollar value of the IFDI stock, which was cut by almost half to US$ 43 billion in 2002.

During the period of 2002-2003, foreign affiliates underwent a phase of reorganization and restructuring after the local crisis, with FDI inflows contracting at the domestic level as well as globally. By 2002, following the peso devaluation, debt levels of foreign affiliates in Argentina rose to 67% of assets.[363] In this context, many companies were forced to reduce and restructure their debt, returning to healthy balance sheets remarkably fast.

Between 2004 and 2008, rapid economic growth, increased domestic demand, high levels of profitability, and renewed competitiveness - combined with a favorable international environment - contributed to a vigorous expansion of FDI inflows. For five consecutive years, inflows expanded at a compound annual growth rate of 43%, substantially higher than the growth rate for the world (25%) and developing countries (28%) over the same period. As a result, annual inflows reached an average of US$ 6 billion during 2004-2008, surpassing since 2005 average annual flows net of privatizations registered in the 1990s.

The IFDI stock rose steadily, to reach the 2001 level of US$ 80 billion again in 2008 (annex table 1), a level that placed Argentina among the leading FDI recipients in Latin America, below Brazil, Mexico and Chile. In a broader context, Argentina ranked 14th among emerging markets in FDI stock in 2008.

During the 2004-2008 growth phase, FDI was mainly driven by greenfield investments by both already established foreign affiliates and new international companies entering the local market. As a result, changes in ownership (i.e. M&As and privatizations) represented only a fraction (7%) of total FDI flows in the five year period, down from 57% during the 1990s. The new composition of FDI flows is evidence of improvements in the quality of foreign investment in Argentina, as greenfield investments tend to make greater contributions to capital formation and employment than M&A operations.[364] The rise in reinvested earnings as a share of total FDI, which accounted for an average of 25% between 2005-2008, is also noteworthy.

The sectoral distribution of the IFDI stock of Argentina has been relatively stable since 2004 (annex table 3). Manufacturing, natural resources and services (including financial services) each accounted for approximately one third of the total stock on average during this phase (35%, 34%, 31%, respectively). A closer look at FDI flows reveals a trend of a growing share of manufacturing at the expense of natural resources. Specifically, the manufacturing sector's share in FDI inflows rose from

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[363] G. Bezchinsky, M. Dinenzon, L. Giussani, O. Caino, B. Lopez, and S. Amiel, "Inversión extranjera directa en la Argentina. Crisis, reestructuración y nuevas tendencias después de la convertibilidad," in B. Kossacoff, ed., *Crisis, Recuperación y Nuevos Dilemas: La Economía Argentina 2002-2007* (Buenos Aires: ECLAC, 2007), p. 162.
[364] Both greenfield and M&A operations can foster technology transfers that result in productivity gains. However, part of the productivity gains associated with M&As tend to be a consequence of employment rationalization.

40% in 2005 to 58% in 2008, while natural resources, which accounted for 30% in 2005, declined to 12% in 2008. The recent dynamism of the IT and software sector in Argentina is also worth highlighting as the presence of leading global companies in this sector has continued to increase in recent years.[365]

In terms of the geographical distribution of the IFDI stock, Europe remained the main source for FDI in Argentina, followed by North America and South America. The top five investors measured by the value of their FDI stock in Argentina in 2008 were Spain, the United States, the Netherlands, Brazil, and Chile. In terms of flows, Spain led most years, but was surpassed by Brazil for the first time in 2008 (annex table 4).

The importance of Brazil as a home country for FDI in Argentina is a relatively new phenomenon. The upward trend of Brazilian investments since 2002 is a consequence of a combination of four factors: first, opportunities brought about by the recovery and rapid expansion of the Argentine economy following the 2001-2002 crisis; second, Brazil's economic growth combined with the financial support provided by BNDES[366] for the internationalization of its firms; third, the fact that top-tier Argentine companies were, and in some cases still are, relatively undervalued, creating an acquisition opportunity for Brazilian companies, underscored by the relative strength of the Brazilian currency *vis-à-vis* the Argentine peso. Finally, the fourth factor was the regional integration and the close partnership between the two countries, institutionalized by MERCOSUR, which played a key role in making Argentina a natural first step in the internationalization process of Brazilian companies. Brazil's greater share of FDI reflects a broader trend in which capital from developing countries has a growing role in overall FDI in Argentina.

The profitability of foreign affiliates in Argentina rose considerably in recent years. Earnings as a percentage of the FDI stock reached 9.1% on average between 2004 and 2008, compared to 6.1% on average between 1992 and 2000. A national survey of the 500 largest non-financial companies in Argentina also revealed that gross margins (profits/sales) were considerably higher for foreign affiliates (15.3%) than for domestic companies (7.0%).[367]

In sum, FDI's good performance over the past years was driven by three main factors: fast economic growth, high levels of profitability and a favorable international context which prevailed until the onset of the global financial and economic crisis in the second half of 2008.

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[365] Recent investments in the IT and software sector include: Google, Microsoft, Symantec, IBM, Intel, Sap Motorola, NEC, Sabre, and Oracle.
[366] Brazilian Development Bank.
[367] National Bureau of Statistics and Census (INDEC), *Survey of Big Companies in Argentina* (Buenos Aires: Ministry of Economy and Public Finance, February 2009). Data correspond to 2007, last available year.

The corporate players

An estimated 1,800 foreign affiliates operate today in Argentina.[368] MNEs are active in a wide array of sectors and industries. Around 330 of the 500 largest non-financial companies (national and international) in the country were foreign affiliates and accounted for around 405,000 jobs and US$ 121 billion in sales in 2007. Foreign affiliates also produced 84% of gross value added and 90% of total profits of the 500 companies that year.[369] These figures are evidence of the large presence and successful operation of MNEs in the Argentine economy, most of them doing business in the country with a long-term time horizon.

The presence of MNEs in Argentina is particularly relevant in such sectors as oil and gas, telecommunications, the automotive industry, and agribusiness, as reflected in the list of the 20 main foreign affiliates in the country (annex table 5). A further analysis of the affiliates of the top 20 MNEs in Argentina also reveals a high degree of concentration. In 2008, assets in Argentina held by these foreign affiliates represented more than half (53%) of the total FDI stock in the country. Moreover, their combined sales accounted for around 37% of total sales made by the 330 largest non-financial foreign affiliates.[370]

The main greenfield projects announced by MNEs in the past three years are also geared toward the oil and gas and telecommunications sectors, and include large mining projects as well (annex table 7). Changes in ownership were led by metal and steel, food and beverages, agriculture, and cement. The main M&A deals included the sale of a significant share of the steel company Acindar to Arcelor Mittal, the purchase of Grupo Guerrero by the Mexican beverage bottling company Embotelladoras Arca, and the acquisition of a 50% share of the cement plant Cementos Avellaneda by Votorantim L.E., consolidating Brazil's predominance in the sector in Argentina (annex table 6).

Effects of the current global crisis

Until the third quarter of 2008, FDI kept rising in Argentina, reflecting the delayed impact of the international financial and economic crisis. However, beginning in the fourth quarter of 2008, and as a result of the global downturn, a lack of financing and the postponement of investment projects in light of growing international uncertainty, this positive trend was reversed. In 2009, FDI inflows were 50% lower than in 2008, a decline consistent with the contraction registered in Latin America and the Caribbean (-41%) and worldwide (-39%).[371] The contraction was the result of a decrease in equity contributions, a standstill in M&As and a reversal in intercompany debt flows. MNEs operating locally followed a pattern observed elsewhere whereby head offices recalled debt and increased profit remittances from their foreign affiliates as a result of the global economic crisis.

[368] UNCTAD, *World Investment Report 2009*, op. cit.
[369] National Bureau of Statistics and Census (INDEC), *Survey of Big Companies in Argentina* (Buenos Aires: Ministry of Economy and Public Finance, February 2009). Data correspond to 2007, last available year.
[370] National Bureau of Statistics and Census (INDEC), *Survey of Big Companies in Argentina* (Buenos Aires: Ministry of Economy and Public Finance, February 2009). Data correspond to 2007, last available year. The data correspond to the year 2007, the last available year.
[371] As an additional reference, FDI to the two largest economies in Latin America, Brazil and Mexico, dropped 50% and 41%, respectively, in 2009. Source: UNCTAD, *Global Investment Trends Monitor*, No. 2 (New York and Geneva: United Nations, January 2010).

Notwithstanding the effects of the global crisis, and the slow recovery expected for world investment flows, domestic FDI prospects remain positive in the medium term. Argentina could benefit from projected global trends: increased demand for food products and clean and renewable energies, a growing decentralization of global value chains with opportunities to integrate in higher value added segments, and a growing localization of R&D activities in emerging markets, among others. The country's competitive and comparative advantages are well aligned with these emerging structural trends, creating potential investment opportunities. Addressing challenges at the macroeconomic and microeconomic levels would better position Argentina to capitalize fully on these opportunities.

The policy scene

The Argentine Constitution guarantees equal treatment and rights for local and foreign investors. The Foreign Investments Act[372] defines the legal framework for foreign investments and establishes that foreign investors may remit abroad profits; repatriate their investments; make use of any of the legal forms of incorporation foreseen by Argentine legislation; and use domestic credits and loans with the same rights and under the same conditions as domestic companies.

In terms of international treaties, Argentina has signed 58 BITs, 55 of which are in effect. The 2001 economic and financial crisis, the most severe in the country's history, had negative effects on domestic and foreign companies alike.[373] Given the impact of the crisis, some foreign investors chose to file 44 claims against Argentina at the International Centre for Settlement of Investment Disputes.[374] To date, two claims have concluded the annulment process; four awards have been rendered pending annulment proceedings; 13 have been discontinued (concluded); 11 claims have been suspended; and 14 claims are pending.[375]

Argentina has argued that the "essential security" clause contemplated within the signed BITs applies in the context of the 2001 crisis. In support of this stance, UNCTAD stated in reference to the case of Argentina that "several arbitration awards confirmed that the scope of 'essential security' exceptions is not necessarily limited to military threats, but may also cover emergency measures taken in times of major economic crises. Tribunals disagreed, however, on the degree of severity of an economic crisis that would justify invocation of the national security exception."[376] Some

[372] Foreign Investments Act No. 21382, enacted in 1976 and regulated by decree Executive Order 1853/1993.
[373] For more detailed information on the 2001 economic and financial crisis, see B. Nofal, *"Las causas de la crisis de la Argentina," Boletín Informativo Techint* (310) (May-August 2002); J. Stiglitz, "Argentina, shortchanged. Why the nation that followed the rules fell to pieces," *Washington Post*, May 12, 2002; R Hausmann and A. Velasco, *"Hard money's soft underbelly: understanding the Argentine crisis," in* D. Rodrik and S. Collins, eds., *Brookings Trade Forum: 2002* (Washington, DC: Brookings Institution Press, 2003).
[374] Eight additional cases have been filed for arbitration under the rules of the United Nations Commission on International Trade Law while three other cases have been filed for arbitration under the rules of the International Chamber of Commerce (ICC) International Court of Arbitration.
[375] Information based on official data provided by *Procuracion del Tesoro de la Nacion*, consistent with data available at International Centre for Settlement of Investment Disputes.

[376] UNCTAD, *World Investment Report 2009*, op. cit, p. 35.

international agreements signed in subsequent years reflect Argentina's position.[377] The events that have unfolded during the recent international financial and economic crisis are likely to trigger additional discussions on the conditions under which countries can adopt certain measures in emergency situations.

Conclusions and Outlook

Argentina benefitted from the global wave of FDI between 2004 and 2008. The annual growth rate of FDI inflows to the country was twice the rate worldwide for the same period. As a result, Argentina's share of world FDI inflows doubled between 2003 and 2008. Primarily comprised of equity contributions and reinvested earnings (with M&As representing a low percentage), the improved quality of FDI in the country contributed to the expansion of the economy's productive capacity.

Following the sharp decline registered in 2009 as a consequence of the global crisis, FDI inflows are expected gradually to recover in 2010 as growth in the world, and in Argentina, resumes.[378] The evolution of inflows will depend on two main factors. On one hand, how Argentina faces some pending challenges, such as the full normalization of access to international financing, a process initiated in 2005; and, on the other, how the country takes advantage of an auspicious global scenario in which demand patterns match Argentina's competitive and comparative advantages.
Looking ahead, with the lessons learned from the international crisis in mind, the quality of FDI—and not only its quantity—is key to ensure long-term economic benefits. Policies aimed at the development of FDI should encourage long-term projects that integrate locally with global value chains and promote innovation and high environmental and social standards. Attracting sustainable and innovative investments needs to be at the center of Argentina's FDI policy strategy in the new global scenario.

Additional readings

Bezchinsky, G., M. Dinenzon, L. Giussani, O. Caino, B. López, and S. Amiel, "Inversión extranjera directa en la Argentina. Crisis, reestructuración y nuevas tendencias después de la convertibilidad," in B. Kossacoff, ed., *Crisis, Recuperación y Nuevos Dilemas: La Economía Argentina 2002-2007* (Buenos Aires: ECLAC, 2007), pp. 149-185.

Bianco, C., P. Moldovan and F. Porta, *La Internacionalización de las Empresas Brasileñas en Argentina* (Buenos Aires: ECLAC, 2008).

[377] For example, the US-Peru Free Trade Promotion Agreement, signed in 2006, establishes in Article 22.2: Essential Security that "Nothing in this Agreement shall be construed: […] (b) to preclude a Party from applying measures that it considers necessary for the fulfillment of its obligations with respect to the maintenance or restoration of international peace or security, or the protection of its own essential security interests.[2]" and further clarifies within footnote n°2: "For greater certainty, if a Party invokes Article 22.2 in an arbitral proceeding initiated under Chapter Ten (Investment) or Chapter Twenty-One (Dispute Settlement), the tribunal or panel hearing the matter shall find that the exception applies."

[378] Growth projections for Argentina in 2010 are estimated at 4%, in line with growth expected for Latin America and the Caribbean; see ECLAC, *Preliminary Overview of the Economies of Latin America and the Caribbean 2009* (Santiago: United Nations, December 2009).

Lopez, A., and D. Ramos, “Inversión extranjera directa y cadenas de valor en la industria y servicios,” in B. Kosacoff and R. Mercado, eds., *La Argentina Ante la Nueva Internacionalización de la producción: Crisis y oportunidades* (Buenos Aires: UNDP-ECLAC, 2009), pp. 142-215.

ProsperAr 2008, *2008 Investment Report* (Buenos Aires: ProsperAr, 2008).

Statistical annex

Annex table 1. Argentina: inward FDI stock, 2000-2008 (US$ billion)

Economy	**2000**	**2001**	**2002**	**2003**	**2004**	**2005**	**2006**	**2007**	**2008**
Argentina [a]	68	80	43	48	56	62	68	77	80
Memorandum: comparator countries									
Mexico	97	140	164	181	204	226	246	273	295
Brazil	122	122	101	133	161	181	221	310	288
Chile	46	44	42	54	61	74	80	100	101
Colombia	11	15	18	21	25	37	45	56	67
Peru	11	12	13	13	13	16	21	27	30

Source: ProsperAr, based on data from the National Office for International Statistics, at the National Institute of Statistics and Census (INDEC); Argentina's Central Bank (BCRA); and UNCTAD.

[a] Data from 2000 to 2003 cited from INDEC reports. Data from 2004 to 2008 cited from BCRA reports. There was a change in the series in 2001 because of methodological improvements. The abrupt change in stock between 2001 and 2002 is due to the end of the Convertibility Law (1:1 Argentine peso-US dollar parity) and the subsequent devaluation of the Argentine peso.

Annex table 2. Argentina: inward FDI flows, 2000-2009 (US$ million)

Item	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009 [a]
Argentina	**10,418**	**2,166**	**2,149**	**1,652**	**4,125**	**5,265**	**5,537**	**6,473**	**9,726**	**4,895**
Reinvested earnings	261	-3,306	-924	-808	71	1,156	3,108	2,050	396	3,090
Equity contributions	2,793	3,650	4,516	3,011	2,967	3,813	1,939	2,297	3,839	2,056
Intercompany debt	1,088	1,000	-2,992	-515	1,029	-481	263	1,846	4,777	-251
Changes in ownership	6,276	821	1,549	-36	59	777	227	280	714	0
Memorandum: comparator countries										
Brazil	32,779	22,457	16,590	10,144	18,146	15,066	18,822	34,585	45,058	22,800
Chile	4,860	4,200	2,550	4,307	7,173	6,984	7,298	12,577	16,787	12,900
Colombia	2,436	2,542	2,134	1,720	3,016	10,252	6,656	9,049	10,564	8,600
Peru	810	1,144	2,156	1,335	1,599	2,579	3,467	5,491	4,808	6,200

Source: ProsperAr, based on data from the National Office for International Statistics, INDEC, and UNCTAD.

[a] Preliminary data based on INDEC and UNCTAD.

Annex table 3. Argentina: sectoral distribution of inward FDI stock, 2000-2008 [a] (US$ million)

Sector / industry	2000	2001	2002	2003	2004	2005	2006	2007	2008
Total	**67,601**	**79,504**	**43,146**	**48,298**	**55,731**	**61,920**	**68,219**	**76,778**	**79,902**
Natural resources	**17,657**	**19,042**	**12,105**	**13,372**	**18,918**	**21,781**	**23,674**	**26,607**	**26,097**
Petroleum	16,888	18,104	11,749	12,951	15,392	17,161	17,919	19,907	18,031
Mining	769	938	356	421	1,252	1,895	2,750	2,978	3,866
Agriculture, forestry and fishing	...	...	...	...	2,274	2,724	3,005	3,722	4,200
Manufacturing	**19,919**	**22,562**	**13,721**	**14,818**	**19,865**	**21,139**	**23,214**	**26,412**	**29,441**
Chemicals, rubber and plastics	5,740	7,340	4,230	4,638	6,412	6,500	6,563	7,360	7,768
Food products, beverages and tobacco products	5,805	6,751	3,958	3,904	3,342	3,482	3,433	3,755	4,243
Basic metals and fabricated metal products	1,402	1,392	1,115	1,785	2,445	2,639	3,687	4,036	4,655
Machinery and equipment	1,280	1,329	845	585	1,142	1,249	1,422	1,792	1,986
Motor vehicles and transport equipment	3,162	3,146	2,042	2,207	...	...	...	...	...
Automotives	...	...	...	...	2,892	3,356	4,055	4,945	6,227
Paper and paper products	1,517	1,460	832	913	...	...	...	...	...
Paper, publishing and printing	...	...	...	...	928	1,028	1,037	1,101	1,086
Cement and ceramics	750	839	524	618	...	...	...	...	...
Textiles and leather products	262	305	175	168	...	...	...	...	...
Other manufacturing	...	...	...	...	2,704	2,886	3,017	3,423	3,477
Financial services	**7,206**	**7,012**	**2,610**	**2,934**	**2,307**	**2,425**	**2,723**	**3,087**	**3,392**
Other services	**22,819**	**30,888**	**14,710**	**17,173**	**14,639**	**16,576**	**18,608**	**20,672**	**20,972**
Electricity, gas and water supply	7,951	9,043	3,969	4,876	4,989	5,039	4,932	4,977	4,345
Wholesale and retail trade	2,938	5,253	3,086	2,958	2,092	2,266	2,632	3,092	3,423
Communications and transport	6,997	9,473	4,785	4,349	...	...	...	...	...
Communications	...	...	...	...	2,672	3,518	4,267	4,416	4,390
Other services	4,933	7,119	2,870	4,991	4,887	5,752	6,777	8,187	8,814

Source: ProsperAr, based on data from the National Office for International Statistics, INDEC, and Argentina's Central Bank (BCRA).

[a] Data from 2000 to 2003 cited from INDEC reports. Data from 2004 to 2008 cited from BCRA reports. Industry classifications change in some cases due to the combination of two different data sources.

Annex table 4. Argentina: geographical distribution of inward FDI stock, 2000-2008 [a]
(US$ million)

	2000	2001	2002	2003	2004	2005	2006	2007	2008
World	**67,601**	**79,504**	**43,146**	**48,298**	**55,731**	**61,920**	**68,219**	**76,778**	**79,902**
Europe	**36,873**	**44,029**	**23,714**	**26,234**	**32,491**	**36,372**	**39,783**	**44,432**	**44,173**
Spain	16,612	18,413	10,063	11,786	16,901	18,986	21,413	23,259	22,991
Netherlands	5,470	6,426	3,151	3,230	4,115	5,162	5,090	5,662	6,421
France	4,971	6,734	2,685	2,888	2,564	2,597	2,213	2,607	2,400
United Kingdom	2,359	2,239	1,543	1,619	1,349	1,335	1,502	1,451	1,588
Germany	2,090	1,876	1,166	1,472	1,712	1,679	1,702	2,150	2,425
Italy	2,729	3,107	1,215	1,248	1,063	1,211	1,214	1,407	1,295
Other Europe	2,642	5,234	3,891	3,991	4,787	5,401	6,648	7,895	7,053
North America	**17,641**	**21,777**	**12,321**	**12,232**	**11,869**	**13,501**	**14,307**	**16,522**	**17,219**
United States	15,864	19,392	10,888	10,858	10,248	11,794	12,151	13,482	13,622
Canada	...	...	...	...	1,280	1,385	1,600	1,946	2,190
Mexico	...	...	...	...	341	321	555	1,094	1,407
Other North America [b]	1,777	2,385	1,433	1,374	...	...	...	...	...
South America	**5,113**	**6,638**	**4,899**	**5,391**	**5,264**	**6,289**	**7,495**	**9,152**	**11,357**
Chile	3,445	3,616	2,090	2,118	1,878	2,598	2,974	3,493	4,181
Brazil	...	...	...	...	1,727	2,374	2,661	3,567	4,786
Uruguay	...	...	...	...	1,602	1,251	1,767	1,869	1,951
Venezuela	...	...	...	...	23	29	48	113	226
Other South America	1,667	3,022	2,809	3,273	35	39	45	109	213
Central America and Caribbean	**6,388**	**5,014**	**1,267**	**3,607**	**5,209**	**4,892**	**5,617**	**5,426**	**5,773**
Other regions	**1,586**	**2,046**	**945**	**833**	**897**	**866**	**1,017**	**1,247**	**1,379**
Africa	...	...	...	...	11	15	20	23	24
Asia and Oceania	...	...	...	...	710	849	986	1,210	1,332
Australia	...	...	...	...	356	445	573	584	579
Japan	...	...	...	...	132	169	165	252	250
China	...	...	...	...	13	11	44	118	157
Other Asia and Oceania	...	...	...	...	209	225	204	257	347
Other	...	...	...	...	176	2	11	14	24

Source: ProsperAr, based on data from the National Office for International Statistics, INDEC, and Argentina's Central Bank (BCRA).

[a] Data from 2000 to 2003 cited from INDEC reports. Data from 2004 to 2008 cited from BCRA reports. Country classifications change in some cases due to the combination of two different data sources. [b] Data for 2000-2003 correspond to Canada and Mexico together since they are not available for each individual country. For 2004-2008, this category does not apply since individual country data is available.

Annex table 5. Argentina: principal foreign affiliates, ranked by total foreign assets, 2006-2008 [a] (US$ million)

Rank	Name	Industry	Country of origin	Foreign assets [b]			Net sales [b]		
				2006	2007	2008	2006	2007	2008
1	Repsol YPF	Oil and gas	Spain	11,419	12,017	10,949	7,725	8,743	10,170
2	Petrobras Energia	Oil and gas	Brazil	5,079	5,268	5,183	2,439	2,741	3,054
3	Pan American Energy	Oil and gas	United Kingdom	2,335	2,764	3,390	1,743	1,778	1,927
4	Telefonica S.A.	Telecommunications	Spain	4,025	4,219	3,713	2,891	3,333	3,956
5	Telecom Argentina S.A.[c]	Telecommunications	Italy	3,090	3,246	3,230	2,407	2,938	3,425
6	Cargill S.A.	Food and beverage	United States	1,509	1,465	2,101	4,046	3,187	6,808
7	Claro Argentina	Telecommunications	Mexico	1,489	1,731	1,880	1,527	1,985	2,410
8	Shell C.A.P.S.A.	Oil and gas	Netherlands	1,138	1,205	1,257	1,690	1,950	2,177
9	Volkswagen Argentina	Automotive	France	757	828	1,252	1,749	2,257	2,638
10	Peugeot Argentina	Automotive	Germany	840	972	1,169	1,252	1,732	2,135
11	Bunge Argentina S.A.	Food and beverage	United States	570	1,089	1,145	1,836	2,458	3,083
12	Acindar-Arcelor Mittal Group	Metal and steel	Belgium	967	1,083	1,056	891	982	1,245
13	Minera Alumbrera Limited	Mining	Switzerland	1,378	1,033	953	1,584	1,565	1,234
14	Ford Argentina	Automotive	United States	789	856	872	1,561	1,877	2,112
15	Cerveceria y Malteria Quilmes S.A.I.C.A. y G.	Food and beverage	Brazil/ Belgium	801	841	885	721	861	1,061
16	Nidera S.A.	Food and beverage	Netherlands	502	663	764	846	1,186	1,644
17	General Motors	Automotive	United States	426	568	622	1,019	1,614	1,800
18	Toyota Argentina S.A.	Automotive	Japan	439	549	608	1,009	1,504	1,700
19	Fiat Auto Argentina	Automotive	Italy	244	342	524	560	771	1,266
20	Wal Mart Argentina S.R.L.	Retail	United States	313	421	491	426	625	948

Source: Investment Observatory, ProsperAr.

[a] Excludes financial companies.

[b] The following Argentine Peso/USD exchange rates, based on the rates of the International Monetary Fund (http://www.imf.org) at the end of each year, were used throughout for asset values of companies whose financial statements closing date is at the end of each year (the majority): 3.45 (2008); 3.15 (2007); 3.06 (2006). For sales values, the following annual average exchange rates, based on the rates of Argentina's Central Bank, were used throughout for these companies: 3.16 (2008); 3.11 (2007); 3.07 (2006). For those companies whose financial statements closing dates differ from December 31, exchange rates at the end of their accounting year were used for asset values and average exchange rates during their accounting year were used for sales values.

[c] 50% Telecom's shares are owned by Argentine Werthein Group while the remaining 50% of the shares are owned by Telecom Italia.

Annex table 6. Argentina: main M&A deals, by inward investing firm, ranked by value, 2007-2009[a] (US$ million)

Year	Acquiring company	Target company	Target industry	Home country	Announced transaction value (US$ million)	Shares acquired (%)	State of transaction
2009	Alternative Investment Corporation	El Tejar	Agriculture	Europe/ United States	150	17	In process
2009	Votorantim L.E	Cementos Avellaneda	Cement	Brazil	200	50	In process
2008	Marfrig Group	Mirab S.A.	Food and beverage	Brazil	36	100	Completed
2008	Baldwin Enterprises	Cresud	Agriculture	United States	45	9	Completed
2008	Lupatech/Axxon	Aspro	Oil and gas	Brazil	49	100	Completed
2008	Alicorp	The Value Brands Argentina	Chemicals	Peru	66	100	Completed
2008	Cargill Inc.	Friar S.A.	Food and beverage	United States	70	100	Completed
2008	Embotelladora Arca	Yege Argentina	Food and beverage	Mexico	80	100	Completed
2008	Fundo de Investimento em Participacoes (PCP)	Los Grobo	Agriculture	Brazil	100	25	Completed
2008	PSAI-IPH	Exlogan ITL	Transport	Singapur	100	80	Completed
2008	Navios Maritime Holding	Horamar	Transport	Greece	112	64	Completed
2008	Embotelladora Arca	Grupo Guerrero	Food and beverage	Mexico	250	100	Completed
2008	Arcelor Mittal Group	Acindar	Metal and steel	Belgium	542	36	Completed
2007	Arcelor Mittal Group	Compañia Naviera Horamar S.A.	Metal and steel	United Kingdom	50	100	Completed
2007	Grupo Televisa S.A.	Editorial Atlantida	Publishing	Mexico	79	100	Completed
2007	Marfrig Group	Quickfood	Food and beverage	Brazil	141	71	Completed

Source: Investment Observatory, ProsperAr.

[a] Excludes financial companies.

Annex table 7. Argentina: main greenfield projects, by inward investing firm, 2007-2009 [a] (US$ million)

Year	Investing company	Home country	Sector	Announced value (US$ million)
2009	Libra Holdings	United States	Hotels and restaurants	475
2009	Occidental Argentina Exploration & Production, Inc	United States	Oil and gas	342
2009	Wal Mart	United States	Retail	280
2009	Telefonica S.A.	Spain	Telecommunications	433
2009	Grupo Beltrame	Italy	Metal and steel	400
2009	Barrick Gold	Canada	Mining	1,500
2009	Yamana Gold Inc.	Canada	Mining	652
2009	Vale do Rio Doce	Brazil	Mining	2,500
2009	Casino Club S.A.	Argentina-Spain	Media and entertainment	270
2008	Quantum Fund	United States	Agriculture	511
2008	Jumeirah International	United Arab Emirates	Hotels and restaurants	680
2008	British Petroleum/Bridas	United Kingdom	Oil and gas	1,250
2008	Repsol YPF	Spain	Oil and gas	11,700
2008	Telefonica S.A.	Spain	Telecommunications	875
2008	Grupo Mall	Spain	Hotels and restaurants	600
2008	Telecom Italia	Italy	Telecommunications	682
2008	Fiat Automobiles	Italy	Automotive	307
2008	Petroleos Brasileños S.A.	Brazil	Oil and gas	2,400
2008	Gerdau	Brazil	Metal and steel	310
2007	Agco Allis	United States	Machinery and equipment	625
2007	Telefonica S.A.	Spain	Telecommunications	1,069
2007	Xstrata Plc	Chile	Mining	950
2007	Cencosud	Chile	Retail	700
2007	El Plomo	Chile	Construction and real estate	600

Source: Investment Observatory, ProsperAr.

[a] Excludes financial companies. Announcements may correspond to investments to be implemented in a period of up to five years.

Chapter 15 – Brazil

The growth of Brazil's direct investment abroad and the challenges it faces, 2009

Luís Afonso Lima and Octavio de Barros

The internationalization of Brazilian companies is a relatively recent phenomenon. From 2000 to 2003, OFDI averaged USD 0.7 billion a year. Over the four-year period 2004–2008, this average jumped to nearly USD 14 billion. In 2008, when global FDI inflows were estimated to have fallen by 15%, OFDI from Brazil almost tripled, increasing from just over USD 7 billion in 2007 to nearly USD 21 billion in 2008 (annex figure 1 below). Central Bank data put the current stock of Brazilian OFDI at USD 104 billion, an increase of 89% over 2003. Caution is in order about these figures, however, as in Brazilian outflows it is difficult to separate authentic FDI from purely financial investment under the guise of FDI. According to the most recent data, 887 Brazilian companies have invested abroad.

Along with other emerging economies, Brazil is suffering from the effects of the global financial crisis. The OECD forecasts that M&A spending from Brazil, Russia, India, China, South Africa, and Indonesia will be reduced by 85% in 2009, in comparison to 2008.[379] This matches the partial performance captured in the data already released: in the period January-May 2009, Brazilian OFDI shrank by 87% in comparison to the same period in 2008, from somewhat under USD 8 billion to somewhat under USD 1 billion. If this trend persists, OFDI from Brazil will be no higher than USD 4 billion in 2009, as against USD 21 billion in 2008.

Notwithstanding its remarkable recent growth, OFDI from Brazil needs additional support through sound public policies. As we indicate below, this is one lesson that comes home to those who observe Brazilian outward investors closely.

Characteristics of OFDI from Brazil

Despite its relative novelty, the internationalization of Brazilian companies has achieved a wide geographic spread. Brazilian OFDI can today be found in 78 countries. Admittedly, some destinations matter more than others. Putting aside investment in tax havens, which accounts for 67% of the total, by 2007, half the stock of OFDI from Brazil had gone to Denmark, the United States and Spain, with developed economies together accounting for 75% (annex figure 2). Among emerging markets, Argentina leads, followed by Uruguay. When it comes to sectoral distribution (and including tax havens), Central Bank data indicate that 54% of OFDI stock from Brazil had gone into financial services by 2007 (annex table 1). Given the distortion introduced by the inclusion of flows to tax havens, however, it is difficult to arrive at a realistic picture of the final destination of these flows, be it geographical or otherwise.

The internationalization of Brazilian companies is dominated by the private sector, although SOEs also play a role. Petrobras, for example, has expanded its overseas activities to 15

[379] *OECD Investment News*, June 2009, Issue 10.

countries in three continents. In Latin America, the company has energetically pursued a strategy of regional integration in natural gas.

Why are more and more Brazilian companies going abroad? The most frequently cited reason is that they are following clients into international markets. But there are many other reasons as well, such as defending their competitive position, monitoring the competition in international markets, meeting international demand and reducing their dependence on a single (domestic) market. Many Brazilian companies are also interested in natural resources. Yet others are looking for lower costs, better infrastructure and more attractive fiscal incentives. Broadly speaking, Brazilian outward investors are in search of three things: markets, natural resources and investment climates superior to the one they find at home.

In keeping with the usual pattern of early internationalization, one of the main ways in which OFDI from Brazil begins is by setting up offices for overseas sales. This is especially common in the consumer goods industry and the services sector. However, the overseas manufacture of goods and provision of services account for a substantial share of OFDI as well. According to a SOBEET survey[380] of 211 companies, which had a 30% response rate, the OFDI of 38% of the companies consisted of sales offices and only 23% had productive units abroad. However, the latter accounted for a much larger portion of outward investment than the former. Brazilian overseas units also tend to expand into new functions, such as manufacturing goods and providing services, even if not initially set up to do so. It is interesting too to note how other, more sophisticated, functions such as logistics and R&D, already figure among their overseas activities.

Despite the speed and scale of the Brazilian internationalization process since 2004, there are some surprises when it comes to the sources of funding. Most Brazilian companies investing abroad indicate their own capital as the main source of funding. However, many of those that do *not* mention their own capital also do not mention other Brazilian sources. This suggests that access to funds from BNDES (the Brazilian Development Bank) or from domestic banks is still limited. If this were remedied, the process of internationalization might well become more dynamic. But the lack of Brazilian financing is not the only internal barrier to the internationalization of Brazilian companies. Many Brazilian companies also mention the lack of personnel with the necessary skills and the knowledge of potential markets.

Among external obstacles, the tax burden is pre-eminent. According to SOBEET's 2008 survey of Brazilian multinationals, taxation – and especially the prospect of double taxation – is a major problem for internationalization. Brazil has signed only 12 double taxation treaties in the past 10 years. As a matter of fact, the lack of double taxation treaties is a major concern for Brazilian multinationals.

Conclusion: The need for public policies to remove obstacles for Brazilian OFDI

The internationalization of Brazilian companies, like the internationalization of their counterparts in other emerging markets, is not a flash in the pan. And this internationalization is just beginning. Among the known benefits of OFDI is the fact that it stimulates exports.[381] Another is the improved competitiveness of Brazilian enterprises. Given this, it is important

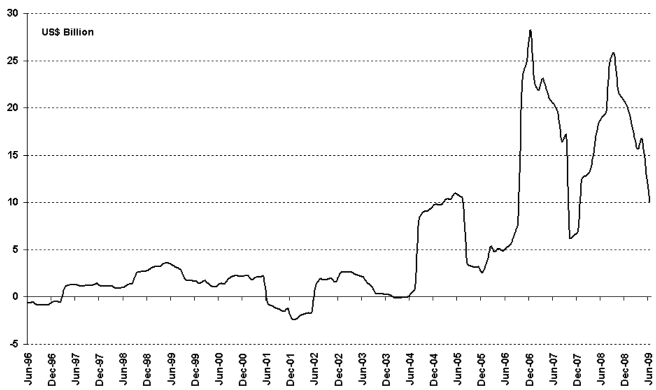
[380] *Carta Sobeet nº. 46*, "Brazilian transnational companies: survey results", November 2008.
[381] See Glauco Arbix, Mário Sérgio Salemo and João Alberto De Negri, *Inovação, via internacionalização, faz bem para as exportações brasileiras* (Brasília: Ipea, 2004). (Texto para Discussão, n. 1.023).

that the Government of Brazil rethink its policies and, in particular, undertake an overhaul of those policies that inhibit Brazilian OFDI.

One group of policies that need rethinking is policies on international taxation. Another group concerns bilateral treaties to protect and promote investment. Perhaps the most important kind of policy that needs reform, however, relates to financing. Despite the fact that BNDES does have specific credit lines for OFDI, a greater availability of funds would be helpful to companies considering cross-border investment, especially at a time when the credit crunch that followed the financial crisis has become near universal.

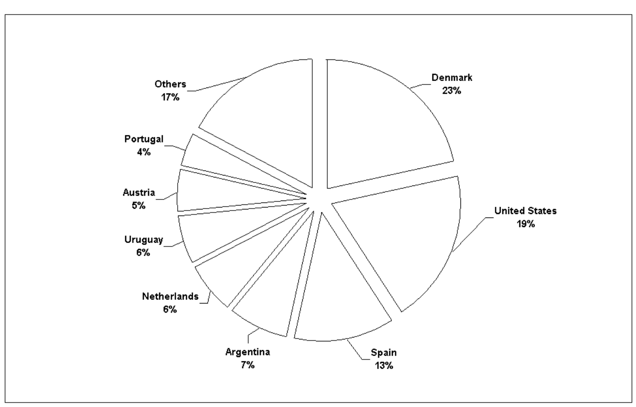
ANNEX

Annex figure 1: Outward foreign direct investment, June 1996–June 2009



Source: Central Bank of Brazil.

Annex figure 2: Destinations of Brazilian OFDI stock as of 2007, excluding tax havens.



Source: Central Bank of Brazil.

Annex table 1: Sectoral distribution of Brazilian OFDI stock as of 2007, as percentage of total (including tax havens)

Activities related to financial services	53.8
Administrative support	10.5
Other technical activities	8.8
Consulting	5.9
Auxiliary financial services	3.5
Whosale activities	3.4
Oil and natural gas	1.9
Others	12.3

Source: Central Bank of Brazil.

Chapter 16 – China

While global FDI falls, China's outward FDI doubles

Ken Davies

In 2008 global FDI fell by around 20%, while outward FDI from China nearly doubled. This disparity is likely to continue in 2009 and 2010 as China invests even more overseas. What is driving this continuing surge in China's outward FDI?

China's FDI outflows took off in the 2000s as a result of the government's adoption and promotion of a "go global" policy aimed at establishing the country's national champions as international players. Having averaged only US$453 million a year in 1982-1989 and US$2.3 billion in 1990-1999, they rose to US$5.5 billion in 2004, US$12.3 billion in 2005, US$17.6 billion in 2006 and US$24.8 billion in 2007.[382] Preliminary figures for 2008 show a rise to US$40.7 billion. **If financial FDI (not counted before 2006) is included, the 2008 total was US$52.2 billion, nearly double the US$26.5 billion in 2007.**

Anecdotal evidence suggests that China's outward FDI growth continued to accelerate in early 2009. China's direct investments in Australia alone reportedly rose from US$1.4 billion in the first quarter of 2008 to US$13 billion in the same period this year. If that trend continues, China's FDI in Australia alone in 2009 will equal its global OFDI in 2008. Chinalco's bid for 18% of Rio Tinto, if successful, would be part of this – at around US$19 billion, this deal is larger than any previous overseas acquisition by a Chinese company. Other large deals in the energy sector are also in view.

Five key drivers of China's OFDI explain this acceleration.[383]

(1) One of the most reported motivations in the international media and in some academic writing is China's need to secure natural resources to fuel rapid growth, though this is actually not the most significant area of China's outward investment, which is service industry. Government backing, including official development assistance (ODA), has been crucial for this resource-seeking investment. (2) While most of China's exports are from foreign-owned enterprises, large domestic firms also export large volumes and need services like shipping and insurance. (3) China's major enterprises are also acquiring global brands (like Lenovo's acquisition of IBM's personal computer business or the SAIC and Nanjing purchase of MG Rover). (4) Large state-owned enterprises (SOEs) losing their monopoly position at home are diversifying internationally. And (5) some enterprises – despite China's ample labour supply – seek to move their labour-intensive operations to cheaper overseas locations like Vietnam and Africa.

The relative strengths of these motivations are reflected in the sectoral and geographical distribution of China's accumulated FDI.

The latest figures published by China's Ministry of Commerce (MOFCOM) in February 2009 show outward FDI cumulated to end-2007 as US$118 billion. The tertiary sector predominated, with over 70% of the total. Manufacturing remained modest at 8%, and construction even lower at 1.4%; so, with other items, the secondary sector contributed around 16% of outward FDI. The remaining 14% is accounted for by mining, quarrying and oil production (13 %) and agriculture, forestry and fisheries (1%).

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[382] *OECD 2008 Investment Policy Review of China: Encouraging Responsible Business Conduct* and China's Ministry of Commerce website www.fdi.gov.cn
[383] Detailed in ibid.

While the sectoral composition tends to fluctuate with "lumpy" greenfield projects or M&A deals, the end-2007 figures give a fair representation. The predominance of services is the result of China's export boom and the extension of China's financial services overseas to utilize the wealth of the Chinese diaspora, learn advanced techniques and diversify earnings sources. Manufacturing OFDI is small, though it may grow faster as domestic production costs rise.

The vast majority of recorded OFDI from China is from large state-owned enterprises (SOEs) (84% of both stocks and flows by end-2005, according to MOFCOM figures[384]), but this appears to be gradually declining and is likely to be an over-estimate because private-sector OFDI is less likely to go through official procedures.

Media reports focus on China's investments in Africa, but the continent that continues to absorb most of China's capital exports is Asia, which accounted for 67% of cumulated Chinese outward FDI to end-2007, with Latin America receiving 21%, Europe 4%, Africa 4%, North America 3% and Oceania 2%. These figures are distorted by the use of tax havens, which obscures actual destinations. China's investment in Latin America, for example, is mainly the 14% of China's OFDI registered as going to the Cayman Islands and the 6% going to the British Virgin Islands. The bulk of China's FDI in Asia goes to Hong Kong, China, which accounted for 58% of outward FDI stock up to end-2007.

Even if the actual figures are higher because of routing via tax havens, China's FDI in the developed world, especially Europe and North America, is disproportionately small considering the high proportion of China's trade with these regions. This probably results more from a lack of readiness to compete with global giants on their home territory than from protectionist pressures, though these have discouraged some large acquisitions.

An unknown proportion of investment in Hong Kong, China and the tax havens consists of "round-tripping" investment to take advantage of tax concessions in China, but this must now be falling since such incentives were abolished at the beginning of 2008 and Hong Kong is therefore unlikely to retain its dominant position. Genuinely outward FDI is therefore likely to be growing even faster than shown by official statistics.

The coastal provinces and municipalities, heavily engaged in international trade, are the main sources of China's OFDI. Guangdong –the largest *recipient* of FDI – provided 20% of total outward FDI in 2008. The second largest source was Zhejiang, with 8% of outward FDI, Shandong following in third place with 8%. This distribution results from several factors: proximity to major seaports and thus overseas markets, strong links to a global diaspora originating from coastal areas, and positive spill-over and demonstration effects of inward FDI in or near the three major coastal economic centres of the Pearl River Delta, the Yangtze Delta and the Bohai Gulf.

How is the crisis affecting China's outward FDI?

As an open economy, China can not escape the effects of the global financial crisis of 2008. The government is countering the downturn with a fiscal stimulus that will limit GDP deceleration, and credit has actually expanded. The OECD forecasts 6.3% GDP growth in 2009 and 8.5% in 2010.

China's resource needs will thus continue to increase, so it is seeking to secure reliable supplies by doing deals with producers. Such deals made in the first quarter of 2009 already reportedly exceed China's record FDI outflow in 2008.

With US$1.9 trillion in foreign-exchange reserves, a current-account surplus forecast by the OECD to rise to 11.7% of GDP in 2009 and no credit crunch, China can afford large investments overseas. Chinese multinationals can snap up companies on the cheap to acquire market share and brands in the

[384] Ibid.

developed world. Unsurprisingly, China is campaigning vociferously against investment protectionism.

China's worries are not unfounded. While there are those who welcome Chinese investment, for example in African countries happy to receive accompanying unconditional aid, there are also widespread suspicions of China's intentions. The predominance of SOEs in China's OFDI has raised fears that such investment may not be governed by normal commercial considerations and may even be an arm of the country's foreign and defense policy.[385]

Other challenges for China's OFDI include raising the efficiency of natural resource exploitation by Chinese companies, coordinating internationally dispersed operations, abandoning the preference for vertical integration of industrial production, and handling the usual aftermath of cross-border M&A, including acquiring sufficient understanding of different management cultures to be able to assimilate and manage foreign companies.

China's OFDI accounts for not much more than 1% of the global total, far below the country's share of world trade. However, this total is rising fast and the country will eventually become a major source of global FDI. Potential recipient countries are beginning to recognize this as they start to offer inducements to attract Chinese MNEs.

[385] Such concerns have also been voiced about the activities of China's sovereign wealth fund, the China Investment Corporation (CIC). CIC and its provincial equivalents have several hundred billion dollars to invest. Following initial investments of dubious profitability – much criticised within China – CIC has become cautious, but experience will embolden it.

Inward FDI and its policy context, 2010

Ken Davies

After opening its doors to foreign trade and investment in 1978, China has become the largest recipient of IFDI among developing and transition economies. The early policy of investment attraction by means of fiscal incentives and special economic zones has been relaxed now that many - though still not all - operating environment deficiencies have been effectively addressed and strong domestic enterprises have developed. While China remains the developing world's favorite investment destination, the government is adopting a more selective approach that may result in slower IFDI growth. Although the global crisis reduced FDI inflows to China, this impact was lower than in many other FDI destinations, and flows have recovered considerably.

Trends and developments

Country level developments

From the establishment of the People's Republic of China in 1949 to the adoption of economic reforms in 1978, there was almost no foreign investment in China. In the 1980s, experiments with joint ventures resulted in a trickle of FDI inflows dominated by the relocation of most of Hong Kong's manufacturing to South China. IFDI first topped US$ 1 billion in 1984 and by 1991 was US$ 4.4 billion.[386] With new urgency given to foreign investment attraction at the beginning of 1992 and the formal establishment of a market economic system in that year, IFDI inflows accelerated rapidly, reaching US$ 11 billion in 1992, continuing up to a plateau of US$ 45 billion per year in 1997-1998. Following a decline to around US$ 40 billion a year in 1999-2000, and after China's accession to the WTO in 2001, FDI inflows have continued to rise steadily.[387]

By 2009, China had accumulated an IFDI stock of US$ 473 billion[388] (annex table 1), well ahead of other large developing and transition economies such as Brazil, with US$ 401 billion, India, with US$ 164 billion, and Russia, with US$ 253 billion (annex table 1). From 2000 to 2009, China received larger FDI inflows than any other developing or transition economy, reaching a record US$ 108 billion in 2008. By comparison, 2008 IFDI flows to Brazil were US$ 45 billion, India US$ 42 billion and Russia US$ 70 billion. In 2009, China's FDI inflows fell to US$ 90 billion as a result of the global economic crisis, while Brazil's fell more sharply to US$ 26 billion, Russia's to US$ 39 billion, and Indian's IFDI to US$ 35 billion (annex table 2). China's FDI inflows recovered strongly in the first eight months of 2010. The relatively good performance of IFDI into China during both the Asian crisis of 1997-1998 and the current crisis reflects international investor perceptions of China as a reliable risk-avoidance haven.

[386] Ministry of Commerce of the People's Republic of China (MOFCOM), Statistics, available at: www.fdi.gov.cn; UNCTAD, FDI/TNC database, available at: http://stats.unctad.org/fdi/.
[387] Ibid.
[388] In 2005, China recalculated its FDI stock figures, which had hitherto been simple additions of annual flows, to bring them more in line with internationally-recognized standards such as the OECD Benchmark Definition of FDI. The result was an approximate halving of the original estimate. Current figures are therefore understood to take account of disinvestments. An explanation of the divergence of Chinese FDI statistics from internationally standard practices is in OECD, *Investment Policy Review of China: Progress and Reform Challenges* (Paris: OECD, 2003).

Partly because of China's WTO commitments to a phased opening up of services to foreign participation during the five years following accession, the share of the tertiary sector in total IFDI flows rose from 31% in 2001 to 52% in 2008, while at the same time the share of the secondary sector declined from 66% to 46% and the always relatively tiny primary sector shrunk from 4% to 2%. While IFDI in manufacturing rose from US$ 31 billion in 2001 to US$ 50 billion in 2008, this represented a decline in the sector's share of total IFDI stock from 66% to 46% (annex table 3). Since 2002, foreigners can participate in China's stock markets as Qualified Foreign Institutional Investors (QFIIs), and as their qualifications have become less strict an increasing number of QFIIs have set up offices in China. Foreign banks have also expanded their operations as these have been increasingly allowed to conduct various banking services, including foreign currency services, for Chinese enterprises since 2002, Chinese yuan services since 2006, and credit card issuance since 2007. At the same time, while the burgeoning domestic market has continued to attract manufacturers, the increase in labor costs, more recently resulting from a wave of strikes in foreign affiliates, has prompted investors to plan new investments in lower-cost economies such as Vietnam and Bangladesh.

China's IFDI appears to be mainly sourced in Asian economies. As of 2008 39% of China's IFDI stock was from Hong Kong (China), 7% from Japan, 5% from Taiwan Province of China, 5% from the Republic of Korea and 4% from Singapore. The United States and the European Union each supplied 7%, of which the major sources were the United Kingdom and Germany (each just under 2% of total IFDI) (annex table 4).

A major obstacle to providing an accurate account of the provenance of China's IFDI is the high proportion circuited through Hong Kong (China), and through Caribbean and other tax havens. Hong Kong's matching IFDI and OFDI figures suggest that much of these flows are pass-through to China,[389] including an element of round-tripping,[390] though it is also important to note substantial investment from Hong Kong (China) in China's burgeoning property sector. As of 2008, Hong Kong (China) accounted for 39% of total IFDI stock, by far the largest share. The British Virgin Islands provided 10%, more than the European Union (7%), Japan (7%) or the United States (7%). The Cayman Islands supplied about the same proportion, 2%, as the United Kingdom.

FDI is concentrated in China's eastern coastal regions, especially in Guangdong and Shanghai.[391] Guangdong's attractiveness as an FDI destination in the 1980s was mainly due to its light regulation, relative remoteness from the capital, Beijing (and therefore from central government control), its proximity to the region's largest port, Hong Kong, that was seeking to shed its manufacturing sector, and the fact that it contained all but one of the country's special economic zones (SEZs). Shanghai, with its strong industrial base and its advantageous location as a major port at the mouth of the Yangtze, also drew large amounts of IFDI. A third major development region in the old industrial heartland of North-East

[389] For example, in 2007, 2008 and 2009, Hong Kong's FDI inflows were US$ 54.3 billion, US$ 59.6 billion and US$ 48.4 billion, respectively, while simultaneous outflows from Hong Kong were US$ 61.1 billion, US$ 50.6 billion and US$ 52.3 billion, see UNCTAD, *World Investment Report 2010: Investing in a Low-Carbon Economy* (New York and Geneva: United Nations, 2010).

[390] "Round-tripping" refers to the practice of setting up special purpose entities in territories outside China, including Hong Kong (China), which is treated as a source of foreign investment by the Chinese authorities to invest in China and so benefit from fiscal incentives offered to foreign investors. Since it is often intended to deceive the authorities, round-tripping is impossible to estimate. The practice may be in decline as a result of the abolition of foreign investment incentives from 2008 and tighter reporting standards for special purpose entities established abroad by Chinese companies since 2006.

[391] Over 80% has gone to the eastern region, see OECD, 2003, op. cit.

coastal China has also developed. Attempts to boost FDI in China's less-developed interior, namely Central and West China, are continuing. But while the physical infrastructure has been greatly improved and lower labor costs are making the hinterland more attractive as wage pressures mount in Guangdong, the developed coastal regions, with their more developed business environments and local markets, remain the largest recipients of IFDI.

The corporate players

Many Fortune Global 500 companies are present in China. The official list of the largest foreign affiliates by sales value in 2008 includes Nokia in second place and GM's Shanghai offshoot in eighth place (annex table 5). The largest foreign affiliate, Hongfujin Precision Industry, is owned by the Foxconn Technology Group of Taiwan Province of China.
Greenfield investment dominated IFDI until the late 1990s for reasons of policy and practicality. Before the reforms in the late 1990s, most firms were state-owned and not available for acquisition, and there was no regulatory provision for foreign M&As. In the first decade of the 21st century, acquisition targets have become available as major enterprises have been divested by the state, the domestic private sector has grown and regulations governing foreign M&As have been enacted.[392] M&As have become a major element of FDI inflows, with many medium-sized acquisitions taking place in the past three years (annex table 6). The rise in cross-border M&As in China has been largely stimulated by the lure of the rapidly expanding domestic consumer market.

Recent large greenfield investments also show a tendency to focus on China's domestic market, but although the country's cost base continues to rise by comparison with regional competitors, large investments in export manufacturing continue to be made. Recent large greenfield investments include automobiles and automobile components (by Daimler, Volkswagen, Yulon, Hyundai and BMW), as China has become the world's largest car market. (annex table 7).

Effects of the current global crisis

China was less seriously affected by the global crisis than its main trading partners. The country's exposure to the US sub-prime market was relatively small[393] and the collapse of consumer confidence in the US had a limited effect on China's exports.[394] In addition, the government initiated an early and rapid-acting stimulus package that helped support continued growth.[395] IFDI flows almost certainly sank not because of any fear of market shrinkage in China, where GDP grew by 9.6%[396] in 2008 and 9.1%[397] in 2009, but because of home-country financing problems. Although no cancellations of large foreign investments in China attributable directly to the crisis have been made public, several foreign affiliates have suffered domestic problems and are likely to suffer as well dampening or delayed planning for overseas expansion.

[392] Details of these regulatory changes are in OECD, *Investment Policy Review of China: Open Policies towards Mergers and Acquisitions* (Paris: OECD, 2006), updated in OECD, *Investment Policy Review of China: Encouraging Responsible Business Conduct* (Paris: OECD, 2008).
[393] Statement by Assistant Governor Yi Gang of the People's Bank of China, *Reuters*, August 28, 2007.
[394] Deutsche Bank Global Markets Research, *Surviving Export Slowdown*, Asia China Macro Strategy series, April 1, 2008.
[395] Economist Intelligence Unit (EIU) special report, *China's Stimulus Package: a Six-Month Report Card* (London: EIU, year?).
[396] The National Bureau of Statistics announced an upward revision from 9% to 9.6% for the 2008 GDP growth figure on December 25, 2009 (available at: www.china.org.cn).
[397] The National Bureau of Statistics announced an upward revision from 8.7% to 9.1% for the 2009 GDP growth figure on July 7, 2010 (*Xinhua News Agency,* available at: http://www.chinaview.cn).

FDI inflows to China decelerated sharply during the course of 2008, from a rate of increase of over 100% year-on-year in January to a decline of 3% in November. IFDI continued to fall over the first seven months of 2009, picking up modestly thereafter. As a result, the annual total shrank from US$ 108 billion in 2008 to US$ 90 billion in 2009. In the first eight months of 2010, FDI inflows were up 18% year-on-year.

The policy scene

Since the 1980s and 1990s, foreign investment has been welcomed by China's government, after three decades of autarky. Unusually for a transition economy, the country's savings rate remained very high throughout the period of reform, with the saving/investment ratio constantly 100% or higher. Yet the lack of effective financial intermediation prevented effective mobilization of savings for investment. Instead, foreign investment filled the financing gap, while bringing along new products, new production processes, modern management techniques, and competition for Chinese firms. Initially, foreign affiliates substituted for the absent domestic private sector.

The government's initial approach was pragmatic and control-oriented. Foreign investment was allowed in a limited number of sectors and a few locations (i.e. SEZs). Two kinds of joint ventures were permitted, as 100% foreign ownership was not allowed. Foreign affiliates had to export their entire output. China lacked the basic elements of an institutional framework for foreign investment, such as adequate physical infrastructure, a mobile labor force, internationally acceptable accounting practices, and the rule of law. In compensation, China offered fiscal incentives to foreign investors in the SEZs, including a five-year tax holiday and a halving of the rate of business income tax.[398]

In the 1990s, as IFDI flow rose and operating conditions improved, China relaxed many restrictions. Wholly-foreign-owned ventures were allowed and became popular. Export requirements were relaxed and sales to domestic consumers allowed. The ban on private car ownership was removed. After the world's largest consumer population became an available market, most of the world's largest MNEs set up operations in China. After these policies spread to other coastal regions in the late 1980s, the government encouraged investors, including foreign ones, to invest in the country's interior, opening up the whole country to foreign investment. Although this policy has resulted in an increase in investment in the country's hinterland, most of this has materialized in the form of government infrastructure construction. Investors, both Chinese and foreign, continue to invest more heavily in the Eastern coastal region.

FDI projects are screened in accordance with laws on each category of foreign ownership, including the 1979 Law on Sino-Foreign Equity Joint Ventures, the 1986 Law on Wholly-Foreign-Owned Enterprises and the 1988 Law on Sino-Foreign Contractual Joint Ventures.[399] In addition to these laws, China operates a catalogue system that combines elements of both open and closed lists. The Catalogues for Guidance of Foreign Investment Projects are four: prohibited, restricted, permitted, and encouraged.[400] The permitted catalogue is not published.

[398] Details of fiscal incentives offered before 2008 are in the tax chapter of OECD, 2003, op. cit.
[399] Ibid.
[400] For details of changes in the catalogues see: OECD, 2003, op. cit.; OECD, 2006, op. cit.; OECD, 2008, op. cit.

The prohibited catalogue is effectively a negative list, detailing sectors in which foreign investment is not permitted. The restricted catalogue contains sectors in which foreign investment is permitted but in which the project examination and approval process may be stricter and take longer; it includes some sectors opened to foreign investment as a result of China's WTO entry. The encouraged catalogue projects are given favorable treatment because they comply with China's development policies, which are focused on promoting high-technology, capital-intensive industry, as well as development in the Central and Western regions. Most recently, the catalogues have emphasized the green objectives of energy conservation, environmental protection and circular economy (i.e. a model of economic development based on the efficient use and recycling of resources).

China has pursued an active investment diplomacy since the early 1980s, having signed 127 BITs by June 1, 2010 and 112 double taxation agreements (DTTs) by June 1, 2009.[401] China is a member of the ASEAN–China Free Trade Area (AFTA), which came into effect on January 1, 2010.

From the mid-2000s, doubts about the desirability of foreign investment have been voiced in China. Fixed investment, the main driver of growth in China, has been increasing at a rate that has aroused fears of overheating. Although FDI has never been more than 15% of total gross fixed capital formation in China, a slowing of IFDI growth has been suggested as one of several levers to restrain breakneck investment growth. Also, several Chinese companies have now developed to the stage where they have an interest in curbing competition from foreign affiliates in their sectors. At the same time, concerns have arisen that the high proportion of output from IFDI might lead to foreign monopoly power in some strategically important sectors, threatening national security. Finally, there have also been some worries that over-dependence on IFDI for economic growth might lead to problems similar to those experienced by Latin America in the 1990s.

As a result, China's government, while rejecting calls to raise barriers against foreign investment, appears to be taking a more selective stance, inviting FDI to plug gaps in the Chinese economy such as high-tech and environmental industries. To satisfy calls from increasingly strong domestic enterprises, the government abolished the fiscal incentives for foreign investment as of 2008, with grandfathering and phasing clauses to ensure existing foreign investments are not disrupted.

Conclusions and Outlook

China's IFDI flows are likely to continue to rise, but less rapidly than the rest of the economy. Government policy, while remaining open to FDI, can afford to become more selective because there is no longer a nationwide absence of financial institutions, basic infrastructure, consumer goods industries, and essential services. While cross-border M&As have been welcomed in the recent past to rescue ailing rustbelt industries, more successful companies may not be so readily available for foreign acquisition. Private companies appear to prefer share issues, namely initial public offerings, to selling out to a foreign investor. Similarly, the government's support for large SOEs encourages such enterprises to be acquirers, both at home and abroad, rather than targets for inbound M&As.

[401] UNCTAD, FDI/TNC database, available at: http://stats.unctad.org.

The Chinese market is expanding rapidly because of the high rate of GDP growth and efforts to rebalance the economy toward private consumption. In the latest UNCTAD survey, market size and market growth are found to be the major factors in China's position as the most favored location for IFDI in 2009-2011.[402] But there are now more and more large Chinese enterprises capable of manufacturing competitive products at prices that foreign investors may find difficult to match as fiscal incentives are phased out. Lower production factor costs in Vietnam, Bangladesh and other developing countries in the region will prompt investors to consider expanding their manufacturing operations in those countries.

Additional readings

Buckley, Peter J., *Foreign Direct Investment, China and the World Economy* (Basingstoke and New York: Palgrave Macmillan, 2010).

Huang, Yasheng, *Selling China: Foreign Direct Investment during the Reform Era* (Cambridge: Cambridge University Press, 2005).

Chantasasawat, Busakorn, K.C. Fung, Hitomi Iizaka and Alan Siu, "Foreign direct investment in China and East Asia". Paper presented at the Third Annual Conference on China Economic Policy Reform, Stanford Center for International Development (2004).

Li, X, Liu, X. and D. Parket, "Foreign direct investment and productivity spillovers in the Chinese manufacturing sector", *Economic Systems*, volume 25, Issue 4 (2001).

Sun, Qian, Wilson Tong and Qiao Yu, "Determinants of foreign direct investment across China", *CREFS Working Paper No*: 99-06 (1999).

Useful websites

Invest in China (maintained by the Ministry of Commerce): http://www.fdi.gov.cn/.

Ministry of Commerce of the People's Republic of China: http://www.mofcom.gov.cn/.

National Bureau of Statistics of China: http://www.stats.gov.cn/.

[402] UNCTAD, *World Investment Prospects Survey 2009-2011* (New York and Geneva: United Nations, 2009).

Statistical annex

Annex table 1. China: inward FDI stock, 2000, 2009 (US$ billion)

Economy	2000	2009
China	193	473
Memorandum: comparator economies		
Brazil	122	401
India	18	164
Russia	32	253
Singapore	111	344

Source: UNCTAD's FDI/TNC database, available at: http://stats.unctad.org/fdi/.

Annex table 2. China: inward FDI flows, 2000-2009 (US$ billion)

Economy	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010[a]
China	41	47	53	54	61	72	69	84	108	90	66
Memorandum: comparator economies											
Brazil	33	23	17	10	18	15	19	35	45	26	17
India	4	6	6	4	6	8	20	25	42	35	13[b]
Russia	3	3	4	8	15	13	30	55	70	39	17
Singapore	17	15	6	12	20	14	28	32	23	17	14[c]

Source: UNCTAD's FDI/TNC database, available at: http://stats.unctad.org/fdi/. MOFCOM press releases at: http://www.fdi.gov.cn; Banco Central do Brasil statistics at: http://www.bcb.gov.br/; Department of Industrial Policy and Promotion, Ministry of Commerce and Industry, Government of India FDI statistics at: http://dipp.nic.in/; Bank of Russia, available at: http://www.cbr.ru/; Monetary Authority of Singapore at: http://www.mas.gov.sg/.
[a] For the first eight months only. [b] For the first seven months only. [c] For the first six months only.

Annex table 3. China: distribution of inward FDI flows, by economic sector and industry, 2000, 2008 (US$ billion and percent of total inflows)

Sector/industry	**2001**	**2008**
Primary	1.7 3.6%	1.8 1.7%
Agriculture	0.9 1.9%	1.2 1.1%
Mining	0.8 1.7%	0.6 0.6%
Secondary	30.9 65.9%	49.9 46.1%
Manufacturing	30.9 65.9%	49.9 46.1%
Tertiary	14.3 30.5%	56.6 52.3%
Utilities	2.3 4.9%	1.7 1.6%
Construction	0.8 1.7%	1.1 1.0%
Real estate	5.1 10.9%	18.6 17.2%
Total	46.9 100.0%	108.3 100.0%

Source: MOFCOM, available at: www.fdi.gov.cn.
Note: The Chinese authorities include "utilities" and "construction" in the secondary sector and the MOFCOM figures do not include all activities; so it is not possible to disaggregate and reconstruct the sectoral statistics entirely from their published tables. See the official definition of sectors from the annual statistical yearbook published by the National Bureau of Statistics. In China economic activities are categorized into the following three strata of industry: (1) "Primary industry" refers to agriculture, forestry, animal husbandry and fishery and services in support of these industries. (2) "Secondary industry" refers to mining and quarrying, manufacturing, production and supply of electricity, water and gas, and construction. (3)"Tertiary industry" refers to all other economic activities not included in the primary or secondary industries.

Annex table 4. China: geographical distribution of inward of FDI stock,[a] 2002, 2008
(US$ billion)

Region/economy	2002	2008
World	448.0	899.1
Developed economies	n.a.	n.a.
Europe	n.a.	n.a.
European Union	**33.9**	**61.6**
Belgium	0.6	1.0
Denmark	0.5	1.3
France	5.5	8.9
Germany	8.0	15.1
Italy	2.2	4.3
Netherlands	4.3	9.3
Spain	0.4	1.5
Sweden	0.8	1.6
United Kingdom	10.7	15.7
North America	**43.2**	**66**
Canada	3.4	6.4
United States	39.9	59.7
Other developed economies	n.a.	n.a.
Australia		
Japan	36.3	65.4
Developing economies	n.a.	n.a.
Africa	n.a.	n.a.
Mauritius	n.a.	7.4
Asia		
Hong Kong, China	204.9	349.6
Macau, China	4.8	1.8
Indonesia	1.1	1.9
Korea, Republic of	15.2	41.9
Malaysia	2.8	4.9
Philippines	1.4	2.5
Singapore	21.5	37.8
Taiwan Province of China	33.1	47.7
Thailand	2.4	3.2
Western Samoa	2.3	12.3
Latin America and Caribbean	n.a.	n.a.
Barbados	n.a.	2.7
British Virgin Islands	24.4	90.1
Cayman Islands	3.8	16.5
Unidentified others	n.a.	**79**

Source: MOFCOM, available at: www.fdi.gov.cn.
[a] This statistic released by MOFCOM for purposes of geographical breakdown is cumulated FDI. As it does not include divestments, it is much larger than the IFDI stock total in table 1, which comes closer to internationally-recognized standards of FDI measurement (see note [3]).

Annex table 5. China: principal foreign affiliates in China, ranked by sales value, 2008
(US$ million)

Rank	Name of affiliate	Industry	Sales
1	Hongfujin Precision Industry (Shenzhen) Co. Ltd.	Computer peripherals	26,974
2	Nokia Telecommunication Co. Ltd.	Cell phones	13,767
3	China Offshore Petroleum (China) Limited	Oil and gas	11,354
4	Dagong (Shanghai) Computer Co. Ltd.	Computers	10,535
5	Fay-Volkswagen Sales Co. Ltd.	Automobile	10,412
6	Daofeng (Shanghai) Computer Co. Ltd.	Computers	9,471
7	Angang Steel Ltd.	Steel	9,424
8	Shanghai GM Automobile Co. Ltd.	Automobile	9,366
9	Fay-Volkswagen Co. Ltd.	Automobile	9,217
10	Motorola (China) Electronic Ltd.	Telecom equipment	8,099
11	Maanshan Steel Co. Ltd.	Steel	7,287
12	Huaneng International Power Co. Ltd.	Electricity generation	7,257
13	Shanghai Volkswagen Automotive Sale Ltd.	Automobile	7,233
14	Dongfeng Toyota Auto Sale Co. Ltd.	Automobile	7,145
15	Dongfeng Auto Company	Automobile	7,057
16	Air China Co. Ltd.	Airline	6,767
17	Shanghai Volkswagen Automotive Ltd.	Automobile	6,734
18	Yingshunda Science & Technology Co. Ltd.	Consumer electronics	6,430
19	Nokia (China) Investment Co. Ltd.	Cell phones	6,393
20	China Southern Airlines Co. Ltd.	Airline	6,350

Source: MOFCOM, available at: www.fdi.gov.cn.

Annex table 6. China: main inward M&A deals, by inward investing firm, 2007-2009
(US$ million)

Year	Acquiring company	Home economy	Target company	Target industry	Shares acquired (%)	Transaction value (US$ million)
2009	Function Well Ltd.	Taiwan Province of China	Champ Tech Optical Foshan Corp	Optical instruments	100	230.6
2009	MAN Finance & Holding Sarl	Luxembourg	Sinotruk (Hong Kong) Ltd	Industrial vehicles manufacturing	25	782.2
2009	GCL-Poly Energey Holdings Ltd	Hong Kong, China	Greatest Joy International Ltd	Semiconductors	100	911.6
2009	GCL-Poly Energy Holdings Ltd	Hong Kong, China	GCL Solar Energy Tech Hldg Inc	Semiconductors	100	3,787.50
2009	TM Entertainment & Media Inc	United States	Hong Kong Mandefu Holdings Ltd	Advertising agencies	100	263.6
2009	HongKong Electric (Holdings) Ltd.	Hong Kong, China	Outram Ltd	Electric services	100	732.6
2009	Asahi Breweries Ltd	Japan	Tsingtao Brewery Co. Ltd.	Beverages	20	667
2009	GIC Real Estate Pte Ltd	Singapore	ProLogis-China Operations	Land developers	100	1,300.00
2009	ADF Phoenix IV Ltd	Singapore	Nanjing International Finance	Building operator	100	232.8
2009	Hana Bank	Korea, Republic of	Bank of Jilin Co Ltd	Financial services	19.7	327.4
2009	Franshion Ppty (China) Ltd	Hong Kong, China	China Jin Mao (Group) Co Ltd	Building operator	45.1	737.5
2009	BBVA	Spain	China Citic Bank	Banking	4.9	1,601.60
2009	CRH PLC	Ireland	Jilin Yatai Grp Cement Invest	Investors	26	296.7
2009	Investor Group	Hong Kong, China	Shanghai Shimao Co Ltd	Land developers	56.8	1,012.10
2009	Middle Kingdom Alliance Corp	United States	Pypo Digital Co Ltd	Electronic equipment	100	378
2008	BP Overseas Development Co Ltd	Thailand	Asian American Coal Inc	Mining	78.4	432.8
2008	Jade Green Investments Ltd	Hong Kong, China	Fortune Dragon Coking Coal	Mining	100	1,350.80
2008	Johnson & Johnson	United States	Beijing Dabao Cosmetics Co Ltd	Cosmetics	100	327.8
2008	Deutsche Bank AG	Germany	Huaxia Bank Co Ltd	Banking	5.3	552.9
2008	Holcim Ltd	Switzerland	Huaxin Cement Co Ltd	Cement	18.6	282.7
2008	Monster Worldwide Inc	United States	ChinaHR.com Holdings Ltd	Employment agencies	55	225
2008	Songzai Intl Holding Group	United States	Heilongjiang Xing An Grp Hong	Mining	90	550

	Inc					
2008	Hong Leong Bank Bhd	Malaysia	Chengdu City Commercial Bank	Banking	20	261
2008	CapitaRetail China Trust	Singapore	Xizhimen Mall	Building operator	100	229.3
2008	Blackstone Group LP	United States	China National Chemical Corp	Chemicals	20	600
2008	Shui On Investment Co Ltd	Hong Kong, China	Shui On Land Ltd	Land developers	5.1	230.2
2008	Beiersdorf AG	Germany	C-BONS Hair Care	Cosmetics	85	381.4
2008	Bank of America Corp	United States	China Construction Bank Corp	Banking	8.4	7,067.40
2008	Bank of America Corp	United States	China Construction Bank Corp	Banking	2.6	1,860.50
2008	CITIC Pacific Ltd	Hong Kong, China	CSSC Complex Property Co Ltd	Real estate	49	213.3
2007	China Merchants Intl Terminals	Hong Kong, China	Zhanjiang Port (Group) Co Ltd	Transportation	45	215.8
2007	China Real Estate Opp	Luxembourg	City Centre Development Phases	Real estate	100	548.1
2007	Asia Bottles (HK) Co Ltd	Hong Kong, China	Zhuhai Zhongfu Entrp Co Ltd	Manufacturing	29	225
2007	China Mining Resources Grp Ltd	Hong Kong, China	Harbin Songjiang Copper (Grp) Ltd	Mining	75.1	233.8
2007	GuocoLand (China) Ltd	Hong Kong, China	Beijing Chengjian Donghua RE	Real estate	90	751.7
2007	Investor Group	United States	Guangzhou Hengda Indl Grp Co	Conglomerate	8	400
2007	Panva Gas Holdings Ltd	Hong Kong, China	Hong Kong & China Gas (Qingdao)	Oil and gas	100	393.5
2007	BBVA	Spain	China Citic Bank	Banking	5	648.5
2007	3Com Corp	United States	Huawei-3com Co Ltd	Telecommunications	49	882
2007	Haier Electronics Group Co Ltd	Hong Kong	Haier Indesit (Qingdao) Washing	Electrical goods	70	385.4
2007	SEB Internationale SAS	France	Zhejiang Supor Cookware Co Ltd	Electrical goods	22.7	311.4
2007	ANZ Banking Group Ltd	Australia	Shanghai Country Coml Bank	Banking	19.9	263
2007	Investor Group	United States	Henan Luohe Shuanghui Industry	Food	100	251.5
2007	FedEx Express Corp	United States	Federal Express-DTW Co Ltd	Transportation	100	400
2007	UBS AG	Switzerland	Beijing Securities Co Ltd	Financial services	20	210.5

Source: Thomson ONE Banker. Thomson Reuters.

Annex table 7. China: main 20 greenfield projects, June 2006-September 2009
(US$ million)

Year	Company name	Home economy	Industry	Estimated/ announced investment value (US$ billion)
2009	Royal Dutch Shell	Netherlands	Coal, oil and natural gas	0.8
2009	Cheng Shin Rubber Industry	Taiwan Province of China	Rubber	1.0
2009	Michelin	France	Rubber	1.0
2009	Chevron Corporation	United States	Coal, oil and natural gas	4.7
2009	Chevron Corporation	United States	Coal, oil and natural gas	0.8
2009	Novartis	Switzerland	Biotechnology	1.0
2009	Hon Hai Precision Industry	Taiwan Province of China	Electronic components	1.0
2009	Charoen Pokphand Group	Thailand	Food & tobacco	1.2
2009	Hon Hai Precision Industry	Taiwan Province of China	Electronic components	1.0
2009	Samsung	Republic of Korea	Electronic components	2.2
2009	Shimao Property Holdings Ltd.	Hong Kong (China)	Real estate	1.2
2009	LG	Republic of Korea	Electronic components	4.0
2009	China Merchants Holdings (International)	Hong Kong (China)	Warehousing & storage	1.2
2009	Daiwa House Industry	Japan	Real estate	0.8
2009	Jumbo Lane Investments	United Kingdom	Coal, oil and natural gas	0.8
2008	Daimler AG	Germany	Automotive OEM	0.9
2008	ROSM	France	Consumer products	2.0
2008	Royal Vopak	Netherlands	Warehousing & storage	1.0
2008	Howard Group Development	Hong Kong (China)	Transportation	1.5
2008	Walt Disney	United States	Leisure & entertainment	3.6
2008	SK Energy	Republic of Korea	Chemicals	2.0
2008	Henderson	Hong Kong (China)	Real estate	1.4

2008	Lotte Group	Republic of Korea	Real estate	1.0
2008	Volkswagen	Germany	Automotive OEM	0.9
2008	Electric Power Development (J-Power)	Japan	Coal, oil and natural gas	0.7
2008	Yulon Motor	Taiwan Province of China	Automotive OEM	0.7
2008	Hyundai Motor	Republic of Korea	Automotive OEM	0.8
2008	Compal Electronics	Taiwan Province of China	Business machines & equipment	0.7
2008	Saudi Basic Industries (SABIC)	Saudi Arabia	Chemicals	1.7
2008	Israel Corp (IC)	Israel	Automotive OEM	0.8
2007	China Resources Power Holdings (CRP)	Hong Kong (China)	Metals	2.8
2007	Mori Building	Japan	Real estate	1.0
2007	Formosa Plastics Group (FPG)	Taiwan Province of China	Metals	0.9
2007	Ben Rautin	Malaysia	Transportation	3.0
2007	Hon Hai Precision Industry	Taiwan Province of China	Electronic components	1.0
2007	IBM	United States	Semiconductors	1.8
2007	Gulf Finance House	Bahrain	Real estate	5.0
2007	Kingdom Hotel Investments (KHI)	UAE	Hotels & tourism	0.9
2007	Hynix Semiconductor	Republic of Korea	Semiconductors	1.5
2007	Sinar Mas Group	Indonesia	Paper, printing & packaging	1.0
2007	Villar Mir Group	Spain	Metals	1.4
2007	DBS Group Holdings	Singapore	Financial services	2.8
2007	STX Corporation	Republic of Korea	Non-automotive transport OEM	1.0
2007	Bayerische Motoren Werke (BMW)	Germany	Automotive OEM	0.8
2007	Intel	United States	Semiconductors	2.5

Source: fDi Intelligence, a service from the Financial Times Ltd.

Outward FDI and its policy context, 2010

Ken Davies

Since 2000, China's OFDI has grown at an accelerating rate as a result of a switch in government policy to strong encouragement of Chinese enterprises to "go global." The bulk of this investment has been into the primary and tertiary sectors, with relatively little so far going into manufacturing. Most has gone to Asia, but Chinese investment is now spreading throughout the world. The precise geographical distribution is veiled, as much of it passes through tax havens. The Government has been slow to tackle administrative obstacles to Chinese companies wishing to invest abroad, but has recently begun to relax them. The global crisis has presented opportunities for Chinese multinationals, which were less seriously affected than their counterparts in the developed world, to raise their stake in the world economy.

Trends and developments

Country-level developments

China's OFDI stock reached US$ 246 billion by the end of 2009, well over eight times the US$ 28 billion recorded in 2000 and far above the negligible US$ 4 billion of 1990. China is a late developer in its outward investment, even among large emerging markets. Brazil had OFDI stock of US$ 41 billion in 1990, way ahead of China, but fell behind with only US$ 158 billion in 2009. China's OFDI stock also now exceeds that of Singapore, with US$ 213 billion. Russia's OFDI stock grew more rapidly than China's, reaching US$ 249 billion in 2009. China, though, did continue to outperform India, with its modest 2009 total IFDI stock of US$ 77 billion (annex table 1).

China's OFDI was minimal during the first two decades of economic reform from end-1978 to 2000. At the turn of the century, government policy switched from mildly permissive to strongly encouraging.[403] Since then, OFDI flows from China have accelerated from less than US$ 1 billion a year in 2000 to US$ 57 billion in 2009 (annex table 2).

The bulk of China's OFDI – around thee-quarters of the total – goes into the tertiary sector: by the end of 2009, the main recipients of China's OFDI stock were financial services (19% of the total) and wholesale and retail trade (15%). The primary sector came second: in 2009, mining, quarrying and petroleum comprised 17% of total OFDI stock. Unlike in the case of China's inward direct investment, the secondary sector is a relatively minor component, making up only 5.5% of the OFDI stock in 2009 (annex table 3).

In recent years, the sectoral distribution of China's OFDI has remained stable. However, this stability may be illusory and it is likely to give way to major shifts in composition in coming years. OFDI in leasing and commercial services may have been initially undertaken in support of the country's rapid growth in merchandise trade. More recently, this service-sector investment may be supporting a move into extractive industries that has yet to be reflected in the drawing down of funds for massive energy and raw materials projects. In the future,

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[403] See *Qiuzhi Xue and Bingjie Han,* "The role of government policies in promoting outward foreign direct investment from emerging markets: China's experience", in Karl P. Sauvant and Geraldine McAllister, with Wolfgang Maschek, eds., *Foreign Direct Investment from Emerging Markets: The Challenges Ahead* (New York: Palgrave, 2010).

Chinese firms may also diversify toward manufacturing to service global consumer goods markets more directly.

The bulk of China's OFDI goes to Asia, which accounted for US$ 186 billion (76%) of total OFDI stock in 2009. However, most (89%) of that stock actually went just to one destination, Hong Kong (China). Media attention worldwide has focused on Chinese OFDI in Africa, which has risen sharply but was still less than 4% of the country's global total OFDI in 2009 (annex table 4).

Some caution needs to be exercised in using official OFDI figures. To the extent that OFDI is used to inject funds into special purpose entities that then return the money to China as IFDI to take advantage of fiscal incentives, i.e. "round-tripping", the official total may be an overestimate. Round-tripping should logically be diminishing since fiscal incentives were abolished at the beginning of 2008, but by its very nature as an illegal activity it is difficult to obtain hard evidence of the actual trend in round-tripping.

Conversely, there are equally strong reasons to suppose the official figures to be underestimates. While most OFDI is from SOEs, a large and unknown proportion is from enterprises that are owned by non-state entities, i.e. privately- or collectively-owned. While SOEs are constrained to go through the official approval process and so be recorded as making OFDIs, non-state entities are more likely to evade approval. Where local OFDI approval is available, it may not always result in projects being included in national data.

The corporate players

According to the most recent Fudan-VCC survey of Chinese multinationals in 2007, the two largest Chinese MNEs were China International Trading and Investment Corporation (Citic), with foreign assets exceeding US$ 25 billion, and China Ocean Shipping (Group) Company (COSCO), with foreign assets of some US$ 21 billion. Both are well-established corporations that have built up an international presence over several decades as their core business. China's oil majors are also important overseas investors, including China National Petroleum Corporation (CNPC, which ranks 10th in the 2010 Fortune Global 500), with foreign assets of US$ 7 billion, Sinochem Group, with US$ 5 billion and China National Offshore Oil Corporation (CNOOC), with US$ 4 billion. Other mineral resource investors include two metallurgy MNEs: Sinosteel Corporation and China Minmetals Corporation, each with foreign assets of about US$ 2 billion. These acquisitions are part of a national strategy aimed at minimizing fluctuations in prices of essential inputs to domestic industry.

These MNEs can be expected to keep expanding as China continues to secure energy and raw material sources for its industrialization. Producers of consumer goods are also starting to become important as Chinese producers seek to penetrate foreign markets by M&As, to acquire brand names and market share, as in the case of Lenovo Group (with foreign assets of US$ 4 billion), which acquired IBM's personal computer division in 2005. Although Lenovo has used the acquisition to reinforce its position as market leader in China and has maintained a large share of the global PC market by continuing to manufacture the Thinkpad range,[404] it has not managed to develop innovative products capable of making a breakthrough to global market leadership. Shanghai Automotive Industry Corporation (SAIC), with foreign assets of US$ 2 billion, is also using cross-border acquisitions to broaden its product range and gain

[404] Lenovo website: http://www.lenovo.com/.

foreign market share. Having attained a strong position in the domestic Chinese market, consumer durables manufacturer Haier, with foreign assets of US$ 768 million, is seeking similar success in the global market (annex table 5). Haier in 2009 overtook Whirlpool (which it had already driven out of China in the 1990s, when Whirlpool closed its two factories there) in global refrigerator sales.[405] Haier has gone further than most Chinese MNEs in becoming truly global: 24 of its 29 factories and 4 of its 16 industrial parks are now outside China and it maintains 58,800 sales outlets in over 160 countries.[406]

Most M&A deals in 2007-2009 were in the energy and minerals sectors, but the largest transactions tended to be purchases of minority stakes in global financial institutions. For example, one of the country's largest steel producers, Shanghai Baosteel, acquired a 15% US$ 240.5 million stake in Aquila Resources in Australia in 2009 as part of a strategic co-operation agreement to expand Aquila's steel raw materials projects, including iron ore, coal and manganese,[407] while Yanzhou Coal Mining, in the same year, made a successful takeover bid for the Australian coal producer Felix Resources at a cost of US$ 2.8 billion. In 2008, the Chinese oil major Sinopec acquired the Canadian company Tanganyika Oil for US$ 2 billion. The largest deal was one that did not happen: in 2009, the Chinese aluminum producer Chinalco abandoned a US$ 19.5 billion bid to raise its stake in Australia's Rio Tinto. In the financial sector, China Merchants Bank purchased Wing Lung Bank of Hong Kong (China) for nearly US$ 4.6 billion in 2008 (in two stages), while, in 2007, Ping An Insurance bought a 4.2% stake in Fortis of Belgium for US$ 2.7 billion to buy half of its asset management business (this is mentioned here because, although this is strictly speaking below the 10% criterion for classification as FDI, Ping An behaved as though it was an FDI operation and it was larger than many Chinese OFDI M&A deals). Also in 2007 the Industrial and Commercial Bank of China (ICBC), then the largest bank in the world by asset value, acquired a 20% stake in South Africa Standard Bank for US$ 5.6 billion.[408]

An important development was the creation of the China Investment Corporation (CIC), China's SWF, in 2007. In the first year of operation, CIC purchased a 9.9% stake in the US investment firm Blackstone for US$ 3 billion, and subsequently undertook to increase this to 12.5%, and also acquired a 9.9% holding in Morgan Stanley for US$ 5 billion. Widespread criticism of the Blackstone deal in China resulting from the fall in Blackstone's share price from US$ 31 at the time of purchase in May 2007 to below US$ 5 in early 2009[409] led to a pause for reappraisal of the SWF's investment strategy during 2008.[410] In 2009, CIC made several smaller purchases, mainly in the commodities industry: 8% of Australia's Goodman Group for US$ 396 million, 15% of the Noble Group of Hong Kong for US$ 854 million, 45% of Russia's Nobel Oil Group for US$ 400 million and 25% of South Gobi Energy Resources of Canada for US$ 500 million (annex table 6). These enabled it to make a return on investment of 11.7% in 2009.[411]

China's overseas greenfield investments are concentrated mainly in the energy, raw materials, automotive, and real estate sectors. A few energy projects are in renewable and alternative

[405] Alibaba News website: http://news.alibaba.com/.
[406] Haier China website: http://www.haier.com.
[407] "Aquila Resources clinches US$ 286m Baosteel investment," *The Australian*, August 28, 2009.
[408] The Economist website: http://www.economist.com/.
[409] Detailed criticisms were voiced on the Chinese Internet, for example the blog article "Zhang Ming feels today is right but yesterday was wrong" (in Chinese), http://blog.ce.cn/, and acknowledged indirectly in official pronouncements, for example "China's CIC chief defends investments, Blackstone", *Reuters*, October 26, 2008.
[410] "China shuns investments in West's finance sector", *The New York Times*, December 3, 2008.
[411] "CIC reaps gains from rosy overseas investments", *China Daily*, July 30, 2010.

energy, a rapidly developing sector of China's economy; such investments include a US$ 271 million project in Malaysia in 2009 by State Grid (ranked 8th in the 2010 Fortune Global 500), a US$ 1.4 billion project in Singapore by China Huaneng and one worth US$ 300 in Cambodia by China Southern Power Grid in the same year. Another of China's largest state-owned companies, Sinopec (7th in the 2010 Fortune Global 500), made a US$ 220 million greenfield investment in Russia. There were also greenfield investments by provincial or municipal enterprises such as Tianjin Pipe, which invested US$ 1 billion in the United States in 2009, and Hebei Jingniu Group, which invested US$ 400 million in a ceramics and glass project in Zimbabwe in 2008 (annex table 7).

Effects of the current global crisis

With a relatively small exposure to the US subprime market, China was less affected by the subprime crisis and its aftermath than the developed economies. GDP growth slowed as the country's export markets suffered, but remained strong, supported by an early, large and fast-acting government stimulus package. With high cash reserves and ample support available from the Government, China's MNEs continued to expand their overseas acquisitions. In 2008, when global OFDI flows fell by 15%, Chinese OFDI flows more than doubled; in 2009, when global OFDI flows plummeted by 43%, OFDI from China edged up by 1%.[412] But for the failure of one large M&A transaction (the Chinalco-Rio Tinto deal, with an expected value of US$ 19.5 billion), the result would have been an increase in China's total OFDI of 36%.

The weakening of companies in the developed world as a result of the credit crunch, stagnation in their domestic consumer markets and impending cuts in public expenditure may present increasing opportunities for Chinese MNEs to expand further, acquiring inputs for industrialization while also gaining market share. With official foreign exchange reserves of US$ 2,454 billion at end-June 2010, China has ample financial resources to support a further acceleration of OFDI growth.

The policy scene

During the first three decades of economic reform, China's OFDI played a supporting role as trade expanded rapidly. From 1979 to 2000, the government actively promoted and facilitated IFDI while its policy towards OFDI remained tentative. A few vehicles, notably China International Trust and Investment Corporation (CITIC) were set up early in the reform period for outward investment, but domestic enterprises were not actively encouraged to invest abroad. It was, indeed, only in the 1990s that more than one or two of China's domestic companies became large and successful enough to try their hand at being global players, especially after the government restructured and consolidated major industries such as oil and petrochemicals.[413] At the turn of the century, government policy switched to a policy of actively promoting OFDI. The new "go global" policy that was adopted from 2000 onward has several objectives, both macroeconomic, including reduction of excessive low-return foreign exchange reserves, and microeconomic, for example, improving the global

[412] UNCTAD, *World Investment Report 2010: Investing in a Low Carbon Economy* (New York and Geneva: United Nations, 2010).
[413] Peter Nolan and Zhang Jin, "The challenge of globalization for large Chinese firms", in Peter Nolan, ed., *Transforming China: Globalization, Transition and Development* (London: Anthem Press, 2004).

competitiveness of China's large enterprises. Another major aim is the securing of future supplies of energy and raw materials for continuing industrialization.[414]

As with IFDI projects, the government operates an examination and approval process through a system of catalogues of various levels of approval, from "prohibited" to "encouraged". Together with the procedures for obtaining approval to remit funds abroad for OFDI, this system constitutes a barrier to OFDI. Companies with an established presence overseas frequently prefer external financing so that they can bypass these cumbersome procedures. The Government is gradually streamlining the process.

The Chinese government has taken several important steps to support OFDI by domestic enterprises. An export credit insurance corporation, Sinosure, which has a mandate to support investment as well as trade, started operations at the end of 2001.[415] Government policy is to encourage banks to fund overseas acquisitions by Chinese MNEs. This policy has been strengthened during the global crisis: M&A financing rules promulgated by the China Banking Regulatory Commission (CBRC) in 2008 in line with the government's crisis-response stimulus package freed the commercial banks to make loans to fund the transaction price of M&A transactions, including cross-border M&As.[416] The establishment of the CIC (see above) is also a major component of the government's OFDI promotion strategy.

China has conducted active investment diplomacy since the early 1980s: it had signed 127 BITs by June 1, 2010 and 112 double taxation agreements (DTTs) by June 1, 2009.[417] China is a member of the world's largest free trade area in terms of population and third largest in nominal GDP, the ASEAN–China Free Trade Area (AFTA), which was agreed in 2002 and came into effect on January 1, 2010.
During the global crisis, the Chinese Government has made numerous declarations against trade and investment protectionism.[418] As some Chinese acquisitions in recent years have failed because of opposition in host countries, even when they had been allowed by the host country authorities, China is concerned to stem what it sees as the rise of a protectionism that targets its investment abroad. China has participated in discussions on this in the G20.[419]

Conclusions and Outlook

Driven mainly by government policy and funded by the country's massive reserves gained from trade and inward investment flows, China's OFDI will continue to grow rapidly and become more geographically and sectorally diverse. The current emphasis on OFDI in energy and raw materials and in the services will shift toward the development of manufacturing and services centers in overseas markets, timed to take advantage of favorable exchange rate and price movements. The increasing exposure of Chinese MNEs to international business practice will prompt them to seek further improvements in China's own institutional framework, which will be beneficial for both domestic and IFDI.

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[414] OECD, *Investment Policy Review of China: Encouraging Responsible Business Conduct* (Paris: OECD, 2008), chapter 3, "China's outward direct investment".
[415] Sinosure website: http://www.sinosure.com.cn/.
[416] International Law Office website: http://www.internationallawoffice.com.
[417] UNCTAD Country-Specific lists of Bilateral Investment Treaties and Double Taxation Treaties http://www.unctad.org/.
[418] For example, in Premier Wen Jiabao's speech on "Four proposals to promote world harmony and prosperity", in which the second proposal is to "fight against trade and investment protectionism", published on September 10, 2009 on the Chinese Foreign Ministry website http://www.fmprc.gov.cn/.
[419] Vice-Premier Wang Qishan "G20 must look beyond the needs of the top 20", *The Sunday Times*, March 27, 2009; "From G8 to G20", *Beijing Review*, July 8, 2010.

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Buckley, Peter J., *Foreign Direct Investment, China and the World Economy* (Basingstoke and New York: Palgrave Macmillan, 2010).

Sauvant, Karl P., with Kristin Mendoza and Irmak Ince, eds., *The Rise of Transnational Corporations from Emerging Markets* (Cheltenham and Northampton, Mass.: Edward Elgar, 2008).

Useful websites

Invest in China (maintained by the Ministry of Commerce): http://www.fdi.gov.cn/.

Ministry of Commerce of the People's Republic of China: http://www.mofcom.gov.cn/.

People's Bank of China: http://www.pbc.gov.cn/.

Statistical annex

Annex table 1. China: outward FDI stock, 1990-2009 (US$ billion)

Economy	1990	2000	2009
China	4 [a]	28 [a]	246
Memorandum: comparator economies			
Brazil	41	52	158
India	0	2	77
Russia	n.a.	20	249
Singapore	8	57	213

Source: UNCTAD's FDI/TNC database, available at:http://stats.unctad.org/fdi/ and Ministry of Commerce of the People's Republic of China, *2009 Statistical Bulletin of China's Outward Foreign Direct Investment* (Beijing: MOFCOM, 2010).
[a] Not including financial OFDI.

Annex table 2. China: outward FDI flows, 2000-2009 (US$ billion)

Economy	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
China	0.9 [a]	6.9 [a]	2.7 [a]	2.9 [a]	5.5 [a]	12.3 [a]	21.2	26.5	55.9	56.5
Memorandum: comparator economies										
Brazil	2.3	-2.3	2.5	0.2	9.8	2.5	28.2	7.1	20.5	-10.1
India	0.5	1.4	1.1	1.3	2.2	3.0	14.3	17.2	18.5	14.9
Russia	3.2	2.5	3.5	0.7	13.8	12.8	23.2	45.9	56.1	46.1
Singapore	5.3	17.1	4.1	3.1	8.1	6.9	13.3	27.6	-8.5	6.0

Source: UNCTAD's FDI/TNC database, available at:http://stats.unctad.org/fdi/ and Ministry of Commerce, 2009 Statistical Bulletin of China's Outward Foreign Direct Investment (Beijing: MOFCOM, 2010).
[a] Not including financial OFDI.

Annex table 3. China: distribution of outward FDI stock, by economic sector and industry, 2004, 2009 (US$ billion and percent of total outward stock)

Sector / industry	**2004** [a]	**2009**
All sectors / industries	44.8 100%	245.8 100%
Primary	6.8 15.2%	42.6 17.3%
Agriculture, forestry, and fishing	0.8 1.8%	2.0 0.8%
Mining, quarrying and petroleum	6.0 13.4%	40.6 16.5%
Secondary	4.5 10.0%	13.6 5.5%
Manufacturing	4.5 10.0%	13.6 5.5%
Tertiary **of which:**	33.5 74.8%	189.6 77.1%
Leasing and commercial services	16.4 36.6%	7.3 3.0%
Financial services	n.a.	46.0 18.7%
Wholesale and retail	7.8 17.4%	35.7 14.5%
Transport, storage and postal services	4.6 10.3%	16.6 6.8%

Ministry of Commerce, *2009 Statistical Bulletin of China's Outward Foreign Direct Investment* (Beijing: MOFCOM, 2010).
[a] Not including financial OFDI.

Annex table 4. China: geographical distribution of outward FDI stock, 2000- 2009
(US$ billion)

Region/economy	2003 [a]	2009
World	**33.2**	**245.8**
Developed economies	n.a.	n.a.
Europe	0.5	8.7
European Union	n.a.	n.a.
Germany	n.a.	1.1
United Kingdom	n.a.	1.0
Netherlands	n.a.	0.3
North America	0.5	5.2
Canada	n.a.	1.7
United States	0.5	3.3
Other developed economies	n.a.	n.a.
Australia	0.4	5.9
Japan	n.a.	0.7
Developing economies	n.a.	n.a.
Africa	0.5	9.3
Asia	26.6	185.5
Hong Kong (China)	24.6	164.5
Singapore	0.2	4.9
Oceania	0.4	6.4
Latin America and Caribbean	4.6	30.6
Cayman Islands	3.7	13.6
British Virgin Islands	0.5	15.1
Transition economies	n.a.	n.a.
Russian Federation	n.a.	2.2

Source: Ministry of Commerce, *2009 Statistical Bulletin of China's Outward Foreign Direct Investment* (Beijing: MOFCOM, 2010).
[a] Not including financial OFDI.

Annex table 5. China: principal MNEs, ranked by foreign assets, 2007 (US$ million)

Rank	Name	Industry	Foreign assets
1	Citic Group	Diversified	25,514
2	China Ocean Shipping (Group) Company [COSCO]	Transport and storage	21,365
3	China State Construction Engineering Corporation	Construction and real estate	11,801
4	China National Petroleum Corporation [CNPC]	Oil and gas	6,814
5	China Shipping (Group) Company	Transport and storage	5,815
6	Sinochem Group	Oil and gas	4,812
7	China Huaneng Group	Power and power facilities	4,250
8	China National Offshore Oil Corporation [CNOOC]	Oil and gas	4,223
9	Lenovo Group	Computers and related products	4,030
10	Sinotrans Corporation	Transport and storage	3,196
11	Shanghai Automotive Industry Corporation (Group) [SAIC]	Automobiles	2,305
12	China Communications Construction Company Ltd.	Construction and real estate	2,134
13	Sinosteel corporation	Metal and metal products	2,130
14	Sinotruk	Heavy-duty trucks	1,870
15	China Minmetals Corporation	Metal and metal products	1,823
16	ZTE Corporation	Telecom products, services and solutions	1,740
17	Baosteel Group Corporation	Metal and metal products	1,077
18	Haier Group	Manufacturing	768
Total			**105,666**

Source: Fudan-VCC survey of Chinese multinationals, available at: www.vcc.columbia.edu.

Annex table 6. China: main M&A deals, by outward investing firm, 2007-2009
(US$ million)

Year	Acquiring company	Target company	Target industry	Target economy	Shares acquired (%)	Transaction value
2009	China Investment Corp (CIC)	South Gobi Energy Resources	Mining	Canada	25.0	500
2009	China Investment Corp (CIC)	Nobel Oil Group	Oil and gas	Russia	45.0	300
2009	Fullbloom Investment Corp	KazMunaiGas Expl & Prodn JSC	Oil and gas	Kazakhstan	11.0	939
2009	China Investment Corp (CIC)	Noble Group Ltd	Investment	Hong Kong, China	15.0	854
2009	Shanghai Baosteel Group Corp	Aquila Resources Ltd	Mining	Australia	15.0	241
2009	Investor Group	Cathay Pacific Airways Ltd	Transportation	Hong Kong, China	14.5	948
2009	Yanzhou Coal Mining Co Ltd	Felix Resources Ltd	Mining	Australia	100.0	2,807
2009	China Investment Corp (CIC)	Goodman Group	Property development	Australia	8.0	396
2009	China CITIC Bank Corp Ltd	CITIC Intl Finl Hldg Ltd	Investment	Hong Kong, China	70.3	403
2009	WISCO	Consolidated Thompson Iron	Mining	Canada	19.9	240
2009	Hunan Hualing Iron & Steel Grp	Fortescue Metals Group Ltd	Mining	Australia	8.4	408
2009	Hunan Hualing Iron & Steel Grp	Fortescue Metals Group Ltd	Mining	Australia	9.8	409
2009	China Minmetals Nonferrous Met	OZ Minerals Ltd-certain assets	Mining	Australia	100.0	1,386
2009	Investor Group	OAO Mangistau MunaiGaz	Oil and gas	Kazakhstan	100.0	2,604
2009	ICBC	Seng Heng Bank	Finance and insurance	Macau, China	20.1	149
2008	CITIC Group Ltd	CITIC Pacific Ltd	Conglomerate	Hong Kong, China	39.9	1,500
2008	Sinopec	Tanganyika Oil Co Ltd	Oil and gas	Canada	100.0	2,029
2008	Investor Group	CIFA SpA	Machinery manufacturing	Italy	100.0	747
2008	Investor Group	CIFA SpA	Machinery manufacturing	Italy	100.0	784
2008	CITIC Group Ltd	CITIC Intl Finl Hldg Ltd	Investment	Hong Kong, China	15.2	855
2008	China Merchants Bank Co Ltd	Wing Lung Bank Ltd	Finance	Hong Kong, China	53.1	2,474
2008	China Merchants Bank Co Ltd	Wing Lung Bank Ltd	Finance	Hong Kong, China	44.7	2,082
2008	China Life Insurance Co Ltd	Visa Inc	Financial services	United States	n.a.	300
2008	Sinopec Intnl	AED Oil-Expl Permits (3)	Oil and gas	Australia	60.0	556
2008	Metallurgical Corp of China	Cape Lambert Iron Ore-Project	Mining	Australia	100.0	373
2008	SINOCHEM	SOCO Yemen Pty	Oil and gas	Australia	100.0	465

	Petro Expl & Prodn	Ltd				
2008	Sinosteel Corp	Midwest Corp Ltd	Mining	Australia	100.0	1,377
2008	Investor Group	Northern Peru Copper Corp	Mining	Canada	100.0	445
2008	ICBC	Standard Bank Group Ltd	Banking	South Africa	20.0	5,617
2008	ICBC	Seng Heng Bank	Finance and insurance	Macau, China	19.9	593
2007	SPC E&P (China) Pte Ltd	Sino-American Energy Corp	Mining	United States	100.0	223
2007	Ping An Ins (Grp) Co of China	Fortis SA/NV	Financial services	Belgium	4.2	2,672
2007	China Investment Corp (CIC)	Morgan Stanley	Financial services	United States	9.9	5,000
2007	Metallurgical Corp of China	Balmoral Iron Holdings Pty Ltd	Mining	Australia	20.0	348
2007	CDB	Barclays PLC	Banking	United Kingdom	3.1	2,980
2007	Xinjiang Zhongxin Resources	Mortuk Oilfield	Oil and gas	Pakistan	100.0	250
2007	Chalco	Peru Copper Inc	Mining	Canada	100.0	771
2007	China Investment Corp (CIC)	Blackstone Group LP	Investment advice	United States	9.9	3,000
2007	Cension Semiconductor Mfr Corp	Hiroshima Elpida-silicon wafer	Semiconductors manufacturing	Japan	100.0	310
2007	Sinochem Petro Expl & Prodn	New XCL-China LLC	Oil and gas	United States	100.0	228
2007	China Mobile Commun Corp	Paktel Ltd	Telecommunications	Pakistan	88.9	284
2007	CapitaRetail China Dvlp Fund	CapitaRetail China	Real estate investment trusts	Singapore	100.0	260
2007	Absolut Invest AG	Absolut Europe AG	Investment advice	Switzerland	87.1	288
2007	Suntech Power Holdings Co Ltd	MSK Corp	Semiconductors manufacturing	Japan	33.3	193
2007	Air China Ltd	CNAC	Transportation	Hong Kong, China	31.6	378

Source: Thomson ONE Banker. Thomson Reuters.

Annex table 7. China: main greenfield projects, by outward investing firm, 2008-2009
(US$ million)

Year	Investing company	Industry	Host economy	Investment value
2009	State Grid Corporation	Metals	Malaysia	240
2009	China Nonferrous Metals Mining (CNMC)	Metals	Zambia	400
2009	State Grid Corporation	Alternative/renewable energy	Malaysia	271
2009	China Petroleum and Chemical (Sinopec)	Coal, oil and natural gas	Russia	220
2009	China North Industries Group (NORINCO)	Building and construction materials	Russia	616
2009	China National Petroleum (CNPC)	Coal, oil and natural gas	Sudan	1,701
2009	China National Petroleum (CNPC)	Transportation	Myanmar	165.8
2009	A-Power Generation Systems	Engines and turbines	United States	300.4
2009	China Nonferrous Metal Industries Engineering and Construction (NFC)	Metals	Laos	500
2009	China Huaneng	Alternative/renewable energy	Singapore	1,431
2009	China Nonferrous Metals Mining (CNMC)	Metals	Zambia	204
2009	China Minmetals Group	Metals	Peru	254
2009	Sinosteel	Metals	South Africa	329
2009	SAIC Chery Automobile	Automotive OEM	Thailand	191
2009	SAIC Chery Automobile	Automotive OEM	Taiwan Province of China	238
2009	China National Petroleum (CNPC)	Coal, oil and natural gas	Costa Rica	1,000
2009	Dongfeng Motor	Automotive OEM	Turkey	250
2009	Yantai Shuchi Vehicle	Automotive OEM	Russia	202
2009	China Nonferrous Metals Mining (CNMC)	Metals	Zambia	179
2009	China Shenhua Energy Company	Coal, oil and natural gas	Indonesia	331
2009	China Metallurgical Group Corporation	Metals	Australia	159
2009	Anhui Jinghuai Automobile Group (JAC)	Automotive OEM	Brazil	299
2009	China Metallurgical Group Corporation	Metals	Afghanistan	2,900
2009	China National Petroleum (CNPC)	Coal, oil and natural gas	Chad	472
2009	Wuhan Iron and Steel Co., Ltd. (Wisco)	Metals	Brazil	4,000
2009	China Singyes Solar Technologies	Electronic components	Hong Kong, China	200
2009	SAIC Chery Automobile	Automotive OEM	Brazil	700

2009	SAIC Chery Automobile	Automotive OEM	Turkey	500
2009	Beijing Vantone Real Estate	Real estate	United States	189
2009	Xiyang Group	Metals	Dem Republic of Korea	173
2009	Sinosteel	Metals	India	517
2009	China Southern Power Grid	Alternative/renewable energy	Cambodia	300
2009	Chongqing Lifan Industry	Automotive OEM	Philippines	228.4
2009	China National Petroleum (CNPC)	Coal, oil and natural gas	Oman	1,656.80
2009	China National Petroleum (CNPC)	Coal, oil and natural gas	Iran	1,760.00
2009	Tianjin Pipe	Tools	United States	1,000
2008	China Union	Metals	Liberia	2,600
2008	Hebei Jingniu Group	Ceramics and glass	Zimbabwe	400
2008	Wuhan Iron and Steel Co., Ltd. (Wisco)	Metals	Australia	357
2008	Jiangxi Rare Earth and Rare Metals Tungsten Grouop	Metals	Philippines	394
2008	China Metallurgical Group Construction (CMCC)	Metals	Philippines	1,000
2008	Shenzhen Energy Group	Coal, oil and natural gas	Nigeria	2,400
2008	Changan Automobile Group	Automotive OEM	Mexico	307
2008	China National Petroleum (CNPC)	Coal, oil and natural gas	Chad	1,587
2008	Sinohydro	Alternative/renewable energy	Zambia	400
2008	China Petroleum and Chemical (Sinopec)	Coal, oil and natural gas	Iran	1,206
2008	Khai De International Group	Real estate	Vietnam	300
2008	Citic Group	Real estate	Angola	3,535
2008	Sunshine 100 Groupo	Real estate	Philippines	362
2008	Fujian Longlin Group	Building and construction materials	Philippines	300
2008	Zhonghao Overseas Construction Engineering Limited	Building and construction materials	Nigeria	362
2008	Shanghai Electric Power	Engines and turbines	India	3,000
2008	China Petroleum and Chemical (Sinopec)	Coal, oil and natural gas	Vietnam	4,500
2008	SAIC Chery Automobile	Automotive OEM	Argentina	500
2008	China Metallurgical Construction (CMCC)	Metals	Philippines	301
2008	China National Petroleum (CNPC)	Coal, oil and natural gas	Turkmenistan	414
2008	China Telecommunications	Communications	United States	500
2008	China National Petroleum (CNPC)	Coal, oil and natural gas	Niger	1,587
2008	China Petroleum and Chemical (Sinopec)	Coal, oil and natural gas	Saudi Arabia	1,657

2008	China National Petroleum (CNPC)	Coal, oil and natural gas	Venezuela	502
2008	Aluminium Corporation of China (Chalco)	Metals	Peru	2,150
2008	Datang International Power Generation	Alternative/renewable energy	Kazakhstan	860
2008	Jiangling Motors (JMC)	Automotive OEM	Algeria	287
2008	China National Petroleum (CNPC)	Coal, oil and natural gas	Syria	1,500
2008	Jiangxi Copper	Metals	Peru	1,400
2008	China Power Investment	Coal, oil and natural gas	Myanmar	670
2008	Xinxing Group	Metals	India	2,159
2008	Sinosteel	Metals	South Africa	440
2008	Bosai Minerals	Metals	Guyana	1,000
2008	Shanghai Union Technology	Electronic components	Portugal	327
2008	China National Petroleum (CNPC)	Coal, oil and natural gas	Turkmenistan	2,200

Source: fDi Intelligence, a service from the Financial Times Ltd.

Chapter 17 – Colombia

Inward FDI and its policy context, 2010

Miguel Posada Betancourt

Colombia used to be a synonym for violence and drugs, but not any more. Today, the country has one of the best performing economies in Latin America, and violence has been dramatically reduced. The outgoing administration made improving investor confidence and the business environment one of the pillars of its policy. Thanks to important reforms and aggressive campaigns to promote the country as an attractive location, IFDI has risen to unprecedented levels. Due to these positive changes, Colombia has been designated a "top reformer" for the past four years in the World Bank's Doing Business reports, and the new Government has promised to maintain and reinforce efforts to attract foreign investment. Even though IFDI flows decreased in the past two years as a consequence of the economic and financial crisis, many foreign affiliates in Colombia achieved positive profits. A country that a decade ago was avoided is now in many investors' plans.

Trends and developments

Back in 2000, Colombia presented a low IFDI stock compared to its neighbors Peru and Venezuela, from where many MNEs preferred to manage their Andean operations. However, in 2008 that trend shifted when Colombia's FDI stock rose to US$ 67 billion, surpassing both countries' IFDI stocks (annex table 1). By the end of 2009, Colombia's FDI stock stood at US$ 74 billion, showing a 10% increase compared to 2008 and a compound annual growth rate of 12.8% for the 2000-2009 period. [420]

Country-level developments

Despite Colombia's size and economic potential, until 2005 FDI in the country registered timid inflows and marginal growth rates. Most IFDI coming in the 1990s was a consequence of privatizations rather than market-led opportunities. In 1999, the worst year of Colombia's economic crisis, the country received US$ 1.5 billion of FDI and by 2000 FDI flows only accounted for 2.6% of the country's' GDP. During the economic recovery period from 2000 to 2003, IFDI flows stayed constant, peaking at US$ 2.5 billion in 2001 (annex table 2). Finally, in 2005, Colombia received US$ 10.3 billion, the highest annual IFDI inflow in its history, led by the acquisition of the largest Colombian brewery, Bavaria, by SAB Miller[421] (South Africa) [422] and by 2009 FDI flows represented 5.3% of the country's total output.

Even though governmental efforts to expand and diversify the sectors receiving foreign capital showed some positive results, the IFDI flows are still largely concentrated in the primary sector (annex table 3). In 2009, 80% of IFDI inflows went into natural resources exploitation, i.e. 37% into the oil industry and the remaining 43% into the mining and

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[420] Author's own calculations, based on data from Colombia's Central Bank on FDI inflows and the National Statistics Department data on GDP.

[421] SAB Miller, "A powerful combination," July 19, 2005, available at: http://www.sabmiller.com/files/presentations/2005/190705/190705_bavaria_transaction_slides.pdf. It is estimated that, out of the US$ 7.8 billion deal, US$ 4.8 billion entered the country as FDI in 2005 through the 71.8% of shares bought from the Santo Domingo family, owner of Bavaria, as well as shares acquired from minority shareholders in the company.

[422] Proexport Colombia, available at: http://www.investincolombia.com.co.

quarrying industry. Commerce, restaurants and hotels captured 9% of inflows, while manufacturing activities attracted around 7% of IFDI.

2009 proved to be a difficult year. In the manufacturing and transportation, storage, and communications sectors, IFDI inflows fell by 69% and 61%, respectively compared to the previous year. Other sectors that suffered diminishing FDI flows were agriculture (65%), financial establishments (50%), utilities (725%) and oil (22%)[423] (annex table 3).

On the other hand, the mining sector, with IFDI of US$ 3.1 billion, experienced a growth of 72% and remains, along with the oil industry, the main recipients of FDI. On average, for the 2000-2005 period, IFDI in the mining and the oil industries amounted, respectively, to 25% and 13% of total IFDI and, during 2006-2009, to 23% and 34%.

More recently, according to Colombia's central bank preliminary numbers, up to the second quarter of 2010, FDI inflows amounted to US$ 4.1 billion, representing a 18% decrease compared to the same period the year before.[424]

In terms of technology intensity, 55% of IFDI in Latin America is directed to medium-low technology industries. Given that 80% of the IFDI flows to Colombia in 2009 were directed to natural resources exploitation, the country shows a low level of technology-intensive investment. From a regional comparative perspective, Colombia captures 0.62% of IFDI with a high technology intensity component directed to manufacturing in Latin America and 0.07% of IFDI with a medium-low technological intensity.[425]

One of the most coveted forms of IFDI are investments with a high component of R&D, as these are high value-added activities with the potential to generate larger positive technological spillovers and larger shares of revenues for the host economy.[426] According to the United Nations Economic Commission for Latin America and the Caribbean (ECLAC), during 2003–2009 a total of 193 R&D greenfield projects were started in the region.[427] Colombia captured 5.5% of all R&D projects, behind Brazil (38.7%), Mexico (27.6%), Argentina (10.6%), and Chile (9.1%).

In terms of geographical localization Bogotá remains the main economic and industrial center, capturing 77% of IFDI, followed by the Department of Antioquia, and its capital, Medellín, the second largest city in Colombia grasping 9% of IFDI. The remainders of incoming flows were invested in the departments of Bolívar (5%), Valle (5%) and Atlántico (2%).[428]

Given the historically strong links between the Colombian economy and the United States, it is not surprising that the United States stands as the largest investor, accounting for 87% of total FDI inflows in Colombia in 2009 (annex table 4).[429] During the 2006-2009 period, The U.S. along with the United Kingdom and Spain accounted for 60% of total average inflows.

Given the still nascent state of industries in the region, FDI from neighboring countries has been marginal and only until recently, with the rise of the translatinas, have these amounts

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[423] Banco de la República de Colombia, "Balance of payments," June 2010.
[424] Banco de la República de Colombia, "Balance of payments," November 2010.
[425] ECLAC, *La inversión extranjera directa en América Latina y el Caribe* (Santiago de Chile: ECLAC, 2010).
[426] High profits must be generated in the country to take into account higher risks for investments in these complex activities being performed in the host country.
[427] ECLAC, *La inversión extranjera directa en América Latina y el Caribe*, op. cit.
[428] Bogotá's Chamber of Commerce, "Tablero de indicadores de Bogotá," 2010.
[429] Data by origin of FDI do not include investments in the oil sector nor the reinvestment of profits.

started to become significant, with investments coming especially from Chile and Brazil. As a consequence, average IFDI inflows from Chile and Brazil surged from US$ 10.2 million and US$ 5.4 million, respectively, during 2000-2005, to US$ 36.6 million and US$ 180.2 million during 2006-2009.

The corporate players

By the end of 2008, there were 645 foreign affiliates in Colombia.[430] In 2007 and 2008, Colombia saw a surge in greenfield projects, when the country attracted 66 and 73 greenfield projects, respectively. Now Colombia, surpassing Chile, became the third largest recipient of IFDI in South America, behind Brazil and Argentina.[431]

As mentioned earlier, Colombia has benefited from the rise of the so called translatinas - Latin American companies that have recently turned into important international players. Chilean companies including Fallabella, Cencosud and Sodimac, and Brazilian firms such as Vale, Gerdau, Votorantim, and the Sinergy group (owner of Avianca) have been regional pioneers in penetrating the Colombian market. Translatinas played a protagonist role in 2009 as the largest deals, primarily in the oil, mining and quarrying industries, were performed by companies such as Xtrata and Vale (annex table 6).

Finally, it is worth mentioning that Phillip Morris' efforts to acquire the Colombian tobacco company Coltabaco were blocked by the Colombian authorities, who expressed concern over the potential creation of a monopoly.[432]

Effects of the current global crisis

Because of the economic and financial crisis, IFDI inflows fell by 32% in 2009 compared to 2008, as important investment decisions were reversed. These included the sales of Corn Products to Bunge and of Prodesal to Mexichem, as well as the acquisition of the Compañía Minera de Caldas (CMC) by Canadian Colombia Goldfields.[433]

However, in spite of the global crisis, profits made by foreign affiliates allowed the acquisition of Colombian companies. The acquisition by Makro (Netherlands) of 37% of shares of Makro Supermayorista (owned by several local firms), the acquisition of Socovig, a private security company, by Burns de Colombia for € 3.4 million[434] and the acquisition of Colsecurity by Wackenhut Colombia are a few examples of investments that went forward.[435]

In the past two years, the economic and financial markets crisis has particularly affected FDI inflows coming from European countries. During 2000–2005, Spain, the third largest investor in Colombia, always had positive investment figures. However, the financial crunch drove Spanish investment down to a disinvestment of US$ 327 million in 2008/2009. Overall flows

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[430] UNCTAD, *World Investment Report* 2009: *Transnational Corporations, Agricultural Production and Development* (New York and Geneva: UNCTAD, 2009). Data for 2008 are the latest available.
[431] ECLAC, *La inversión extranjera directa en América Latina y el Caribe*, op. cit.
[432] Superintendencia de Industria y Comercio, "Resolución No 29937," June 11, 2010, available at: http://www.sic.gov.co/Articulos_Pagina_Principal/Noticias/2010/Competencia/SIC_Objeto.php.
[433]Rolando Lozano, "Crisis financiera no impidió nuevos movimientos empresariales en el país," December 12, 2008, available at: http://www.portafolio.com.co/negocios/empresas/2008-12-12/ARTICULO-WEB-NOTA_INTERIOR_PORTA-4719909.html.
[434] Burns de Colombia is a subsidiary of Securitas AB (Sweden).
[435] "Crisis económica afecto la inversión y los negocios en Latinoamérica," *Cambio*, February 10, 2010, available at: http://www.cambio.com.co/economiacambio/865/ARTICULO-WEB-NOTA_INTERIOR_CAMBIO-7111547.html.

coming from Europe plummeted from US$ 392 million in 2008 to disinvestments of US$ 1,532 million in 2009. (annex table 4)

The policy scene

By law,[436] foreign investment in Colombia is governed by three basic principles: 1) universality, 2) automatic authorization and 3) equality of treatment. Given these principles, foreign investment is subject to the same treatment as domestic investment. The only sectors with restrictions for foreign capital are:

- activities concerning national defense and security;
- the treatment and disposal of toxic, dangerous or radioactive waste not produced in Colombia; and
- broadcast services, in which foreign investment cannot exceed 40% of the total capital of a dealership.

One of the main policy pillars of the Government of President Álvaro Uribe Vélez over the past eight years was to improve the business environment and the protection of investors' rights and interests. The Government entrusted the official national agency for promotion of exports, Proexport, with the task of promoting FDI by endorsing industrial sectors with potential high economic and employment growth. Several regional agencies, such as Probarranquilla, the Agency of Cooperation and Investment of Medellín, and Invest in Bogotá, have also started ambitious plans to bring investors to their cities and regions. The latter agency was recently ranked as the 16th best investment promotion agency worldwide out of 216 agencies in a study performed by the World Bank.[437]

Simultaneously, the Ministry of Commerce, Industry and Tourism, along with Proexport, were inquiring for a successful policy model to benchmark and draft the country's own policies turning its attention to Ireland. Consequently, the Government drew important lessons from the Irish model and shaped several policies accordingly in order to achieve similar results.[438]

One of the first reforms to improve the business environment and the investor-protection practices was the creation of Legal Stability Agreements (LSA). These agreements, effective for up to 20 years,[439] protect investors against changes that could be made in the future to laws, regulations or rulings impacting negatively their operations.

Furthermore, in addition to investment incentives concerning tax exemption in the sectors of hotels and ecotourism services, late yield crops, medical and software products, aeolian, biomass and agricultural energy generation, and publishing companies, the Government introduced significant changes to the tax system with the creation of law 1111 of 2006. The law allowed the Government to lower the corporate income tax rate from an effective rate of 38.5% to 34% in 2007 to 33% in 2008.

[436] Law 9 of 991, "Nuevo estatuto cambiario," January 17, 1991.
[437] World Bank, *Global Investment Promotion Benchmarking 2009* (Washington: The World Bank, 2009).
[438] For further information refer to "Misión de Colombia de alto nivel estudiará en Dublin el "Milagro Irlandés", Presidencia de la Republica, Bogotá, February 2008, available at: http://web.presidencia.gov.co/sp/2008/febrero/29/21292008.html.
[439] Law 963 of 2005. Ley de estabilidad Jurídica, July 8, 2005.

Colombia has multiple free trade zones, where companies can benefit from a lower (15%) corporate income tax.[440] The Government, in a further effort to gain competitiveness, created "single enterprise" free trade zones (SEFTZ), where companies complying with certain requisites of investment and job creation can establish themselves as SEFTZ anywhere in the country with the same benefits that a regular permanent free trade zone. During 2007–2010, 39 zones were approved and nine more were awaiting approval from the tax authority, the Departamento de Impuestos y Aduanas Nacionales (DIAN).[441]

Recently, as part of the tax reform passed on December 30, 2009,[442] changes in the fixed assets investment deduction were introduced; these reforms affect companies located in free trade zones.[443] Finally, in 2010, Colombia added three FTAs to the three already in place, with the United States, Canada and the European Free Trade Association (EFTA).[444] Colombia has signed international conventions for the protection of FDI with the Multilateral Investment Guarantee Agency (MIGA), the International Centre for Settlement of Investment Disputes (ICSID), the Overseas Private Investment Corporation (OPIC), and the Program for Cooperation in Upcoming Markets (PSOM). According to official statistics, in 2010, Colombia will be negotiating nineteen international investment agreements with 39 countries and 21 double taxation treaties (DTTs) with 22 countries. So far, the country has already signed DTTs with Canada, Chile, Mexico, the Andean Community of Nations (CAN), Spain, and Switzerland.[445] The rising numbers of agreements negotiated are based on the Government's desire to globalize the Colombian economy, which was lacking bilateral and multilateral tools to foster the country's competitiveness.

Conclusions and Outlook

The new president, Juan Manuel Santos Calderón, has clearly stated that foreign investors can expect a smooth transition, as transparent and business-friendly rules will be maintained during his mandate. Certain goals that were not reached during Mr. Uribe's terms, including achieving investment grade from international rating agencies and the implementation of the FTA with the United States, are expected to be achieved under Mr. Santos's mandate.

Although tax benefits are seen by some analysts as unfair and distortive incentives, it is unlikely that the new Government will dismantle them, as it could be a signal of a volatile and unstable legal environment, an image that the country is trying to leave behind.

The return of IFDI to the country is good news for Colombia, and all factors are coming together to maintain the country as an attractive location for investment. Hence, it is important for policy makers to step up projects and programs and create a better business environment, if they want to make Colombia a really first-class location for foreign firms.

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[440] The most important change of the FTZ regime was to allow companies located within a FTZ to sell goods without any limit to the domestic market. Before 2005, enterprises in a FTZ were allowed to sell their goods exclusively abroad.
[441] Ministerio de Industria y Comercio.
[442] Tax Reform Act No. 1370-2009.
[443] In the past, a company investing in fixed assets was entitled to a 40% deduction in its income tax. With the tax reform, the deduction is reduced to 30%. However, free trade zones' income taxpayers eligible for the reduced 15% income tax rate are not entitled to benefit from the 30% fixed assets investment income tax deduction, as the Congress deemed both benefits to erode fair competition.
[444] The US Free Trade Agreement has been signed by the Colombian Congress and is awaiting ratification by the US Congress. The Canada-Colombia FTA was signed in 2008; Canada's legislature approved this FTA in June 2010 and, as of September 2010, it was awaiting approval from the Colombian Congress. Finally, the FTA with the European Free Trade Association was signed by both parties in 2008 and approved by the Colombian legislature in June 2009, but it was still not in force in August 2010.
[445] Proexport, Ministerio de Industria y Comercio (Bogotá: 2010).

Infrastructure has to be improved. Colombia has relied for years on the promotion of the country as a low-cost location, but this strategy has its limits. Low income countries might find tax incentives a successful tool to attract FDI but in the long run countries with good infrastructure will have a competitive edge and will attract most FDI.[446] The legal framework also needs some improvement. In spite of the Government's efforts, paying taxes and starting a business can be a complicated, lengthy and burdensome process. An education system of high quality, oriented toward relevant skills, would allow Colombia to meet MNEs' needs of specific talent at every level and attract more high value-added operations. Finally**,** easier access to finance is an imperative. Currently, foreign companies are prohibited from holding bank accounts in foreign currency, a restriction only shared with Brazil and Venezuela.

Additional readings

Bénassy-Quéré, Agnes, Nicolas Gobalraja and Alain Trannoy, "Tax and public input competition," 22 *Economic Policy* 385 (Paris: CEPII, Centre d'Etudes Prospectives et d'Info. Internationales, 2007).

World Bank, *Global Investment Promotion Benchmarking 2009* (Washington: World Bank, 2009).

ECLAC, *La Inversión Extranjera Directa en América Latina y el Caribe* (Santiago de Chile: ECLAC, 2010).

World Bank, *Doing Business 2010: Colombia* (Washington: World Bank, 2009).
Rendón Acevedo, Jaime Alberto, "Los impactos de la inversión extranjera directa en la economía colombiana: el caso de la industria de bebidas," 9(18) *Semestre Económico* 11 (Medellín: Universidad de Medellín, 2006).

Proexport, PricewaterhouseCoopers, *Doing Business and Investing in Colombia* (Bogotá: Proexport, PricewaterhouseCoopers, 2010).

Useful websites

For National Economic and Social Statistics: National Department of Statistics, available at: www.dane.gov.co.
For economic statistics: Banco de la Republica, available at: www.banrep.gov.co.
For FDI statistics and operational costs: Proexport, available at:
http://www.investincolombia.com.co.
For International Trade information: Ministry of Commerce, Industry and Tourism, available at: www.mincomercio.gov.co.

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[446] As suggested in C. Bellak, M. Leibrecht and J. Damijan, "Infrastructure endowment and corporate income taxes as determinants of foreign direct investment in Central and Eastern European Countries", *The World Economy*, vol. 32, issue 2 (2009), pp. 267-290; and Agnès Bénassy-Quéré, A., N. Gobalraja and A. Trannoy, "Tax and public input competition," 22 *Economic Policy* 385 (Paris: CEPII, Centre d'Etudes Prospectives et d'Info. Internationales, 2007).

Statistical annex

Annex table 1. Colombia: inward FDI stock, 2000-2009 (US$ billion)

Economy	2000	2008	2009
Colombia	11	67	74
Memorandum: comparator economies			
Brazil	122	288	401
Venezuela	35	43	41
Peru	11	30	37

Source: For Colombia, Banco de La República, Exchange Balance (Bogotá: Banco de la Republica, May 2010). For comparator economies, see UNCTAD's FDI/TNC database, available at: http://stats.unctad.org/fdi/.

Annex table 2. Colombia: inward FDI flows, 2000-2009 (US$ billion)

Economy	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009[a]	2010[a]
Colombia	2.4	2.5	2.1	1.7	3.0	10.3	6.7	9.1	10.6	7.2	2.1
Memorandum: comparator economies											
Brazil	32.8	22.5	16.6	10.1	18.2	15.1	18.8	34.6	45.1	22.8	n.a.
Venezuela	4.7	3.7	0.8	2.0	1.5	2.6	-0.6	0.6	1.7	n.a.	n.a.
Peru	0.8	1.1	2.2	1.3	1.6	2.6	3.5	5.5	4.8	6.2	n.a.

Source: Banco de la República, Balance of Payments (Bogotá: Banco de la República, June 2010) for 2000-2009 data, for comparator economies see UNCTAD's FDI/TNC database, available at: http://stats.unctad.org/fdi/.
[a] Preliminary

Annex table 3. Colombia: distribution of inward FDI flows, by economic sector and industry, 2000-2009 (US$ million)

Sector / industry	2000	2009[b]	2000-2005[a]	2006-2009[a]
All sectors / industries	**2,436**	**7,201**	**1,606**	**3,770**
Primary	**123**	**5,742**	**614**	**2,167**
Agriculture, forestry, and fishing	0	14	2	12
Mining, quarrying and petroleum	123	5,727	612	2,155
Mining and quarrying	507	3,094	406	860
Petroleum	-384	2,633	206	1,294
Secondary	**535**	**822**	**524**	**688**
Manufactures	556	536	526	569
Construction	-21	286	-2	119
Services	**1,179**	**638**	**445**	**915**
Commerce, restaurants, hotels	10	644	81	345
Utilities	13	-977	-2	-121
Transport, warehouse and communications	876	337	204	267
Financial establishments	792	549	153	400
Communal services	88	85	9	25

Source: Banco de la República, "Balance of payments" (Bogotá: Banco de la República, June 2010).
[a] Average
[b] Prelimiary

Annex table 4. Colombia: geographical distribution of inward FDI flows, 2000-2009
(US$ million)

Region/economy	2000	2009[b]	2000-2005[c]	2006-2009[c]
World	**3,266.1**	**2,669.3**	**2,987.4**	**3,619.8**
Developed economies	**2,158.8**	**904.4**	**2,054.4**	**1,588.7**
Europe	**1,369.5**	**-1,531.6**	**1,278.9**	**-212.4**
European Union	**1,317.0**	**-1,598.6**	**1,245.1**	**-206.9**
United Kingdom	405.0	385.6	732.0	159.4
France	2.9	113.0	30.8	81.6
Luxembourg	105.2	99.6	21.9	55.6
Sweden	15.6	32.4	10.8	8.5
Spain	479.2	-326.9	272.9	254.5
Netherlands	156.2	-1,859.2	125.9	-849.6
North America[d]	**784.2**	**2,400.6**	**760.9**	**1,783.7**
Canada	663.9	78.3	146.6	39.2
United States	120.3	2,313.6	614.2	1,742.1
Other developed economies	**5.1**	**35.4**	**14.6**	**17.5**
Australia	0.0	34.6	4.5	11.6
Japan	5.1	0.7	10.1	5.9
Developing economies	**1,125.2**	**1,764.9**	**933.0**	**2,023.2**
Asia and Oceania	**4.5**	**2.1**	**4.4**	**12.6**
China	4.5	0.3	2.3	0.0
India	0.0	0.5	0.0	2.4
Latin America and Caribbean	**1,120.7**	**1,760.2**	**928.7**	**2,010.6**
Bermuda	253.4	287.1	216.5	84.6
Brazil	4.6	47.4	5.4	180.2
Chile	9.7	53.7	10.2	36.6
Mexico	23.1	202.8	192.3	246.6
Panama	259.0	337.1	130.3	453.4
Virgin Islands	488.8	4.6	240.9	108.0
Profit reinvestments	**-445.8**	**1,898.7**	**282.1**	**1,914.2**
Petroleum sector	**-383.9**	**2,633.1**	**413.9**	**2,838.2**

Source: Banco de la República, Balance of Payments (Bogotá: Banco de la República, June 2010).
[a] Excluding petroleum and profits reinvestments.
[b] Preliminary.
[c] Average.
[d] Including Puerto Rico

Annex table 5. Colombia: principal foreign affiliates in country, ranked by sales and assets, 2009 (US$ million)

Rank	Name of affiliate	Industry	Sales	Assets
1	Almacenes Exito	Wholesale distribution	3,233	3,094
2	Exxon Mobil Colombia	Oil and gas operations	2,272	512
3	Telefonica Colombia	Telecommunications	1,773	4,364
4	Carrefour Colombia	Wholesale distribution	1,726	1,703
5	Bavaria	Beverages	1,717	4,757
6	Avianca	Transport	1,621	1,581
7	Drummond	Coal	1,508	2,316
8	Chevron Petroleum	Natural gas	1,224	692
9	GM Colmotores	Automotive	1,047	554
10	Alkosto	Wholesale distribution	780	527

Source: La nota económica, *Empresas Platinum de Colombia 2009*.

Annex table 6. Colombia: main M&A deals, by inward investing firm, 2007-2009
(US$ million)

Year	Acquiring company	Home economy	Target company	Target industry	Shares acquired (%)	Estimated/ announced transaction value
2009	Vale	Brazil	Cementos Argos SA-Coal Mine	Cement, hydraulic	100.0	373.0
2009	Kimberly-Clark Corp	United States	Colombiana Kimberly Colpapel	Sanitary paper products	100.0	289.0
2009	Investor Group	Chile	Bavaria SA-Agua Brisa Bottled	Bottled & canned soft drinks & carbonated waters	100.0	92.0
2009	Cencosud	Chile	Easy Colombia SA	Grocery stores	100.0	60.0
2008	GE Money	United States	Banco Colpatria SA	Banks	39.3	227.95
2008	Pacific Rubiales Energy Corp	Canada	Kappa Energy Holdings Ltd	Crude petroleum and natural gas	100.0	168.0
2008	Indura SA	Chile	Cyrogas SA	General industrial machinery and equipment	100.0	139.2
2008	Brysam Global Partners	United States	Banco Caja Social SA	Banks	18.8	101.7
2007	Telefonica SA	Spain	Colombia Telecomunicaciones SA	Telephone communications, except radiotelephone	50.0	2,627.2
2007	Ashmore Energy Intl Ltd	United States	Promigas SA	Natural gas transmission	52.9	510.0
2007	Grupo Votorantim	Brazil	Acerias Paz del Rio SA	Steel works, blast furnaces, and rolling mills	51.9	488.6
2007	Groupe Casino	France	Almacenes Exito SA	Grocery stores	61.5	326.6

Source: Thomson ONE Banker, Thomson Reuters.

Annex table 7. Colombia: main greenfield projects, by inward investing firm, 2007-2009
(US$ million)

Year	Investing company	Home economy	I Industry	Estimated/ announced investment value
2009	Xstrata	Switzerland	Bituminous coal and lignite	1,962
2009	Vale	Brazil	Bituminous coal and lignite	305
2009	Grupo Cisneros	Venezuela	Entertainment	250
2008	Glencore International	Switzerland	Coal, oil and natural gas	3,000
2008	Votorantim Group	Brazil	Metals	1,500
2008	Endesa	Spain	Alternative/renewable energy	900
2007	Millicom International Cellular	Luxembourg	Communications	500
2007	ED&F Man	United Kingdom	Food and tobacco	270
2007	Ample Auto	China	Automotive OEM	323

Source: fDi Intelligence, a service from the Financial Times Ltd.; Proexport, "Inversion extranjera directa en Colombia, business analysis."

Chapter 18 – India

Inward FDI and its policy context, 2010

Premila Nazareth Satyanand and Pramila Raghavendran

A minor global FDI player in 2000, India is now the world's thirteenth largest FDI host country. With 2008 inflows of US$ 42 billion and 2009 inflows of US$ 27 billion, it is also a global top three preferred investment destination. Notable liberalizations in FDI policy and in several economic sectors, a globally competitive workforce, and rapid GDP and market growth are the main drivers of foreign investment in India. Yet, equity caps limit the size of potential new inflows, while national security concerns might prompt more oversight of FDI approval processes.

Trends and developments

Average annual foreign direct investment (FDI) inflows into India have grown fifteen-fold since 2000. While, initially, investors concentrated in manufacturing, power and telecommunications, they now focus in services activities. Developed country firms dominated investment in the 1990s, but in the past decade developing country investors have also become significant.

Country level developments

India had received some US$ 169 billion of cumulative FDI inflows by the end of 2009 since it first opened itself to foreign direct investors in 1991 (annex table 1). Though India's IFDI stock is considerably smaller than those of the BRIC countries and other counterparts (annex table 1), its post-2004 inflows have grown two times faster than Brazil's and four times faster than China's (annex table 2a), pointing to fundamental shifts in the Indian economy and global investor perceptions about India.

Annual FDI inflows averaged US$ 2 billion a year in the 1990s (annex table 2b) but, starting 1997, policy liberalizations in the telecommunications, infrastructure and insurance sectors caused average annual inflows to double to US$ 4 billion between 2000 and 2005.

From 2005 onwards, further liberalizations – including the opening up of real estate to FDI, the raising of the telecom equity cap to 74% and a variety of sectoral policy reforms – triggered another upward shift in FDI flows. Inflows rocketed to US$ 20 billion in 2006, further doubling to US$ 42 billion in 2008, transforming India into the world's thirteenth largest host to FDI globally.[447] The global economic and financial crisis reduced 2009 inflows to US$ 27 billion, but these were nonetheless larger than 2007 levels.

Which sectors draw the most FDI?

Currently, some 61% of India's annual FDI inflows go into the services sector, while manufacturing receives 27% and primary sector activities, mainly mining and petroleum,

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[447] UNCTAD, *World Investment Report 2009: Transnational Corporations, Agricultural Production and Development* (Geneva: UNCTAD, 2009).

some 9% (annex table 3). In this respect, India's service-dominated FDI inflows parallel those of Brazil, and contrast with those of China and Russia where manufacturing is dominant.

Ten years ago, in 2000, 45% of all FDI inflows went into manufacturing, with services attracting just 17% and the primary sector less than 1%.[448] The importance of the manufacturing sector was due to the earlier opening up of this sector to foreign investment in 1991, while most services and primary sector activities remained closed until the end of that decade. As more services (particularly insurance, banking, construction, and real estate) were liberalized, inflows into these activities burgeoned (annex table 3).

Services account for the largest share – a fifth – of the cumulative FDI stock since 2000, totaling US$ 23 billion.[449] Computer hardware/software, telecommunications, housing, real estate, and construction follow, in that order.[450] Other key sectors are power, automobiles, metallurgical industries, petroleum and natural gas, and chemicals. Since 2005, inflows into "sunrise" and newly-opened sectors have also jumped, among them non-conventional energy and the electronic and print media.

As the size of inflows, the number of investors, and India's strategic importance have grown, so has FDI's developmental impact on the Indian economy. According to a recent Government study,[451] foreign affiliates pay higher wages and are more productive than purely domestic firms. They are also now more export[452] and R&D[453] intensive than domestic firms, in striking contrast to the mid-1990s when these two groups displayed no statistically significant difference.[454] They have also helped to build skills and new technology and R&D capabilities through a variety of organic local linkages with suppliers, contractors and others. In the manufacturing sector alone, foreign affiliates directly or indirectly employ 1.6 million workers; over a half are in small cities and semi-urban areas. Transport equipment, crop growing and processing, construction parts, textiles, and non-metallic mineral products employ the highest number of small town workers.[455]

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[448] Due to shortcomings in the Indian Government's FDI data, it is impossible to account for the sectoral direction of 38.5% of the 2000 inflows, as annex table 3 indicates.
[449] FDI stock data until November 2009.
[450] These three activities have together received some US$ 15 billion, most of it after 2005, when housing and real estate were opened to FDI.
[451] National Council for Applied Economic Research, *FDI in India and its Growth Linkages* (New Delhi: NCAER, 2009), available at: http://www.dipp.nic.in/ncear_Report/FDI_NCAER.pdf.
[452] Aradhna Aggarwal, "Liberalization, multinational enterprises and export performance: evidence from Indian manufacturing," *Journal of Development Studies* 38 (3) (2002), pp. 119–137.
[453] Nagesh Kumar, and Aradhna Aggarwal, "Liberalization, outward orientation and in-house R&D activity of multinational and local firms: a quantitative exploration for Indian manufacturing," *Research Policy* 34(4) (2005), pp. 441–460; Jaya Prakash Pradhan, "R&D strategy of small and medium enterprises in India: trends and determinants," *Munich Personal RePEc Archive Paper,* No. 20951 (2010); Nagesh Kumar and Jaya Prakash Pradhan, "Knowledge-based Exports from India: A Firm-level Analysis of Determinants," in Nagesh Kumar and KJ Joseph, eds., *International Competitiveness & Knowledge-based Industries* (New Delhi: Oxford University Press, 2007), pp. 53–96.
[454] Nagesh Kumar and N.S. Siddharthan, "*Technology, firm size and export behaviour in developing countries: the case of Indian Enterprises," The Journal of Development Studies* 31 (1994), pp. 289-308.
[455] According to the study, sectors with the strongest backward linkages include electrical equipment, drugs and pharmaceuticals, food processing and textiles; those with the strongest forward linkages are service sectors, telecommunications, and consultancy services; and those with both types of linkages are construction, fuels, chemicals, and metallurgical industries.

From where does FDI come?

Mauritius excluded,[456] Singapore is currently India's largest inward foreign direct investor, accounting for 17% (US$ 9 billion) of cumulative post-2000 inflows. The United States follow with 14% (US$ 7.6 billion) and the United Kingdom with 10% (US$ 5.5 billion). Other key investors are the Netherlands, Japan, Germany, France, and the United Arabian Emirates. Interestingly, Singapore is also the largest host to cumulative Indian OFDI, followed by the Netherlands, the United States, Mauritius, and the United Kingdom.

Singapore's current pre-eminence reverses the 1990s pattern of dominance of developed country firms, especially from the United States and Japan (annex tables 5a and 5b). Starting in 2000, inflows from developing countries have begun to grow, since their firms often have a cost and operating advantage in India's newly-opened economic sectors. Many of their products and services are cheaper and more relevant to the Indian consumer than those of many developed country firms, and they are used to operating in an emerging market environment. For instance, FDI liberalization in the real estate sector expanded United Arabian Emirates inflows from US$ 0.75 million in 2000 to US$ 239 million in 2008. Similarly, Malaysian firms are now very active in highway and urban water projects.

Home country shifts have, in turn, both driven and emanated from sectoral changes. Thus, while early United States' and Japanese investments concentrated in manufacturing and power, Singapore's investments focus on telecommunications, services, shipping, and oil refining (annex tables 5c offers a glimpse into the sectoral variety of the largest FDI projects of this past decade). BIT protection and economic cooperation agreements have also played a role. As government FDI data show, Singapore's investment stock tripled[457] after its Comprehensive Economic Cooperation Agreement with India in 2005.

Where does FDI go, and in what form does it come?

A third of the post-2000 inflow is invested around Mumbai, a manufacturing hub, and one-fifth around Delhi, a services hub. Ahmedabad, Bangalore, Chennai, and Hyderabad are other key destinations.[458]

Eighty percent of post-2000 FDI inflows have been in the form of greenfield investments.[459] The average investment size also quadrupled from US$ 9 million to US$ 34 million over this period.[460] While the largest recent greenfield investments span various sectors (annex table 4), the largest recent M&As focus on telecommunications, energy and pharmaceutics/healthcare (annex table 6).

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[456] FDI inflows from Mauritius are excluded. These inflows account for 42% of total inward FDI into India and from "unspecified destinations." Mauritius provides tax exemption for foreign companies setting up businesses in the country. This, along with its double taxation agreement with India, gives greater tax advantage to companies routing their Indian investments through Mauritius. Cyprus, accounting for 5% of current inflows, is also emerging as an attractive destination for routing investments into India for similar reasons. Many investments from these locations also appear to be instances of "round-tripping".

[457] Singapore's total investment in India was US$ 3 billion in 2005; it is now US$ 9 billion.

[458] These four cities have each received an average of about 5% of the total post-2000 inflows. However, it is important to note that there are no data available on the geographic distribution of about a fifth of the inflows since 2000.

[459] The total amount of greenfield investments rose from US$ 2.3 billion in 2000 to US$ 33 billion in 2008, and US$ 15 billion by end-of September 2009.

[460] These figures are based on data from UNCTAD's *World Investment Report* 2009, op. cit., and the National Council for Applied Economic Research's op. cit.

Effects of the current global crisis

The global financial and economic crisis has hit inbound M&A activity in India the most. While 2007 and 2008 each saw an average of 99 inbound M&A deals, totaling an average of US$ 14 billion, 2009 saw just 53 M&As amounting to US$ 2.25 billion. As annex table 5 shows, 2009's largest M&As were considerably smaller than their predecessors in 2007 and 2008.

Although the global crisis has slowed the rate of FDI growth into India in 2009, it has reinforced India's position in global investor perceptions. Since most global firms found that their Indian and Chinese operations considerably outperformed their developed market investments, they now accord even greater strategic value to these two destinations.[461]

The policy scene

In India, all except four[462] sectors are open to FDI, and most investors no longer need to seek investment approvals.[463] Furthermore, current account transactions are now completely convertible.[464] However, equity caps remain in strategic sectors such as telecommunications, insurance, banking, airlines, and media and broadcasting for national security reasons.

In early 2009, the Government of India liberalized the manner in which it calculates "Indian" versus "foreign" equity. It eased investment between Indian firms with foreign shareholders, particularly in equity-capped sectors, while strengthening local management control.[465] Now, companies with less than 50% foreign equity will be regulated as "Indian" and any downstream investments will not be regulated as "foreign" equity, and vice-versa. However, a change from "Indian" to "foreign" control will need governmental approval in sectors subject to equity caps, most particularly in sensitive sectors like telecommunications, insurance, defense, airlines, and broadcasting and media.

Other liberalization measures appear to be on the anvil, following the Communist Party's defeat in the 2009 general election. Most notable is a bill to permit foreign universities to set up branches in India. The Government might also find it politically possible gradually to liberalize the equity caps in insurance, broadcasting and print media. The Indo-US nuclear deal should trigger FDI relaxations in defense and atomic energy, since it creates a variety of commercial opportunities for Indian firms. Retail is the only sector in which further liberalization does not seem imminent, due to widespread fears that an opening up of this sector would destroy India's "corner store" industry and create widespread unemployment.

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[461] UK Department of Trade and Industry and EIU, *Survive and Prosper: Emerging Markets in the Global Recession* (London: DTI and EIU, 2009); press reports.

[462] Retail trading, atomic energy, gambling and betting, and agriculture and plantations. However, while FDI is prohibited in multi-brand retailing, it is permitted up to 51% of equity in single-brand retailing. Similarly, 100% FDI is allowed in horticulture, floriculture, animal husbandry, pisciculture, and seed development, as also in tea plantations, on a case-by-case basis. In 2009, the 24% cap on FDI in small enterprises (with capital expenditure of up to US$1 million) was also raised to 100%.

[463] Clearances are required for projects in which (1) an industrial license is required, (2) where the foreign collaborator has an existing local joint venture in the same sector, (3) the local joint venture is defunct, or "sick," as defined by Indian law, or (4) investments are being made by a venture capital fund.

[464] There are still some restrictions on capital account transactions.

[465] Earlier rules had made it complicated for Indian firms, with foreign investment, particularly in the telecommunications and financial services sectors, to improve competitiveness through strategic investments in other domestic companies.

Border tensions with China, and the growth in FDI through tax havens, have triggered Government thinking on FDI protectionist measures, such as the tightening of investment approval procedures[466] and the possible enactment of a national law to empower the Government to ensure that national security is not compromised by FDI projects. There have also been rising local and political concerns about large FDI projects (particularly in mining) that involve land acquisition, resettlement and significant environmental impact.

India has thus far signed 75 bilateral investment protection agreements,[467] 60 double taxation avoidance agreements, and a number of comprehensive economic partnership agreements.[468] The number of investment disputes has dropped since the 1990s. While, initially, the dominant issue was breach of contract, it now is taxation, as in the much-publicized Vodafone case.[469]

Conclusions and Outlook

India's attractive GDP growth rate[470] and superior market performance are likely to attract growing FDI inflows.[471] CEOs consistently rank India as one of the world's top 3-5 preferred investment destinations in recent global surveys.[472] Despite the crisis, a number of leading global firms – including Volkswagen, Telenor, LG, Cairn, and a number of IT companies - have announced large-scale investments in various sectors. In contrast to the favorable development of economic drivers of IFDI, the security-induced tightening of approval procedures and oversight policies might limit the potential inflow of FDI, as might the difficulty in obtaining operational clearances.[473]

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[466] According to press reports, the following measures are being suggested: (1) Investments from tax havens into "sensitive" sectors must obtain governmental approval; (2) the approval process should involve security agencies; (3) post-approval cancellations should be permitted; and (4) India should expand the list of countries from which it restricts FDI.

[467] 66 of these are already in force.

[468] India is now finalizing or negotiating 25 more investment protection agreements, including with the United States, Brazil, Canada, Norway, and the UAE.

[469] In 2007, Vodafone bought out Max Hutchison's assets in Hutch Essar, one of India's largest mobile phone companies. Though the financial transaction occurred overseas, the Indian Government holds that Vodafone should pay capital gains on this transaction, since the assets are in India.

[470] As of late 2009, India's GDP growth had been between 6 -7%.

[471] DTI and EIU, 2009, op. cit.

[472] These surveys were conducted by EIU, UNCTAD, AT Kearney, and others.

[473] Given India's federal policy, state governments have the power operationally to hold up FDI projects cleared by the national Government. For this reason, a national FDI law (replacing the existing plethora of state and sectoral regulation with a single legal instrument) might be very useful.

Additional readings

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Government of India, *Technical Monitoring Group on Foreign Direct Investment: First Action Taken Report* (New Delhi: Department of Industrial Promotion and Policy, Ministry of Commerce and Industry, 2003).

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Singh, Kulwindar, "Foreign direct investment in India: a critical analysis of FDI from 1991-2005," *New Delhi Centre for Civil Society Working Paper* (2005), available at: http://ssrn.com/abstract=822584.

Useful websites

For FDI policy and regulation: Government of India, Ministry of Commerce and Industry (www.dipp.nic.in) and India Brand Equity Foundation (www.ibef.org).
For Government FDI statistics: Secretariat of Industrial Approvals, Ministry of Commerce and Industry (www.dipp.nic.in/fdi_statistics/india_fdi_index.htm).

Annex table 1. India: inward FDI stock, 2000, 2008, 2009 (US$ billion)

Economy	**2000**	**2008**	**2009**
India	**18**	**123**	**169**
Memorandum: comparator countries			
Brazil	122	288	…
China	193	378	…
Russia	32	214	…
Singapore	111	326	…

Source: Based on UNCTAD, *World Investment Report 2009: Transnational Corporations, Agricultural Production and Development* (New York and Geneva: United Nations, 2009), and Secretariat for Industrial Assistance, Government of India.

Annex table 2a. India: inward FDI flows in comparison, 2000-2009 (US$ billion)

Economy	**2000**	**2001**	**2002**	**2003**	**2004**	**2005**	**2006**	**2007**	**2008**	**2009**
India	**2.3**	**3.4**	**3.5**	**4.3**	**5.3**	**6.7**	**20.3**	**25.1**	**41.6**	**27.0**
Memorandum: comparator countries										
Brazil	32.8	22.5	16.6	10.1	18.2	15.1	18.8	34.6	45.1	22.8 [a]
China	40.8	46.9	52.7	53.5	60.6	72.4	72.7	83.5	108.3	90.0 [a]
Russia	2.7	2.5	3.5	8.0	11.7	12.8	29.7	55.1	70.3	41.4 [a]
Singapore	12.5	11.0	5.8	9.3	16.1	15.0	27.7	31.6	22.7	18.3 [a]

Source: UNCTAD, *World Investment Reports 2003, 2005, 2007 and 2009; and* Secretariat for Industrial Assistance, Department of Industrial Promotion and Policy, Ministry of Commerce and Industry, Government of India.
[a] Estimated.

Annex table 2b. India: inward FDI flows, 1991-1999 (US$ billion)

Economy	**1991**	**1992**	**1993**	**1994**	**1995**	**1996**	**1997**	**1998**	**1999**
India	0.2	0.3	0.6	1.0	2.1	2.5	3.6	3.4	2.4

Source: Secretariat for Industrial Assistance, Department of Industrial Promotion and Policy, Ministry of Commerce and Industry, Government of India.

Annex table 3. India: sectoral breakdown of FDI inflows,[a] 2000 and 2008 (US$ million and percent of total inflows)

Foreign company	**Home country**	**Indian company**	**Value** *(US$ billlion)*	**Industry**

Sector / industry	**2000**	**2008**	**2009 [b]**
All sectors / industries	**2347.1**	**33,029.3**	**27,044**
Primary	**2.8 (0.12%)**	**1420.9 (4.3%)**	**2397 (8.86%)**
Agriculture, forestry, and fishing	0.1	10.7	1307
Mining, quarrying and petroleum	2.7	1410.2	545
Mining and quarrying	0.8	42.7	171
Petroleum	1.9	1367.5	374
Secondary (manufacturing) [c]	**1051.8 (44.8%)**	**10156.4 (30.8%)**	**7223.1 (26.7%)**
Automobile industry	279.7	1134.1	1338.4
Drugs & pharmaceuticals	48.4	263.7	205.1
Industrial machinery	4.9	154.2	193.4
Chemicals(other than fertilizers)	125.1	602.1	451.4
Textiles	1.9	204.0	198.5
Paper & pulp and paper products	60.5	227.4	59.6
Food processing industries	51.7	150.4	202.5
Cement & gypsum products	73.9	674.9	80.7
Ceramics	1.9	223.3	5.8
Electronics	8.1	169.7	34.9
Computer software & hardware	194.4	1,828.0	717.0
Power	110.7	1,339.3	1643.3
Services	**388.2 (16.5%)**	**19812.1 (60%)**	**16598 (61.4%)**
Financial services	43.3	8043.8	1570.0
Telecom services	79.7	2577.8	2557.7
Information & Broadcasting(including Print Media)	79.7	539.3	782.8
Ports	-	1,404.5	72.3
Consultancy services	4.9	364.7	420.1
Hotel & tourism services	12.2	539.0	592.9
Trading	28.8	654.6	524.8
Construction activities	23.1	2484.3	2459.6
Housing & real estate	-	2679.0	3198.8
Unspecified other sectors/industries	**904.2 (38.5%)**	**1639.8 (5%)**	**825.5 (3.0%)**

Source: Secretariat for Industrial Assistance, Department of Industrial Promotion and Policy, Ministry of Commerce and Industry, Government of India.

[a] Inflows are equity inflows; reinvested earnings are not available sector-wise.

[b] Data up to November 2009.

[c] Secondary sectors listed are selective.

Annex table 4. India: top 20 greenfield investments, June 2006- September 2009 [a]

TMI, Mauritius	Mauritius	Idea Cellular	1.6	Telecommunications
Cairn UK Holding	United Kingdom	Cairn India	1.5	Power and energy
Mauritius Debt Management	Mauritius	India Debt Management Ltd.	0.95	Financial services
Coca Cola Singapore	Singapore	Hindustan Coca Cola	0.84	Beverages
Vodafone Mauritius	Mauritius	Bhaik Infotel	0.8	Telecommunications
Morgan Stanley Investment Managment	Mauritius	Morgan Stanley India	0.7	Financial services
Etisalat Mauritius	Mauritius	Etisalat DB Telecom	0.66	Telecommunications
CMP Asia	Mauritius	Housing Development Finance Corporation	0.65	Financial services
Biometrix Marketing	Singapore	Reliance Gas Transportation Infrastructure	0.6	Oil refinery; transportation
Horizon	Netherlands	Emaar MGF Land	0.43	Housing and real estate
Barclays Bank	Singapore	AAA Global Ventures	0.37	Financial services
Sistema Joint Stock Financial Corp.	Russia	Shyam Telelink	0.3	Telecommunications
Travorto	Cyprus	Tata Capital	0.29	Financial service
Fiat Auto	Italy	Fiat Automobiles; Fiat India	0.26	Automobiles
Volvo	Sweden	VE Commercial Vehicles	0.22	Automobiles
HSBC Investment Bank Holdings	Mauritius	HSCB Security and Cap Market	0.19	Banking
Walt Disney (South East Asia)	Singapore	UTV Software Communication	0.17	Radio broadcasting
BOC Group	United Kingdom	BOC India	0.14	Industrial gases
FBG Holdings	Mauritius	Fosters India	0.16	Fermentation Industries
Suzuki Motor	Japan	Suzuki Motorcycle; Suzuki Power train	0.12	Automobiles; machine tools

Source: Secretariat for Industrial Assistance, Department of Industrial Promotion and Policy, Ministry of Commerce and Industry, Government of India, data on investment inflow transactions.

Annex table 5a. India: geographical source of inward FDI flows, 2000, 2008 and 2009

Country/ region	Shares in %			US$ million		
	2000	2008	2009 [a]	2000	2008	2009 [a]
World				**2,347.1**	**33, 029.32**	**27,044**
Developed economies	**56.2**	**26.9**	**20.9**	**1,318.0**	**8,871.7**	**8,117.8**
Europe	**27.9**	**19.4**	**16.2**	**655.3**	**6,415.1**	**4,715.7**
European Union	**23.8**	**18.6**	**15.4**	**559.9**	**6,157.4**	**4562.7**
Belgium	0.3	0.3	0.1	8.0	103.1	30.9
Cyprus	0.1	4.2	5.0	0.6	1,318.1	1609.60
France	3.4	1.5	1.1	79.4	467.9	296.9
Germany	3.7	2.4	2.0	79.4	788.8	599.9
Italy	5.8	1.1	0.4	135.6	366.2	150.8
Netherlands	5.4	3.1	2.9	127.2	988.9	832.8
Spain and Gibraltar	0.1	0.9	0.3	1.4	291.7	91.7
Sweden	2.5	0.3	1.1	59.2	92.8	245.4
United Kingdom	2.8	5.0	1.7	65.5	1,681.6	468.2
Other European countries	**4.1**	**0.8**	**0.8**	**95.4**	**257.7**	**152.96**
Switzerland	1.9	0.5	0.6	43.5	144.7	142.7
North America	**17.9**	**5.8**	**8.0**	**420.7**	**1,923.6**	**2,096**
Canada	0.1	0.4	02	2.2	126.4	45.2
United States	17.8	5.4	7.9	418.4	1,797.2	2051
Other developed countries	**10.3**	**1.6**	**4.8**	**242.1**	**533.0**	**1305.9**
Australia	0.4	0.2	0.2	9.5	71.4	40.2
Israel	-	0.1	0	-	15.1	1.3
Japan	9.8	1.2	4.5	229.2	405.1	1257.8
Developing economies	**43.5**	**58.6**	**59.5**	**1061.2**	**19355.0**	**16078.6**
Africa	**35.4**	**42.8**	**42.9**	**830.8**	**14,148.8**	**11,592**
Mauritius	35.4	42.8	42.7	829.9	14,138.1	11,536.2
Asia and Oceania	**7.6**	**13.6**	**15.8**	**182.2**	**4,487.9**	**4,185.24**
China	-	-	0.2	-	-	41.4
Hong Kong (China)	0.6	0.4	0.6	13.4	132.6	144.5
Indonesia	-	-	0.9	-	-	138.3
Malaysia	0.5	0.3	0.1	10.5	100.3	38.6
Republic of Korea	0.8	0.4	0.2	17.7	148.1	66.9
Singapore	5.0	11.3	11.8	116.6	3,763.5	3059.5
United Arab Emirates (UAE)	0.0	0.9	2.4	0.8	293.4	625.3

Commonwealth of Independent States	**1.7**	**1.0**	**0.06**	**41.05**	**322.0**	**16.6**
Kazakhstan	-	-	0.1	-	-	10.4
Russia	1.7	1.1	0.0	40.9	305.9	6.2
Latin America and Caribbean	**0.3**	**1.2**	**0.86**	**7.2**	**396.2**	**284.72**
Bermuda	0.1	0.1	0.05	2.8	33.11	10.1
British Virgin Islands	0.1	0.4	0.5	3.0	137.2	137.7
Cayman Islands	0.2	0.6	0.1	4.0	222.4	50.2
Chile	-	-	0.2	-	-	39.9
Unspecified destination	**0.1**	**8.5**	**8.1**	**2.2**	**2,853.9**	**2051.3**
Non-resident Indians	**0.0**	**5.9**	**3.3**	**0.2**	**1,948.8**	**791.9**

Source: Secretariat for Industrial Assistance, Department of Industrial Promotion and Policy, Ministry of Commerce and Industry, Government of India.

[a] January – November 2009.

[b] Inflows represent only equity capital, i.e. they do not include reinvested earnings, other capital and inter-company debts.

Annex table 5b. India: the 10 leading home countries; 2000, 2005, 2008, and 2009

2000 (US$4.5 bn)		**2005 (US$4.4 bn)**		**2008 (US$33 bn)**		**2009[a] (US$27 bn)**	
Country	**% and amount of inflows**	**Country**	**% and amount of inflows**	**Country**	**% and amount of inflows**	**Country**	**% and amount of inflows**
Mauritius	35% 823 mn	Mauritius	49% 2.1 bn	Mauritius	43% 14 bn	Mauritius	43% 11.5 bn
USA	18% 418 mn	USA	11% 472 mn	Singapore	11% 3.8 bn	Singapore	11% 3.1 bn
Japan	10% 229 mn	Singapore	7% 321 mn	USA	5% 1.8 bn	USA	7.6% 2.0 bn
Italy	6% 136 mn	U.K.	5% 219 mn	U.K.	5% 1.7 bn	Cyprus	6% 1.6 bn
Netherlands	5% 127 mn	Japan	4% 168 mn	Cyprus	4% 1.3 bn	Japan	5% 1.3bn
Singapore	5% 117 mn	Netherlands	3% 119 mn	Germany	2% 800 mn	Netherlands	3.1% 833 mn
Germany	3% 79 mn	Switzerland	2% 83 mn	France	1% 500 mn	U.A.E.	2.3% 625 mn
France	3% 79 mn	Germany	2% 83 mn	Japan	1% 400 mn	Germany	2.2% 600 mn
UK	3% 65 mn	Cyprus	2% 69 mn	Italy	1% 300 mn	U.K.	1.7% 468mn
Sweden	2.5% 59 mn	Republic of Korea	2% 66 mn	Russia	1% 300 mn	Sweden	0.9% 245mn
Unknown	0.1% 2.23mn	Unknown	3% 148mn	Unknown	9% 2.9 bn	Unknown	7.6% 2.0 bn
Non-resident Indians	0.01% 0.18mn	**Non-resident Indians**	1% 43mn	**Non-resident Indians**	6% 1.9 bn	**Non-resident Indians**	2.9% 792 mn

Source: Secretariat for Industrial Assistance, Department of Industrial Promotion and Policy, Ministry of Commerce and Industry, Government of India.

[a] Data up to November 2009.

Annex table 5c. India: selected large foreign affiliates, ranked by size of cumulative investments from 2000-2009 (US$ million)

Rank	Name [a]	Industry	Cumulative investments in India [b] (2000-2009)
1	Oracle Global Ltd. (Mauritius)	Software development	1.64
2	Biometrix Marketing Pvt. Ltd. (Singapore)	Petroleum & natural gas	1.62
3	TMI Mauritius Ltd. (Mauritius)	Telecommunications	1.6
4	Cairn (UK)	Business services	1.49
5	Vodafone (Mauritius)	Telecommunications	0.8
6	Hindustan Coca Cola Overseas Holding Pte (Singapore)	Investment research & counseling activities	0.78
7.	HSBC Bank Plc (UK)	Ports	0.75
8.	Suzuki Motors (Japan)	Automobile	0.57
9.	Essar Logistics Holdings (USA)	Steel manufacture	0.45
10.	Matsushita Electric Works (Japan)	Manufacture of electrical products	0.44
11.	Yamaha Motor Co. (Japan)	Automobile	0.39
12.	Barclays Bank (Singapore)	Financial services	0.36
13.	Petronas International (USA)	Business services	0.29
14.	Hewlett Packard Leiden BV(Netherlands)	Software	0.25
15.	Allianz SE (Germany)	Insurance	0.24
6	SAB Miller (Netherlands)	Brewery	0.24
17.	NTT Docomo (Japan)	Telecommunications	0.2
18.	Walt Disney (Singapore)	Motion pictures distribution	0.16
19.	Volkswagen AG (Netherlands)	Automobile	0.15
20.	Ford Motor Co. (USA)	Automobile	0.15
21.	TNT Express Worldwide, (Netherlands)	Courier service	0.08
22.	Posco Ltd. (Republic of Korea)	Steel	0.07
23.	Samsung Electronic Co. Ltd. (Republic of Korea)	Electronic	0.05
24.	Hyundai Heavy Industries (Republic of Korea)	Construction & transport equipment	0.04
25.	Schneider Electric Industries SAS (France)	Industrial machinery	0.04

Source: Database of the Secretariat of Industrial Approvals, Department of Industrial Promotion and Policy, Ministry of Commerce and Industry, Government of India.

[a] Data on FDI inflows captures the country from where the investment into India is flowing and not the original home country of the company.

[b] Company-wise inflows from January 2000 and November 2009 have been counted as total Indian assets.

Annex table 6. India: the top 15 inward mergers and acquisitions, 2007-2009

Year	Acquirer/ home country	Target	Value *(US$ billion)*	Shares bought (%)	Industry
2007	Vodafone, UK	Hutchison Essar	10.8	67%	Telecommunications
2008	Daichii Sankyo, Japan	Ranbaxy Laboratories	4.5	60.63%	Pharma, healthcare, biotech
2008	NTT DOCOMO, Japan	Tata Teleservices	2.7	26%	Telecommunications
2008	Telenor , Norway	Unitech Wireless	1.36	60%	Telecommunications
2007[a]	Oracle Global, USA	I Flex Solutions	1.1	NA	Computer software
2007	Vedanta Resources, UK	Sesa Goa	1	51%	Metals and ores
2008	Emirates Telecommunications, U.A.E	Swan Telecom	0.9	45%	Telecommunications
2007	Mittal Investments, Luxembourg	Guru Gobind Singh Refineries	0.7	49%	Oil and natural gas
2009	Sanofi Pasteur, France [b]	Shantha Biotechnics	0.68	80%	Pharma, healthcare, biotech
2007	Matsushita Electric Works, Japan	Anchor Electricals	0.42	80%	Electricals and electronics
2008	Lafarge, France	Larsen and Toubro's ready-mix concrete business	0.37	100%	Engineering
2008	Petroliam Nasional Berhad (Petronas), Malaysia	Cairn India	0.36	2.77%	Power and energy
2008	HSBC Holdings, UK	IL&FS Investmart	0.24	73.21%	Banking and financial services
2009	Petroliam Nasional Berhad (Petronas), Malaysia [c]	Cairn India	0.24	2.3%	Power and energy
2009	Bahrain Telecommunications Co. and Millennium Private Equity, Bahrain	S Tel	0.23	49%	Telecommunications
2007	Holci, Switzerland	Ambuja Cements	0.22	3.9%	Cement

Source: Grant Thornton Deal Tracker.
[a] Secretariat of Industrial Approvals, Department of Industrial Promotion and Policy, Ministry of Commerce and Industry, Government of India. Acquisition announced in 2006 (thus, not listed in the Grant Thornton Deal Tracker data base), but inflows received in January 2007.
[b] Vaccines division of Sanofi-Aventis.
[c] Through its overseas arm, Petronas International Corporation Ltd.

Outward FDI: Indian FDI falls in global economic crisis: Indian multinationals tread cautiously

Jaya Prakash Pradhan

Just over a year ago, outward foreign direct investment (OFDI) from India seemed to be on a path of rapid and sustained growth. Its annual average growth of 98% during 2004–07 had been unprecedented, much ahead of OFDI growth from other emerging markets like China (74%), Malaysia (70%), Russia (53%), and the Republic of Korea (51%), although from a much lower base. Much of this recent growth had been fuelled by large-scale overseas acquisitions, however, and it faltered when the global financial crisis that started in late 2007 made financing acquisitions harder.

How will internationalizing Indian firms deal with the global crisis? Will they benefit from the global meltdown – for example, from cheaper asset prices – or become cautious and retreat?

Slowdown in 2008, with dim prospects for 2009

The global economic crisis has made Indian firms wary of further expansion abroad. Consequently, actual Indian FDI outflows, which rose to a historic level of nearly USD 18 billion in 2007, fell by 6% in 2008 to under USD 17 billion (annex table 1).[474] This is the first absolute decline in OFDI since 1999. The fall in Indian OFDI is in line with the worldwide decline of 15% in 2008,[475] although it contrasts with China's doubling of its OFDI in 2008.[476] The contraction in Indian OFDI is continuing in 2009, falling to USD 4.7 billion in the first quarter of the current year, a 14% decline over the same quarter last year.

The trend in Indian overseas acquisitions in January–June 2009, as compared to the corresponding period in 2008, confirms the decline. Between these two periods, the value of such acquisitions fell by 65%, from USD 8 billion to under USD 3 billion, and their number fell from 140 to 28 (annex table 2).

This 2008 and early 2009 plunge in Indian OFDI has been asymmetrical across sectors and host regions (annex tables 3, 4 and 5). Indian OFDI in the primary and tertiary sectors has been more resilient in the crisis than OFDI in manufacturing. Between 2007 and 2008, acquisition-led[477] Indian OFDI grew in the primary sector (10%) and in services (19%), while it fell steeply in manufacturing (-79%). The share of manufacturing in Indian OFDI flows thus fell, unsurprisingly, from 84% in 2007 to 49% in 2008. The share of the primary and services sectors in Indian brownfield (i.e., made through mergers and acquisitions) OFDI, on the other hand, grew to 20% and 31%, respectively. In the first half of 2009, the negative impact of the global slowdown spread to the services sector as well. Only the primary sector remained robust, led by ongoing increases in OFDI in the oil segment and the revival of OFDI in mining.

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[474] The Reserve Bank of India (RBI), from which these figures are taken, tends to underestimate FDI in general, as it does not count re-invested earnings.

[475] UNCTAD (2009), "Global crisis now having strong, wide impact on foreign direct investment, study shows", Press Release, UNCTAD/PRESS/PR/2009/020, May 20.

[476] Kenneth Davies (2009), "While global FDI falls, China's outward FDI doubles", *Columbia FDI Perspectives*, No. 5, May 26, at www.vcc.columbia.edu.

[477] Much of the discussion in this *Perspective* draws on data on M&As compiled by the author. As the funds used for cross-border acquisitions need not come just from the home country, the sectoral and geographic distribution of such acquisitions may be different from the distribution of direct investment from India. The reason for using the M&A data in this context is that data on the distribution of OFDI proper is not available.

The current decline in Indian investment is widespread among recipients. Among host regions, the fall in Indian brownfield investment was steepest in the developing world (-79%) in 2008, with Asia, which had accounted for 8% of the investment in 2007, falling by 85% in 2008 (annex table 4). Africa did much better, by receiving 69% more brownfield investment in 2008, but this from a very low base of USD 111 million. Acquisitions in the developed world in 2007 had been led by Europe and fell by nearly 54% in 2008. In North America, they fell by 75%.

In the first half of 2009, Indian FDI flows into Africa were sharply higher than the first half of 2008, because of the region's oil and gas resources, while they fell in all other regions. Looking at countries, the two countries accounting for most of the value of Indian acquisitions in both 2007 and 2008 differed sharply in 2009. Indian brownfield investment in the United States during the first half of 2009 actually grew by 6% over the first half of 2008, while it fell by 99% in the United Kingdom.

Undertaken mostly by private enterprises, except for a few public-sector firms in the energy sector,[478] Indian OFDI has been driven by several factors, including global growth, business opportunities and increased competition. The effect of market conditions turning adverse in 2008 can be seen in the actions of such Indian companies such as Sakthi Sugars, Reliance Industries, Vardhman Polytex, and Suzlon Energy, which are reportedly wrapping up (or disinvesting from) some of their overseas affiliates because of the current economic meltdown (annex table 6).

What led to the downturn?

Several factors account for the decline in Indian OFDI. The global and domestic slowdown in growth was one of these. The advanced economies are predicted to see a sharp fall in their aggregate real GDP growth rate from 2.7% in 2007 to 0.8% in 2008 and -3.8% in 2009, signifying further reduction in overseas demand.[479] Real GDP growth within India fell from above 9% in October–December 2007 to just 5% in October–December 2008. This has led to an erosion of business confidence, reduced consumption and slowing investment, choking off both the domestic and overseas expansion of Indian firms.

The credit crunch in both Indian and overseas markets was another factor. Although the Indian banking sector did not suffer quite as much from its exposure to distressed global financial instruments and institutions as banks in some major economies, suffer it did and therefore adopted a cautious lending policy in 2008.[480] This in turn led to several domestic and overseas projects being postponed.

In addition, the global financial crisis had a significantly negative impact on other financial sub-sectors like the Indian equity, money and foreign-exchange markets. India's benchmark equity index, the Sensex, had fallen sharply by December 2008, by 48% from its highest-ever level reached in December 2007. All this has restricted Indian firms' access to cheap sources of finance and reduced their profitability. Many Indian companies that had acquired overseas units in the recent past, such as Suzlon Energy, Tata Motors and Hindlaco, had to suspend their rights issues and faced difficulties in raising resources.

The sudden depreciation of the Indian rupee against the US dollar in 2008 also led to heavy losses for many export-oriented Indian companies that had acquired long-term forex derivatives.[481] Several Indian companies, which had borrowed heavily abroad to finance their global acquisitions and

[478] For a list of large Indian outward investors, see "The growth story of Indian multinationals", The Indian School of Business (ISB) and the Vale Columbia Center on Sustainable International Investment (VCC), 2009, at www.vcc.columbia.edu.
[479] International Monetary Fund (2009), "World economic outlook update", July 8, 2009, http://www.imf.org/external/pubs/ft/weo/2009/update/02/index.htm.
[480] *Hindu Business Line* (2007), "Banks' loss due to sub-prime crisis put at $2 b", Saturday, October 6.
[481] *Business Standard* (2009), "46 companies suffer forex losses of Rs 1,365cr", May 8.

greenfield projects during the period of rapid appreciation of the rupee against the dollar, encountered difficulties in meeting mounting overseas debt obligations after its sudden depreciation in late 2008.[482] The depreciating domestic currency, combined with the collapsing stock prices of Indian companies, reduced these companies' ability to engage in M&As.

Continued falls in export earnings, especially during October–December 2008, further aggravated the condition of export-dependent Indian firms in a large number of sectors, including software, gems and jewellery, leather, textiles, auto parts, pharmaceuticals, and food processing. Since exporters are leading outward investors, lower export earnings had a significant impact on Indian OFDI in 2008. The sudden collapse of commodity prices like crude oil, natural gas and metals also moderated the outward expansion of natural-resource-seeking Indian firms. Finally, anecdotal reports suggest that Indian firms with overseas affiliates – Bharat Forge, Havells India, Hindalco, Punj Lloyd, Tata Communications – have suffered severe consolidated losses in recent quarters on account of their overseas operations.[483]

Future prospects

Recovery in Indian OFDI will depend on the revival of global and domestic growth, improvements in corporate profitability, and the easing of financing from banks and the equity market. The first quarter of 2009 registered stronger GDP growth in India than expected, even though global growth went down. If domestic growth turns out not to be sustainable, however, OFDI may not recover.

Recently announced overseas deals, such as the proposed merger of Bharti Airtel and South Africa's MTN for USD 23 billion and Sterlite Industries' USD 1.7 billion bid for US-based copper-mining firm Asarco, suggest that 2009 might see some positive surprises. Moreover, not every Indian company has financing problems. There are some cash-rich Indian firms, including SMEs, which have not undertaken FDI in the past but may be interested in doing so in the future. These firms can be expected to explore acquisitions, given the cheap valuations of foreign assets.

ANNEX

Annex table 1. Actual Indian FDI outflows, 2008 and early 2009[a]

Year	Quarter	FDI in USD million			% change over previous year
		Equity	Loan	Total	
2008	January–March	3981	1422	5403	20.6
	April–June	1346	451	1797	-65.4
	July–September	2640	494	3134	5.4
	October–December	4254	1314	5569	-2.0
	All Quarters (January–December)	12926	3778	16704	-6.3
2009	January–March	4159	488	4647	-14.0

Sources: (i) RBI Bulletin (2009), "Indian investment abroad in joint ventures and wholly owned subsidiaries : 2008-09 (April-March)", July 10; (ii) RBI Bulletin (2009), "Indian investment abroad in joint ventures and wholly owned subsidiaries: 2008-09 (April-December)", April 17; (iii) RBI Bulletin (2009), "Indian investment abroad in joint ventures and wholly owned subsidiaries: 2008-09 (April-September)", January 14; (iv) RBI Bulletin (2008), "Indian investment abroad in joint ventures and wholly owned subsidiaries : 2008-09 (April-June)", October 13; and (v) RBI Bulletin (2008), "Indian investment abroad in joint ventures and wholly owned subsidiaries: 2007-08 (April-March)", July 14.

[a]The equity data do not include equity of individuals and banks. Quarterly figures may not add up to annual totals due to revision in data

[482] Pradhan, J.P. (2009) "The global economic crisis: impact on Indian outward investment", *MPRA Paper* No. 1657, Munich University Library, Germany.

[483] *Economic Times* (2009), "Foreign acquisitions: No love across the border", April 20.

Annex table 2. Overseas acquisitions by Indian firms, January–June 2009

Month	Value (USD million)		% change over previous year	Number of deals		% change over previous year
	2008	2009		2008	2009	
January	1304	29	-97.8	28	6	-78.6
February	602	132	-78.1	19	5	-73.7
March	3019	2316	-23.3	23	10	-56.5
April	746	40	-94.6	28	1	-96.4
May	569	54	-90.5	19	4	-78.9
June	1731	243	-86.0	23	2	-91.3
All above months	7971	2814	-64.7	140	28	-80.0

Sources: Based on a dataset constructed from reports from newspapers, magazines and financial consulting firms like *Hindu Business Line, Economic Times, Financial Express, Business World,* Grant Thornton India, and ISI Emerging Markets.

Annex table 3. Sectoral composition of Indian overseas acquisitions, 2008 and early 2009

Sector	Value (USD million)		% change over previous year	Value (USD million)		% change over previous year
	2007 (Jan.–Dec.)	2008 (Jan.–Dec.)		2008 (Jan.-Jun.)	2009 (Jan.-Jun.)	
Primary	2314	2533	9.5	411	2230	442.6
Agricultural & allied products	10	24	140	24		-100
Mining	1239	421	-66	277	1780	542.6
Oil & natural gas	1065	2088	96.1	110	450	309.1
Manufacturing	29919	6306	-78.9	5394	319	-94.1
Food & beverages	1269	56	-95.6	54		-100
Textiles & apparel	126	136	7.9	136	119	-12.5
Paper & paper products		9		9		-100
Gems & jewellery	43	40	-7	40		-100
Rubber & plastic products	65	124	90.8	68		-100
Non-metallic mineral products	37	9	-75.7	9		-100
Metal & fabricated metal products	22346	162	-99.3	162		-100

Machinery & equipment	1351	173	-87.2	152		-100
Electrical machinery & equipment	1560	827	-47	556	164	-70.5
Transport equipment	475	2758	480.6	2701	32	-98.8
Telecommunication equipment	757		-100			
Chemicals	1117	1427	27.8	1087		-100
Pharmaceuticals	773	585	-24.3	420	4	-99
Services	3350	3989	19.1	2137	265	-87.6
Business advisory	9		-100			
Media & entertainment	81	148	82.7	144	25	-82.6
Hospitality & tourism	521	45	-91.4	45	13	-71.2
Banking & financial services	26	141	442.3	110		-100
Telecommunication services	330	84	-74.5	84	26	-69
IT & ITES	2383	2565	7.6	786	201	-74.4
Power generation & distribution		1006		968		-100
Others	244	126	-48.4	29		-100
Grand total	35827	12954	-63.8	7971	2814	-64.7

Sources: Based on a dataset constructed from reports from newspapers, magazines and financial consulting firms like *Hindu Business Line, Economic Times, Financial Express, Business World,* Grant Thornton India, and ISI Emerging Markets.

Annex table 4. Regional direction of Indian overseas acquisitions, 2008 and early 2009

Host region	**Value (USD million)**		**% change over previous year**	**Value (USD million)**		**% change over previous year**
	2007 (Jan.–Dec.)	**2008 (Jan.–Dec.)**		**2008 (Jan.-Jun.)**	**2009 (Jan.-Jun.)**	
Developing economies	3234	685	-78.8	496	531	7.1
Africa	111	188	69.4	80	451	463.8
Latin America & Caribbean	232	68	-70.7	68		-100
Asia	2891	429	-85.2	348	80	-77
Transition economies	37	20	-45.9			
Europe	37	20	-45.9			
Developed economies	32556	12249	-62.4	7475	2283	-69.5

America	14372	3570	-75.2	2313	2046	-11.5
Asia	492		-100			
Europe	17579	8122	-53.8	4997	196	-96.1
Oceania	113	557	392.9	165	41	-75.2
Grand Total	35827	12954	-63.8	7971	2814	-64.7
Memorandum item						
Number of host countries	40	42		35	14	
Number of acquiring Indian companies	150	164		109	24	

Sources: Based on a dataset constructed from reports from newspapers, magazines and financial consulting firms like *Hindu Business Line, Economic Times, Financial Express, Business World,* Grant Thornton India, and ISI Emerging Markets.

Annex table 5. Indian overseas acquisitions by selected host countries, 2008 and early 2009

Host economy	Value (USD million)		% change over previous year	Value (USD million)		% change over previous year
	2007 (Jan.–Dec.)	2008 (Jan.–Dec.)		2008 (Jan.-Jun.)	2009 (Jan.-Jun.)	
UK	15374	5384	-65.0	2681	32	-98.8
USA	12003	3165	-73.6	1932	2045.94	5.9
Canada	1805	405	-77.6	381		-100.0
Indonesia	1124	258	-77.0	258	80	-69.0
Norway	900	302	-66.4	300		-100.0
Singapore	818	39	-95.2	22		-100.0
Republic of Korea	752		-100.0			
Germany	745	812	9.0	554	164	-70.4
Bermuda	564		-100.0			
Israel	489		-100.0			
Netherlands	355	954	168.7	954		-100.0
Brazil	224		-100.0			
Malaysia	133		-100.0			
Australia	113	557	392.9	165	41	-75.2
Mozambique	86	78	-9.3			
France	71	35	-50.7	2		-100.0
Italy	61	272	345.9	187		-100.0
Vietnam	44	2	-95.5			

Russia	37	20	-45.9			
Czech Republic	25	3	-88.0	3		-100.0

Sources: Based on a dataset constructed from reports from newspapers, magazines and financial consulting firms like *Hindu Business Line, Economic Times, Financial Express, Business World,* Grant Thornton India, and ISI Emerging Markets.

Annex table 6. Illustrative cases of overseas disinvestment by Indian firms, 2009

Indian company	Action taken
Suzlon Energy Ltd.	SEL sold 10% stake in Hansen Transmissions International on January 2, 2009 to raise Rs 600 crore (about USD120 million). According to news reports, Suzlon has taken this step because of the tight liquidity situation and its obligation to buy the stake of the Portuguese company Martifer in REpower, Germany.
Sakthi Sugars Ltd.	Sakthi Germany GmbH and Sakthi Sweden AB have filed for bankruptcy and Arvika Gjuteri AB, Sweden, for financial reconstruction. According to a parent company source, these measures were taken on account of the economic meltdown in the US and Europe and the consequent drastic reduction in orders.
Reliance Industries Ltd.	RIL's German subsidiary, Trevira GmbH, has started insolvency proceedings. RIL took this step to overcome the impact of the industrial slowdown in Europe, particularly in the automotive and textile sectors, to which it is an important supplier.
Vardhman Polytex Ltd.	VPL has decided to close down its Austrian subsidiary, FM Hammerle Nfg GmbH, as part of a business restructuring demanded by the current recession in Europe.

Sources: (i) *Hindu Business Line* (2009), "Suzlon Energy sells 10% stake in Hansen", January 3; (ii) *Financial Express* (2009), "Sakthi Sugars' European units file for bankruptcy"**,** February 6; (iii) *Economic Times* (2009), "RIL's German textile arm files for bankruptcy", June 4; and (iv) BSE (2009), "Corporate communication of Vardhman Polytex", June 23.

Outward FDI from India and its policy context

Premila Nazareth Satyanand and Pramila Raghavendran

India is now the world's 21st largest outward investor, which is significant given its historically miniscule foreign direct investment (FDI) outflows. Annual FDI outflows have jumped fifty-fold after 2000, and Indian firms have invested over US$ 75 billion overseas in the past decade, in some cases to attain global status by acquiring world-leading firms. Substantial improvements in the country's economic performance and the competitiveness of its firms and their strategy, resulting from ongoing liberalization in economic and outward FDI (OFDI) policies, made these developments possible. Indian firms now invest across a wide variety of sectors and countries, departing from their historical focus on trading and textile investments in developing countries. Following the 25% crisis-induced drop in Indian OFDI in 2009, Indian firms are once again increasing their overseas investment, including through mergers and acquisitions (M&As). India's OFDI should continue its rapid upward trend over the next few years, as more companies seek to transfer their products and service innovations to new markets, and acquire strategic international know-how and market shares, particularly in crisis-hit developed economies.

Trends and developments

Indian firms began to invest overseas in the 1960s, but India's restrictive OFDI regime limited them to small, minority joint ventures in developing economies. After 1991, intense domestic economic competition, the growing global competitiveness of Indian firms and liberalizations in OFDI and capital market policy triggered a rush of international investments by Indian companies, especially in the IT, pharmaceuticals, telecommunication, automotive, metal, and service sectors. In most of these sectors, Indian companies have sought to be global leaders.

Country level developments

Indian OFDI shows three major structural shifts during the past decade. First, annual OFDI flows rose fifty-fold, from US$ 340 million in 2000 to an average of US$ 18 billion in 2007/2008 (annex tables 2 and 2a). India has become the world's 21st largest outward investor.[484] Its average annual OFDI flows are now higher than those of many developed market economies. Moreover, while India's OFDI gradually increased during the past three decades, OFDI of the Republic of Korea, Malaysia and South Africa declined during the same time period.[485] This strong performance is reflected in the surge of the country's OFDI stock, from US$ 1.9 billion in 2000 to US$ 76.3 billion in 2009 (annex table 1).

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[484] India was the world's 43rd largest investor in 2000. By 2007, it had become the 23rd largest, even before the global crisis caused a near-halving of OFDI from many of the world's leading outward investing economies. These are authors' calculations, based on UNCTAD's FDI/TNC database, available at: http://stats.unctad.org/fdi.

[485] The strong performance of Indian OFDI in comparison to other countries is analyzed in Karl P. Sauvant and Jaya Prakash Pradhan, with Ayesha Chatterjee and Brian Harley, eds., *The Rise of Indian Multinationals: Perspectives on Indian Outward Foreign Direct Investment* (New York: Palgrave, 2010) and Michael W. Hansen, "Outward foreign direct investment from India: theory and evidence," *CBDS Working Paper* No. 8 (Copenhagen: Copenhagen Business School, 2007), available at: www.hdl.handle.net/10398/6754.

Second, manufacturing has displaced services as the principal OFDI sector,[486]which dominated Indian OFDI flows at the turn of the decade (annex table 3), even as the primary sector's share is now growing quickly.[487] While pharmaceuticals, consumer electronics and automotives accounted for the bulk of manufacturing OFDI in the first half of the decade, the second half has seen a concentration in metals, energy and natural resource investments, and increasing activity by consumer goods and food and beverage firms. Similarly, while IT initially dominated services OFDI, investment in other services industries, such as financial and insurance services, entertainment and broadcasting, construction, and telecommunications, is now mounting.

Third, over a half of India's total 2002-2009 OFDI flows went into developed economies (annex table 4a), most of them in the form of M&As.[488] In fact, since 2000, Indian firms have tended to use cross-border M&As as the main mode of entry into developed economies, and greenfield investments into developing ones (annex tables 6 and 7), in a competitive strategy approach. They have systematically acquired leading developed country firms, rapidly to boost domain expertise, technological competitiveness, market size, and brand recognition. In some cases, these acquisitions were specifically undertaken to attain global size and status, and to build new competitive advantages by combining the best international technology with low-cost Indian labor. Energy and mineral security have driven large greenfield investments in developing countries, though many telecom, consumer goods, food, IT, metal, and power firms are now also using M&As to build market size or secure raw materials in these countries.

Singapore is now the largest host to Indian OFDI (annex table 4b). This is due to a sudden jump in investments after the two countries signed a Comprehensive Economic Cooperation Agreement in 2005.[489] In the 1990s, Russia dominated Indian OFDI flows, largely due to the "Rupee-Rouble" agreement, which enabled Indian firms to conduct Russian trade and investment in rupees.

The corporate players

Indian OFDI is undertaken primarily by publicly-listed, private firms and, as yet, only a handful of Indian public-sector firms have internationalized (annex table 5).[490] Unlike multinational enterprises (MNEs) in China and Singapore, they do not enjoy globalization privileges. In fact, domestic business rules and taxes weigh heavily on globalizing Indian firms.[491]

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[486] The following sectoral and geographical analysis of Indian OFDI is based on the Indian Government's investment *approval* data, since it does not yet publish these data based on actual OFDI outflows.
[487] Sauvant and Pradhan, *op. cit*., show that the primary sector accounts for close to a quarter of Indian OFDI stock
[488] According to Sauvant and Pradhan, *ibid*., developed economies account for roughly 83% of the total value of all Indian overseas M&As from 2000 to June 2009.
[489] For the same reason, Singapore is also the largest source of inward FDI into India.
[490] Leading among these are the Oil and Natural Gas Commission (ONGC), the National Thermal Power Corporation (NTPC) and the Gas Authority of India Limited (GAIL).
[491] Foreign dividend repatriations by Indian outward investors are taxed at the normal corporate rate (currently 30%) plus applicable surcharges and levies. There is also double taxation as Indian companies are taxed on overseas dividend repatriations without receiving any credit for foreign taxes. See Lubna Kably, "Globetrotting anew," *Economic Times*, April 30, 2010.

Though relatively small in a global context, Indian MNEs are notable for their global buy-outs of enterprises far larger than themselves,[492] and for their higher intensity of international sales and developed market M&A activity compared to other emerging market MNEs.[493]
Early Indian OFDI was market-seeking and concentrated in developing economies, where there was little technological competition. Until the 1990s, Indian trading, textile, agrochemicals, paper, and light engineering firms dominated Indian OFDI. Indian MNEs invested overseas largely to circumvent domestic restrictions on firm size stemming from the Monopolies and Trade Restrictive Practices Act.[494]

In the 1990s, Indian OFDI became more high-tech and also more trade supporting, as Indian IT firms – such as Tata Consultancy Services, Infosys, WIPRO, and Satyam – began to win large global contracts and located in developed economies to be close to key clients. Indian pharmaceutical firms – such as Ranbaxy, Dr Reddy's Laboratories, Sun Pharmaceuticals, Biocon – followed the same route to break into Western generic markets. Battling global competition, both groups began to make strategic acquisitions to build rapidly specialized expertise, market share, brandnames, and certification to succeed internationally.[495]

Severe domestic competition and growing Indian corporate self-confidence also triggered increasingly larger strategic asset-seeking, cross-border M&As from other sectors, including automotives (Tata Motors, Mahindra & Mahindra), auto-components (Bharat Forge), electronics (Videocon), and electrical machinery (Crompton Greaves). Yet India's largest M&As have tended to be in the metals sector (Tata Steel, Hindalco, Essar Steel, Jindal Steel).[496] While the largest M&As were smaller than US$ 500 million in the early 2000s, they were higher than US$ 5 billion by 2007.

Many firms also used M&As to bring home new products and services and build competitive strength in India, now one of the world's largest markets. This trend is particularly evident for telecommunications (Tata Communications, Reliance Communications, Bharti Airtel, Essar Communications),[497] energy (Oil and Natural Gas Corporation, Reliance Industries, Tata Power),[498] infrastructure (GMR, DS Constructions), media and entertainment (Reliance Entertainment),[499] and agricultural firms (Karuthuri Global, Global Green, Renuka Sugars).[500] It

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[492] Most of these were leveraged buyouts, with much of the capital raised in international financial markets.
[493] Nagesh Kumar, "Internationalization of Indian enterprises: patterns, strategies, ownership advantages and implications," RIS Discussion Paper No. 140 (New Delhi: RIS, 2008).
[494] The Monopolies and Trade Restrictive Practices Act (1969) was intended to prevent the concentration of economic power, provide for control of monopolies and probation of monopolistic, restrictive and unfair trade practice, and to protect the consumer interest.
[495] Nagesh Kumar and K.J. Joseph, eds., *International Competitiveness & Knowledge-based Industries in India* (Oxford: Oxford University Press, 2007).
[496] Tata Steel's US$ 12.2 billion takeover of Corus Steel in 2007, India's largest cross-border M&A to date, accounted for two-thirds of the total Indian OFDI that year.
[497] Bharti Airtel, Tata Communications and Reliance Communications made a number of strategic international acquisitions in the mid-2000s to expand and control India's booming new telecommunications market.
[498] Public and private sector firms are buying oil and gas fields and coal mines overseas to secure supplies for their local Indian operations. Also, since 2006, new firms in the power and infrastructure sectors are using global acquisitions to build the expertise required to bid for power, airport and infrastructure projects, both at home and overseas.
[499] These firms are seeking to build or consolidate film, TV and animation production and distribution operations both at home and overseas. The largest investment so far is Reliance Entertainment's US$ 825 million production and distribution tie-up with Steven Spielberg, the US film maker.

also explains the dominance of natural resource-seeking investments in India's largest recent outward greenfield and M&A investments (annex tables 6 and annex 7). Agricultural and resource investments are also being driven by mounting local resistance to large-scale projects involving community displacement and environmental disruption.

Also important to note, is that smaller Indian firms and not just large conglomerates are active outward investors for many of the same reasons.[501] In fact, in the period 2000-2008, 34% out of the total number of Indian M&As abroad were made by such firms, though they account for just 8% of the total investment value and are less geographically diverse than larger counterparts.[502]

Effects of the current global crisis

The global crisis caused Indian OFDI flows to fall from their high of US$ 18.8 billion in 2007 to US$ 14.5 billion in 2009, largely because Indian MNEs had borrowed heavily in dollars to finance mega cross-border M&As. They were thus hit badly by the sharp rupee depreciation and tightened international credit conditions.[503] Outward M&As dropped radically both in number and in size, resulting in a four-fifths drop in the value of manufacturing (including metals) M&As and an overall drop in this sector's share (annex table 3).[504] Between 2007 and 2009, the number of overseas M&As plummeted from 243 to 82; the total cross-border M&A value fell from US$ 32.8 billion to US$ 1.4 billion; and the average M&A size decreased from US$ 135 million in 2007 to US$ 17 million in 2009.[505]

Given the minimal impact of the worldwide financial and economic crisis on the Indian economy, which remained on its strong economic growth path, Indian MNEs have weathered the crisis well, and have once again begun to make sizeable foreign investments. Indian firms are more bullish in their outward investment plans than MNEs of other BRIC countries. Despite the crisis, Indian MNEs do not seem to plan a reduction of outward investments, in contrast to their competitors in other countries.[506]

The policy scene

Three important regulatory developments have underpinned India's emergence as a global outward investor. First, the number of sectors/activities requiring industrial licensing was

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[500] Led by firms such as Karuthuri Global, Global Green, Renuka Sugars, and Shree Shakti Sugars, Indian agricultural producers are internationalizing to circumvent domestic restrictions on corporate ownership of agricultural land and agricultural production. They are acquiring agricultural operations or land in Africa, Europe and Latin America, to service both the Indian and international markets.

[501] UNCTAD, *Global Players from Emerging Markets: Strengthening Enterprise Competitiveness through Outward Investment* (New York and Geneva: United Nations, 2007).

[502] Jaya Prakash Pradhan and Neelam Singh, "Group affiliation and location of Indian firms' foreign acquisitions," *MPRA Paper*, No. 24018, University Library of Munich, 2010.

[503] Some experts argue that Indian MNEs "imported" the global financial crisis into India, due to their heavy reliance on foreign borrowings. See, for example, Jahangir Aziz, Ila Patnaik and Ajay Shah, "The current liquidity crunch in India: diagnosis and policy response," Technical report for NIPFP DEA Research Program, October 28, 2008, available at: http://www.mayin.org/ajayshah/PDFDOCS/APS2008_crisis_and_response.pdf

[504] Jaya Prakash Pradhan, "Indian FDI falls in global crisis: Indian multinationals tread cautiously," *Columbia FDI Perspectives No. 11*, August 17, 2009.

[505] *Grant Thornton Deal Tracker* (New Delhi: 2009).

[506] Multilateral Investment Guarantee Agency, *World Investment and Political Risk 2009*, available at: http://www.miga.org/documents/flagship09ebook.pdf

reduced in a calibrated manner. This means that Government-determined production quotas were lifted, permitting Indian firms to produce what and how much they want, using the technology they want, without government planners on their backs. Licensing is now applicable only to 14 manufacturing activities through periodical amendments to the Industries (Development & Regulation) Act, 1951.

Second, ongoing liberalizations of India's historically restrictive OFDI regime encouraged outward FDI. The introduction of the Foreign Exchange Management Act (2000) brought about significant policy liberalization. Indian firms were allowed to invest in 100% subsidiaries, in any line of business, in any country, and the earlier investment limit of US$ 50 million over a three-year period began to apply annually. Before that Act, Indian firms were only permitted to make overseas investments in their core business in developing countries and only with Governmental approval. Indian companies have also been relieved of foreign exchange matching obligations. Earlier, Indian firms had to compensate for foreign exchange outflows with matching export earnings. They are now allowed to borrow abroad to finance overseas investments, and to use domestic bank borrowing for the same purpose. In 2005, they were allowed to float international special purpose vehicles to finance foreign acquisitions and, in 2006, the prudential limit on bank financing was raised from 10% to 20% of overseas investment. The outward investment cap is now four times the adjusted net worth invested in foreign affiliates. The cap was just US$ 2 million in the 1990s.

Third, capital market liberalization enabled foreign investors to buy Indian stocks and Indian firms to borrow money internationally (even for overseas investments). This radically cut the cost of capital,[507] made it far more available[508] and transformed the Indian industry's standing in global financial markets.[509]

Bilateral investment treaties (BITs) and double taxation treaties (DDTs) have also played a role, particularly in the case of small firms.[510] While India had 40 BITs in force in 2000, it now has 68, and is negotiating 24 more. The number of DDTs has jumped from 66 to 79 over the same period.

Conclusions

The growth of Indian OFDI is expected to continue. The sectoral and regional distribution of Indian outward FDI is broadening. The liberalization of such sectors as medical services, defence and education is prompting Indian firms to explore overseas acquisitions to build both domestic strength and global presence. It can also be expected that foreign investments in the natural resource sectors will surge, given the continuing difficulty in acquiring large tracts of land for agricultural purposes and the growing resistance to large mining projects in India.

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[507] Interest rates averaged 18% during the 1980s, due to minimal competition and capital controls.

[508] Between 2003 and 2007, foreign institutional investors, keen to profit from India's accelerating growth, poured over US$ 50 billion into Indian stocks, causing share prices to quintuple.

[509] Due to the quintupling of share prices, over 80 Indian firms had market capitalizations of above US$ 1 billion by early 2008, making it easy for them to raise money overseas to finance large international investments.

[510] Pradhan and Singh (2010), *op. cit.* The authors find that smaller firms are particularly influenced by double taxation agreements.

Indian MNEs will continue to invest in developed-country based companies, particularly now that they are more affordable due to the global crisis.[511] In addition, Indian MNEs are seeking more strategic investments in emerging markets, particularly in Africa.[512] According to a recent report, India might be the largest source of emerging market MNEs by 2024, with 20% more new MNEs than China, and over 2,200 Indian firms are likely to invest overseas in the next fifteen years.[513]

Additional readings

Hansen, Michael W., "Outward foreign direct investment from India: theory and evidence," CBDS Working Paper No. 8 (Copenhagen: Copenhagen Business School, 2007), available at: www.hdl.handle.net/10398/6754.

India Brand Equity Foundation, *Going Global: Indian Multinationals* (New Delhi: 2006), available at: http://ibef.org/artdisplay.aspx?cat_id=410&art_id=13725.

Indian School of Business and Vale Columbia Center on Sustainable International Investment, "The growth story of Indian multinationals" (New York, 2009), available at: www.vcc.columbia.edu/files/vale/documents/India_2009.pdf.

Kumar, Nagesh, "Internationalization of Indian enterprises: patterns, strategies, ownership advantages and implications," *RIS Discussion Paper*, No 140 (New Dehli: 2008), available at: www.ris.org.in/dp140_pap.pdfhttp://www.ris.org.in/dp140_pap.pdf.

Sauvant, Karl P. and Jaya Prakash Pradhan, with Ayesha Chatterjee and Brian Harley, eds., *The Rise of Indian Multinationals: Perspectives on Indian Outward Foreign Direct Investment* (New York: Palgrave, 2010).

Pradhan, Jaya Prakash, *Indian Multinationals in the World Economy: Implications for Development* (New Delhi: Bookwell Publishers, 2008).

Useful websites:

For OFDI statistics: Website of the Department of Economic Affairs (International Cooperation Division), Ministry of Finance, Government of India, available at:
www.finmin.nic.in/the_ministry/dept_eco_affairs/
icsection/icsec_index.html

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[511] According to a study by Virtus Global Partners, half of Indian acquisitions in the US in the past two years have been buyouts of distressed assets, whose parent firms were badly hit by the global crisis. Virtus Global Partners (2010), *US-bound Acquisitions by Indian Companies,* vol.3.2 (New York, July 2010).

[512] Over the past few months, Indian telecommunications and consumer goods firms have begun to make large African investments, both greenfield investments and cross-border M&As. Among these are the Bharti, Essar and Godrej groups.

[513] PricewaterhouseCoopers, "Emerging multinationals," April 2010, available at: http://www.pwc.fr/assets/files/pdf/2010/04/pwc_emerging_multinationals.pdf

Statistical annex

Annex table 1. India: outward FDI stock, 1990, 2000, 2008, 2009

(US$ billion)

Economy	**1990**	**2000**	**2008**	**2009**
India	0	2	62	77
Memorandum: comparator economies				
Brazil	41	52	162	158
China	4	28	148	230
Russia	-	20	203	249
Singapore	8	57	207	213

Source: UNCTAD's FDI/TNC database, available at: http://stats.unctad.org/fdi/.

Annex table 2. India: outward FDI flows, 2000-2009

(US$ billion)

Economy	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
India	0.5	1.4	1.7	1.9	2.2	3.0	14.3	17.2	18.5	14.9
Memorandum: comparator economies										
Brazil	2.3	-2.3	2.5	0.2	9.8	2.5	28.2	7.1	20.5	-10.1
China	0.9	6.9	2.5	2.9	5.5	12.3	21.2	22.5	52.2	48.0
Russia	3.2	2.6	3.5	9.7	13.8	12.8	23.2	45.9	56.1	46.1
Singapore	5.9	20.0	2.3	2.7	10.8	11.2	18.8	27.6	-8.5	6.0

Source: UNCTAD's FDI/TNC database, available at: http://stats.unctad.org/fdi/.

Annex table 2a. India: outward FDI flows, 1991-1999

(US$ billion)

Economy	1991-1996[a]	1997	1998	1999
India	0.1	0.1	0.1	0.1
Memorandum: comparator economies				
Brazil	0.5	1.1	2.8	1.7
China	2.6	2.6	2.6	1.8
Russia	0.5	3.2	1.3	2.2
Singapore	3.0	9.0	0.4	5.4

Source: UNCTAD's FDI/TNC database, available at: http://stats.unctad.org/fdi/.

[s] Annual average.

Annex table 3. India: distribution of outward FDI flows, by economic sector and industry,[a] selected years
(US$ billion, and percent of total outflows)

Sector/industry	2000/2001	2004/2005	Cumulative 2000-01 to 2004-05	2008/2009	2009/2010	Cumulative 2005-06 to 2009-10
Total	1.4	2.8	10.1	22.1	14.3	77.5
Manufacturing	0.4 (27%)	2.0 (72%)	6.4 (63 %)	10.4 (47%)	6.0 (42%)	31.9 (41%)
Financial services	0.0 (1%)	0.0 (0%)	0.1 (0.1%)	0.3 (1%)	0.1 (0.7%)	0.7 (0.9%)
Non-financial services	0.9 (63%)	0.6 (21%)	2.7 (27%)	1.2 (6%)	1.5 (10.5%)	14.4 (19%)
Trade	0.1 (7%)	0.1 (2%)	0.4 (4%)	1.9 (9%)	0.8 (5.6%)	25.5 (33%)
Others	0.0 (2%)	0.2 (5%)	0.4 (4%)	8.3 (37%)	5.9 (41.3%)	4.8 (6%)

Source: Indian Ministry of Finance www.finmin.nic.in/the_ministry/dept_eco_affairs/icsection/icsec_index.html

[a] This table relies on investment approval data, since the Government does not yet publish a sectoral breakdown of outflows. Data are by fiscal year (1 April – 31 March).

Annex table 4a. India: geographical distribution of outward FDI flows,[a] 1996-2010

Region/economy	Shares in %			US$ million		
	1996-2002	2002-09	2009-10	1996-2002	2002-09	2009-10
World	**100**	**100**	**100**	**7,525**	**75,985**	**10,623**
Developed economies	**35**	**52**	**32**	**5,267**	**39,487**	**3,384**
Europe	**11**	**40**	**20**	**827**	**30, 715**	**2,134**
European Union	11	32	17	806	24,199	1,844
Austria	1	0	0	78	91	7
Cyprus	-	6	5	-	4,679	556
Ireland	1	0	0	44	91	2
Italy	1	1	0	42	530	35

Netherlands	2	14	6	158	10,714	591
United Kingdom	5	7	3	411	5,624	277
Other European economies	0	9	3	21	6,516	290
Channel Island	0	7	2	14	5,446	158
Switzerland	0	1	1	7	1,070	133
North America	**21**	**10**	**11**	**1,546**	**7,185**	**1191**
Canada	0	1	0	6	568	47
United States	21	9	11	1541	6,617	1,144
Other developed economies	**3**	**2**	**1**	**248**	**1,587**	**59**
Australia	0	1	0	7	799	12
Bermuda	3	1	0	233	746	46
Japan	0	0	0	6	23	2
Developing economies	**65**	**48**	**68**	**-**	**36,498**	**7,239**
Africa	**10**	**12**	**14**	**750**	**9,321**	**1,521**
North Africa	1	3	0	54	2739	9
Egypt	0	1	0	9	821	7
Libya	0	0	0	13	143	1
Morocco	0	0	-	33	36	-
Nigeria	0	0	-	7	301	-
Sudan	-	2	-	-	1,191	-
West Africa	0	1	0	29	542	11
Central Africa	-	0	-	-	85	-
East Africa	9	8	14	638	6342	1430
Mauritius	8	8	13	618	6,165	1,426
Kenya	0	0	-	13	149	-
Southern Africa	0	0	1	29	154	72
South Africa	0	0	1	22	118	69
Asia and Oceania	**21**	**28**	**46**	**1544**	**21,032**	**4,923**
Asia	**21**	**28**	46	1544	**21,032**	**4,923**
West Asia	5	4	7	362	2,817	707
Oman	3	0	0	205	271	14
United Arab Emirates	2	3	6	110	2,232	665
East Asia	6	3	1	484	2,003	74

China	1	1	0	38	949	24
Hong Kong (China)	6	1	1	445	999	49
South Asia	3	1	0	224	654	47
South East Asia	6.3	20.5	38.6	474.5	15,559.0	4096.5
Singapore	2	19	38	153	14,384	4,017
Vietnam	3	0	0	229	341	2
Oceania	-	-	-	-	-	-
South East Europe/ Commonwealth of Independent States	**24**	**5**	**1**	**1,787**	**3,448**	**76**
South East Europe	-	-	-	-	-	-
CIS	24	5	1	1,787	3,448	76
Russia	23	4	1	1,749	3,106	73
Latin America and Caribbean	**11**	**4**	**7**	**821**	**2,697**	**718**
South and Central America	**0**	**1**	**0**	**31**	**766**	**46**
South America	0	1	0	30	622	14
Brazil	0	1	0	13	508	11
Uruguay	-	0.1	-	-	91	-
Central America	0	0	0	1	144	32
Caribbean and other America	11	3	6	**790**	**1930**	672
British Virgin Islands	10	2	5	777	1,627	567
Cayman Islands	0	0	1	12	221	104

*Source***:** Author's calculations, using data published by the Department of Economic Affairs in the Indian Ministry of Finance.
[a] This table relies on investment approval data, since the Indian Government does not yet publish a geographic breakdown of outward FDI flows. Data are by fiscal year (April 1 – March 31).

Annex table 4b. India's top 15 outward FDI destinations,[a] 1996-2002 and 2002-2009

1996-2002			**2002-2009**		
Economy	**Outflows received** (%)	**Outflows received** (US$ billion)	**Economy**	**Outflows received** (%)	**Outflows received** (US$ billion)
1. Russia	23.8	1.7	1. Singapore	20.8	14.2
2. United States	20.5	1.5	2. Netherlands	15.4	10. 6
3. British Virgin Islands	10.3	0.8	3. Mauritius	8.1	5. 6
4. Mauritius	8.2	0.6	4. Channel Island	7.9	5.4
5. Hong Kong (China)	5.9	0.4	5. United Kingdom	7.6	5.2
6. United Kingdom	5.5	0.4	6. United States	7.4	5. 1
7. Bermuda	3.1	0.2	7. Cyprus	6.8	4. 7
8. Vietnam	3.0	0.2	8. United Arab Emirates	3.1	2.1
9. Oman	2.7	0.2	9. Russia	2.0	1. 4
10. Netherlands	2.1	0.1	10. Sudan	1.7	1. 2
11. Singapore	2.0	0.1	11. Switzerland	1.6	1. 1
12. United Arab Emirates	1.5	0.1	12. China	1.3	0.9
13. Austria	1.0	0. 1	13. British Virgin Islands	1.2	0. 9
14. Nepal	0.9	0. 1	14. Egypt	1.2	0.8
15. Sri Lanka	0.8	0. 1	15. Denmark	1.2	0.8

Source: Author's calculations, using data published by the Department of Economic Affairs in the Indian Ministry of Finance,
[a] Rankings are based on the cumulative stock of outward investment approvals for each period.

Annex table 5. India: principal foreign affiliates, ranked by foreign assets, 2006
(US$ million)

Rank	Name	Industry	Foreign assets
1	Oil and Natural Gas Corporation (ONGC)	Oil and gas operations	4,700
2	Tata Group of companies	Conglomerate	4,200
3	Videocon Industries	Conglomerate	1,600
4	Ranbaxy Laboratories	Pharmaceuticals	1,000
5	Dr. Reddy's Laboratories	Pharmaceuticals	870
6	HCL Technologies	IT services	780
7	Hindalco Industries	Aluminum manufacturer	580
8	Sun Pharmaceuticals	Pharmaceuticals	280
9	Reliance Industries	Oil and gas	250
10	Suzlon Energy	Power and energy	140
11	Larsen and Toubro	Engineering and construction	130
12	WIPRO Technologies	IT services	130
13	Bharat Forge	Auto component solution provider (forging)	110
14	Patni Computer Systems	IT services	81
15	Hexaware Technologies	IT services	70
16	Biocon Limited	Pharmaceuticals	50
17	i-Gate Global Solutions	IT services	49
18	Max India Limited	Conglomerate	37
19	Mahindra & Mahindra	Automobile manufacturer	35
20	NIIT Limited	IT services	31
21	Piramal Healthcare Limited	Pharmaceuticals	26
22	Birlasoft (India) Limited	IT services	21
23	Raymond Limited	Fabric manufacturer	18
24	Infosys Technologies Limited	IT services	9

Source: Indian School of Business' and Vale Columbia Center on Sustainable International Investment's ranking of Indian multinationals, 2009, available at http://www.vcc.columbia.edu/files/vale/documents/India_2009.pdf

Annex table 6. India: main M&A deals, by outward investing firm, 2007-2009

Rank	Year	Acquiring company	Target company	Target industry	Target economy	Shares acquired (%)	Value (US$ billion)
1	2007	Tata Steel	Corus Goup	Metals and mining	United Kingdom	100%	12.2
2	2007	Hindalco Industries	Novelis	Metals and mining	Canada	100%	6.0
3	2008	Oil and Natural Gas Commission	Imperial Energy	Energy and power	United Kingdom	100%	2.8
4	2008	Tata Motors	Jaguar and Land Rover	Automotives	United States	100%	2.3
5	2007	Suzlon Energy	REpower Systems	Energy and power	Germany	66%	1.7
6	2007	Essar Global	Algoma	Metals and mining	Canada	100%	1.6
7	2007	Tata Power	Kaltim Prima Coal	Metals and mining	Indonesia	100%	1.3
8	2007	United Spirits	Whyte and Mackay	Food and beverage	United Kingdom	100%	1.2
9	2008	GMR Infrastructure	Intergen	Energy and power	Netherlands	50%	1.1
10	2008	Tata Chemicals	General Chemical Industrial	Plastic and chemicals	United States	100%	1.1
11	2007	JSW Steel	Jindal United Steel/ Saw Pipes	Metals and mining	United States	90%	0.9
12	2008	HCL-EAS	Axon Group	IT & ITES	United Kingdom	100%	0.8
13	2007	Wipro Technologies	Infocrossing	IT & ITES	United States	100%	0.6
14	2007	Rain Calcining	CII Carbon	Energy and power	United States	100%	0.6
15	2007	DS Constructions[a]	Globeleq (Latin America business)	Energy, power, and infrastructure	Bermuda	100%	0. 6
16	2008	Tata Consultancy Services	Citigroup Global Services	IT & ITES	India	100%	0.5
17	2007	Videocon/Bharat Petro Resources	Encana Brasil Petroleo	Energy and power	Brazil	50%	0.4
18	2007	Firstsource Solutions	MedAssist Inc	IT & ITES	United States	100%	0.3
19	2007	Reliance Communications	Yipes Holding Inc	Telecommunications	United States	100%	0.3
20	2009	Kiri Dyes and Chemicals	DyStar Group (selective assets)	Plastics and chemicals	Germany	100%	0. 2
21	2009	Essar Group	Warid Telecom (Uganda/Congo ops)	Telecommunications	Uganda/ Congo	51%	0. 2
22	2009	Inox India	Cryogenic Vessel Initiatives	Logistics	United States	51%	0. 1
23	2009	S. Kumar's	Hartmarx Corporation	Textiles and apparels	United States	100%	0.1

Source: Grant Thornton Deal Tracker *(*2007, 2008, 2009); Thomson One Banker, Thomson Reuters; and press reports.
[a]DS Constructions undertook this acquisition in a 50:50% JV with Israel Corporation.

Annex table 7. India: top 25 greenfield projects, by outward investing firm, 2007-2009

(US$ million)

Rank	Year	Investing company	Sector	Host economy	Estimated / announced transaction value
1	2008/09	National Thermal Power Corporation	Coal, oil and natural gas	Iran	5,150
2	2007	GAIL India	Chemicals	Saudi Arabia	4,150
3	2008	Tata Group	Metals	Vietnam	3,500
4	2008	ONGC	Coal, oil and natural gas	Iran	3,000
5	2006	ONGC	Coal, oil and natural gas	Iran	2,000
6	2008	Era Group	Coal, oil and natural gas	Zambia	1,800
7	2007	Mahindra Satyam *(earlier known as Satyam Computers Services)*	Software and ITES	Malaysia	1,714[a]
8	2009	Essar Group	Coal, oil and natural gas	Kenya	1,701[a]
9	2007	Videocon Industries	Consumer Electronics	Poland	1,700
10	2007	Ispat Industries	Metals	Philippines	1,600
11	2008	Essar Group	Metals	United States	1,600
12	2007	Videocon Industries	Consumer Electronics	Italy	1,576
13	2008	National Aluminium Company	Coal, oil and natural gas	Indonesia	1,500
14	2008/09	ONGC	Coal, oil and natural gas	Iraq	1,450
15	2008	SKIL Infrastructure	Real estate	Oman	1,200
16	2007	Ispat Industries	Coal, oil and natural gas	Montenegro	1,100
17	2007	Reliance Industries	Chemicals	Egypt	1,000
18	2007	Jindal Organisation	Metals	United States	1,000
19	2008	BSEL Infrastructure Realty	Real estate	Malaysia	940
20	2007	Tata Group	Automotive OEM	Argentina	905
21	2006/07	Darvash Group	Metals	United Arab Emirates	817
22	2008	Indian Farmers' Fertiliser Cooperative (IFFCO)	Minerals	Australia	800
23	2009	Sanghi	Coal, oil and natural gas	Kenya	749[a]
24	2008	Jindal Organisation	Metals	Indonesia	700
25	2007	Krishak Bharati Cooperative	Chemicals	Oman	675[a]

Source: fDi Intelligence, a service from the Financial Times Ltd.

[a] Estimated.

Chapter 19 – Pakistan

Inward FDI and its policy context, 2010

Khalil Hamdani

Pakistan's large domestic market and policy environment are generally attractive to foreign direct investment, but terrorist violence and natural disasters are keeping investors at bay. Pakistan was the tenth largest recipient of IFDI in Asia in 2006-2008. Pakistan has also been successful in attracting investment from other developing countries. There are successful joint ventures with parastatals. The policy regime is investor-friendly, and doing business in Pakistan is easier than in any of its neighboring countries. These advantages notwithstanding, IFDI flows shrank by 60% in 2009-2010, a reflection of global trends and internal difficulties. Governance and terrorism are overriding preoccupations. Retaining the confidence of both foreign and domestic investors is vital. Determined efforts are needed to realize the country's considerable market potential.

Trends and developments

Country-level developments

Foreign direct investment (FDI) has played a small but important role in Pakistan's economic development. The share of IFDI to GDP has been less than 1% in most years. Nevertheless, FDI was crucial for the success of import substitution and infant industry policies in the formative years after independence in 1947, through joint ventures or licensing, franchising and distribution arrangements between start-up Pakistani firms and foreign companies.[514] Non-equity ties facilitated technology transfer. Food processing, manufacturing (consumer goods, pharmaceuticals, machinery, auto parts, vehicle assembly), and services (banking and insurance) attracted FDI geared to the domestic market.

In the early years, Pakistan attracted more FDI than its much larger neighbors. Annual IFDI flows to Pakistan were greater than those to India for most years from 1947 to 1993, although the amounts involved for both countries were relatively small (averaging less than US$ 200 million annually). As late as 1995, the two countries had about the same level of IFDI stock, approximately US$ 5.6 billion. Since then India has emerged as one of the world's preferred investment destinations.[515]

Pakistan's stock of IFDI increased at an average annual rate of 12.5% between 1990 and 2009, reaching US$ 18 billion in 2009 (annex table 1). This relatively good performance, driven by policy liberalization and investment promotion, was comparable to that of other developing countries that have opened up in an expansive period of worldwide FDI growth.[516]

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[514] The entry conditions permitted FDI in a positive list of (mainly manufacturing) industries and otherwise required, for large investments, formation of joint stock companies with local equity participation. These restrictions were removed in the 1990s.

[515] Premila Nazareth Satyanand and Pramila Raghavendran, "Inward FDI in India and its policy context," *Columbia FDI Profiles*, March 12, 2010, available at: http://www.vcc.columbia.edu.

[516] See, for instance, the comparator data for Iran and Peru in annex table 1.

The main distinctive feature was the large FDI inflow from 2005 onwards. IFDI flows averaged US$ 4 billion annually in 2005-2009 (annex table 2), a level commensurate with the size of Pakistan's population (175 million) and its economy. During this period, FDI comprised 15% of gross fixed capital formation compared with an average for developing countries of 12%. Pakistan ranked briefly among the top 10 FDI recipients in Asia.

As a consequence, the stock of Pakistan's IFDI more than doubled from 2000 to 2009, and its composition (annex table 3) and origin (annex table 4) have become further diversified. The sectoral composition of IFDI had already shifted in the 1990s from manufacturing to services. Manufacturing was predominant in the early years (75% of IFDI flows in 1980), but from 1994 onward the services sector attracted much IFDI. By 2001, the share of services in the stock of IFDI had risen to 72% while that of manufacturing had fallen to 22%.[517] Deregulation and fiscal incentives attracted FDI into power projects. In the past decade privatization attracted sizeable cross-border acquisitions in banking and telecommunications. These were noteworthy for being South-South deals.

The traditional home countries for Pakistan's IFDI have been the United Kingdom and the United States, followed by Switzerland, Japan, the Netherlands, and Germany. Pakistan has also been successful in attracting investment from Asia and the Middle East, with the United Arab Emirates (U.A.E.) being the largest investor in 2006-2008. A third of the IFDI stock in 2006 originated from developing countries and was diversified in a wide range of industries, including telecommunications, financial services, cement, textiles, construction, real estate, logistics, airlines, and oil and gas.

The principal home countries, whether developed or developing, have investments in all sectors (primary, secondary, tertiary). At the same time, IFDI from developed countries is concentrated more in manufacturing, while that from developing countries is stronger in services.

IFDI flows to Pakistan receded during the global crisis and short-run prospects are not encouraging. FDI inflows in the period January to November 2010 totaled US$ 1.8 billion and, given the widespread devastation caused by this year's monsoon floods, inflows are unlikely to exceed US$ 2 billion for the whole year - a decline of more than 60% over two years.

The corporate players

Foreign companies have operated in Pakistan for many years, even before independence. The first Swiss cotton trading subsidiary was set up by the Volkart Brothers in 1861 and the London-based Chartered Bank set up operations in Karachi in 1863. Other early entrants and continuing major players include Shell Petroleum (1903), Siemens (1922) and Imperial Chemical Industries (1944).

The initial years after independence (1947-1972) were largely "laissez-faire", attracting market-seeking FDI in a wide range of manufacturing industries. The investments were often undertaken with local partners. The first foreign affiliate, Pakistan Tobacco (British-

[517] UNCTAD, *World Investment Report 2004: The Shift towards Services* (New York and Geneva: United Nations, 2004), p. 55.

American Tobacco), was incorporated in 1947. Lever Brothers Pakistan Limited (Unilever) incorporated in 1948; it is today the largest consumer goods manufacturer in the country. Pharmaceuticals have attracted a number of foreign players (from Switzerland, the United Kingdom and the United States), of which GlaxoSmithKline is the largest in the country. The transport equipment industry has been popular with Japanese companies, whose activity has been mainly assembly operations.

A general failure of manufacturing affiliates in all industries has been the reluctance to develop an export-oriented approach, even within the global network of their parent companies. This is in part attributable to the protected markets within which they have operated – the downside of earlier trade and industrial policies that successfully attracted IFDI.[518] Departures from this insular trend include recent vehicle exports by Suzuki to Bangladesh and sheet metal parts exports to Europe, and school buses exports by Hinopak to the U.A.E. ICI Pakistan exports to regional markets in the Middle East and Central Asia. As part of an offset deal for the purchase of aircraft, Boeing has transferred technology to enable the manufacture of spare parts in Pakistan for its global supply chain.[519]

There are several cross-border joint ventures between parastatals. Notable among these is the Pak-Arab Refinery (PARCO), a US$ 1.2 billion joint venture between the governments of Pakistan and the Emirate of Abu Dhabi.

Financial services were privatized in 1991 and now account for nearly 20% of IFDI stock, much of it originating from developing countries (Bahrain, Kuwait, Malaysia, Oman, U.A.E.). Islamic banking is an emerging niche subsector.

The country's largest privatized bank, Habib Bank (HBL), has a curious history, with ownership changing hands from the Pakistani private sector to the public sector to a foreign investor. The bank was privately established in 1947 and was also Pakistan's first MNE (when it opened a branch in Sri Lanka in 1951). After the industry was nationalized in 1972, the original owners set up a new bank in Switzerland with operations in Pakistan.[520] HBL was later privatized in 2003 and is now majority-owned and controlled by the Aga Khan Fund for Economic Development (Switzerland).

Communications (13% of IFDI stock) has also benefited from privatization and FDI from China, Egypt and U.A.E. The 2006 acquisition by Etisalat (U.A.E.) of a 26% share of the national telecommunications company was valued at US$ 2.6 billion. China Mobile established its first overseas subsidiary with investments of US$ 1.7 billion and plans for an additional US$ 300 million in 2010. Orascom (Egypt) operates the largest GSM network and subscriber base. The second largest GSM provider is Norway's Telenor, which is also innovating in mobile banking.

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[518] For a discussion of trade policy see Parvez Hasan, "Pakistan's trade strategies and performance: missed opportunities and current challenges," in Michael Kugelman and Robert M. Hathaway, eds., *Hard Sell: Attaining Pakistani Competitiveness in Global Trade* (Washington D.C.: Woodrow Wilson International Center for Scholars, April 2008), available at: www.wilsoncenter.org/topics/pubs/asia_hard.sell.pdf.

[519] The US$ 1.8 billion purchase order was made in 2002, the aircrafts were delivered in 2004-2008 and the manufacturing facility for spare parts became operational in 2006.

[520] The irony of the Habib family operating as a multinational in their own country was commemorated with a 5-rupee postage stamp issued by the Pakistan Post Office in March 2001 displaying the logo and headquarters of the Swiss multinational, *Habib Bank AG Zurich*.

The power sector has attracted IFDI, but not without cost. Independent power producers (domestic and foreign) proliferated in the 1990s under a generous incentive structure,[521] which entailed large foreign exchange outflows (interest, dividend and fuel payments).[522] Public utilities had difficulty maintaining the payment schedule necessary to sustain the supply of uninterrupted power, contributing to recent power shortages, which abruptly disrupted all industries. Net FDI inflows have so far been negative in 2010, notwithstanding 2008 announcements of US$ 4 billion in alternative energy greenfield projects originating mainly from China, Turkey and the United States.

Extractive industries account for 11% of IFDI stock and are the main attraction for IFDI in Pakistan at the present time. The Government of Pakistan is aggressively awarding concessions for oil and gas exploration. A dozen foreign companies have invested, including BP, ENI (Italy), BHP Billiton (Australia), OMV (Austria), Petronas (Malaysia), and Premier Oil (UK), and one specifically plans to explore offshore, Petrobras (Brazil).

There was foreign equity participation in about 1,100 enterprises in 2008[523], by approximately 100 British, 66 US and 15 Swiss companies.[524] Dutch multinationals are also big corporate players in Pakistan (Shell, ICI, Lever Brothers, Philips).[525]

Effects of the current global crisis

Pakistan is in a better position than most countries in attracting foreign investment in the current global crisis as it has a large domestic market and untapped natural resources. Pakistan has also been able to maintain economic growth (4% in 2009 and 2010), thanks to a US$ 11.3 billion IMF Stand-By Arrangement, continued inflows of remittances from migrants abroad (US$ 8 billion per year in 2009-2010) and reasonably good harvests (though probably not recently after the 2010 deluge).

Nevertheless, some decline in FDI inflows was to be expected, as Pakistan's main FDI sources are developed countries where the current crisis has been most acute. Also, with the current uncertainty in the global environment, investors are particularly risk averse. On balance, political risk appears to have been an overriding consideration, as FDI inflows to Pakistan in 2009 contracted by more than twice as much as that to developing countries as a whole.[526]

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521 The 1994 Power Policy guaranteed purchase of the power produced at a pre-set, dollar-indexed tariff structure, ensured fuel supply, protected against changes in duties and taxes and also provided foreign exchange convertibility and duty free import of plant and equipment; up to 40% of the capital costs of the project; free repatriation of equity along with dividends; and foreign exchange risk insurance on foreign currency loans. See Ashfaque H. Khan and Yun-Hwan Kim, "Foreign direct investment in Pakistan: Policy issues and operational implications," EDRC Report Series No. 66, Asian Development Bank, July 1999, available at: www.adb.org/documents/edrc/reports/er066.pdf.

522 The 1994 Power Policy had the support of the World Bank and other agencies, while the United Nations (this author, in particular) had cautioned against the incentive scheme.

523 The State Bank of Pakistan conducts an annual survey of foreign liabilities and assets (available at: www.sbp.org.pk/publications/iipp). The 2008 survey recorded 81 branches of foreign companies and 698 Pakistani companies with foreign equity participation. The response rate was 70% in 2007, which suggests an overall size of 1,100.

524 The numbers are rough, culled from membership in chambers of commerce, business councils and embassy press releases.

525 ICI Pakistan is now Dutch-owned after the global acquisition of ICI by AkzoNobel in 2008.

526 FDI inflows to developing countries contracted by 27% in 2009. See UNCTAD, *World Investment Report 2010: Investing in a Low-carbon Economy* (Geneva: United Nations, 2010), available at: www.unctad.org/en/docs/wir2010_en.pdf.

This contraction suggests an erosion of investor confidence. One-third of the fall in FDI inflows since 2008 is explained by lower reinvested earnings and two-thirds are due to lower equity inflows and fewer intra-company loans. Reinvested earnings of foreign affiliates declined by almost 75% in 2009. Recent surveys indicate that foreign companies have lower investment plans for 2010 and that business confidence fell in the second quarter of 2010.[527] The three concerns most cited by business are: law and order, the energy deficit (frequent power cuts) and government stability.

A US$ 5 billion greenfield investment by Boeing to manufacture aircraft spare parts, following its 2006 offset arrangement, was postponed in 2010.[528]

At the corporate level, the global crisis has prompted parent companies to rationalize activities and in some cases to divest entirely in the host economy. Thus, the worldwide consolidation of the Royal Bank of Scotland led to the 2010 fire sale of its former-ABN AMRO operation in Pakistan to the Faysal Bank (majority-owned by the Ithmaar Bank of Bahrain).

There was also consolidation in the pharmaceuticals industry, when Merck Sharp & Dohme, which had entered Pakistan in 1962, departed in 2008, and when Bristol Meyers Squibb, another long-time investor, sold its operations in 2009.

A feature of the current global crisis is increased market-seeking activity of multinationals in emerging markets (so as to sustain revenue growth through worldwide sales). Examples in Pakistan include the expansion of Coca-Cola (through its affiliate in Turkey), Metro Cash & Carry (Germany) and similar greenfield investments from Saudi Arabia and U.A.E. in retail and wholesale trade, hotels and shopping complexes.[529]

The policy scene

Pakistan's investment regime is as open as in any other developing country, and the country has an investment incentive structure more generous than most.[530] The welcome to foreign investors is longstanding. A notable milestone was the signing with Germany in 1959 of the first BIT in the world. The early 1970s were marred by nationalization, which was prevalent in the region, including India and Sri Lanka.[531] Although foreign enterprises were exempted,[532] new equity inflows collapsed.[533] A process of policy liberalization ensued from the mid-1970s onward.

[527] The surveys (available at: www.oicci.org/forms/publication.aspx) were conducted by the Overseas Investors Chamber of Commerce & Industry, Karachi. The Chamber is the oldest in Pakistan and has 185 member companies with output accounting for 14% of GNP.
[528] The decision was also attributed to unfavorable government policy, as reported by Azhar Masood, "Boeing puts investment in Pakistan on hold", 4 July 2010, available at: http://arabnews.com/saudiarabia/article78632.ece.
[529] These investments are reflected in relatively large shares of trade and of other services in IFDI flows for 2009 (annex table 3a).
[530] For a review of the policy regime see Khan and Kim, op. cit.
[531] In the case of Pakistan, the mood was exemplified by the observation of the Chief Economist of the Planning Commission, Mahbub ul Haq, in April 1968 that Pakistan's industry was largely owned by just 22 families.
[532] The American Life Insurance Company (ALICO), with an investment of more than US$ 36 million, was nationalized in 1972; it was denationalized in 1994 and is the largest foreign investment in insurance. The petroleum operations of ESSO were taken over in 1976 and placed under Pakistan State Oil; however, the ESSO fertilizer plant (US$ 43 million), the largest foreign investment in Pakistan at the time, was not affected. Some foreign companies (e.g., Shell) reduced shareholdings to below 50% in their locally registered affiliates.
[533] Direct investment fell from US$ 70 million in 1972 to zero in 1973, and turned negative (to -US$ 6 million) in 1974. It did not recover until 1981.

By the mid-1990s, restrictions to entry, ownership, admission, and repatriation had been greatly relaxed or eliminated. Investor guarantees, property protections and national treatment are stipulated in the constitution and relevant laws.[534] Incentives for foreign investors include a variety of credit facilities, concessional customs duties, tax holidays, a favorable visa policy, and special investment zones. It is easier to do business in Pakistan than in any of the neighboring countries of South Asia.[535]

The privatization program and incentive packages have not been without controversy (i.e., surrounding the transparency of the deals, job losses and/or profit repatriations).[536] The privatization process was set back in 2006 when the Supreme Court, citing irregularities, annulled the divestment of Pakistan Steel Mills.[537]

A major dispute is looming in the minerals sector, which is governed at the provincial level, unlike oil and gas, which is regulated at the federal level. The authorities in Balochistan Province have threatened to cancel the mining licence of the Reko Diq copper and gold mine held by a consortium led by the Canadian Barrick Gold Corporation and the Chilean mining company Antofagasta. The exploration license grants exclusive rights to explore and, subject to certain investment requirements, also to develop, mine and sell minerals discovered within the license area. The exploration has found significant deposits, and provincial authorities are unhappy with the terms of the development project (involving new FDI inflows of US$ 3.2 billion). The federal government (i.e. the Prime Minister) has intervened between the provincial authorities and the mining companies. In the interim, the dispute is a blemish on the country's otherwise welcoming attitude toward FDI.

New developments: handling terrorism risk

Although the weight of terrorism on investment decisions is unclear,[538] a recent survey ranks political risk as a major investor concern in developing countries and places Pakistan among the five most risky investment destinations.[539] In order to provide insurance cover against terrorism, a Political Risk Guarantee Facility was created by the Asian Development Bank in 2002. The facility is counter guaranteed and indemnified by the Pakistani Government. The liability coverage (up to US$ 175 million) may be increased through commercial reinsurance arrangements. There have so far been no terrorist incidents targeting FDI in Pakistan.[540]

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[534] As of May 2010, Pakistan had concluded 47 BITs and 51 DTTs (UNCTAD, op. cit.).

[535] For example, it takes less time and costs to start a business in Pakistan than in India or any other country in the subcontinent. Pakistan also scores high on investor protection. See: World Bank Group, *Doing Business 2010*, available at: www.doingbusiness.org/reports/doing-business/doing-business-2010.

[536] Pakistan ranks low on perception of public sector transparency, lower than (but not by much) other South Asian countries; see the 2010 index of Transparency International (available at: transparency.org/policy_research/surveys_indices/cpi/2010/results).

[537] Judgment of the Supreme Court in Pakistan Steel Mills Privatization Case, August 9, 2006.

[538] Daniel Wagner, "The impact of terrorism on foreign direct investment", February 2006, available at: www.irmi.com/expert/ articles/2006/wagner02.aspx.

[539] World Bank Group, *World Investment and Political Risk Report 2009*, available at: www.miga.org/documents/ flagship09ebook.pdf.

[540] In the view of the largest home country investors as expressed by the Executive Director of the U.S.-Pakistan Business Council: "Although the perception of Pakistan in the United States is often dominated by issues surrounding security and terrorism, a story that lacks attention from the mainstream media is that many American companies have successful operations and continue to explore opportunities for investment in Pakistan." See Esperanza Gomez Jelalian, "A perspective from the U.S. business community in Pakistan: Key issues and opportunities," in Kugelman and Hathaway, op. cit.

The United States Congress is also considering a new US$ 300 million enterprise fund to provide upfront risk capital to spur IFDI in Pakistan. This fund would be financed from within the foreign aid allocation. Such facilities are not entirely new. The U.S. Overseas Private Investment Corporation and MIGA provide risk insurance for Afghanistan. The United States has also set up enterprise funds for the transition economies of Eastern and Central Europe, and countries of the former Soviet Union.

Conclusions and Outlook

Pakistan welcomes foreign investors and had experienced large FDI inflows before the global downturn. The economy has overcome government instability in the past, and recovered relatively quickly after the 2005 earthquake. Nevertheless, current circumstances are dire: FDI inflows have declined by 60% since 2008, and the downslide is continuing. Pakistan can expect to continue to receive FDI in extractive industries (which tend to be impervious to the investment climate) and also from the more resilient economies of developing Asia. However, these inflows are offset by an overall fall in reinvested earnings.

Thus, immediate prospects for reversing the current decline of IFDI hinge on efforts made by the Government of Pakistan to retain the confidence of investors. They include potential as well as existing investors, some of whom have been operating in Pakistan for many years. They also include domestic investors, whose actions shape perceptions of new investors. Determined efforts need to be made, through dialogue and partnership with the private sector, to tap into the country's substantial resource capacity and its considerable market potential.

Additional readings

Amjad, Rashid, *Private Industrial Investment in Pakistan, 1960-1970* (Cambridge: Cambridge University Press, 1982).

Khan, Ashfaque H. and Yun-Hwan Kim, "Foreign direct investment in Pakistan: Policy issues and operational implications," *EDRC Report Series No. 66*, Asian Development Bank, July 1999.

Kugelman, Michael and Robert M. Hathaway, eds., *Hard Sell: Attaining Pakistani Competitiveness in Global Trade* (Washington D.C.: Woodrow Wilson International Center for Scholars, April 2008).

Useful websites

For FDI policy and regulation: Government of Pakistan, Board of Investment, available at: www.pakboi.gov.pk.

For FDI statistics: State Bank of Pakistan, available at: www.sbp.org.pk.

For economic statistics: Government of Pakistan, Ministry of Finance, available at: http://www.finance.gov.pk.

For economic research: Pakistan Institute of Development Economic, available at: www.pide.org.pk.

Statistical annex

Annex table 1. Pakistan: inward FDI stock, 2000-2009 (US$ billion)

Economy	1990	2000	2009
Pakistan	1.9	6.9	17.8
Memorandum: comparator economies			
India	1.7	16.3	164.0
Iran	2.0	2.6	24.0
Peru	1.3	11.1	36.9
Philippines	4.5	18.2	23.6

Source: UNCTAD's FDI/TNC database, available at: http://stats.unctad.org/fdi/.

Annex table 2. Pakistan: inward FDI flows, 2000-2009 (US$ billion)

Economy	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
Pakistan	0.3	0.4	0.8	0.5	1.1	2.2	4.3	5.6	5.4	2.4
Memorandum: comparator economies										
India	2.3	3.4	3.5	4.3	5.3	6.7	20.3	25.0	40.4	34.6
Iran	0.2	1.1	3.7	2.7	2.9	3.1	1.6	1.7	1.6	3.0
Peru	0.8	1.1	2.2	1.3	1.6	2.6	3.5	5.5	6.9	4.8
Philippines	2.2	0.2	1.5	0.5	0.7	1.9	2.9	2.9	1.5	1.9

Source: UNCTAD's FDI/TNC database, available at: http://stats.unctad.org/fdi/.

Annex table 3. Pakistan: distribution of inward FDI stock, by economic sector and industry, 2006, 2008 (US$ million or percentage shares)

Sector/industry	2006	2008
All sectors/industries	**13,681.9**	**16,472.9**
Primary (%)	**10.6%**	**10.4%**
Oil and gas exploration	1,450.0	1,706.5
Secondary (%)	**34.8%**	**30.5%**
Food	651.4	847.5
Chemicals	986.9	711.8
Petroleum refining	349.9	481.2
Pharmaceuticals	586.7	711.3
Transport equipment	1,014.2	823.3
Other manufacturing	1,167.3	1449.9
Tertiary (%)	**51.2%**	**58.0%**
Power	1,551.5	1,563.0
Trade	586.1	1,284.6
Communications	1,766.6	2,593.3
Finance	2,569.6	3,831.1
Other services	534.2	277.2
Unspecified (%)	**3.4%**	**1.1%**

Source: State Bank of Pakistan, available at: www.sbp.org.pk/publications/iipp.

Annex table 3a. Pakistan: distribution of inward FDI flows, by economic sector and industry, 2001, 2009 (US$ million or percentage shares)

Sector/industry	2001[a]	2009
All sectors/industries	**484.8**	**2,387.7**
Primary (%)	**56.7%**	**27.8%**
Mining	6.6	6.5
Oil and gas exploration	268.2	657.8
Secondary (%)	**13.6%**	**28.6%**
Food	7.6	65.8
Chemicals	12.9	121.2
Petroleum refining	2.8	108.2
Pharmaceuticals	7.2	12.9
Transport equipment	1.1	44.2
Other manufacturing	34.5	330.8
Tertiary (%)	**27.1%**	**40.0%**
Power	36.4	145.9
Trade	34.2	118.9
Communications	12.7	189.6
Finance	3.6	169.9
Other services	57.2	331.4
Unspecified (%)	**2.6%**	**3.6%**

Source: State Bank of Pakistan, available at: www.sbp.org.pk/ecodata/nifp_arch/index.asp.
[a] Data for fiscal year, from July 2001 to June 2002.

Annex table 4. Pakistan: geographical distribution of inward FDI stock, 2006, 2008
(US$ million or percentage shares)

Region/economy	**2006**	**2008**
World	**13,681.9**	**16,472.9**
Developed economies (%)	**57.6**	**65.4**
Australia	61.5	212.0
Austria	86.9	136.6
France	32.0	172.7
Germany	419.3	436.5
Ireland	62.4	58.7
Japan	871.0	812.9
Luxembourg	48.9	34.9
Netherlands	798.4	787.3
Switzerland	998.0	1707.8
Sweden	40.1	59.6
United Kingdom	2,664.9	4241.7
United States	1,754.7	1638.5
Others	44.1	480.5
Developing economies (%)	**32.4**	**32.8**
Bahrain	78.1	183.3
British Virgin Island	6.4	114.9
Cayman Island	170.8	224.0
China	34.1	694.8
Hong Kong (China)	110.7	254.6
Kuwait	130.6	258.9
Libya	37.8	53.1
Malaysia	64.6	353.0
Mauritius	379.0	608.1
Oman	123.8	196.3
Saudi Arabia	581.0	148.9
Singapore	12.7	201.2
United Arab Emirates	2,573.5	1663.9
Others	126.1	447.1
Unspecified (%)	**10.0**	**1.8**

Source: State Bank of Pakistan, available at: www.sbp.org.pk/publications/iipp.

Annex table 4a. Pakistan: geographical distribution of inward FDI flows, 2001, 2009
(US$ million or percentage shares)

Country/region	2001 [a]	2009
World	**484.8**	**2387.7**
Developed economies (%)	**77.8**	**61.5**
Australia	0.4	90.4
Canada	3.5	1.3
Denmark	0.8	0.9
France	-6.9	5.9
Germany	11.2	79.4
Japan	6.5	36.7
Luxembourg	0.0	1.4
Netherlands	-5.1	149.1
Norway	0.1	37.3
Switzerland	7.4	182.8
Sweden	0.8	1.5
United Kingdom	30.3	197.0
United States	326.4	610.0
Others	1.8	74
Developing economies (%)	**14.7**	**16.1**
Bahamas	0.0	8.9
Bahrain	21.9	17.0
Bangladesh	1.7	0.2
Cayman Island	0.6	111.7
China	0.3	-109.9
Egypt	0.3	0.7
Hong Kong (China)	2.8	14.5
India	0.0	0.5
Iran	0.0	7.4
Korea, Rep. of	0.5	2.7
Kuwait	2.2	2.8
Libya	0.0	3.3
Malaysia	0.9	-2.5
Mauritius	0.0	57.9
Oman	3.2	-5.2
Qatar	1.0	0.9
Saudi Arabia	1.3	-82.3
Singapore	3.9	102.1
Turkey	0.0	15.9
United Arab Emirates	20.5	166.1
Others	10.2	71.3
Unspecified (%)	**7.5**	**22.4**

Source: State Bank of Pakistan, available at: www.sbp.org.pk/ecodata/nifp_arch/index.asp.
[a] Data for fiscal year, from July 2001 to June 2002.

Annex table 5. Pakistan: principal foreign affiliates,[a] ranked by sales, 2008-2009
(Pakistan Rupee billion)

Name of affiliate or local company	Home country of parent company or foreign partner	Industry	Annual sales in 2008-2009 [b]
A. Secondary Sector			
Attock Oil Group [c]	U.K./Saudi Arabia	Diversified	170
Shell Pakistan	U.K./Netherlands	Petroleum	100
Indus Motor	Japan	Transport equipment	61
Nestle Pakistan	Switzerland	Food	41
Lotte Pakistan PTA	Korea, Rep. of	Chemicals	39
Unilever Pakistan	U.K./Netherlands	Consumer goods	38
Atlas Honda Group [d]	Japan	Transport equipment	36
Siemens Pakistan	Germany	Electrical equipment	36
ICI Pakistan	Netherlands	Chemicals	32
Pak Suzuki Motors	Japan	Transport equipment	26
Pakistan Tobacco	U.K.	Tobacco	21
GalxoSmithKline Pakistan	U.K.	Pharmaceuticals	15
Lakson Tobacco	U.S.	Tobacco	13
Colgate-Palmolive Pakistan	U.S.	Consumer goods	12
Hinopak Motors	Japan	Transport equipment	11
Dawood Hercules Chemicals	U.S.	Fertilizers	11
B. Tertiary Sector			
Habib Bank	Switzerland	Finance	87
United Bank	U.A.E.	Finance	74
MCB Bank	Malaysia	Finance	61
Bank Alfalah	U.A.E.	Finance	40
Standard Chartered Bank	U.K.	Finance	34
Habib Metropolitan Bank	Switzerland	Finance	25
Faysal Bank	Bahrain	Finance	20
Royal Bank of Scotland	U.K.	Finance	14

Source: Author's compilation, based on UNCTAD, *World Investment Directory, Volume VII: Asia and the Pacific*, (Geneva: United Nations, 2000); and company websites. For sales data: Wright Investors' Service, available at: www.corporateinformation.com.

[a] Foreign affiliates include firms owned by individual multinationals, even if these firms are registered in Pakistan as separate limited companies. The list excludes affiliates in which foreign shareholdings exceed 10%, when these affiliates are controlled by local investors or government, such as two of the largest enterprises in Pakistan, the HUBCO power company (with Saudi Arabia/U.K. equity) and the PARCO refinery (with U.A.E. equity), as well as the Pakistan Telecommunication Company (with U.A.E. equity).

[b] The sales data are not strictly comparable, as these vary by definition (e.g. income in the case of financial institutions) and year, and are presented only to illustrate rough rank.

[c] Includes Attock Oil (incorporated in the U.K. in 1913), Pakistan Oilfields, Attock Refinery, National Refinery, Attock Petroleum, Attock Cement and Attock Information Technology Services; majority owned by the Saudi based Pharaon Group. The sales data is for some of these entities.

[d] Includes two entities, Atlas Honda (motorcycles) and Atlas Honda Cars.

Annex table 6. Pakistan: main cross-border M&A deals (completed transactions), 2007-2009 (US$ million)

Year	Acquiring company	Home economy	Target company	Target industry	Shares acquired (%)	Value
2009	GlaxoSmithKline PLC	United Kingdom	Bristol-Myers Squibb Pakistan	Pharmaceuticals	100.0	36.7
2009	KP Chemical Corp	Korea, Rep. of	Pakistan PTA Ltd	Chemicals	75.0	12.0
2008	Maybank	Malaysia	MCB Bank Ltd	Finance	20.0[a]	886.5
2008	Oman Telecomm. Co	Oman	Worldcall Telecom Ltd	Communications	65.0	204.0
2008	Investor Group	Oman	Saudi Pak Commercial Bank Ltd	Finance	86.6	202.5
2008	Investor Group	Japan	Indus Motors Co Ltd	Transport equipment	12.5	56.5
2008	Noor Finl Invest KSCC	Kuwait	Meezan Bank Ltd	Finance	11.2[a]	23.5
2008	International Resorts Co KSCC	Kuwait	Al Marwa Haj & Umrah Svcs Co	Transport services	22.7	10.8
2007	SingTel	Singapore	Warid Telecom(Pvt)Ltd	Communications	30.0	758.0
2007	Philip Morris Intl Inc	Switzerland	Lakson Tobacco Co Ltd	Tobacco	50.2	339.0
2007	Orascom Telecom Holding SAE	Egypt	Mobilink	Communications	31.3[a]	290.9
2007	China Mobile Commun Corp	China	Paktel Ltd	Communications	88.9	284.0
2007	Xinjiang Zhongxin Resources	China	Mortuk Oilfield	Petroleum	100.0	250.0
2007	ABN-AMRO Holding NV	Netherlands	Prime Commercial Bank Ltd	Finance	96.2[a]	234.2
2007	Noor Finl Invest KSCC	Kuwait	Meezan Bank Ltd	Finance	19.0	38.1
2007	Investor Group	United Kingdom	KASB Capital Ltd	Finance	-	33.0
2007	Investor Group	Qatar	Burraq Telecom Co Ltd	Communications	75.0	12.3

Source: Thomson ONE Banker. Thomson Reuters.
[a] Comprises 2 transactions.

Annex table 7. Pakistan: main announced greenfield projects, by inward investing firm, 2007-2009 (US$ million)

Year	Investing company	Home economy	Industry	Investment value	Notes
2009	Wartsila	Finland	Power	666	*a*
2009	Xenel Industries	Saudi Arabia	Power	659	*a*
2009	China Mobile	China	Communications	500	
2009	Dubai Islamic Bank	U.A.E.	Finance	448	*a, b*
2009	Total	France	Petroleum	406	*a*
2009	OMV	Austria	Oil and gas	112	*a*
2009	Yamaha	Japan	Transport equipment	150	
2009	Metro	Germany	Trade	55	*a*
2009	MOL	Hungary	Oil and gas	40	
2009	Laboratorios Bago	Argentina	Pharmaceuticals	10	
2008	Global EnviroScience Technologies	U.S.	Power	2,950	*c*
2008	Zorlu Holding	Turkey	Power	950	*a*
2008	Dana Gas	U.A.E.	Oil and gas	414	*a*
2008	MAF Group	U.A.E.	Trade	403	*a*
2008	Al-Tuwairqi Group	Saudi Arabia	Metals	265	
2008	Tetra Laval	Switzerland	Plastics	141	
2008	Jura Energy	Canada	Oil and gas	112	*a*
2008	ENI	Italy	Oil and gas	162	*a, c*
2008	Coca-Cola	U.S.	Beverages	100	
2008	Procter & Gamble	U.S.	Chemicals	100	
2008	Nanjing Sunec Wind Generator Equip. Factory	China	Power	98	
2008	BASF	Germany	Chemicals	91	*a*
2008	DTS Corporation	Japan	Communications	50	
2007	Hutchison Whampoa	Hong Kong (China)	Logistics	1,000	
2007	China Mobile	China	Communications	860	*c*
2007	Enshaa Holdings	U.A.E.	Construction	362	*a*
2007	Daewoo International	Korea, Rep. of	Transport equipment	229	*a*
2007	Toyota Motor	Japan	Transport equipment	180	
2007	Carlson Companies	U.S.	Hotels	339	*a, c*
2007	Fair Energy	Switzerland	Petroleum	100	
2007	Temasek Holdings	Singapore	Logistics	92	*a*

2007	Metro	Germany	Trade	59	*a*
2007	SHV Holdings	Netherlands	Trade	59	*a*
2007	Credit Suisse Group	Switzerland	Finance	33	*a*
2007	JP Morgan Chase & Co	United States	Finance	33	*a*

Source: fDi Intelligence, a service from the Financial Times Ltd.
[a] Estimated value.
[b] Comprises 11 projects.
[c] Comprises 2 projects.

Chapter 20 – Peru

Inward FDI and its policy context, 2010

Benjamin Chavez and Jaime Dupuy

Peru has shifted from being a small FDI player in the Latin America and Caribbean region in the 1990s to being the sixth largest FDI host country in 2008. With inflows of US$ 6.9 and US$ 4.8 billions in 2008 and 2009, respectively, Peru has managed to contain the impact of the financial crisis on IFDI. The main determinants of the improved FDI performance were: a stable economic and FDI policy since 1992;) vast natural resources; strong GDP and market growth; and an export-oriented economy, especially during the past decade. In recent years, Peru has become one of the fastest growing economies in Latin America and a diversified commercial hub for IFDI in the region.

Trends and developments

Country-level developments

In 1990, before liberalization started, Peru had accumulated only US$ 1.3 billion of IFDI stock. After the enactment of the 1993 Constitution, Peru was able to attract substantial IFDI to major such extractive industries as mining, oil and gas, and the country experienced remarkable IFDI growth in the secondary and tertiary sectors.

In 2009, Peru's IFDI stock reached US$ 35 billion (annex table 1). The main drivers of IFDI in the past two decades were policy liberalization, vast natural resources, relatively strong GDP and market growth, and the recent export orientation.[541] Policy liberalization included privatizations and open access to almost all sectors.[542]

Peru's average annual IFDI flows almost tripled, from US$ 1 billion during 1990-1999 to US$ 2.7 billion during 2000-2009 (annex table 2). Although the country is still far from the level of inflows reached by Chile and Colombia (natural competitor countries at the South Pacific coast), its importance as a host country in the region has shifted significantly. In 2008, Peru reached the sixth place among recipients of IFDI flows in Latin America.[543] It is remarkable that reinvested earnings accounted for 70%, 47% and 102%[544] of IFDI flows in 2007, 2008 and 2009, respectively, demonstrating the soundness of the Peruvian economy and reflecting the high returns earned by investors on their Peruvian operations.

From 1990 to 2000, Peru's IFDI stock was markedly oriented toward services (annex table 3). In 2000, services industries (energy excluded) accounted for 58% of the IFDI stock, energy for 12%, manufacturing for 13%, and oil and mining for 16%. These numbers are explained by the privatizations that took place in the first stage of Peru's new FDI policy during the

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[541] An overview of the main determinants of FDI flows can be found in UNCTAD, *World Investment Report 1998: Trends and Determinants* (New York and Geneva: United Nations, 1998).

[542] The exceptions are broadcasting, notary, air transport, and maritime transport services. See, Peru - United States Trade Promotion Agreement, signed April 12, 2006. Peru Annex I, Non-Conforming Measures for Services and Investment, available at: http://www.ustr.gov/trade-agreements/free-trade-agreements/peru-tpa/final-text.

[543] UNCTAD's FDI/TNC database, available at: http://stats.unctad.org/fdi/.

[544] The amount is higher than 100% because the net liabilities of foreign affiliates were negative and higher than equity capital in absolute terms.

1990s: as state companies were mostly in the tertiary sector; the privatizations caused a shift toward FDI in such industries as telecommunications, financial services and energy (mainly electricity generation, transmission and distribution). In the secondary sector (specifically, in the food industry), the acquisition of two traditional Peruvian companies have to be highlighted: Arturo Field Co. (acquired by Kraft Foods) and D'Onofrio (acquired by Nestle).

However, during the past decade, the bulk of IFDI went into the exploitation of natural resources (copper, gold, silver, oil, natural gas, electricity based on water and oil), to infrastructure concessions and to manufacturing. Although services and energy together still accounted for most of the IFDI stock in 2009 (in part because of IFDI in infrastructure concessions), the relative importance of manufacturing (15%) and mining and oil (23%) has considerably risen due to important greenfield investments. Investments in agriculture have also increased considerably, driven by growing demand for new Peruvian export products such as asparagus (annex table 3). IFDI in extractive industries[545] and agriculture in Peru is highly decentralized, which creates considerable economic impact in the interior of the country, bringing wealth to regions faraway from the capital. In addition to this, striking GDP and market growth in the past decade (on average 5.4% per year[546]) has generated attractive returns in the finance, construction and housing industries, pushing up IFDI in them.

From 2000 to 2009, according to the Peruvian Investment Agency (Proinversion), concessions in infrastructure projects represented an estimated investment of US$ 8.9 billion, including US$ 2.7 billion for the Camisea natural gas project,[547] US$ 1.2 billion for the Lima Airport, US$ 0.6 billion for the Callao Port (South Dock), and US$ 1.1 billion for the inter-oceanic road that will join the southern regions of Peru with Brazil. Other important concessions have been given in the transport, telecommunications, hydrocarbons, energy, sanitation, and agriculture (irrigation) industries.

Europe has been the major IFDI player in Peru. In 2000, 66% of Peru's IFDI stock came from Europe, compared to 19% from North America, 12% from Latin America and 2% from Asia. In 2009, Europe remained the major inward foreign direct investor, with 56%. On the other hand, North America's share accounted for 16%, Asia's doubled to 4% and, what is more remarkable, Latin America's soared to 22%, becoming the second largest source region for IFDI in Peru.

Spain is the most important investor country in Peru, accounting for 23% of the IFDI stock as of 2009 (annex table 4). The United Kingdom (20%), the United States (15%), the Netherlands (7.5%), Chile (6.9%), and Panama (4.9%) follow, in that order. However, the lower relative standing of Spain and the United States, compared to 2000, contrasts with larger investments from the United Kingdom and the emergence of new players from the developing world. Brazil, Colombia and Singapore have become very active inward foreign direct investors in recent years, along with Chile and Panama. Likewise, China deserves special attention given its unique investment in Shougang Hierro Peru, an iron mining operation privatized in 1993 for US$ 118 millions plus a three-year investment commitment of US$ 150 millions. Currently, China is participating in many of the biggest greenfield

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[545] The term "extractive industries" refers to industries involved in (i) prospecting and exploring for (non-renewable) natural resources, (ii) acquiring them, (iii) further exploring them, (iv) developing them, and (v) producing (extracting) them from the earth. The term does not encompass forestry, fishing, agriculture, animal husbandry, and any other industries that might be involved with resources of a renewable nature.

[546] Central Reserve Bank of Peru (BCRP), "Inflation report: recent trends and macroeconomic forecasts 2010-2011" (Lima: BRCP, 2010).

[547] It includes two concessions: exploitation and transportation and distribution.

projects in the mining and steel industries, and its role as a source of IFDI is increasing (see the next section)

The corporate players

Peru had an estimated 330 foreign affiliates in 2008.[548] The top ten foreign affiliates measured by foreign equity capital are in the telecommunications, beverages, mining, energy, and distribution industries (annex table 5). The remaining foreign affiliates are concentrated in the finance, energy, mining, and manufacturing industries.[549]

Cross-border M&As in Peru during 2007-2009 accounted for US$ 3.8 billion (annex table 6). Most of them were in the mining and electricity industries, with Canada as the most active player in terms of number of M&As, but not in transaction value (US$ 0.3 billion). In spite of this, Canadian acquisitions of promising junior mining projects may increase the country's role in IFDI greenfield transactions in the future. The most eye-catching M&A was the acquisition of Wong Group, a Peruvian flagship retail firm, by Cencosud, a leading Chilean retail firm, for US$ 0.5 billion in 2007.[550] Other relevant M&As were Petro-Tech Peruana (oil), Edegel and Electroandes (electricity), acquired by French/Colombian, Spanish and Norwegian enterprises, respectively.

Greenfield investments announced during 2007-2009 accounted for US$ 19.6 billion. According to these announcements, the bulk of greenfield IFDI is in mining (US$ 6.3 billion) and natural gas and renewable energy (US$ 4.3 billion). The chemical (US$ 4.9 billion) and steel (US$ 1.4 billion) industries also received high investments. Therefore, for the first time since Peru's liberalization policy in 1992,[551] important amounts have been invested into industries with higher value-added than extractive industries. In the chemical industry, most of investments are directed toward petrochemical complexes, highly promoted by the government as a means of taking advantage of the country's natural gas reserves (annex table 7).

Announced investments in the petrochemical industry include the acquisitions of Braskem (Brazil), CF Industries (USA) and Sigdo Koppers Group (Peruvian-Chilean Joint venture), for a total of US$ 4.4 billion (annex table 7). The Braskem's project by itself would create 41,000 direct and indirect jobs.[552] The development of the complex is subject to the amount of feedstock available from the gas fields and will probably be located in San Juan de Marcona (Ica region), a depressed coastal city located 530 km south of Lima. In another industry, the Brazilian steelmaker Gerdau will invest US$ 1.4 billions at its SiderPeru unit. The company expects the project to generate more than 4,000 temporary jobs during construction, and 2,000 new permanent jobs. The investment will make Peru a large steel producer and an exporter to Latin America.[553] SiderPeru is located in Chimbote (Ancash region), a coastal city located 420 km north of Lima. Both regions, Ica and Ancash, are already important export-oriented producers of agricultural and fishing products, respectively.

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[548] UNCTAD, *World Investment Report 2009: Transnational Corporations, Agricultural Production and Development* (New York and Geneva: United Nations, 2009).
[549] Proinversion, FDI Statistics, unpublished..
[550] As part of the transaction, Wong Group bought 5% of Cencosud.
[551] Privatizations aside.
[552] Andina Peru News Agency, "Braskem, Petrobras and Petroperú to invest $ 2.500 million in Peru petrochemical plant," May 18, 2008, available at: http://www.andina.com.pe/Espanol/Noticia.aspx?Id=SUrFGYWryL4.
[553] Todd Benson, "Gerdau to spend $1.4 bn to boost output in Peru," Reuters, September 1, 2008, available at: **http://uk.reuters.com/article/idUKN0129584620080901**.

An anchor project for these developments has been the Peru LNG project,[554] which includes a liquefaction plant, related marine facilities and 408 km of pipeline for the transportation of natural gas from the mountains to the LNG Plant at Pampa Melchorita on the coast. The total estimated investment was US$ 3.8 billion and the project is considered the largest and most important energy project in Peru. Peru LNG is expected to generate roughly US$ 0.8 billion of export revenues annually. During the construction phase, 35,000 direct and indirect jobs were generated.

Effects of the current global crisis

The global economic and financial market crisis hit IFDI in Peru in 2009. After continuous growth from 2003 to 2008, IFDI flows plummeted to US$ 4.7 billion, 35% less than 2008. Since Peru's terms of trade deteriorated because of the fall in commodities prices in the first quarter of 2009, some investment projects were postponed. In addition, foreign affiliates located in Peru lent money to their headquarters abroad, causing net capital outflows of US$ -0.86 billion in 2009.

On the other hand, reinvested earnings and cross-border M&A investments sustained IFDI flows. Reinvestments in 2009 were equal to US$ 4.9 billion, 49% more than in 2008. M&As accounted for US$ 1.5 billion, 137% higher than in 2008. These numbers reflect the soundness of Peru's economic performance. Furthermore, Peru's GDP grew by 0.9%[555] in 2009, one of the best performances in Latin America. Thus, Peru may capitalize on its performance and become an even more attractive place for FDI.

The policy scene

In the late 1980s, the Peruvian economy was facing the greatest economic crisis of its recent history, characterized by macroeconomic chaos, irresponsible fiscal policy and hyper-inflation (7000% by 1990). The macroeconomic imbalance was worsened by a fall in tax revenues.[556] Furthermore, government policies induced economic distortions through price and wage control, artificial exchange and interest rates and trade protectionism (e.g. 32 different tariff levels went from 0% to 108%). The most important economic activities were controlled by the State, through public enterprises that subsidized the price of public services and further worsened the fiscal balance.

Since 1990, the main objective of the Government has been to create a steady economic and political environment that allows privately-owned businesses to emerge and develop. Since then, the Government has shifted its role from an over-regulator and producer to a private sector promoter, to make it the driving force of a free-market economy.

The redefinition of the State's role was reflected in the 1993 Constitution, which strongly encouraged private sector activity. The Constitution defines the subsidiary role of the State in economic activity, restricting public economic activity to market failures. The Constitution also guarantees national treatment to foreign investors and gives them the right to submit disputes arising from contractual relationships with the State to national or international

[554] The Peru LNG project was finalized on June 10, 2010.
[555] BCRP, "Inflation report: recent trends and macroeconomic forecasts 2010-2011," op. cit.
[556] Government income in 1990 was 4% of GDP, which was not enough to cover the State's payroll.

arbitration.[557] For this purpose, Peru joined the International Centre for Settlement of Investment Disputes (ICSID) in 1993. Peru also became a member of the Multilateral Investment Guarantee Agency (MIGA) in 1991, which means that foreign investors can obtain political risk insurance from that agency to increase their level of comfort when investing in the country.

The inviolability of property is also constitutionally protected. Foreign investments are allowed without restrictions in most economic sectors. Nevertheless, the 1993 Constitution states that foreigners may not acquire mines, lands, woods, water, fuels, and energy sources within fifty kilometers from the borders, except in case of public necessity, expressly declared by Supreme Decree and approved by the Cabinet.[558]

In order to reinforce investment protection, under the Law on Legal Stability Regime for Foreign Investment and the Framework Law for the Growth of the Private Investment,[559] the State guarantees foreign investors' legal stability for up to ten years, through Stabilization Agreements, which have a law-contract status. Such Agreements reassure investors that a particular legal framework in place at the time they entered into a contract will continue to apply to their investments for a set period of time. However, in the case of public service concessions, this period is extended to the term of the concession.

There are also tax incentives to investments,[560] such as a special regime of value-added tax. It allows investors to obtain a refund of taxes paid or transferred on imports and/or the domestic acquisition of capital assets, intermediate goods, services, and construction contracts during the pre-operation stage of infrastructure projects and public utilities, provided that these have been destined for operations not burdened with such tax and are used directly in the execution of investment projects in infrastructure works and public utilities. This regime is subject to investment contracts.

As part of its policy of promoting private investment and boost the country's development, the Peruvian Investment Promotion Agency, Proinversion, was created in 2002. One of the most important goals of Peru's economic strategy is to attract foreign investment into the country. As a complement to its internal legal framework, the Government seeks to negotiate international investment agreements, including BITs and chapters on investment in FTAs, as part of a comprehensive economic and commercial policy that encourages the creation of employment, technology transfer and the growth of goods and services trade with international partners.

Since 1991, Peru has signed BITs with over 30 countries. Likewise, Peru has entered into FTAs with the United States, Chile, Canada, Singapore, China, the European Free Trade Association (EFTA), and the European Union. Negotiations of FTAs are ongoing with Japan, Republic of Korea, Mexico, Thailand, and the Trans-Pacific Partnership. Peru has also entered into double taxation treaties with Brazil, Canada, Chile, and Spain (not yet in force). Negotiations with Sweden, France, Italy, the United Kingdom, Switzerland, and Thailand are pending. These agreements not only reinforce the country's credibility, but also open new opportunities for investors.

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[557] Peru's Political Constitution, Article 63.
[558] Peru's Political Constitution, Economic Regime, Chapter III, Article 71.
[559] Legislative Decree 662, "Law on Legal Stability Regime for Foreign Investment," and Legislative Decree 757, "Framework Law for the Growth of the Private Investment," both enacted in 1991.
[560] Legislative Decree 821, "Law on Value-added Tax and Selective Consumption Act," enacted in 1996.

Conclusions and Outlook

Peru's economic performance has attracted increasing IFDI flows in the past decade. To continue attracting IFDI, the Peruvian Government must maintain sound macroeconomic fundamentals. In addition, a more active promotion of IFDI in sectors with higher value-added would allow Peru to reap more benefits from its natural resources. The emerging role of IFDI in petrochemical complexes and the steel industry should only be a first step toward attracting human capital, knowledge and technology through IFDI. For that purpose, Peru needs to continue to improve institutions, reduce bureaucratic regulations and to invest in infrastructure, education, R&D, and health to further improve the country's attractiveness as a business location. Peru's economic outlook for the coming years is very favourable, considering the announced investment projects and the expected rise of domestic consumption. Although mining investments are likely to continue at high levels, the service industry is expected to continue to expand as well.

Additional readings

Central Reserve Bank of Peru (BCRP), "Inflation report: recent trends and macroeconomic forecasts 2010-2011" (Lima: BCRP, March 2010).

UNCTAD, *World Investment Report 2009: Transnational Corporations, Agricultural Production and Development* (New York and Geneva: United Nations, 2009).

UK Department of Trade and Industry and EIU, *Survive and Prosper: Emerging Markets in the Global Recession* (London: DTI and EIU, 2009).

Useful websites

For FDI policy and and BITs: Proinversion, available at: www.proinversion.gob.pe

For FDI statistics: Proinversion, available at: www.proinversion.gob.pe and

Central Reserve Bank of Peru (BCRP), available at: www.bcrp.gob.pe

For FTAs: Ministry of Foreign Trade and Tourism, available at: www.mincetur.gob.pe

For Double Taxation Treaties: Ministry of Finance, available at: www.mef.gob.pe

Statistical annex

Annex table 1. Peru: inward FDI stock, 2000-2009 (US$ billion)

Economy	2000	2004	2005	2006	2007	2008	2009
Peru	**11**	**13**	**16**	**20**	**27**	**32**	**37**
Peru [a] (Proinversion)	12	14	14	16	16	18	19[b]
Memorandum: comparator economies							
Brazil	122	161	181	221	310	288	401
Chile	46	61	74	80	99	100	122
Colombia	11	25	37	45	56	67	74
Malaysia	53	43	44	54	77	73	75
Thailand	30	53	60	77	94	93	99

Source: UNCTAD's FDI/TNC database, available at: http://stats.unctad.org/fdi/
[a] FDI stock registered by Proinversion includes equity capital only. In addition, not all FDI inflows are registered by Proinversion. Thus, Proinversion's FDI statistics are only a part of the Central Reserve Bank of Peru's FDI statistics.
[b] Calculated indirectly. Stock $Year_t$ = Stock $Year_{t-1}$ + Flow $Year_t$. t = 2009.

Annex table 2. Peru: inward FDI flows, 2000-2009 (US$ billion)

Economy	2000	2004	2005	2006	2007	2008	2009
Peru	0.8	1.6	2.6	3.5	5.5	6.9 [a]	4.8 [a]
Memorandum: comparator economies							
Brazil	32.8	18.1	15.1	18.8	34.6	45.1	25.9[b]
Chile[c]	4.8	7.1	7.0	7.3	12.5	15.2	12.7
Colombia	2.4	3.0	10.3	6.7	9.0	10.6	7.2[d]
Malaysia	3.8	4.6	4.1	6.1	8.5	7.3	1.4
Thailand	3.4[d]	5.9[d]	8.1	9.5	11.3	8.5	5.9[e]

Source: UNCTAD's FDI/TNC database, available at: http://stats.unctad.org/fdi/ (When differences with national statistics exist, the values are specified through [a] to [d])..
[a] Central Reserve Bank of Peru.
[b] Central Bank of Brazil, Preliminary data.
[c] Central Bank of Chile, Economic Indicators.
[d] Bank of Republic, Colombia, Economic Indicators, Foreign Sector Annex.
[e] Bank of Thailand.

Annex table 3. Peru: distribution of inward FDI stock, by economic sector and industry, 2000, 2009 (US$ million)

Sector / industry	**2000**[a]	**2009**[ab]
All sectors / industries	12,306	18,840
Primary	2,004	4,529
Agriculture, forestry, and fishing	51	209
Mining, quarrying and petroleum	1,953	4,320
Mining and quarrying	1,855	3,964
Petroleum	98	356
Secondary	1,554	2842
Manufacturing	1,554	2842
Services	7,211	8,866
Communications	4,588	3675
Construction (and housing)	60	718
Finance	1,683	2,872
Transport	28	295
Tourism	58	64
Other services	794	1,242
Energy	1,537	2,603

Source: Proinversion, Peruvian Investment Promotion Agency.
[a] FDI stock registered by Proinversion includes only equity capital. In addition, not all FDI inflows are registered by Proinversion. Thus, Proinversion's FDI statistics are only a part of the Central Reserve Bank of Peru's FDI statistics.
[b] Preliminary.

Annex table 4. Peru: geographical distribution of inward FDI stock, 2000, 2009
(US$ million)

Region/economy	**2000[a]**	**2009[ab]**
World	**12,306**	**18,840**
Developed economies	**10,616**	**13,826**
Europe	8,168	10,542
European Union	7,909	10,210
France	224	205
Germany	75	171
Netherlands	847	1,404
Spain	4,382	4,292
United Kingdom	2,175	3,783
EFTA States	259	332
Liechtenstein	14	19
Switzerland	245	313
North America	2,334	3,083
Canada	183	323
United States	2,151	2,760
Other developed countries	114	201
Australia	5	7
Japan	102	187
New Zealand	7	7
Developing economies	**1,572**	**4,814**
Africa	0	0
Asia and Oceania	143	565
China	122	122
Korea, Republic of	21	41
Singapore	0	399
Russia	0	3
Latin America and the Caribbean	1,429	4,249
Brazil	59	487
Chile	476	1,290
Colombia	76	751
Mexico	19	455
Panama	551	929
Unspecified destination	**119**	**200**

Source: Proinversion, Peruvian Investment Promotion Agency.
[a] FDI stock registered by Proinversion includes only equity capital. In addition, not all FDI inflows are registered by Proinversion. Thus, Proinversion's FDI statistics are only a part of the Central Reserve Bank of Peru's FDI statistics.
[b] Preliminary.

Annex table 5. Peru: principal foreign affiliates, ranked by assets, 2009 (US$ million)

Rank	Name	Industry	Foreign assets[a]
1	Telefonica Peru Holding S.A	Communications	2,002
2	Union de Cervecerias Peruanas Backus y Johnston S.A.A.	Manufacturing	1,300
3	Telefonica del Peru S.A.A.	Communications	853
4	Xstrata Peru S.A.	Mining	657
5	Generalima S.A.	Energy	502
6	Cencosud Peru S.A.	Distribution	500
7	Compania Minera Antamina S.A.	Mining	460
8	Sociedad Minera Cerro Verde S.A.	Mining	454
9	Gold Fields La Cimas S.A.	Mining	447
10	Telefonica Moviles Peru Holding S.A.A.	Communications	436
11	America Movil Peru S.A.C. (before Tim Peru)	Communications	386
12	Southern Peru Limited, Sucursal Del Peru	Mining	373
13	Peru Beverage Limitada S.R.L.	Manufacturing	303
14	SN Power Peru Holding S.R.L.	Energy	296
15	Scotiabank Peru S.A.A.	Finance	282
TOTAL			9,252

Source: Proinversion, Peruvian Investment Promotion Agency.
[a] December 2009. Includes equity capital only.

Annex table 6. Peru: main M&A deals, by inward investing firm, 2007-2009

Year	Acquiring company	Source economy	Target company	Target industry	Shares acquired (%)	Estimated/ announced transaction value (US$ million)[a]
2009	Enersis SA [a]	Spain	Edelnor	Electricity/distribution	12.35	75.14
2009	Endesa [a]	Spain	Edegel	Electricity	62.46	379.72
2009	Monthiers SA	Belgium/ Brazil	AmBev Peru	Beverages	30.00	16.00
2009	Nyrstar NV	United Kingdom	Cia Minera San Juan(Peru)SA	Mining	85.00	28.00
2009	Aquiline Resources Inc	Canada	Monterrico Metals PLC-Pico	Mining	100.00	7.80
2009	Prosegur Compania de Seguridad	Spain	Orus SA	Other business services/security	100.00	25.60
2009	Solex Resources Corp	Canada	Minera Frontera Pacifica SA	Mining	100.00	3.78
2009	Corficolombiana	Colombia	Cia de Gas Comprimido del Peru	Natural gas	80.00	2.02
2009	ADM Investment Ltd	United States	Molinos del Peru SAC	Food/manufacturing	100.00	4.50
2009	Zibo Hongda Mining Co Ltd	China	Pampa de Pongo Property,Peru	Mining	100.00	100.10
2009	Focus Ventures Ltd	Canada	Radius Gold Inc-Nueva	Mining	100.00	3.20
2009	China Tel Group Inc	United States	Perusat SA	Telecommunications	95.00	2.78
2009	SK/Ecopetrol Group	France/ Colombia	Petro-Tech Peruana SA	Oil	100.00	892.78
2008	Iberian Minerals Corp	Canada	Cia Minera Condestable SA	Mining	98.73	9.45
2008	Grupo Votorantim	Brazil	Cia Minera Milpo SAA	Mining	32.92	132.85
2008	Bank of Nova Scotia,Toronto	Canada	AFP Profuturo SA	Finance	47.50	33.00
2008	Sprott Resource Corp	Canada	Mantaro phosphate project	Chemicals	100.00	8.87
2008	Strike Resources Ltd	Australia	Apurimac Ferrum SA	Mining	51.00	34.50
2008	Black Tusk Minerals Inc	Canada	Undisclosed Mining Concessions	Mining	100.00	2.00
2008	Nevtah Capital Mgmt Corp	United States	Electrocondor SAC	Electricity	100.00	22.50
2008	Grupo Votorantim	Brazil	Cia Minera Milpo SAA	Mining	25.03	3.39
2008	Bear Creek Mining Corp	Canada	Bear Creek Mining Corp-Corani	Mining	100.00	77.49
2008	Vena Resources Inc	Canada	Sudamericana de Carbon SAC	Mining	70.00	2.50
2008	Iberian Minerals Corp	Canada	Cia Minera Condestable SA	Mining	92.00	97.55
2008	Norsemont Mining Inc	Canada	Constancia Mining Project,Lima	Mining	70.00	13.00
2008	Petrobras Intl Braspetro BVc	Brazil	Petrobras Energia Peru SA	Oil	-	138.84

2007	Cencosud	Chile	Grupo Wong	Retail	100.00	500.00
2007	Norsemont Mining Inc	Canada	Constancia Mining Project,Lima	Mining	30.00	9.80
2007	Statkraft Norfund (SN) Power	Norway	Electroandes SA	Electricity	100.00	390.00
2007	Thunderbird Resorts Inc	Panama	Hoteles Las Americas	Tourism and hotels	100.00	43.50
2007	Century Mining Corp	United States	Cia Minera Algamarca SA	Mining	100.00	31.00
2007	Pure Biofuels Corp	United States	Interpacific Oil SAC	Biofuel (Ethanol)	100.00	6.30
2007	Northern Peru Copper Corp	Canada	Mineral Concessions	Mining	100.00	5.12
2007	Panoro Minerals Ltd	Canada	Cordillera de las Minas SA	Mining	100.00	15.15
2007	Strike Resources Ltd.	Canada	Apurimac & Cuzco Iron Project	Mining	75.50	6.55
2007	Investor Group	Colombia	Consorcio TransMantaro SA	Electricity	100.00	33.00
2007	China Fishery Group Investment	Hong Kong (China)	Alexandra SAC	Fishing	100.00	103.58

Source: Thomson ONE Banker. Thomson Reuters.
[a] Enersis Chile and Endesa Chile are subsidiaries of Endesa Spain.
[b] Monthiers (Uruguay) is a subsidiary of Ambev Co. (Belgium/Brazil).
[c] Announced investment is reported as Netherlands, but the Petrobras Headquarter is in Brazil.

Annex table 7. Peru: main greenfield projects, by inward investing firm, 2007-2009
(US$ million)

Year	Investing company	Source economy	Industry	Estimated/ announced investment value
2009	Malaga	Canada	Mining	327
2009	Rio Alto Mining	Canada	Mining	330
2009	Falabella	Chile	Retail	350
2009	Grupo Mexico	Mexico	Mining	600
2009	Braskem	Brazil	Petrochemical	2,500
2009	Centrais Eletricas Brasileira (Eletrobras)	Brazil	Electricity	321
2009	Perenco	France	Oil	2,000
2009	Reliance Industries	India	Natural gas	500
2009	Construtora OAS	Brazil	Electricity	321
2009	Votorantim Group	Brazil	Mining/manufacturing	500
2009	Sigdo Koppers Group	Chile	Petrochemical	650
2008	Stratos Renewables	United States	Renewable energy (ethanol)	119
2008	Conduit Capital Partners, LLC[a]	United States	Gas pipeline/transportation	1,400
2008	Endesa	Spain	Electricity	229
2008	Maple Energy	Ireland	Renewable energy (Ethanol)	222
2008	Vale (Companhia Vale do Rio Doce)	Brazil	Chemicals/extraction	479
2008	Duke Energy	United States	Electricity	229
2008	Horcona	Spain	Renewable energy	4
2008	Gerdau	Brazil	Steel	1,400
2008	Royal Dutch Shell Plc	Netherlands	Oil and natural gas	300
2008	Pure Biofuels	United States	Biofuel/manufacturing	119
2008	Aluminium Corporation of China (Chinalco)	China	Mining	2,150
2008	Global Crossing	Bermuda	Telecommunications	149
2008	CF Industries	United States	Petrochemicals	1,000
2008	Jiangxi Copper	China	Mining	1,400
2008	Constructora OAS (water	Brazil	Construction/sanitation	76.9

	transfer system)			
2007	Ecopetrol	Colombia	Oil	50
2007	Cimpor	Portugal	Cement	125
2007	MAN	Germany	Renewable energy	100
2007	Starwood Hotels & Resorts	United States	Hotels and tourism/construction	85
2007	Anglo American PLC (Michiquillay Project)	United Kingdom	Mining	430
2007	Shougang	China	Mining/manufacturing	1,000
2007	Sigdo Koppers Group[b]	Chile	Petrochemical	200
2007	Doe Run	United States	Mining/manufacturing	50
2007	Petrobras	Brazil	Oil	90
2007	Salfacorp	Chile	Real estate	40.7
2007	Caribbean Land	Dominican Republic	Hotels and tourism/construction	166
2007	SABMiller	United Kingdom	Beverages/manufacturing	50

Source: fDI Intelligence, a service from the Financial Times Ltd.
[a] Peruvian-Chilean joint venture.
[b] Conduit Capital Partners sold its 51% stake in its US$ 1.5 billion Peruvian gas pipeline project to Odebretch, subject to the confirmation of reserves.

Chapter 21 – Russia

Inward FDI and its policy context, 2010

Alexey Kuznetsov

In the 2000s, Russia became a significant host for IFDI. But its investment climate problems, especially corruption, do not allow Russia to exploit its locational advantages to the full. Russia attracts mainly European investors in a rather narrow range of industries (although the share of mining is decreasing) and regions (mainly in Moscow, St. Petersburg and oil-rich Sakhalin). However, even during the crisis, a new industrial cluster has developed near Kaluga and some large M&As and greenfield projects have been realized outside the Central and North-West federal districts. Russia is trying to diversify the structure and geography of IFDI using incentives (e.g. in special economic zones).

Trends and developments

Country-level developments

Despite the devaluation of the assets of foreign MNEs during the current downturn, Russia's IFDI stock was 12 times larger at the end of 2009 than in 2000. However, the global share of Russia's IFDI is still only 1-2%. Although its relative position as an international business location looks good in comparison with the other three BRIC countries, some other post-communist countries have been more successful in attracting FDI, especially in IFDI per capita terms (annex table 1). Russia has recently been narrowing this gap and has become the leader among post-communist countries in total FDI inflows (annex table 2). According to the Bank of Russia, FDI inflows in Russia were US$ 75.5 billion in 2008 and US$ 38.7 billion in 2009 (while its population was 141 million). At the same time, FDI inflows in 27 other European and Central Asia post-communist states were US$ 164.1 billion in 2008 and US$ 52.5 billion in 2009 (while their total population was 261 million).

UNCTAD uses the aggregate figures provided by the Bank of Russia which are compatible with international statistics and can be used for cross-country comparisons. At the same time, the Federal State Statistics Service (Rosstat) published smaller figures (US$ 27.0 billion for 2008 and US$ 15.9 billion for 2009). Rosstat's database is useful for researchers because it provides much more detailed information on sectoral and regional distribution of IFDI flows and stocks. However, Rosstat uses only special statistical forms from companies (form No. 1-invest), while the Bank of Russia tries to estimate information for its balance-of-payments statistics from various sources, including companies' annual and other reports, information from stock exchanges and FDI data compiled by central banks in other countries.

Despite its intellectual capital (e.g. its relatively high level of education, well-qualified workforce and significant achievements in R&D – all of which can attract efficiency-seeking investors), Russia primarily attracts market-seeking foreign investment. This can be explained by the combination of the rapid growth of Russia's economy (e.g. the country's GDP in 2008 was equal to 194% of the level of 1998) and its investment climate problems, which are crucial for efficiency-seeking investors (for details see the policy scene paragraph of this paper). At the same time, FDI inflows in industries with high value-added remain small. Although Russia is rich in resources, the share of IFDI stock in mining has decreased while that in the wood and pulp industry remains stable (annex table 3). The dominance of oil and gas extraction in FDI from India, Vietnam and (to some extent) the Netherlands is unusual. The most rapid growth in IFDI has been taking place in electricity (due to its partial privatization), real estate (caused by extremely high prices), and financial activities (although only subsidiaries are permitted, not affiliates).

A significant part of Russian IFDI comes from Cyprus and Caribbean territories. These investments mainly consist of round-tripping capital investment originating from Russia itself (annex tables 3 and 4). In the FDI statistics of some European countries, trans-shipped FDI from other countries into Russia's economy are combined with capital of national MNEs. For example, FDI from the Netherlands is in second place, but this includes not only indisputably Dutch companies such as Royal Dutch Shell, Heineken and ING Bank, but also holdings from the Netherlands under the control of foreign MNEs, some of them probably Russian. In general, the geographical distribution of IFDI reflects Russia's strong trade relationship with the European Union (EU), which contributes half of Russia's foreign trade turnover and more than three quarters of Russian IFDI. Large countries are among the leaders, but some smaller countries also have significant investment volumes and a diversified structure of FDI in Russia (e.g. Finland, Sweden). In the case of some small European countries, a large IFDI stock figure can be explained by one large deal. For instance, Czech FDI stock in Russia doubled when PPF (Prvni Privatizacni Fond) acquired 50% of the Russian retail network Eldorado in 2009.

Some Commonwealth of Independent States (CIS) countries are also noticeable sources of Russian IFDI because their medium-size investors exploit advantages of proximity, common language, business contacts from the Soviet era and so on. Asian investors have rapidly expanded their FDI activities in Russia in recent years. In contrast, United States FDI stock in Russia is constantly decreasing, though several U.S. companies are major investors (annex table 5).

The corporate players

Foreign MNEs play a key role in only a few Russian industries (e.g. beer, tobacco). TNK BP is the only large oil and gas corporation where foreign control has reached 50% (annex table 5). Russian citizens own all the leading metals companies, although some of these firms are registered abroad. Foreign banks are rapidly expanding in Russia (annex table 5a) but they control less than a third of the financial sector. Only three firms received significant FDI among more than 20 large electricity companies (annex table 6).

One of the main reasons for the relatively low foreign share in Russian companies is the history of privatization in Russia, beginning in the 1990s. While many Central European countries invited foreign MNEs to privatize their companies and replenish their national budgets during the difficult period of post-communist transformation, the Russian political elite chose another way of privatization in the 1990s. Many large Soviet enterprises were sold for symbolic prices or even stolen by a small number of Russian citizens. As a result, several Russian billionaires with questionable property rights appeared. The Russian state did not receive any money for attempting to solve the acute social and economic problems of the Soviet heritage.

In general, foreign investment has always accounted for less than 10% of gross fixed capital formation in Russia. Their highest share was 8.2% in 2005, then it decreased to 6% in 2009. The share of companies under joint Russian and foreign control fell from 11.2% in 2005 to 7.2% in 2009. More than 90% of current investments in fixed capital are thus under full Russian control.

Companies with foreign participation employed only 4.9% of the Russian workforce in 2008. This is a rather low share for a transition country, especially in comparison with Hungary or the Czech Republic.

Nevertheless, MNEs have a great influence in the development of some Russian industries. Although the share of EU trading companies is still modest, these determine the competitive character of the Russian retail sector. Another example is telecommunications, where foreign minority investors help to modernize the sector through technology transfer. Similarly, impressive prospects for Russian motorists have been opened by foreign producers of motor vehicles, who have introduced relatively cheap but comfortable cars to the Russian market, while former Soviet giants continue to dominate the market for cars of low quality. Economic modernization in Russia depends to some extent on medium-size investors too. For example, Knauf, KBE and other German firms have begun to promote new products in construction while Slovenia's Krka and Hungary's Gedeon Richter have become pioneers of IFDI in the Russian pharmaceuticals industry.

Effects of the current global crisis

Russia experienced the worst slump among G-20 and especially BRIC countries during the global economic and financial crisis. For instance, while Russia's GDP fell by 7.9% year-on-year in real terms in 2009, China's GDP rose by 8.7% and India's by 5.7%. Many of the largest Russian private companies demonstrated that they could not survive without state support. Thus, the global crisis revealed that the 2000s were a "lost decade" for Russian economic modernization. As a result, a sense of uncertainty has grown throughout Russia's economy. The economic impact of the crisis – especially the decline of consumer demand, which had previously stimulated IFDI in import substitution industries – caused cancellations or postponements of many previously announced greenfield projects in Russia.

As a result, major IFDI flows in 2009 were mainly connected with the realization of investment plans arranged in 2007 and 2008 (annex table 6 and 7) or earlier. The best examples are Volkswagen's industrial project in Kaluga, which began in 2006, and Korean Lotte & Resorts's office and hotel project in Moscow which started in 2002. New IFDI projects have begun recently, nevertheless, and their number increased in 2010. Balance of payments statistics show that FDI inflows grew in 2009, although it was still well below its 2008 peak.

The policy scene

According to official statements, Russia tries to liberalize its FDI climate and supports economic modernization with the help of foreign investment. In practice, however, many old problems of the Russian investment climate have still not been solved. One of the main problems, the high level of corruption, has become even worse. Russia ranked in 154th place among 180 countries in the Corruption Perception Index in 2010, down from 149th place in 2009. There is also a problem of investment image, as evidenced by the fact that MNEs with Russian affiliates are more optimistic than potential foreign investors.

Some ambiguous investment cases can be seen from opposite points of view. For instance, foreign partners of Yukos knew about the high level of corruption and the political power of the oligarchs in Russia. Therefore, foreign investors were very surprised that the richest man in Russia could be punished for his crimes. However, these investors lost their money in Yukos and blamed the Russian investment climate. Another example is connected with ecological damage allegedly caused by foreign oil MNEs in Sakhalin. It may well be that many oil companies underestimate ecological risks, but in the case of the Sakhalin-2 project, their "punishment" was very specific because foreign investors were forced to sell half of their shares to Gazprom.

The modern Russian IFDI federal law was passed in 1999. In general, it can be characterized as a typical liberal FDI law. For example, it announces equal rights for Russian and foreign investors (article 4), although some exceptions are possible that are more favorable to IFDI or else constitute barriers to foreign investment. The Russian investment climate is also determined by other federal laws and various decisions of the Russian Federal Government. For example, changes to customs rules have been adopted in an attempt to stimulate IFDI in motor vehicle production. IFDI in the banking and insurance sectors is regulated by special laws that introduce rules that apply to both Russian and foreign financial institutions in non-discriminatory fashion. However, barriers for foreign investors can be introduced by special laws or governmental decisions. For example, the federal law on banks and banking activities (articles 17 and 18) demands additional reports and documents from foreign investors, and allows special barriers in certain circumstances (e.g. against banks from countries that introduce such barriers against Russian banks).

The 2005 federal law allowed several types of special economic zone (SEZ). Locations of SEZs were determined by competition, though not according to transparent criteria. Industrial zones were founded in Elabuga (Tatarstan) and Lipetsk, while innovative zones appeared in Dubna, Zelenograd, Strelna and Tomsk. These SEZs have already attracted more than 100 foreign investors. Amendments in 2006 to the same law established tourist zones (seven places appeared in 2007 while Russky Island received the status in 2010) and transport zones (Ulyanovsk airport and the seaport of Sovietskaya Gavan' in 2009). The enclave of the Kaliningrad Region remains the largest SEZ by a separate law. Recently a high-tech area was also established in Skolkovo, near Moscow (although many Russian experts are very skeptical about its prospects). Some Russian regions have introduced their own additional IFDI incentives.

Russia has recently diversified the geography of its double taxation treaties (DTTs) and BITs that in the past were mostly with European countries. Russia has DTTs in effect with 76 countries. Recent DTTs were ratified with Algeria, Mexico and Thailand (in 2008) and with Botswana, Brazil, Venezuela, and Singapore (in 2009). Russia has BITs with approximately 60 countries. In 2009, BITs were ratified with China (the second such treaty), Indonesia, Jordan, Qatar, and Venezuela. In the summer of 2010, BITs were ratified with Belarus, Kazakhstan, Kyrgyztan, Tajikistan, and Turkmenistan (as a result, Azerbaijan became the only CIS country without such a BIT).

In 2008, some limitations on IFDI were introduced in "strategic" branches (including nuclear power, weapons and aircraft production, and mass media) by a special federal law. Such barriers are typical for many countries, even among OECD members. However, there are problems in the Russian case with the range of "strategic" branches. For example, large foreign investors in the Russian oil and gas industry are worried about so-called mineral resources specified as having "federal importance". This law does not determine the criteria by which oil and gas fields are deemed to be of federal importance (however, in 2009, this gap was eliminated by an amendment to the federal law on subsoil). Moreover, the law can negatively influence IFDI in some sectors outside "strategic" branches (e.g. in the banking sector because of limitations on cryptography). There is also a special federal law on production sharing

agreements. Yet only a few such agreements were signed in the 1990s, as their experience was considered to have been unsuccessful by many Russian experts and politicians.
To complicate matters further, the main problems of the Russian investment climate are not these deficiencies in laws and governmental decisions but rather implementation inadequacies arising from excessive bureaucracy, artificial barriers of customs and migration offices, unequal access to infrastructure, and weak property rights. Officials admit that these problems explain the bad rankings of Russia in various international surveys. For example, Russia ranked in 63rd place among 139 countries in the Global Competitiveness Index 2010-2011. In the 2010 Index of Economic Freedom, Russia ranked 143rd among 179 countries. Despite some methodological problems inherent in these rankings, the general problem is clear.

Nevertheless, Russian officials have taken some steps toward good governance. One such example is the prime minister's recent idea of introducing an informal post of investment ombudsperson in addition to annual sessions of the Foreign Investment Advisory Council, with its regular direct contacts between investors and leading officials. One caveat is that these can only help some of the largest foreign investors. The lack of political competition does not allow the country to overcome the low level of its officials' competence, which leads to the promulgation of imperfect laws and regulations. Moreover, the censorship of influential media and the lack of independent courts suppress activities of civil society in the struggle against corruption. Despite their declarations, both Russian and foreign large investors usually solve their problems with the bureaucracy in informal ways. As a result, the burden of corruption imposed on other investors has become more severe.

New developments in the regions

There are 83 regions in Russia, but 72% of the IFDI stock is concentrated in five regions (annex table 8). The predominance of Moscow is explained by its status as a political, financial, transport, industrial and consumer center. The city and its surroundings in the Moscow region often become the starting point of spatial FDI diffusion for foreign multinationals. St. Petersburg plays a similar role for Finnish and Swedish investors; the city is also an important market for companies from other countries. Sakhalin Island attracts large FDI in the oil and gas industry. Lipetsk is among the top locations mainly due to round-tripping FDI in the metals industry via Cyprus (2004), although there are also some Italian and other European projects there.

Some new FDI locations have become important. For example, a modern industrial cluster appeared in the Kaluga region in 2006-2010 with Volkswagen's and several other greenfield projects (annex table 7). The Arkhangelsk region has attracted much FDI in the oil and gas industry from Total while the Republic of Komi is the center of Timan Oil & Gas's activities. Some foreign companies have tried to invest in all large cities, including the main centers in the Urals, Siberia and the South (trading and beer companies are good examples).

Conclusions and Outlook

The post-crisis recovery of IFDI activities has already begun in Russia, although the growth of IFDI flows appears to be weak in 2010. Many investors will continue their expansion, especially in retail trade, banks and some manufacturing industries. Some large foreign MNEs are likely to invest in Russia for the first time (at least, some of their top managers regularly announce their post-crisis plans in Russia). However, problems in the Russian investment climate will probably not allow the country to attract many medium-size foreign companies, who prefer to invest in other emerging markets. As a result, the Russian President's ambitious aim of modernizing the economy with IFDI will be difficult to achieve.

Additional readings

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Useful websites

For statistical material about Russia, see Federal State Statistics Service (Rosstat), available at: http://www.gks.ru.

For texts of Russian laws, see ConsultantPlus, available at: http://www.consultant.ru.

Statistical annex

Annex table 1. Russia: inward FDI stock, 2000-2009 (US$ billion)

Economy		2000	2005	2007	2008	2009	*2009 IFDI stock per capita, US$*
Russia [a]	*Data of Bank of Russia*	32	180	491	216	383	*2,700*
	Data of Rosstat	16	50	103	122	109	*770*
Memorandum: Comparator economies							
Brazil		122	181	310	288	401	*2,090*
China (without Hong Kong)		193	272	327	378	473	*360*
Hungary		23	62	199	252	249	*24,850*
India		16	43	106	123	164	*140*
Kazakhstan		10	26	45	60	72	*4,660*
Poland		34	91	178	163	183	*4,800*
Ukraine		4	17	38	47	52	*1,130*

Sources: Bank of Russia, *International Investment Position of Russia for 2000-2009*, available at: http://www.cbr.ru/eng/statistics; Rosstat database, available at: http://www.gks.ru. For comparator economies: UNCTAD's FDI/TNC database, available at: http://stats.unctad.org/fdi; *UNCTAD Handbook of Statistics*, 2009, table 8.4.1.

[a] There are two official sources for FDI statistics in Russia. The Bank of Russia estimates FDI figures by using balance of payments data. As a result, it includes all forms of FDI. Its statistics are the source for UNCTAD's FDI database (though UNCTAD usually receives preliminary data). However, the Bank of Russia's data lack detailed information on the regional and sectoral structure of FDI. The Federal State Statistics Service (Rosstat) collects data from companies and publishes detailed information (since 2005). Its data are solid for inward FDI and less useful for outward FDI because the levels of transparency of Western and Russian multinationals are different.

Annex table 2. Russia: inward FDI flows, 2000-2009 (US$ billion)

Economy		2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
Russia	*Data of Bank of Russia*	2.7	2.7	3.5	8.0	15.4	12.9	29.7	55.1	75.5	38.7
	Data of Rosstat	4.4	4.0	4.0	6.8	9.4	13.1	13.7	27.8	27.0	15.9
Memorandum: Comparator economies											
Brazil		32.8	22.5	16.6	10.1	18.1	15.1	18.8	34.6	45.1	25.9
China (without Hong Kong)		40.7	46.9	52.7	53.5	60.6	72.4	72.7	83.5	108.3	95.0
India		3.6	5.5	5.6	4.3	5.8	7.6	20.3	25.0	40.4	34.6
Hungary		2.8	3.9	3.0	2.1	4.5	7.7	19.8	71.5	62.0	-5.6
Kazakhstan		1.3	2.8	2.6	2.1	4.1	2.0	6.4	11.1	15.8	12.6
Poland		9.4	5.7	4.1	4.6	12.9	10.3	19.6	23.6	14.7	11.4
Ukraine		0.6	0.8	0.7	1.4	1.7	7.8	5.6	9.9	10.9	4.8

Sources: UNCTAD's FDI/TNC database, available at: http://stats.unctad.org/fdi; Bank of Russia, *Balance of Payments of the Russian Federation*, available at: http://www.cbr.ru/eng/statistics; Rosstat database, available at: http://www.gks.ru.

Annex table 3. Russia: distribution of inward FDI stock, by economic sector and industry, 2005-2009 (US$ million)

Sector/industry	2005 [a]		2009	
	Total	Without three main round-tripping FDI economies [b]	Total	Without three main round-tripping FDI economies [b]
All sectors/industries	**49,751**	**33,986**	**109,022**	**68,504**
Primary	**13,392**	**12,229**	**26,123**	**21,153**
Agriculture, forestry, and fishing	520	354	1,343	948
Mining and quarrying	12,872	11,875	24,780	20,207
Extraction of crude petroleum and gas	12,200	11,460	22,567	19,212
Secondary	**20,217**	**12,068**	**42,811**	**25,926**
Manufacturing	19,405	11,389	37,095	22,043
Manufacture of food products and beverages	3,164	2,824	4,782	3,688
Manufacture of wood and of products of wood and cork, except furniture	959	682	1,905	1,476
Manufacture of paper and paper products	499	401	1,234	1,011
Manufacture of refined petroleum products	3,589	2,939	4,365	4,331
Manufacture of chemicals, chemical and pharmaceutical products	607	587	1,847	1,574
Manufacture of rubber and plastics products	436	391	1,041	836
Manufacture of other non-metallic mineral products	1,222	1,066	3,340	2,422
Manufacture of basic metals and metal products, except machinery and equipment	6,601	313	12,886	1,464
Manufacture of machinery and equipment	378	369	1,493	1,367
Manufacture of electrical equipment and electronic products	255	228	948	849
Manufacture of transport equipment	753	735	1,992	1,899
Electricity, gas, steam and water supply	255	218	3,038	2,466
Construction	557	461	2,678	1,417
Services	**16,142**	**9,689**	**40,088**	**21,425**
Wholesale and retail trade and repairing	3,274	2,871	11,311	7,498
Wholesale trade, except of motor vehicles and motorcycles	2,591	2,222	7,794	4,550
Retail trade and repairing, except of motor vehicles and motorcycles	536	521	2,802	2,305
Transportation and communication	3,625	2,908	4,270	2,636
Transport via pipelines	2,290	1,938	1,515	1,179
Telecommunication	864	698	808	284
Financial activities	3,448	796	5,674	2,924
Real estate activities	1,406	856	8,066	4,047

Source: Rosstat database, available at: http://www.gks.ru.

[a] Rosstat began to publish data on sectoral distribution of inward FDI stock only in 2005.

[b] Almost all IFDI from Cyprus, the British Virgin Islands and Bahamas are round-tripping investments of Russian companies. The share of these destinations was 32% of the total inward FDI stock in 2005 and 37% in 2009. There are also some smaller round-tripping FDI destinations (e.g. Gibraltar, US Virgin Islands).

Annex table 4. Russia: geographical distribution of inward FDI stock, 2005-2009 (US$ million)

Region/economy	**2005**	**2007**	**2009**	**Rank in 2009**
World	**49,751**	**103,060**	**109,022**	**n.a**
Developed economies	**46,038**	**95,134**	**94,859**	**n.a.**
Europe	**41,334**	**90,828**	**90,542**	**n.a.**
European Union	39,428	88,526	87,809	n.a.
Austria	497	1,592	2,855	7
Belgium	377	633	815	19
Cyprus	13,915	35,425	33,547	1
Czech Republic	21	84	198	32
Denmark	164	468	598	20
Estonia	38	126	95	42
Finland	627	1,208	1,909	11
France	905	1,554	2,182	9
Germany	2,714	4,494	7,834	3
Hungary	82	136	139	36
Ireland	265	428	415	24
Italy	333	818	1,054	15
Latvia	29	103	49	50
Lithuania	56	161	158	34
Luxembourg	451	735	1,184	13
Netherlands	16,125	35,254	29,065	2
Poland	155	331	497	23
Slovenia	57	64	57	49
Spain	106	818	403	25
Sweden	401	545	1,033	16
United Kingdom	2,044	3,438	3,625	5
Gibraltar	220	251	150	35
Liechtenstein	117	273	348	27
Norway	417	112	126	38
Switzerland	1,128	1,620	2,072	10
North America	**4,417**	**3,864**	**3,332**	**n.a.**
Canada	56	229	368	26
United States	4,361	3,635	2,964	6
Other developed economies	**287**	**442**	**985**	**n.a.**
Israel	83	73	83	43
Japan	175	322	875	18
Developing economies	**3,526**	**7,315**	**13,420**	**n.a.**
Africa	**214**	**551**	**620**	**n.a.**
Seychelles	167	490	515	22
Asia and Oceania	**752**	**2,145**	**4,989**	**n.a.**
China	149	415	938	17
Hong Kong (China)	8	156	114	40
India	15	593	1,327	12
Iran	1	223	177	33
Republic of Korea	140	373	1,129	14
Malaysia	56	79	63	47
Turkey	253	401	593	21
Vietnam	29	29	228	30

Annex table 4. Continued

Region/economy	2005	2007	2009	Place in 2009
Latin America and Caribbean	**2,560**	**4,619**	**7,811**	**n.a.**
Bahamas	649	858	2,244	8
Belize	136	179	238	29
British Virgin Islands	1,200	2,882	4,727	4
Dominican Republic	2	15	118	39
Panama	179	223	213	31
Saint Kitts and Nevis	120	135	107	41
United States Virgin Islands	52	58	70	46
Transition economies	**187**	**611**	**743**	**n.a.**
Serbia	14	45	70	45
CIS	**168**	**554**	**636**	**n.a.**
Azerbaijan	57	181	136	37
Belarus	8	30	60	48
Kazakhstan	37	227	322	28
Ukraine	39	86	78	44

Source: Rosstat database, available at: http://www.gks.ru.

Annex table 5. Russia: principal foreign non-financial affiliates (with at least 50% foreign held shares), ranked by turnover [a], 2008 (US$ million)

Rank	Name	Industry	Country	Turnover
1	BP (*TNK-BP Holding*)	Petroleum [b]	United Kingdom	30,723
2	Ford Motor	Motor vehicles	United States	5,953
3	Auchan	Trade	France	5,151
4	Metro Cash and Carry	Trade	Germany	4,470
5	PPF (*Eldorado*)	Trade	Czech Republic	4,200
6	Carlsberg (*Baltika*)	Beverages	Denmark	3,720
7	JTI	Tobacco	Japan	2,892
8	Philip Morris	Tobacco	United States	2,847
9	Procter & Gamble	Chemicals	United States	2,664
10	Nestlé	Food	Switzerland	1,909
11	Enel (*OGK-5*)	Electricity	Italy	1,722
12	Anheuser-Busch InBev (*SUN InBev*)	Beverages	Belgium	1,594
13	Coca-Cola HBC	Beverages	Greece	1,531
14	E.On (*OGK-4*)	Electricity	Germany	1,529
15	Ilim	Wood and paper	Switzerland	1,526
16	Mars	Food	United States	1,505
17	PepsiCo	Beverages	United States	1,488
18	Renault (*Avtoframos*)	Motor vehicles	France	1,406
19	IKEA	Trade	Sweden	1,247
20	Volkswagen	Motor vehicles	Germany	1,092

Source: Expert-400, *Expert,* 2009, no. 38 (5 October), http://www.raexpert.ru/ratings/expert400/2009.
[a] In many cases the data on assets of Russian affiliates of foreign multinationals are not available.
[b] Shell (Netherlands) and Total (France) are the main foreign investors in the Russian oil industry but they own only minor stakes in Russian petroleum projects.

Annex table 5a. Russia: principal banks under foreign control, ranked by net assets, 2009
(US$ million)

Place in Russia	Bank	Source economy	Net assets
8	UniCredit	Italy	16,660
9	Raiffeisen	Austria	15,540
11	Rosbank (Société Générale)	France	14,690
19	Citibank	United States	6,270
21	Nordea Bank	Sweden	5,080
24	Bank Société Générale Vostok	France	4,760
40	OTP Bank	Hungary	2,950
43	ING Bank (Eurasia)	Netherlands	2,680
44	Deutsche Bank	Germany	2,590
46	Rusfinans Bank (Société Générale)	France	2,490

Source: Krupneyshiye banki Rossii. Reyting po aktivam-netto na 1 yanvarya 2010 goda, http://www.allbanks.ru.

Annex table 6. Russia: main M&A deals, by inward investing firm, 2007-2009

Year	Acquiring company	Target company	Target industry	Source economy	Shares acquired (%)	Estimated/ announced transaction value (US$ million)
2007	E.On	OGK-4	Electricity	Germany	70.4 [a]	5,836
2007	Eni	Gazpromneft	Oil and gas	Italy	20.0	5,835
2009	E.On	Severneftegazprom	Oil and gas	Germany	25.0	3,959
2008	Fortum	TGK-10	Electricity	Finland	92.9 [a]	3,892
2007	ENEL	OGK-5	Electricity	Netherlands [b]	32.2 [a]	1,951
2007	Société Générale	Rosbank	Banks	France	30.0	1,700
2008	ENEL	OGK-5	Electricity	Netherlands [b]	22.7	1,448
2009	Wandle Holdings	Polyus Zoloto	Gold ores	Cyprus [c]	29.6	1,249
2008	Renault	Avtovaz	Motor vehicles	France	25.0	1,166
2008	AXA	RESO-Garantiya	Insurance	France	36.7	1,165
2007	KBC Groep	Absolut Bank	Banks	Belgium	92.5	1,030
2007	Sibir Energy	MOGC	Oil and gas	United Kingdom [c]	69.0	875
2007	Wintershall	Severneftegazprom	Oil and gas	Germany	25.0	857
2007	Allianz	ROSNO	Insurance	Germany	49.2	750
2008	Barclays	Expobank	Banks	United Kingdom	100.0	745
2008	Arcelor Mittal	Berezovskaya Mine	Coal mining	Luxembourg	97.9	720
2007	International Paper	Ilim Pulp	Pulp and paper	United States	50.0	620
2007	Urals Energy	Taas-Yuriakh Neftegazodobycha	Oil and gas	Cyprus [c]	35.3	590
2008	Bank of Cyprus	Uniastrum Bank	Banks	Cyprus	80.0	576
2007	Enka Insaat ve Sanayi	Ramenka	Retail trade	Turkey [d]	50.0	544

Source: Thomson ONE Banker, Thomson Reuters.

[a] The acquisition was made in two separate deals.
[b] ENEL is the largest Italian energy company but it makes its FDI in Russia via the Netherlands.
[c] This is a case of round-tripping Russian investments.
[d] The change of foreign investors took place without new inward FDI.

Annex table 7. Russia: main successful greenfield projects [a], by inward investing firm, 2007-2009

Year	Investing company	Target region of Russia	Sector	Home economy	Shares owned (%)	Estimated investment value (US$ million)
2007	PSA Peugeot Citroën	Kaluga region	Motor vehicles	France	70	620
	Mitsubishi			Japan	30	
2007	Timan Oil & Gas	Republic of Komi	Oil and gas	United Kingdom	100	600
2008	Ferrero	Vladimir region	Food products	Italy	100	270
2008	SABMiller	Ulyanovsk region	Beverages	South Africa	100	220
2007	Samsung Electronics	Kaluga region	Electronics	Korea, Rep. of	100	200
2007	BBH (Baltika)	Novosibirsk region	Beverages	Denmark	100	180
2007	Coca-Cola HBC	Rostov region	Beverages	Greece	100	160
2007	IKEA	Omsk region	Retail trade, real estate	Sweden	100	150
2007	Volvo Trucks	Kaluga region	Motor vehicles	Sweden	100	140
2007	Mayer-Melnhof Holz	Leningrad region	Wood products, biofuels	Austria	100	130

Source: Author's estimates based on Rosstat's and companies' information.

[a] *"Successful project" means that its production has already started (earlier than in August 2010). The largest announced but still not realized greenfield project of the period is Shtockman Development (Total – 25%, StatoilHydro – 24%, Gazprom – 51%). Its investments can exceed US$ 15 billion.*

Annex table 8. Russia: inward FDI stock and flows in various regions, 2009 (US$ million)

Region	Total stock	Flows								
		Total	Cyprus, BVI, Bahamas [a]	Germany	Netherlands	France	Finland	UK	Belgium	Korea, Rep. of
Russia, total	**109,022**	**15,906**	**5,055**	**2,313**	**1,441**	**758**	**676**	**542**	**494**	**490**
Central Federal District	**56,641**	**9,248**	**2,864**	**1,776**	**1,269**	**310**	**135**	**139**	**417**	**396**
Moscow	30,490	5,657	2,080	1,109	1,052	148	20	102	2	28
Lipetsk region	10,970	58	2	1	28	n.a.	n.a.	n.a.	n.a.	n.a.
Moscow region	9,827	2,138	656	377	67	141	43	28	413[b]	1
Kaluga region	1,418	530	5	19	104	n.a.	19	n.a.	n.a.	356
Vladimir region	953	221	0	126	1	6	n.a.	n.a.	n.a.	n.a.
Tula region	625	228	8	103	16	n.a.	n.a.	4	n.a.	n.a.
North-West Federal District	**14,197**	**2,530**	**155**	**209**	**105**	**420**	**530**	**180**	**73**	**70**
St. Petersburg	9,287	1,199	46	170	11	23	393	10	73	70
Leningrad region	2,107	335	2	18	22	n.a.	90	n.a.	n.a.	n.a.
Rep. of Komi	866	213	35	n.a.	n.a.	n.a.	n.a.	143	n.a.	n.a.
Novgorod region	826	160	2	16	n.a.	n.a.	37	26	n.a.	n.a.
Arkhangelsk reg.	248	455	43	1	n.a.	395	n.a.	n.a.	n.a.	n.a.
South Federal District	**4,122**	**460**	**224**	**119**	**4**	**5**	**0**	**4**	**n.a.**	**n.a.**
Krasnodar krai	2,621	235	63	105	3	5	n.a.	2	n.a.	n.a.
Rostov region	758	132	81	11	0	n.a.	0	1	n.a.	n.a.
Volga Federal District	**3,966**	**936**	**389**	**165**	**28**	**16**	**0**	**1**	**n.a.**	**9**
Nizhny Novgorod region	911	222	8	143	20	0	0	n.a.	n.a.	n.a.
Samara region	638	48	12	1	4	0	n.a.	0	n.a.	n.a.
Ural Federal District	**5,553**	**233**	**122**	**2**	**23**	**5**	**15**	**15**	**n.a.**	**n.a.**
Tumen region	2,326	94	67	0	0	n.a.	n.a.	14	n.a.	n.a.
Chelyabinsk reg.	1,886	22	19	n.a.	0	n.a.	n.a.	n.a.	n.a.	n.a.
Sverdlovsk reg.	1,275	88	35	1	2	-	15	1	n.a.	n.a.
Siberian Federal District	**4,171**	**999**	**451**	**42**	**3**	**0**	**0**	**37**	**0**	**0**
Tomsk region	1,301	192	89	1	n.a.	n.a.	n.a.	0	n.a.	n.a.
Irkutsk region	580	246	1	37	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Far East Federal District	**20,370**	**1,500**	**851**	**0**	**9**	**n.a.**	**n.a.**	**167**	**n.a.**	**20**
Sakhalin region	18,306	1,187	749	n.a.	n.a.	n.a.	n.a.	17	n.a.	12
Primorsky krai	733	32	3	0	n.a.	n.a.	n.a.	n.a.	n.a.	3

Source: Rosstat database, http://www.gks.ru.

[a] In 2009 FDI inflows from Cyprus were US$ 3,704 million, inflows from the British Virgin Islands (BVI) were US$ 703 million and inflows from the Bahamas were US$ 649 million. These FDI are mostly round-tripping.

[b] This figure shows all FDI of InBev in Russia (its headquarters is in Klin of the Moscow region).

Outward FDI and its policy context, 2010

Andrey V. Panibratov and Kalman Kalotay

OFDI from Russia often surprises outside observers by its landmark deals. One of them was the purchase in September 2009 of a 55% stake in General Motors' German affiliate Opel by a consortium of the Canadian car maker Magna and the Russian state-owned bank Sberbank. The latter is the largest creditor of the Russian car maker GAZ, and may represent its commercial interests in the contract. With this deal, Russia has bought into the industrial heartland of the world economy and could potentially access more advanced technology. This acquisition hints at the growth of Russian OFDI in general, which has prospered despite fears in many host countries that the investors are subject to Russian political interference, a fear that recently announced Russian policy intentions may allay.

Trends and developments

A decade ago, following the disintegration of the Soviet Union and the deep post-transition fall in output, Russia seemed to have become an economy of secondary importance. Since 1999, however, the Russian economy has staged a spectacular comeback thanks to various favorable international factors, such as the consistently high prices of its main export products, and is now again a major player in the world economy. One clear expression of this reality is to be found in its direct investment abroad.

Country level developments

OFDI from Russia in recent years has been much deeper than the pre-transition OFDI of the 'red multinationals', which had focused mostly on trading relations rather than on productive facilities.[561] It has also been a strikingly fast-growing phenomenon. Indeed, Russia produces three different data sets on OFDI, measuring it in different ways,[562] and each set of statistics indicates a major rise in Russian OFDI in recent years. For example, while from 2001 to 2005, Russian OFDI averaged USD 7 billion a year on a balance-of-payments basis, over the next three-year period, 2006–2008, this average jumped to USD 34 billion.[563]

Because of this rapid expansion of Russian MNEs abroad, Russia now has the second largest stock of direct investments abroad among the emerging economies (USD 203 billion in 2008), behind the special case of Hong Kong (China) (USD 776 billion in 2008). Russian MNEs hold more FDI assets than Brazil (USD 162 billion), China (USD 148 billion) and India (USD 62 billion) (annex table 1). Between 1995 and 2007, Russia's OFDI stock was growing more

[561] See G. Hamilton (ed.), *Red Multinationals or Red Herrings? The Activities of Enterprises from Socialist Countries in the West* (London: F. Pinter, 1986).
[562] FDI statistics collected by the *Bank of Russia* and international organizations such as *UNCTAD* register transactions on a net payment basis; cross-border M&A data from UNCTAD are recorded mostly on a gross value and announcement basis; the statistics of *Rosstat* are based on company surveys of investment intentions. Even though there are a number of steps between investment intentions and cash flow, Rosstat data are useful for the information contained on the geographical composition of OFDI, something that balance-of-payments data do not currently provide. All these sources have difficulties with registering complex flows passing various borders.
[563] According to UNCTAD's FDI/TNC database (http://stats.unctad.org/fdi/) and the balance-of-payments data of the Bank of Russia (www.cbr.ru/eng/statistics/?Prtid=svs).

rapidly than the OFDI stock of the other emerging economies mentioned. However, as a result of the global financial crisis, a sharp downward revaluation of Russian assets held abroad reduced Russia's lead vis-à-vis other large emerging economies by the end of 2008 (annex table 1).

Detailed data on Russian OFDI are not available, but given the large role played by foreign takeovers as the mode of their expansion abroad, features of the dynamics of Russian OFDI can be gleaned from data on cross-border M&As.[564] In the period January 2005–June 2008, such M&As increased by more than ten times compared with the period 2001–2004, from USD 5.5 billion to USD 56.8 billion. Most of these cross-border purchases were in the primary sector, which accounted for 59% of M&As in January 1997–June 2008 (annex table 2). Within manufacturing, which accounted for 23%, machinery, metals and motor vehicles were the three most important industries. The share of services was 18%, of which telecommunications was much the most important industry.

As to the geographical distribution of acquisitions abroad, the data show that Russian firms have generally targeted developed country firms, especially in Europe and North America (annex table 3 and section on companies below). One part of the world that has been particularly open to Russian investment is the Commonwealth of Independent States (CIS). Most CIS countries have close relations with the Russian Federation. Benefiting from these historical ties and from a deep knowledge of the local business environment, Russian FDI in these countries is relatively large and has been growing. Rosstat data show that Russian investment in the CIS economies (including FDI, portfolio and other foreign investment) grew rapidly from 2000, in which year it was USD 130 million, to 2008, when it was well over USD 10 billion (annex table 4). The leading CIS destinations in 2008 were Belarus and Ukraine, followed at some considerable distance by Kazakhstan and Armenia. For some of these countries, Russia is a major source of IFDI.

The data set on cross-border M&As also allows us to measure the size of round-tripping transactions in OFDI, under which foreign affiliates of Russian firms, typically established in offshore financial centers such as such as Cyprus, the Netherlands and the British Virgin Islands (annex table 5), invest back to the Russian Federation: such deals amounted to almost $7 billion over January 1997–June 2008, accounting for 10% of the total (annex table 3).[565]

The corporate players

Some 50 to 60 MNEs account for a large part of Russian assets abroad, with OFDI among this group dominated by such behemoths as Gazprom, Lukoil, Sberbank, AFK Systema, Norilsk Nickel, Evraz, Rusal, and Severstal, all of them global players, some of which in turn are part of larger and looser business groups (e.g. Rusal is part of the Basic Element Group).[566] The majority of Russian MNEs operate in four major industries: oil and gas, metallurgy, finance, and telecommunications. Despite the concentration of OFDI among a limited number of large MNEs, the total number of Russian firms investing abroad probably exceeds 1,000.

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[564] These data need to be treated with some caution as they register announced deals, whose payment could take place over various years, and in some other cases could be canceled.
[565] This measurement is possible because the data base records both the immediate and the ultimate buyers and sellers.
[566] See Alexei V. Kuznetsov, "Russian companies expand foreign investments", *Russian Analytical Digest*, 2008, No.34 (www.res.ethz.ch).

In particular, the 10 largest announced M&A transactions in January 2005–December 2008 mainly involved Russian resource-based firms (e.g., Norilsk Nickel, Evraz Group, Gazprom, Lukoil) targeting purchases mostly in Canada, Italy and the United States (annex table 6). So far, the largest transaction has been Norilsk Nickel's full acquisition of Lion Ore Mining in Canada in 2007.

The state has played an important role in the emergence of Russian OFDI. SOEs, such as Gazprom, possess a set of advantages (financial capabilities, access to loans from the central bank, administrative support, etc.) that facilitate their internationalization. At the same time, even in fully or partly privatized enterprises, state influence remains, sometimes directly (for example through residual ownership, as in Rosneft) and sometimes indirectly, through State support and other measure of State influence. When it comes to companies in the energy sector, the law makes Russian – state or private – majority ownership mandatory.

Russian OFDI has been driven by various motives, including a desire of managers and private equity owners to mitigate the economic and political risks still inherent in their home market through holding a large portion of assets offshore (a variety of post-transition "capital flight" related to "system-escape" motives, which decreased sharply after 1999 but bounced back during the global crisis). Expected profitability of FDI has been another primary driver. However, there is no clear evidence as to what degree the expectations of Russian firms about the ease and low transaction cost of M&A purchases facilitating vertical integration and increasing control of the value chain of products (from the extraction of natural resources at home to the processing and distribution abroad) have materialized. Aspirations for better global recognition and an improved image abroad have also been among the drivers of Russia OFDI.

Effects of the current global crisis

The dynamism of Russian OFDI has weakened lately, in part due to the onset of the global economic and financial crisis. From 2007 to 2008, it still grew, but only by about 15% (from USD 46 billion to USD 53 billion). In the first quarter of 2009, however, OFDI fell by 15% (from USD 16 billion to USD 13 billion) on a year-to-year basis.[567] These data, as compiled by the Bank of Russia, differ from the OFDI data of Rosstat, the Russian statistical agency, which show Russian OFDI jumping in the first quarter of 2009 to nearly USD 10 billion, an increase by a factor of eight over the first quarter of 2008.[568] The discrepancy between the two data sources reflects fundamental differences between the statistical methodologies of the two agencies.[569]

The sharp downward revaluation of Russian assets held abroad in 2008 (annex table 1) could indicate major problems at the international affiliates of Russian MNEs, although reliable reports on eventual downsizings or closures are impossible to find for the moment. It seems that, despite their mounting difficulties, the financial crisis has not stopped Russian companies from seeking to expand internationally, although it may have made it harder, as the prices of their commodity exports decline and their market capitalization shrinks. Through the first quarter of 2009, however, there were no signs of the repatriation of Russian financial assets abroad, from

[567] According to the Bank of Russia (www.cbr.ru/eng/statistics/?Prtid=svs).
[568] www.gks.ru/bgd/free/b04_03/IssWWW.exe/Stg/d02/29inv24.htm.
[569] As noted in footnote 2, the Bank of Russia registers a transaction only when it is fully paid for, so its statistics are very sensitive to events affecting the financing of MNEs such as the current crisis. Rosstat, on the other hand, reports transactions when intentions to undertake them are announced by companies and thus points to resumed dynamism in the future.

international financial centers such as Cyprus, the Netherlands, the British Virgin Islands, and Gibraltar, which partly serve as tax havens for Russian firms as well. These locations still figured prominently (first, second, sixth, and eighth positions) in the OFDI flows of Russia in the first quarter of 2009 (annex table 5).

Indeed, a number of large transactions were announced in the first quarter of 2009; notably, the Russian company Surgutneftegaz purchased 21% of the shares of MOL Hungarian Oil and Gas Plc. (bought from Austria's OMV Group) and TNK bought 49% of the shares of the US manufacturer of steel pipes NS Group Inc. In another notable case, Lukoil paid €852 million to Italy's ERG to acquire a 49% share in the joint venture refinery ISAB in Sicily. The crisis has had also some positive impacts: it has cut down the prices of foreign assets that some Russian companies intended to acquire. For example, at the end of 2008, Severstal saved USD 302 million (from an original price of USD 1 billion) when purchasing the Canadian coal-mining firm PBS Coals,[570] and NLMK saved USD 50 million (from an original price of USD 400 billion) when purchasing the US steelmaking firm Beta Steel,[571] both as a result of declining asset prices.

A full evaluation of how the crisis continues to affect Russian OFDI is not yet possible. The financial difficulties of the natural-resource-based MNEs may however indicate that these companies need to slow down or cancel their investment plans in the future. Alternatively, they may rely more on State help, including financing obtained from State-owned banks. The crisis may have also altered the political context of Russian OFDI, especially the bilateral relationships of Russia with its main partners (the EU and the United States). It also remains to be seen to what degree "covert" FDI protectionism[572] will gain influence in those partner countries and to what degree that may result in additional obstacles to Russian OFDI. These factors together could potentially change the Russian OFDI landscape, resulting perhaps even in the disappearance of some of today's FDI giants.

The policy scene

One idiosyncratic impediment to Russian investment abroad is the perception in certain countries that Russian companies, especially some of Russia's largest companies, are more subject to political interference than MNEs in general. One sign that the perception exists was cited by the vice-president of Lukoil, Leonid Fedun, who told the *Financial Times* that Russian investors have started to withdraw from countries such as Poland and Lithuania because of political antagonism.[573] Also, according to Fedun, Lukoil was interested in purchasing two oil refineries belonging to the Polish power concern PKN Orlen, but the Polish government saw the "long hand of the Kremlin" behind the deal and feared the misuse of market power for political ends. Another case of putative political antagonism concerned the aforementioned purchase by Surgutneftegaz of the Austrian oil company OMV's holdings in MOL, the Hungarian power company.[574] MOL, although privately owned, is seen as strategic by the Hungarian government, and OMV had itself been accused of being a front for Russian interests in 2007. Although the

[570] www.reuters.com/article/mergersNews/idUSN2526880020081026.
[571] http://expert.ru/news/2008/11/17/nlmkotkaz/.
[572] See UNCTAD, *World Investment Report 2009: Transnational Corporations, Agricultural Production and Development* (New York and Geneva: United Nations, 2009).
[573] "Russian investors face 'antagonism'", *Financial Times*, April 9, 2009, p. 2.
[574] "OMV closes sale of 21.2% of MOL to Russia's Surgutneftegas for EUR1.4 bln", *Interfax Russia & CIS Oil and Gas Weekly*, April 15, 2009.

transaction went through, it was a source of political concern in Hungary.[575]

Anxieties about Russian OFDI have also been expressed by authorities in other European countries, for example in the Czech Republic and Spain. Not all such concerns are over security or possible political interference. Some relate to other factors common to emerging-market OFDI generally, such as the quality of corporate governance or actions that do not meet professional standards. In practice, nevertheless, such concerns are often outweighed by the crisis-generated need for additional equity capital and financial inflows to cover balance-of-payments deficits.

Conclusions and Outlook

Despite various difficulties, Russian direct investors are continuing to penetrate foreign markets. The one thing perhaps lacking is a carefully thought out government policy that recognizes the economic benefits of OFDI, in particular, for competitiveness. Such a policy would also have to convince potential host countries that Russia's government will eschew political interference in Russian MNE operations. It could also support Russian OFDI in a systematic way, as is the practice of many other countries, especially in promoting investment in developing countries (political risk insurance, support for pre-investment studies, etc). It may be that this is changing, as President Medvedev has recently announced the intention of supporting outward investors from Russia.[576] If carried through, this can only promote Russian OFDI and intensify the internationalization process of Russian firms.

Additional readings

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[576] "Medvedev dvinet bizness za granitsu", February 4, 2008, http://businnestalk.ru/content/view/1180/28/.

For analyses of outward FDI from Brazil, China, India and Latin America, please see the following *Columbia FDI Perspectives*, available at: http://www.vcc.columbia.edu/pubs/#Perspectives:

- *Columbia FDI Perspective No. 13*. Luís Afonso Lima and Octavio de Barros, "The growth of Brazil's direct investment abroad and the challenges it faces," August 17, 2009.
- *Columbia FDI Perspective No. 12*. Michael Mortimore and Carlos Razo, "Outward investment by trans-Latin enterprises: reasons for optimism," August 17, 2009.
- *Columbia FDI Perspective No. 11*. Jaya Prakash Pradhan, "Indian FDI falls in global economic crisis: Indian multinationals tread cautiously,"August 17, 2009.
- *Columbia FDI Perspective No. 5*. Ken Davies, "While Global FDI Falls, China's Outward FDI Doubles," May 26, 2009.

Statistical annex

Annex table 1. Outward FDI stock of selected economies, various years (USD billion)

Economy	1995	2000	2005	2007	2008
United States	1,363.8	2,694.0	3,638.0	5,228.0	3,071.2
Hong Kong, China	78.8	388.4	471.3	1,011.2	775.9
Russian Federation	3.3	20.1	146.7	370.2	202.8
Brazil	44.5	51.9	79.3	136.1	162.2
China	17.8	27.8	57.2	95.8	147.9
India	0.5	1.9	10.0	44.1	61.8

Source: UNCTAD's FDI/TNC database, http://stats.unctad.org/fdi/ and United States, *Survey of Current Business*, September 2009 and 2006.
Note: In 2008, the decline in OFDI stock of certain countries reflects a sharp downward revaluation of assets held abroad due to the global financial crisis.

Annex table 2. Cross-border purchases by Russian multinationals, by sector/industry, January 1992–June 2008 (USD million)

Sector / industry	1992–1996	1997–2000	2001–2004	2005–2008
All sectors / industries	511	1,700	5,498	55,850[a]
Primary	45	1,098	2,980	33,485
Agriculture, forestry, and fishing	-	-	5	-
Mining, quarrying and petroleum	45	1,098	2,976	33,485
Mining and quarrying	-	-	1,546	15,742
Petroleum	45	1,098	1,430	17,743
Secondary	451	146	661	13,430
Food, beverages and tobacco	-	90	9	2
Wood and wood products	3	-	-	34
Oil and gas; petroleum refining	-	7	161	589
Chemicals and chemical products	-	-	164	113
Metal and metal products	-	31	306	2,914

Machinery	6	-	17	7,575
Electrical and electronic equipment	-	2	-	453
Electronic equipment	-	2	-	217
Communications equipment	-	-	-	143
Transportation equipment	442	15	-	1,537
Motor vehicles	200	15	-	1,537
Services	15	456	1,857	8,935
Electricity, gas, and water	-	177	60	1,042
Construction firms	-	-	100	1,637
Hotels and casinos	-	-	2	468
Trade	-	235	536	350
Transport, storage and communications	15	13	1,106	3,880
Telecommunications	-	10	1,021	3,637
Finance	-	23	30	1,773
Business activities	-	2	23	116
Business services	-	2	19	250
Community, social and personal services	-	7	-	888

Source: UNCTAD, cross-border M&A database, http://stats.unctad.org/fdi/.
[a] Excluding unspecified industries.

Annex table 3. Cross-border M&A purchases by Russian multinationals, by host country/region, January 1992–June 2008 (USD million)

Country / region	1992–1996	1997–2000	2001–2004	2005–2008
World	511	2,211	5,498	56,794
Developed economies	511	2,151	3,962	44,287
Europe	311	1,749	2,766	30,575
European Union	311	1,749	2,566	30,160
Austria	-	-	4	1,662
Belgium	-	90	-	-
Bulgaria	-	816	37	-
Cyprus	-	-	-	511
Finland	45	45	-	276
Greece	-	-	-	806
Hungary	6	6	-	177
Italy	-	-	-	1,280
Luxembourg	-	-	-	1,660
Netherlands	245	245	-	-
Romania	-	300	121	-
Slovakia	-	-	72	-
Slovenia	-	-	-	50
Sweden	-	-	-	4,652
United Kingdom	-	211	2,273	19,016
North America	-	170	1,195	13,247
Canada	-	-	68	7,937
United States	-	170	1,127	5,310
Other developed countries	200	232	-	465
Australia	-	2	-	461
Japan	200	200	-	-
Developing economies	-	-	-	3,210

Africa	-	-	-	250
Nigeria	-	-	-	250
Asia and Oceania	-	-	-	2,945
Turkey	-	-	-	2,006
China	-	-	-	786
Malaysia	-	-	-	92
South-East Europe and the CIS	-	61	1,536	9,297
Southeast Europe	-	-	303	257
Bosnia and Herzegovina	-	-	-	157
Croatia	-	-	76	-
Serbia and Montenegro	-	-	225	59
Commonwealth of Independent States (CIS)	-	61	1,233	9,039
Armenia	-	-	27	423
Kyrgyzstan	-	-	-	150
Russian Federation	-	47	990	5,614
Ukraine	-	13	199	2,769

Source: UNCTAD, cross-border M&A database, http://stats.unctad.org/fdi/.

Annex table 4. Russia's investment flows [a] to the Commonwealth of Independent States, commitment data, 2000, 2005, 2007 and 2008

Country	2000		2005		2007		2008	
	USD thousand	% of total	USD thousand	% of total	USD thousand	% of total	USD thousand	% of total
Azerbaijan	26	0	6,734	1.1	8,994	0.3	20,034	0.2
Armenia	5	0	138,185	22.3	3,907	0.1	444,676	4.3
Belarus	77,238	59	102,438	16.5	1,314,092	48.7	5,945,951	58
Georgia	133	0.1	60	0	433	0	3,924	0
Kazakhstan	3,453	2.6	204,314	32.9	445,068	16.5	762,159	7.4
Kyrgyzstan	7	0	1,247	0.2	207,718	7.7	386,029	3.8
Republic of Moldova	31,224	23.8	4,904	0.8	4,248	0.2	22,377	0.2
Tajikistan	-	-	496	0.1	105,683	3.9	171,962	1.7
Turkmenistan	2,934	2.3	-	-	0,4	0	6,357	0.1
Uzbekistan	929	0.7	6,968	1.1	93,040	3.6	96,823	0.9
Ukraine	15,032	11.5	155,176	25	513,580	19	2,397,847	23.4
Total to CIS countries	**130,981**	**100**	**620,522**	**100**	**2,696,763**	**100**	**10,258,139**	**100**

Source: Rosstat, www.gks.ru/bgd/regl/b08_11/IssWWW.exe/Stg/d03/24-13.htm

[a] Included are not only FDI, but also portfolio and other foreign investments.

Annex table 5. Russia's OFDI flows, commitment data,[a] first quarter of 2009 (USD million)

Main destinations	Amount
Cyprus	12,559
Netherlands	11,065
United States	4,944
United Kingdom	2,045
Belarus	1,943
British Virgin Islands	1,298
Switzerland	1,181
Gibraltar	1,000
Germany	107
Ukraine	102
Total outward foreign investment flows	**38,454**

Source: Rosstat, www.gks.ru/bgd/free/b04_03/IssWWW.exe/Stg/d02/91inv21.htm.

[a] Included are not only projects that have been paid for, but also FDI that is in the phase of announcement or approval.

Annex table 6. Ten largest M&A deals by Russian MNEs, 2005-2008

Year	Acquiring Russian company	Target company	Target industry	Target country	Shares acquired (%)	Estimated/ announced transaction value (USD mn)
2007	Norilsk Nickel	LionOre Mining	Gold	Canada	100	6,287
2008	Evraz Group	IPSCO –Canadian operations	Steel pipes and tubes	Canada	100	4,025
2007	Gazprom	Beltransgaz	Natural gas distribution	Belarus	50	2,500
2008	Evraz Group	Sukhaya Balka GOK	Iron ore	Ukraine	99	2,189
2008	Lukoil	ERG SpA – ISAB Refinery	Oil and natural gas	Italy	100	2,098
2007	Evraz Group	Oregon Steel Mills	Steel works	United States	90	2,088
2005	Lukoil	Nelson Resources	Gold	United Kingdom	100	2,000
2007	Rasperia Trading (Basic Element)	Bauholding Strabag	Industrial buildings	Austria	30	1,637
2005	Alfa Group	Turkcell	Telecommunication	Turkey	13	1,602
2007	Basic Element	Magna International	Motor vehicles	Canada	18	1,537

Source: UNCTAD, cross-border M&A database, http://stats.unctad.org/fdi/.

Chapter 22 – Ukraine

Ukraine's inward FDI and its policy context

Oleksiy Kononov

With a population of more than 46 million people, Ukraine is a sizeable potential market for foreign direct investment (FDI). Domestic firms are not very competitive. Together with a favorable geographic location and low costs of labor and other inputs, Ukraine offers attractive opportunities for foreign investors. This potential, however, is not yet exploited, as indicated by relatively low cumulative inflows of FDI, due to the slow progress of transition toward a market economy, a high level of corruption, absence of effective guarantees protecting foreign investors, and political instability. In the wake of the global financial crisis and recession, the Ukrainian Government introduced policy measures that can potentially make inward foreign direct investment (IFDI) to Ukraine more complicated. Overcoming the crisis, improving the investment framework, accelerating economic reforms (including transparent privatizations) and association with the European Union (EU) would all be key factors permitting Ukraine to exploit its considerable FDI potential.

Trends and developments

Following the collapse of the Soviet Union, Ukraine suffered serious economic problems. The absence of clear property rights, insider privatization policies and hyperinflation did not make the country an appealing investment destination in the early 1990s. Stabilization measures in the mid-1990s curbed hyperinflation and stabilized the economy, leading to the resumption of economic growth and higher FDI inflows. The Ukrainian market (which is twice as big as the Romanian one and six times as big as the Bulgarian one, measured by population size) is attractive both for market- and efficiency-seeking FDI because of its well-qualified low-cost labor force and the availability of natural resources like fertile land, iron ore and coal.[577]

Country-level developments

In 2000, the inward FDI stock of Ukraine was low, amounting to US$ 3.8 billion. But, in the subsequent years it grew steadily (annex tables 1 and 2). At the end of 2008, Ukraine (with an estimated inward FDI stock of US$ 47 billion) was the third biggest recipient of inward FDI among the countries of South-East Europe and the Commonwealth of Independent States (CIS), after the Russian Federation and Kazakhstan.[578] However, Ukraine's FDI performance lags behind smaller countries of the region such as Slovakia or Bulgaria.

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[577] These are main IFDI drivers identified by respondents to a survey on the investment climate of Ukraine. *See* SEOLA Group Ideas Factory, "Global survey of foreign investors," October 2009, in Valentyna Kuzyk, Vilen and Veremko, Resursna anemiya, Ukrainsky Tyzhden, No. 50 (111), December 11, 2009; also available at: http://www.prometr.com.ua/category/analytic/all/3657/mode/print. The survey covered 397 multinational enterprises from 33 countries.

[578] UNCTAD, *World Investment Report 2009: Transnational Corporations, Agricultural Production and Development* (New York and Geneva: United Nations, 2009), p. 74.

The distribution of FDI inflows (annex table 3) demonstrates that foreign investors prefer to invest in the following sectors of the Ukrainian economy: financial services (22% of all FDI inflows), industry (23%), retail services (11%), and real estate (10%). Only 2% of total cumulated IFDI went into the agricultural sector, despite the fact that Ukraine is one of the top ten world exporters of agricultural commodities (wheat, soya beans, maize).[579] This can be explained by governmental policies (see the policy section below) and competition on the part of domestic companies and farmers.

From 2004 onwards, a large part of FDI was invested in activities driven by speculative motives (financial services, construction, real estate, retail trade). Banks did not use foreign capital and loans to invest in the manufacturing sectors of the economy, or the modernization of the infrastructure or to promote innovation. Instead, they stimulated consumer finance in the form of mortgages and retail loans.[580] To some extent, this behavior can be explained by very high real estate prices (especially in Kyiv)[581] and an unfriendly business climate in Ukraine[582] that makes long-term projects unfeasible.

Around 80% of cumulated FDI inflows originate in the European Union (annex table 4). Cyprus ranks first among the investor home countries, but it is very difficult to identify ultimate investors for this FDI. Most likely, many of them are Ukrainian and Russian companies, using Cyprus to protect their capital (see notes to annex table 4). Russian investments in Ukraine (23 % of all Russian FDI in other CIS countries in 2008)[583] deserve special attention. Russian capital is concentrated in those sectors of Ukraine's economy that significantly affect the industrial growth of the country and budget revenues (annex table 5).[584] As one can see from annex table 5, the share of Russian capital in some economic sectors is very high (*e.g.,* in gas, aluminum, oil refineries). This situation raises certain national security concerns as well as political issues related to recent gas-related conflicts between Ukraine and Russia. On the other hand, there are no statutory prohibitions to invest in "sensitive" sectors for Russian or any other foreign investors.[585] Moreover, it is quite possible that, after recent political changes, the share of Russian investments in the gas sector will increase substantially.

The regional distribution of IFDI within Ukraine is very uneven. Kyiv, the country's political and economic capital, accounts for 39% of all FDI inflows, while the industrial regions of Dnipropetrovsk, Kharkiv and Donetsk account for 7%, 5% and 4%, respectively. The share of FDI inflows to the other 22 regions varies between 0.2 - 4 %.[586]

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[579] UNCTAD, *World Investment Report* 2009, op. cit., p. 236.

[580] SEOLA Group Ideas Factory, op. cit.

[581] Helen Fawkes, "Kiev becomes latest property hotspot," *BBC News*, January 5, 2007, available at: http://news.bbc.co.uk/2/hi/business/6228205.stm; Institute for Economic Research and Policy Consulting in Ukraine, German Advisory Group on Economic Reform, "Mortgage lending in Ukraine: three strategic questions and answers," 2003, p. 2, available at: http://ierpc.org/ierpc/papers/t3_en.pdf.

[582] See further explanations in the policy section below.

[583] Andrei Panibratov and Kalman Kalotay, "Russian outward FDI and its policy context," *Columbia FDI Profiles*, No. 1 (October 31, 2009), p. 8.

[584] Nataliya Blyakha, "Russian foreign direct investment in Ukraine," *Electronic Publications of Pan-European Institute 7/2009*, p. 7, available at: http://www.tse.fi/FI/yksikot/erillislaitokset/pei/Documents/Julkaisut/Blyakha%200709%20web.pdf.

[585] Art. 117(2) of the *Commercial Code* prohibits the establishment of foreign enterprises in economic sectors of strategic importance. Those sectors are to be defined by law. However, no such law has been adopted so far. Currently, criteria for acknowledgement of enterprises as strategically important are established by non-statutory Government Resolution No. 695 of May 15, 2003. The practical application of this Resolution in the field of IFDI is rather controversial.

[586] State Statistics Committee of Ukraine (Ukrstat), "Investytsiyi zovnishnyoekonomichnoyi diyalnosti u 2009 rotsi," February 2010, p. 6, available at: http://www.ukrstat.gov.ua.

The corporate players

Affiliates of the largest multinational enterprises (MNEs) in the world can be found in Ukraine (annex table 5).[587] Arcelor Mittal has been the leading foreign investor in Ukraine since 2005. Its acquisition of Kryvorizhstal became the biggest transaction not only in Ukraine but in the whole CIS.[588] The year 2005 became a landmark in the history of FDI in Ukraine not only due to the Kryvorizhstal deal but also due to the purchase of the Ukrainian Aval bank by Austrian Reiffeisen, which raised annual inward FDI flows to a much higher level of US$ 8 billion (annex table 2). After this, a wave of other acquisitions by foreign banks and financial institutions followed. Among other leading foreign investors in Ukraine are the Russian companies RUSAL, ISTIL and Evraz (aluminum and metallurgical sectors), as well as MTS and Norwegian Telenor (mobile communications) (annex tables 5 and 6).

Effects of the current global crisis

The global economic and financial crisis had a strong negative impact on the Ukrainian economy. In 2009, the real GDP of Ukraine declined by 14% and its manufacturing production shrank by 30%.[589] The metallurgy sector that produces Ukraine's main export commodity suffered the most due to the sharp decline of steal prices on world markets.[590] The protracted political crisis and the inability of the Ukrainian Government to cope with the consequences of the crisis generated major investment risks for prospective foreign investors.[591] In 2009, inward FDI flows amounted to US$ 5.6 billion, down by 49 % against 2008.[592]

The banking and real estate sectors (which had attracted large investments in past years) lost their attractiveness. As of December 1, 2009, twelve Ukrainian banks have gone into liquidation, three banks have been nationalized; and more than sixty Ukrainian banks were offered for sale (out of 180 banks operating in the country).[593] According to the SEOLA October 2009 survey, only 9% of respondents were still interested to invest in the Ukrainian financial sector, compared to 88% in October 2008.[594] The construction sector experienced a similar decline.[595]

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[587] As detailed statistical data on MNEs in Ukraine are not available, in annex table 5 it was impossible to rank MNEs based on a single criterion like assets, revenues, sales or total FDI in Ukraine.

[588] UNCTAD, *World Investment Report 2006: Foreign Direct Investment from Developing and Transition Economies: Implications for Development* (New York and Geneva: United Nations), p. 79.

[589] As of October 2009, Ukraine's GDP was US$ 115.7 billion, compared to US$ 44.7 billion in Bulgaria and US$ 160.6 billion in Romania. See IMF World Economic Outlook Database, October 2009, available at: http://www.imf.org/external/pubs/ft/weo/2009/02/weodata/index.aspx.

[590] International Monetary Fund, *World Economic Outlook, October 2009: Sustaining the Recovery* (Washington: IMF), p. 81, available at: http://www.imf.org/external/pubs/ft/weo/2009/02/pdf/text.pdf; RT Business News, "Ukraine waits on IMF bailout funds," December 15, 2009, available at: http://rt.com/Business/2009-12-15/ukraine-sweats-imf-bailout.html.

[591] SEOLA Group Ideas Factory, op. cit.

[592] Ukrstat, "Investitsiyi zovnishnyoekonomichnoyi diyalnosti u sichni-veresni 2009 roku," November 2009, p. 1.

[593] National Bank of Ukraine, "Osnovni pokaznyky diyalnosti bankiv," February 2010, available at: http://bank.gov.ua/Bank_supervision/dynamics.htm.

[594] SEOLA Group Ideas Factory, op. cit.

[595] SEOLA Group Ideas Factory, op. cit.

The policy scene

According to the law, foreigners are free to invest in Ukraine and are entitled to enjoy, at least formally, national and most-favored-nation treatment. Denial of FDI admission is possible on grounds of national security and public safety. Legal entities in which more than 25% of the capital stock is owned by a foreign state cannot participate in the privatization of state and municipal property.[596] Foreign citizens, foreign legal entities and stateless persons are banned from the creation of television and/or broadcasting organizations in Ukraine.[597] Direct branching of foreign insurers is not allowed either; however, this restriction must be lifted before May 2013, due to WTO requirements.[598]

Pursuant to the latest amendments[599] to the *Law on the Regime of Foreign Investment*, all foreign investments have to be registered, otherwise state guarantees on investment protection and free transfer of profits shall not apply. Monetary investments must be registered with the National Bank of Ukraine; regional authorities register investments in kind.[600] Failure to register investments does not, however, result in compulsory divestment. The same amendments also introduced a new rule, according to which foreign investments can be made only through so-called investment accounts opened in Ukrainian banks. Investments in foreign currency are subject to conversion in the Ukrainian currency.[601] These measures were adopted with the purpose to increase the efficiency of state authorities in the financial and credit sectors and to stabilize the macroeconomic situation in the country[602] and will be in force until January 1, 2011. Together with the existing currency restrictions and very bureaucratic rules for the repatriation of profits and/or investments,[603] the above mentioned statutory enactments create more obstacles for inward FDI.

Foreign natural and legal persons, as well as companies with foreign participation cannot own farmland plots in Ukraine.[604] Besides, existing procedures for land acquisition and the leasing of land plots are very burdensome and corrupted. This has been one of the main issues criticized by prospective foreign investors willing to invest in the Ukrainian agricultural sector or to start greenfield projects in other economic sectors.[605]

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[596] Art. 8(3) of the *Law on Privatization of State Property* of March 4, 1992; Art. 5(2) of the *Law on Privatization of Small State Enterprises (Small Privatization)* of March 6, 1992.

[597] Art. 12(2)-(3) of the *Law on Television and Broadcasting* of December 21, 1993. However, according to the *Commercial Code*, foreigners can become shareholders after incorporation.

[598] Art. 2 of the *Law on Insurance* of March 7, 1996; WTO (2008), *Working Party Report on the Accession of Ukraine to the WTO*, WT/ACC/UKR/152 (January 25, 2008), p. 123.

[599] *Law of Ukraine on "Amending Some Laws of Ukraine with the Purpose to Mitigate Negative Consequences of the Financial Crisis* of June 23, 2009."

[600] Prior to November 24, 2009 (the op. cit. Law of June 23, 2009 entry into force), all foreign investments were registered by the regional authorities (Government of the Autonomous Republic of Crimea, 24 regional state administrations , Kyiv and Sevastopol city state administrations).

[601] Prior to November 2009, there were no compulsory exchange requirements.

[602] Preamble of the op. cit. Law of June 23, 2009.

[603] For more details on these restrictions see European Business Association, *Overcoming Obstacles to Business Success* (Kyiv: EBA, 2009), pp. 26-30, available at: http://www.eba.com.ua/files/documents/IPAPER_2009_eng_web.pdf.

[604] Arts. 81, 82 of the *Land Code*.

[605] Keith Crane and Stephen Larrabee, *Encouraging Trade and Foreign Direct Investment in Ukraine* (Santa Monica, CA: Rand Corporation, 2007), pp. 29-30.

As of June 1, 2009, Ukraine had signed 62 bilateral investment treaties (BITs),[606] as well as the Energy Charter Treaty (ECT). As of January 1, 2009, Ukraine concluded double taxation agreements with 65 countries.[607] At present, negotiations about a free trade agreement with the European Union are taking place. The conclusion of such an agreement would increase Ukraine's attractiveness as a business location and perhaps repeat the success of other Central and East European countries in attracting FDI.

Overall, the Ukrainian investment climate is characterized by unpredictable changes of the legal environment, low respect for existing guarantees for foreign investors, the absence of real protection of property rights, and high corruption. The Transparency International Corruption Perceptions Index 2009[608] ranked Ukraine as the 28th most corrupted country in the world (among 180 countries monitored), *ex aequo* with Russia, Zimbabwe, Cameroon, Sierra-Leone, Timor-Leste, Kenya, and Ecuador. The World Bank Group Doing Business Project 2010 ranked Ukraine 142nd among 183 economies of the world in terms of easiness of doing business.[609] However, Ukraine's rank for protecting investors improved in 2010 compared with 2009, perhaps the result of a new Law on Joint Stock Companies that came into force on April 29, 2009.[610]

Finally, Ukraine is a frequent participant in international investment arbitration. In the International Centre for Settlement of Investment Disputes (ICSID), there are ten cases against Ukraine (four concluded and six pending).[611] It should be noted, however, that so far Ukraine has not lost any of the ICSID cases. The same can be said about the recent *Limited Liability Company AMTO v. Ukraine* case[612] in the Arbitration Institute of the Stockholm Chamber of Commerce, where the Latvian investor failed to prove violations of the ECT by Ukraine.

Outlook

Despite existing difficulties with the legal framework, political risks and corruption, Ukraine can still offer investment opportunities for international investors attracted by its big internal market, a qualified labor force and low wages, its natural resources, and a favorable geographic location. In 2012, Ukraine will host the UEFA European Football Championships, offering investment opportunities for foreign companies in the infrastructure, telecommunications and tourist sectors.[613] In response to conflicts with Russia concerning energy resources and Ukraine's dependence on imported gas and oil, the Government has recently started to stimulate usage of alternative energy sources, which could offer opportunities for foreign investors possessing these technologies. On the other hand, the new Government of President Viktor Yanykovich may change the situation by renegotiating gas supply contracts with Russia and offering certain political concessions. Such changes might affect alternative energy policies, as well as the foreign investors involved.

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[606] UNCTAD, *Country-Specific Lists of Bilateral Investment Treaties* (New York and Geneva: United Nations, 2009), available at: http://www.unctad.org/Templates/Page.asp?intItemID=2344&lang=1.
[607] Database of the State Tax Administration of Ukraine, available at: http://www.sta.gov.ua.
[608] Available at http://www.transparency.org/policy_research/surveys_indices/cpi/2009/cpi_2009_table
[609] The World Bank, *Doing Business 2010: Ukraine* (Washington, IBRD/World Bank, 2009), p. 2.
[610] *Law of Ukraine on Joint Stock Companies* of September 17, 2008.
[611] Database of the International Centre for Settlement of Investment Disputes, available at: http://icsid.worldbank.org/ICSID/FrontServlet
[612] Limited Liability Company AMTO v. Ukraine (Latvia v. Ukraine), (Arbitration Institute of the Stockholm Chamber of Commerce, Arbitration No. 080/2005), Final Award, March 26, 2008, available at: http://www.investmenttreatynews.org/documents/p/37.aspx.
[613] See the *Law on Organizing and Hosting the European Football Cup Finals of 2012 in Ukraine* of April 19, 2007.

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Ukrainian Center for Foreign Investment Promotion, http://www.investukraine.org/

Statistical annex

Annex table 1. Ukraine: inward FDI stock, 2000-2008 (US$ billion)

Economy	**2000**	**2001**	**2002**	**2003**	**2004**	**2005**	**2006**	**2007**	**2008**
Ukraine	**3.8**	**4.8**	**5.9**	**7.5**	**9.6**	**17.2**	**23.1**	**38.1**	**47.0**
Memorandum: comparator economies									
Bulgaria	2.7	2.9	4.0	6.3	10.1	13.8	23.3	39.4	46.0
Poland	34.2	41.2	48.3	57.8	86.6	90.7	125.5	175.8	161.4
Slovakia	4.7	5.5	8.5	14.5	21.8	23.6	33.6	45.2	45.9

Source: UNCTAD, FDI/TNC database, available at: http://stats.unctad.org/fdi.

Annex table 2. Ukraine: inward FDI flows, 2000-2009 (US$ billion)

Economy	**2000**	**2001**	**2002**	**2003**	**2004**	**2005**	**2006**	**2007**	**2008**	**2009 1st – 2nd quarter**[a]
Ukraine	**0.6**	**0.8**	**0.7**	**1.4**	**1.7**	**7.8**	**5.6**	**9.9**	**10.6**	**3.8**
Memorandum: comparator economies										
Bulgaria	1.0	0.8	0.9	2,1	3.4	3.9	7.6	11.7	9.2	2.1
Poland	9.3	5.7	4.1	4.8	12.7	10.2	19.6	22.6	16.5	15.9
Slovakia	1.9	1.5	4.1	2.1	3	2.4	4.6	3.2	3.4	4.7

Sources: UNCTAD, FDI/TNC database, available at: http://stats.unctad.org/fdi:
Ukrstat, "Investitsiyi Zovnishnyoekonomichnoyi Diyalnosti u I Pivricchi 2009 roku", August 2009;
Bulgarian National Bank, "Direct investments" (January-December 2009), available at:
http://bnb.bg/bnbweb/groups/public/documents/bnb_publication/200912_s_fdi_pub_en.pdf;
Polish National Bank, "International investment position of the Republic of Poland" (2004-2009, quarterly data), available at:
http://www.nbp.pl/homen.aspx?f=en/statystyka/iip_k.html;
Slovak National Bank, "International investment position for Slovak Republic for 2009", available at:
http://www.nbs.sk/en/statistics/balance-of-payments-statistics/international-investment-position/mip/2009.

[a] As quarterly IFDI data for all four countries are not available, it is impossible to provide comparable 2008 figures.

Annex table 3. Ukraine: sectoral distribution of cumulative FDI inflows, 2000, 2005, 2009 [a] (US$ million)

Sector/industry	**2000**	**2005**	**2009**
All sectors/industries	**3875**	**11109**	**40027**
Primary	**195**	**611**	**2005**
Agriculture, forestry and fishing	74	301	877
Mining and quarrying	121	310	1128
Secondary	**2042**	**5134**	**10107**
Food, beverages, and tobacco	796	1170	1837
Light industry	48	129	146
Timber (excluding manufacture of furniture)	42	156	281
Cellulose, paper, and publishing	44	160	237
Coke and petroleum	151	211	452
Chemical	206	586	1206
Other mineral manufacture (excluding metal)	64	221	834
Metallurgy	167	1232	1401
Machine-building	303	694	1094
Other industries	100	136	254
Electric energy, gas, and water	22	53	153
Construction	100	387	2213
Services	**1639**	**5365**	**19854**
Retail trade and retail services	647	1953	4225
Hotels and restaurants	109	283	429
Transport and communications	245	744	1506
Financial services	313	1053	8968
Real estate	152	927	4065
Other services	172	406	662
Other unspecified sectors	N/A	N/A	8061

Source: Ukrstat, *Investitsiyi Zovnishnyoekonomichnoyi Diyalnosti u 2009 Rotsi* (Ukrstat, February 2010), p. 8, available at: http://www.ukrstat.gov.ua; Ukrstat, *Investitsiyi Zovnishnyoekonomichnoyi Diyalnosti u 2000 Rotsi: Statystuchny Buleten Derzhkomstatu Ukrainy* (Kyiv: Ukrstat, 2001); Ukrstat, *Investitsiyi Zovnishnyoekonomichnoyi Diyalnosti u 2005 Rotsi: Statystuchny Buleten Derzhkomstatu Ukrainy* (Kyiv, 2006).

[a] Cumulative figures as of beginning of investment (early 1990s). Stock data are not available.

Annex table 4. Ukraine: geographical distribution of cumulated FDI inflows, [a] **2005, 2009** [b] (US$ million)

Region/economy	**2005**	**2009**
World (total)	**16,375.2**	**40,026.8**
Developed economies		
Europe		
European Union		
Cyprus	1,562.0	8,593.2
Germany	5,505.5	6,613.0
Netherlands	721.8	4,002.0
Austria	1,423.6	2,604.1
United Kingdom	1,155.3	2,375.9
Sweden	N/A	1,272.3
Italy	N/A	992.2
Poland	224.0	864.9
Hungary	191.1	675.1
Non-EU		
Switzerland	445.9	805.5
North America		
USA	1,374.1	1,387.1
Caribbean		
British Virgin Islands	688.7	1,371.0
Commonwealth of Independent States		
Russian Federation	799.7	2,674.6
Other economies[c]	2,283.5	4,155.8

Source: Ukrstat database, available at: http://ukrstat.gov.ua.

[a] The true origin of the invested capital is problematic. Many Ukrainian and Russian investors use offshore zones and companies located in other economies (Cyprus, British Virgin Islands, Netherlands) to disguise their real identity and to protect their capital from unpredictable actions of the Ukrainian Government. Data on ultimate investors are not available.

[b] Cumulative figures since the beginning of foreign investment. Stock data are not available.

[c] Data on particular countries are not available.

Annex table 5. Ukraine: principal foreign affiliates in the country, ranked by invested amount, 2004 - 2009 (US$ millions)

Name	Industry	Invested amount
Arcelor Mittal	Metallurgy	7,800
Telenor	Mobile communications	… [a]
Reemtsma	Tobacco	… [b]
OTP Banking Group	Banking	860
MTS	Mobile communications	… [c]
METRO Cash & Carry	Wholesales	371
Coca Cola	Non-alcoholic beverages	270
Procter & Gamble	Personal care products	200
Kraft Foods	Food	150
ISTIL Group	Metallurgy	111
British American Tobacco	Tobacco	110
Erste Banking Group	Banking	104
Nestle	Food	40
Shell	Oil	…
Philip Morris	Tobacco	… [d]
Lukoil	Oil	… [e]
TNK-BP	Oil	… [e]
Tatneft	Oil	… [e]
Gazprom	Gas	… [f]
RUSAL	Aluminum	… [g]

Sources: Companies' websites; Financial Times – fDi Markets | Global Investments; Nataliya Blyakha, "Russian foreign direct investment in Ukraine," *Electronic Publications of Pan-European Institute 7/2009*, p. 7, available at: http://www.tse.fi/FI/yksikot/erillislaitokset/pei/Documents/Julkaisut/Blyakha%200709%20web.pdf

[a] In 2009-3Q, total revenue in Ukraine amounted to US$ 2,200 million.
[b] In 2004, total sales in Ukraine amounted to US$ 179.8 million.
[c] In 2007, total revenue in Ukraine amounted to US$ 438.5 million.
[d] In 2004, Philip Morris had a 31 % share in the Ukrainian tobacco industry sector.
[e] Data on exact amounts of IFDI are not available; in 2007, Lukoil, TNK-BP and Tatneft altogether controlled 90 % of the Ukrainian oil refinery sector.
[f] In 2007, Gazprom's share in the Ukrainian gas sector was 20% .
[g] In 2007, RUSAL's share in the Ukrainian aluminum sector was 90%.

Annex table 6. Ukraine: main M&A deals, by inward investing firm, 2005 – 2009

Year	Acquiring company	Source economy	Target company	Target industry	Shares acquired (%)	Transaction value (US$ million)
2009	JSC Vneshekonombank	Russia	Prominvestbank	Banking	75	156
2009	Central European Media Entrp	Bermuda	Glavred Media Holding	Mass media	10	12
2009	Central European Media Entrp	Bermuda	KINO	Mass media	40	10
2008	Unicredito Italiano SpA	Italy	OJSC Ukrsotsbank	Banking	94	2,231
2008	Evraz Group SA	Russia	Sukhaya Balka GOK	Iron ore	99	2,189
2008	Intesa SanPaolo SA	Italy	JSC Pravex-Bank	Banking	100	746
2007	Pepsi Cola	USA	Sandora LLC	Non-alcoholic beverages	60	542
2007	Commerzbank	Germany	Forum Bank	Banking	60	600
2006	OTP Bank	Hungary	Reiffeisenbank Ukraine	Banking	100	860
2006	BNP Paribas	France	Ukrsibbank	Banking	51	360
2005	Reiffeisen International AG	Austria	Aval Bank	Banking	94	1,000
2005	Mittal Steel Co NV	Netherlands	Kryvorizhstal	Metallurgy	93	4,800

Sources: UNCTAD, cross-border M&A database, available at: http://stats.unctad.org/fdi; UNCTAD, *World Investment Report 2009: Transnational Corporations, Agricultural Production and Developments* (New York and Geneva: United Nations, 2009), pp 73-75; PricewaterHouseCoopers, *Ukraine, Mergers & Acquisitions Market Value Tripled Since 2004 in CEE*, Press Release of April 20, 2007, available at: http://www.pwc.com/ua/en/press-room/release039.jhtml; Pismennaya, Tatyana, *Bolee 60 Bankov Vystavleno na Prodazhu*, Kommentarii, December 25, 2009 – January 10, 2010; Thomson ONE Banker, Thompson Reuters.

Annex table 7. Ukraine: main greenfield projects, by inward investing firm[a] 2007, 2008, 2009

Year	Investing company	Target industry	Source economy	Estimated/ announced transaction value (US$ million)
2009	EcoEnergy	Alternative/ renewable energy	Sweden	270
2009	Novaport	Real estate	Russia	265
2009	Mitsubishi	Alternative/ renewable energy	Japan	234
2009	Aisi Realty	Real estate	Cyprus	205
2009	BT Invest	Real estate	Lithuania	201
2008	ArcelorMittal	Metallurgy	Luxembourg	3,000
2008	Asamer	Real estate	Austria	941
2008	VS energy International NV	Coal, oil and natural gas	Netherlands	750
2008	GLD Invest Group	Real estate	Austria	464
2008	Hyundai Motors	Automotive	Republic of Korea	365
2008	Michaniki	Real estate	Greece	300
2008	Evraz Group	Coal, oil and natural gas	Russia	300
2008	The Outlet Company	Real estate	Poland	201
2007	Meinl European Land	Real estate	USA	1,600
2007	ING Group	Financial services	Netherlands	822
2007	Antonio Merloni	Consumer electronics	Italy	262

Source: fDi Intelligence, a service from the Financial Times Ltd.

[a] Data on shares acquired and joint venture partners (if any) are not available.

Outward FDI and its policy context, 2010

Oleksiy Kononov

Despite Ukraine's reputation as a poor country with a relatively modest OFDI performance, Ukrainian direct investments can be found all over the world, from Europe to Australia. Unfavorable domestic economic conditions and unpredictable political practices, together with a penchant for penetrating closed foreign markets, are among the main OFDI drivers for Ukrainian companies. Ukrainian OFDI declined during the global economic and financial crisis in 2009 but has begun to recover in 2010 and is forecast to increase thereafter.

Trends and developments

In terms of the value of its total OFDI stock, Ukraine ranks far behind Hungary and Poland, though outperforming neighbours like Slovakia and Romania. Among the countries of the Commonwealth of Independent States (CIS), Ukraine ranks second after Russia.[614]

It should be noted, however, that Ukrainian OFDI statistics are rather unreliable. First of all, Ukrainian investors do not always report outward investments.[615] Secondly, foreign affiliates often serve as a mechanism to circumvent restrictions and financial monitoring, as well as to avoid publicity and official statistical recording.[616] Finally, Ukrainian law provides an opportunity to classify certain statistical data on OFDI based on the investor's wish to do so.[617] Official statistics provided by the State Statistics Committee of Ukraine (Ukrstat) are based on residents' reports and information received from the National Bank (NBU) and the State Property Fund of Ukraine. The difference between available OFDI figures is rather remarkable. For example, NBU reported a total Ukrainian OFDI stock of US$ 7 billion in 2009 compared to US$ 6 billion for the same year reported to UNCTAD by NBU earlier.[618]

Country-level developments

The drivers of Ukrainian OFDI are among the main peculiarities of the country's outward investment. Ukrainian companies often invest abroad to secure their assets from the unpredictable political environment in Ukraine, including seizures and raids. Ultimate owners of Ukrainian companies who are able to undertake foreign acquisitions are mostly linked to certain political groups.[619] When the pendulum of Ukrainian politics swings in favor of one group, another one may face the full power of the state aimed at destroying its rival's means of support. Such investments represent capital flight rather than deliberate internationalization strategies of Ukrainian companies.

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[614] UNCTAD, *World Investment Report 2010: Investing in a Low-Carbon Economy* (New York and Geneva: United Nations, 2010), p. 176.

[615] "Mapa investytsiy," *Ukrainsky Tyzhden*, No. 17 (26), April 25 – May 1, 2008.

[616] See further explanations in the policy section below.

[617] This right is embedded in art. 21 of the *Law on State Statistics* of September 17, 1992.

[618] UNCTAD,*2010,* op. cit., pp. 66, 176; Ukrstat, *Investitsiyi zovnishnyoekonomichnoyi diyalnosti u 2009 rotsi* (Kyiv: Ukrstat, February 2010), p. 3.

[619] For speculative information on this issue, see dossiers available in Russian at: http://file.liga.net/. Many Ukrainian tycoons are listed among the richest people in the world by *Forbes*, see http://www.forbes.com/.

Market-seeking, tariffs-jumping and trade-barrier jumping are also major drivers of Ukrainian OFDI. Exporters of steel, the country's main export commodity,[620] have been facing severe anti-dumping restrictions imposed by the European Union (EU) and other developed countries. Moreover, domestic export restrictions lobbied for by large steel producers complicate the situation for smaller market players.[621] To circumvent these obstacles, Ukrainian exporters have invested in foreign companies,[622] sometimes incurring great financial risks. For example, in 2004, Industrialny Soyuz Donbassa (ISD) acquired the Hungarian company Dunaferr for US$ 475 million (with debts amounting to US$ 300 million). In July 2005, after a severe battle with the Polish Government, which had been reluctant to transfer ownership to a non-EU bidder,[623] ISD purchased the metallurgical plant Huta Stali Częstochowa for US$ 374 million and agreed to pay the company's debt of US$ 400 million.[624] Outward investors in the food sector have been more cautious in terms of financial risks. In 2001, to avoid Russia's import limits on Ukrainian caramel, Roshen Corporation (the Ukrainian confectionery leader) bought Likonf Confectionary Factory (Lipetsk, Russia); by the same token, in 2006 Roshen invested US$ 2 million to purchase a 100% stake in Klaipeda Confectionary Factory (Lithuania).

The large cross-border M&As of Ukrainian companies in the metallurgical sector coincided with great political turmoil in the winter of 2004/05, during the Ukrainian "Orange Revolution". In this period, Ukrainian OFDI rose sharply (annex tables 1 and 2). Allies of the defeated Presidential candidate, Victor Yanukovich, were afraid of retaliatory measures by the winners of the Presidential elections, Viktor Yushchenko and Yuliya Tymoshenko, and undertook decisive measures to secure assets abroad. For example, in November 2005 System Capital Management (SCM) increased its stake in the Italian Ferriera Valsider SpA from 49% to 70%.[625] However, the new government did not take retaliatory measures, with the exception of the re-privatization of Kryvorizhstal[626] and its further re-sale to Mittal Steel. Nevertheless, OFDI grew as steel-exporting companies from eastern Ukraine, including ISD and SCM, both open supporters of Viktor Yanukovich, went abroad. From 2005 onwards, Ukrainian OFDI, especially in Cyprus and Russia, started to increase, peaking in 2007 (annex table 4).

The analysis of the regional and sectoral distribution of Ukrainian OFDI is extremely difficult due to the poor statistical data. According to official Ukrainian statistics (annex table 3), Ukrainian companies prefer to invest in the following sectors: real estate (86% of OFDI flows), financial services (2.5%), retail trade and retail services (2%), transport and communications (0.7%), and machine-building (0.3%), while metallurgy accounts for only 0.1% of total OFDI flows. The sectoral breakdown of official Ukrainian FDI statistics does not seem reliable. While

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620 In 2009, Ukraine ranked eighth among 40 world leaders in crude steel production, see The World Steel Association, "The largest steel producing countries," January 22, 2010, available at: http://www.worldsteel.org/pictures/newsfiles/2009%20graphs%20and%20figures.pdf .

621 For more information on domestic restrictions, see Alan H. Price and Scott Nance, *Export Barriers and Global Trade in Raw Materials: The Steel Industry Experience* (Washington, DC: Wiley Rein LLP, 2009).

622 Beata Ślusarczuk, "Investments in iron and steel industry in Poland under globalization conditions", available at: http://www.oeconomica.uab.ro/upload/lucrari/1020081/39.pdf .

623 Konrad Niklewicz, "Donbas domaga się Huty Częstochowa," *Gazeta Wyborcza*, March 2, 2004; Konrad Niklewicz, "Donbas grozi sądem", *Gazeta Wyborcza*, March 16, 2004; "Privatization process of Huta Stali Częstochowa S.A.", available at: http://www.msp.gov.pl/portal/en/16/235/Privatisation_process_of_Huta_Stali_Czestochowa_SA.html.

624 Igor Goshovskiy, "Kreditnaya lovushka dlya ISD," March 25, 2009.

625 "SCM uvelichila dolyu v UF metalloprokatnogo zavoda Ferriera Valsider (Italia) do 70%," *Ukrrudprom*, November 25, 2005, available at: http://www.ukrrudprom.com/news/n1234.html?print; "Ukraine fears the rise of new oligarchs," *BBC News*, June 25, 2005, available at: http://news.bbc.co.uk/2/hi/business/4114342.stm.

626 For more information on legal and policy aspects of Kryvorizhstal's re-privatization, see Leonila Guglya, "Ukrainian privatization: six rounds of the Kryvorizhstal' case, courts and the impact of politics", in Stefan Messmann and Tibor Tajti, eds., *The Case Law of Central and Eastern Europe. Leasing: Piercing the Corporate Veil and the Liability of Managers & Controlling Shareholders, Privatization, Takeovers and the Problems with Collateral Law* (Berlin: European University Press, 2007), pp. 461-499.

in 2008 UNCTAD reported Ukrainian companies' worldwide net purchases worth more than US$ 2 billion[627] and OFDI flows of more than US$ 1 billion (annex table 2), Ukrstat data reported 2008 OFDI flows of only US$ 85 million.[628] Evidently the data did not include the 2008 acquisition of Consolidated Minerals Ltd., the Australian manganese giant, by Palmary Enterprises Ltd (whose registered seat is in Belize) for more than US$ 1 billion.[629] Australia has never been mentioned in Ukrstat data on the regional distribution of OFDI either. It also seems that many cross-border M&As as well as greenfield investments (annex tables 6 and 7) are not recorded or reported by Ukrstat.[630]

According to official Ukrainian data, around 95% of OFDI flows are directed to the European Union (EU), only 3.5 % to CIS countries and 1.5% to other countries (annex table 4). Cyprus is the leading destination for Ukrainian FDI; according to Ukrstat, it accounts for more than US$ 5 billion (92 % of cumulative OFDI). However, based on Eurostat data, in 2008 Ukrainian FDI stock in the EU amounted to US$ 1.1 billion and in Cyprus to only US$ 143 million.[631] In most cases, Ukrainian companies use Cyprus's off-shore opportunities to re-invest money in Ukraine.[632] In other words, if one deducts Cyprus from the calculations, total Ukrainian OFDI stock would be US$ 445 million, split between Russia (37%), Poland (11%), Georgia (7%), Kazakhstan (6%), and other economies. The leadership of Russia and Poland[633] as destinations for Ukrainian FDI might be explained by historical and economic ties as well as neighborhood effects. Besides, Poland's location with its outlet to the Baltic Sea and EU membership is very favorable for Ukrainian steel producers in terms of transportation opportunities both for import and export purposes.

In fact, re-investment in Ukraine via third states like Cyprus is not unique. In 2004, for example, the issue of a 99% Ukrainian equity in a Lithuanian company (an investor under the Lithuania-Ukraine BIT) resulted in a controversial ICSID decision holding that Ukrainian shareholding and Ukrainian majority in the management are irrelevant to contest jurisdiction since the Lithuanian company *"[w]as an entity established in the territory of the Republic of Lithuania in conformity with its laws and regulations*" and "*[i]t is not for tribunals to impose limits on the scope of BITs not found in the text.*"[634]

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[627] UNCTAD, *World Investment Report 2009: Transnational Corporations, Agricultural Production and Development* (New York and Geneva: United Nations, 2009), p. 77.
[628] Ukrstat, *Investitsiyi zovnishnyoekonomichnoyi diyalnosti u 2008 rotsi* (Ukrstat, February 2009), p. 3.
[629] "Palmary announces intention to increase its cash takeover offer for Consolidated Minerals," available at: http://www.rns-pdf.londonstockexchange.com/rns/7475d_1-2007-9-12.pdf; UNCTAD, *2009,* op. cit.; Jason Scott, "Bogolyubov's Consolidated Minerals raising Australian manganese production", *Bloomberg*, July 29, 2010, available at: http://www.bloomberg.com/news/2010-07-28/bogolyubov-s-consolidated-minerals-raising-australian-manganese-production.html; "The world market for manganese: group "Private" closer to the monopoly", *RUSmergers*, January 23, 2009, available at: http://rusmergers.com/en/analitika-ma/2388-mirovoj-rynok-marganca-gruppa-privat-vse-blizhe-k-monopolii.html.
[630] As one can see from annex table 3, the difference between 2008 and 2009 OFDI is roughly US$ 23 million. It is not clear to what extent the 2009 greenfield projects worth several hundreds of millions (see annex table 7) have been implemented and recorded as OFDI in the official statistics, including perhaps because they were not financed by FDI.
[631] Eurostat, "EU direct investment inward stocks by extra EU investing country" [tec00054].
[632] Oleksiy Kononov, "Ukraine's inward FDI and its policy context," *Columbia FDI Profiles*, April 13, 2010, pp. 2 and 9.
[633] In 2008, the Polish ambassador to Ukraine, HE Jacek Kluczkowski, noted that Ukrainian oligarchs invested much more in Poland compared to Poland's investments to Ukraine; see Yuriy Goncharenko, "Posol Polschi Jacek Kluczkowski: ukrainski oligarchy investuvaly za kordonom nabagato bilshe nizh polski pidpryemtsi v Ukraini," *Forpost*, December 2, 2008, available at: http://www.4post.com.ua/world/117582.html.
[634] Tokios Tokeles v. Ukraine, (ICSID Case No. ARB/02/18), Decision on Jurisdiction, paras 36, 52, April 29, 2004, 20 *ICSID Revue - FILJ* 205 (2005). Prosper Weil in his dissenting opinion argued that the ICSID system could not be used for treaty shopping.

The corporate players

Ukrainian OFDI is mainly undertaken by large corporations and industrial groups (annex table 5). MNEs in the steel and ore industries are among the leaders. Metinvest Group (75% of shares controlled by SCM) comprises 21 industrial companies leading in the mining and steel industry of Ukraine and the CIS. In the EU, Metinvest is represented by Ferriera Valsider and Metinvest Trametal (Italian re-rolling companies), British carbon steel plate producer Spartan UK, and Bulgarian long products manufacturer Promet Steel.[635] Another large Ukrainian player, Pryvat Group, controls almost 14% of the world's high-grade manganese production, after a series of successful acquisitions in Australia, Georgia, Ghana, Romania, and the United States.[636]

Ukrainian automotive producers and retailers (AutoKraz, AutoZAZ, UTECH, Ukrauto) invested mainly in obsolete manufacturing facilities in Cuba, Poland and Russia. Rather than modernize domestic plants, these companies strive to find new markets for otherwise uncompetitive Ukrainian cars and trucks. For example, AutoKraz has invested in large greenfield projects in Cuba, a country that still uses an obsolete park of trucks manufactured decades ago in the USSR and in desperate need of modernization.[637]

Effects of the current global crisis

In 2009, Ukrainian officially-recorded OFDI flows declined to US$ 162 million, compared to more than US$ 1 billion in 2008 (annex table 2). Nevertheless, the strong negative impact of the global economic and financial crisis on the Ukrainian economy (IFDI in 2009 was US$ 5.6 billion, down by 49% against 2008)[638] did not prevent Ukrainian companies from making several large investments abroad (annex tables 6 and 7). At the same time, some of the previous foreign acquisitions together with unfavorable steel prices on world markets caused trouble for Ukrainian investors. For example, in 2009 ISD could not cope with the debts of its foreign affiliates;[639] consequently, rather than divert indebted foreign assets, ultimate ISD owners had to sell the controlling stake in ISD itself (50 % + 2 shares) to a Russian investor for about US$ 2 billion.[640] Similarly, Pryvat Group decided to sell the Alapaevsk steel mill in Russia.[641] In late 2009, the global financial crisis forced Soyuz-Viktan to initiate bankruptcy proceedings both in Ukraine and Russia, where the company had two large distilleries.

Judging from the 2009 OFDI greenfield projects and M&As with Ukrainian participation (annex tables 6 and 7), Ukrainian OFDI seems to have recovered in 2010. According to Ukrstat, Ukrainian companies invested abroad almost US$ 630 million in the first six months of 2010, compared to only US$ 26 million in the same period of 2009.[642] Ukrainian companies are

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[635] Information from the company's web site, available at: http://www.metinvestholding.com/en/company/.

[636] "The world market for manganese: group "Private" closer to the monopoly," op. cit.; Vivian Wai-yin Kwok, "Bogolyubov triumphs in Consolidated Minerals takeover," *Forbes,* January 3, 2008, available at: http://www.forbes.com/2008/01/03/bogolyubov-consolidated-minerals-markets-equity-cx_vk_0103markets01.html.

[637] Dariya Ryabkova, "Okno v Latinskuyu Ameriku," *Investgazeta*, No. 99, March 4, 2007; "Ukrainian trucks to be built in Cuba," *The Miami Herald*, December 3, 2008.

[638] Official Ukrstat data, see Kononov, op. cit., pp. 3-4. Recent 2010 UNCTAD data show a lower figure of US$ 4.8 billion; see UNCTAD, *2010,* op. cit., p. 171.

[639] Goshovskiy, op. cit.

[640] "Ukraine's ISD sells 50 percent plus two shares to Russian investors", *SteelOrbis*, January 11, 2010, available at: http://www.steelorbis.com/steel-news/latest-news/ukraines-isd-sells-50-percent-plus-two-shares-to-russian-investors-506928.htm.

[641] "NLMK vyveli na "Privat," *Kommersant (Voronezh),* September 29, 2009.

[642] Ukrstat, *Investitsiyi zovnishnyoekonomichnoyi diyalnosti u I pivricchi 2009 roku* (Ukrstat, August 2009), p. 3; Ukrstat, *Investitsiyi zovnishnyoekonomichnoyi diyalnosti u I pivricchi 2010 roku* (Ukrstat, August 2010), p. 3.

seeking to expand abroad. For example, Ferrexpo group, via its foreign affiliates, plans to bid for the large Bulgarian Kremikovtzi metallurgical plant (the auction is supposed to start at US$ 375 million).[643]

The policy scene

Ukraine is signatory to numerous BITs and other international investment agreements.[644] However, in contrast to IFDI regulations, Ukraine's legal framework for OFDI is rather restrictive. The Government does not support OFDI: there are no investment risks insurance schemes or any public promotion services for Ukrainian companies intending to invest abroad. Pursuant to the Decree on the System of Currency Regulation and Currency Control,[645] all residents' money transfers abroad with the purpose of investment (direct or portfolio) are subject to individual approval by the National Bank of Ukraine (NBU).[646] In other words, the acquisition of a single share in a foreign company requires compliance with a very burdensome and costly process of obtaining an NBU license.[647] Money transfers above a specified minimum are also subject to financial monitoring.[648] On the other hand, as can be seen from the capital outflows from Ukraine, these strict requirements do not stop big corporate players (which in most cases have ties with the government) -- they instead prevent smaller Ukrainian businesses from investing abroad.

Factors stimulating OFDI include the recent change in taxation of Ukrainian holding companies' profits. As of May 19, 2010, dividends received from foreign affiliates are no longer subject to the Ukrainian corporate profits tax.[649] This change applies, however, only to dividend recipients holding at least 20% of the shares of a foreign affiliate, having the largest share therein, or having the largest number of votes therein. The tax exemption does not apply to foreign affiliates located in jurisdictions blacklisted for tax purposes.[650] On the other hand, smaller Ukrainian OFDI players might be adversely affected if the Tax Code supported by the new Prime Minister, Mykola Azarov,[651] is adopted. The draft Tax Code broadens the competencies of the tax authorities and increases the tax burden on SMEs, while granting tax holidays and other tax privileges to large companies (which are controlled by Ukrainian oligarchs).[652]

Conclusions and Outlook

Despite rather modest OFDI, Ukrainian investments are scattered all over the world, often driven by the unfavorable domestic business climate or political threats. The new Ukrainian

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[643] "Vorskla Steel expresses interests in acquiring Kremikovtzi," *SteelOrbis*, July 30, 2010, available at: http://www.steelorbis.com/steel-news/latest-news/vorskla-steel-expresses-interest-in-acquiring-kremikovtzi-546923.htm.

[644] For more details on Ukraine's BITs and other IIAs see Kononov, op. cit., p. 5.

[645] *Decree of the Cabinet of Ministers of Ukraine on the System of Currency Regulation and Currency Control*, February 19, 1993.

[646] Art. 5 of the *Currency Decree.*

[647] Detailed procedures for getting a license can be found in *the Instruction on Procedures of Issuing Individual Licenses for Investments Abroad* approved by the NBU Regulation No. 122 of March 16, 1999.

[648] Pursuant to art. 15(1) of the *Law on Prevention of Money Laundering* of May 18, 2010, this applies to operations exceeding the equivalent of UAH 150,000 (US$ 19,000).

[649] *Law of Ukraine on Amending Corporate Profits Tax Regarding Taxation of Dividends* of April 27, 2010.

[650] Cyprus and the British Virgin Islands are not blacklisted.

[651] In 1996-2002, Mykola Azarov was the Head of the State Tax Administration of Ukraine. The main tax collector of the country became known for extreme fiscal pressure and constant attacks on Ukrainian private businesses.

[652] The World Bank Group's *Doing Business Project 2010* rates Ukraine 181 among 183 countries of the world in terms of procedures for paying taxes, it is worse only in Venezuela and Belarus. See IBRD/World Bank: *Doing Business 2010: Ukraine* (Washington, DC: The World Bank, 2009), p. 34; *Doing Business Project: Paying Taxes 2010 – The Global Picture,* available at: http://www.doingbusiness.org/features/taxes2010.aspx.

President and his Cabinet have brought some political stability.[653] However, in the short run it is unlikely that Ukraine's OFDI trends will change much. The lack of reforms, together with continuing trade restrictions for Ukrainian steel and other products, will continue to force Ukrainian companies to seek investment opportunities abroad. Stabilization of the world steel market and new gas arrangements with Russia that provide cheap gas for industrial needs will discourage domestic companies from modernizing local manufacturing facilities. Therefore capital will probably be invested abroad, especially in Russia, in view of the growing political and economic co-operation between the two countries and the pro-Russian stance of President Yanukovich. By the same token, growing hostilities between the new government and the opposition parties might lead to attacks on companies associated with the latter. Consequently, it is unlikely that capital flight to Cyprus, the British Virgin Islands and other offshore jurisdictions will decline.

Additional readings

Åslund, Anders, *How Ukraine Became a Market Economy and Democracy* (Washington, DC: Peter G. Peterson Institute for International Economics, 2009).

Sarna, Arkadiusz J., "Ukrainian metallurgy: the economic link in the oligarchic power system," *CES studies*, March 2002, available at: http://pdc.ceu.hu/archive/00001679/01/ukr_metal.pdf.

The World Bank: *Ukraine's Trade Policy: A Strategy for Integration into Global Trade* (Washington, DC: The World Bank, 2005).

Useful websites

Metal-Forum of Ukraine, available at: **http://www.metal-forum.org/MFU_News_market.htm**.

Ukrainian Ferro-Alloy **Producers** Association, available at: **http://www.ukrfa.org.ua/**.

Ukrainian State Statistics Committee (Ukrstat), available at: **http://www.ukrstat.gov.ua/.**

653 Roman Olearchyk, "Progress depends on a successful reform effort," *Financial Times*, June 1, 2010.

Statistical annex

Annex table 1. Ukraine: outward FDI stock, 2000-2009 (US$ million)

Economy	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
Ukraine	170	156	144	166	198	468	344	6,077	7,005	7,259
Memorandum: comparator economies										
Bulgaria	67	34	40	52	n.a.	123	285	582	1,248	1,309
Hungary	1,280	1,556	2,166	3,509	6,018	7,810	57,114	133,141	184,745	174,941
Kazakhstan	16	n.a.	420	300	n.a.	n.a.	n.a.	2,166	3,045	6,786
Poland	1,018	1,156	1,457	2,147	3,356	6,279	14,319	19,369	21,814	26,211
Romania	136	116	145	208	272	213	879	1,240	1,466	1,731
Russia	20,141	44,219	62,350	90,873	107,291	146,679	216,488	370,161	202,837	248,894
Slovakia	373	448	486	823	835	597	1,325	1,509	1,901	2,744

Source: UNCTAD's, FDI/TNC database, available at: http://stats.unctad.org/fdi

Annex table 2. Ukraine: outward FDI flows, 2000-2009 (US$ million)

Economy	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
Ukraine	1	23	-5	13	4	275	-133	673	1,010	162
Memorandum: comparator economies										
Bulgaria	3	10	28	27	-217	308	175	270	707	-136
Hungary	2,764	3,936	2,994	2,137	4,506	7,709	19,802	71,485	61,993	-6,886
Kazakhstan	4	-25	422	-122	-1,235	-151	-329	3,142	1,001	3,119
Poland	16	-90	230	300	915	3,399	8,875	4,748	3,582	2,852
Russia	3,177	2,533	3,533	9,727	13,782	12,767	23,151	45,916	56,091	46,057
Romania	-13	-16	17	41	70	-31	423	279	274	218
Slovakia	29	65	11	247	-21	150	511	384	258	432

Source: UNCTAD's, FDI/TNC database, available at: http://stats.unctad.org/fdi

Annex table 3. Ukraine: distribution of cumulated outward FDI flows, by economic sector and industry, 2001, 2004, 2008, 2009[a] (US$ million)

Sector/industry	2001	2004	2008	2009
All sectors/industries	**170.3**	**163.5**	**6203.1**	**6226.0**
Primary	**0**	**0.1**	**0.5**	**0.6**
Agriculture, forestry and fishing	0	n.a.	0.3	0.3
Mining and quarrying	0	0.1	0.2	0.3
Secondary	**n.a.**	**n.a.**	**n.a.**	**n.a.**
Food, beverages, and tobacco	n.a.	n.a.	13.8	58.7
Light industry	0.3	0	0.3	0.3
Cellulose, paper, and publishing	n.a.	0.4	n.a.	Confidential [b]
Timber	3.7	n.a.	n.a.	n.a.
Coke, petroleum and chemical	6.4	4.3	Confidential [b] (US$ 4.7 million for chemical industry)	4.8
Other mineral manufacture (excluding metal)	n.a.	n.a.	Confidential [b]	Confidential [b]
Metallurgy	2.6	2.5	9.1	8.9
Machine-building	6.5	6.3	14.9	19.8
Other industries	0.1	0.3	2.9	2.6
Construction	3.5	3.4	2	1.9
Services	**147.3**	**146.2**	**n.a.**	**n.a.**
Retail trade and retail services	0.6	1	142.5	124.9
Hotels and restaurants	0	0.6	Confidential [b]	Confidential [b]
Transport and communications	84.8	55.1	44.8	44.8
Financial services	2.1	8.3	175.9	596.1
Real estate	51.9	66.4	5333.1	5347
Other services	7.8	14.8	Confidential [b]	Confidential [b]
Other unspecified sectors	**n.a.**	**n.a.**	**442.4**	**n.a.**

Sources: Ukrstat database, available at: http://ukrstat.gov.ua; Ukrstat, *Investitsiyi zovnishnyoekonomichnoyi diyalnosti u I kvartali 2010 roku* (Ukrstat, May 2010), p. 15; Ukrstat, *Investitsiyi zovnishnyoekonomichnoyi diyalnosti u 2009 rotsi* (Ukrstat, February 2010), p. 15, available at: http://www.ukrstat.gov.ua; Ukrstat, *Investitsiyi zovnishnyoekonomichnoyi diyalnosti u 2001 rotsi: Statystuchny buleten Derzhkomstatu Ukrainy* (Kyiv: Ukrstat, 2002); Ukrstat, *Investitsiyi zovnishnyoekonomichnoyi diyalnosti u 2004 rotsi: Statystuchny buleten Derzhkomstatu Ukrainy* (Kyiv: 2005).

[a] Cumulative figures as of beginning of investment (early 1990s). Stock data are not available. Despite being official OFDI data published by Ukrstat, the figures do not reflect substantive OFDI in a number of sectors, especially metallurgy, mining and quarrying (compare with Reuters and Financial Times data in annex tables 6 and 7).
[b] Information classified according to art. 21 of the Law of Ukraine *on State Statistics.*

Annex table 4. Ukraine: geographical distribution of cumulated OFDI flows, selected years [a] (US$ million)

Region/economy	2004	2005	2007	2009
World	**175.9**	**218.2**	**6,196.0**	**6,223.3** [b]
Developed economies				
Europe				
European Union (EU)				
Austria	3	4.6	n.a.	n.a.
Cyprus	2	2.1	5,825.0	5,778.5
Estonia	1.1	n.a.	n.a.	n.a.
Greece	1.6	n.a.	n.a.	n.a.
Latvia	n.a.	n.a.	30.7	31.9
Lithuania	n.a.	n.a.	4.0	n.a.
Poland	n.a.	20.3 [c]	30.1	49.4 [c]
Spain	13.8	13.8	13.8	n.a.
UK	n.a.	13.9	13.8	n.a.
Non-EU				
Armenia	n.a.	n.a.	12.8	n.a.
Georgia	2.3	2.2	28	32.6
Switzerland	4.7	4	4.6	n.a.
North America				
United States	n.a.	5.6	5.9	n.a.
Central America				
Panama	18.9	18.9	18.9	n.a.
Caribbean				
British Virgin Islands	n.a.	n.a.	10.9	20.8
Asia				
Hong Kong (China)	5.4	5.4	n.a.	n.a.
Vietnam	15.9	15.9	3.9	n.a.
Commonwealth of Independent States				
Kazakhstan	n.a.	n.a.	n.a.	27.1
Moldova	n.a.	n.a.	26.7	n.a.
Russia	94.6	102.5	148.6	165.5
Uzbekistan	1.9	n.a.	n.a.	n.a.
Other economies [d]	5	9	17.9	117.5

Source: Ukrstat database, available at: http://ukrstat.gov.ua.
[a] Cumulative figures since the beginning of foreign investment (as of January 1, 2010). Stock data are not available.
[b] Ukrstat data reflect figures of countries to which the highest amounts of Ukrainian FDI were directed.
[c] For some reason, official Ukrstat statistics do not reflect extensive Ukrainian investments in Poland's metallurgical sector.
[d] Data on particular countries are not available. Ukrstat reports outward investments to 51 countries of the world (as of January 1, 2010).

Annex table 5. Ukraine: principal MNEs, 2004 - 2009

Name	Industry	Available indicators
System Capital Management (SCM)	Metallurgy, banking, chemical industry	8,151[a]
Interpipe Group	Metallurgy, machine-building, banking, mass-media, retail trade	3,000[b]
Ukrauto	Automotive	2,100[c]
Palmary Enterprises Ltd	Metallurgy	1,008
Roshen	Food	850[d]
Ukrprominvest Group	Automotive	700[e]
Industrialny Soyuz Donbassa (ISD)	Metallurgy	849[f]
Soyuz-Viktan	Alcoholic beverages	420[g]
Pryvat Group	Banking, metallurgy, manganese, chemical industry	n.a.[h]
Ferrexpo	Metallurgy, manganese	n.a.[i]
DF Group (The Firtash Group of Companies)	Energy, metallurgy, chemical industry, real estate	n.a.[j]

Sources: Companies' websites; *Financial Times* – fDi Markets | Global Investments; "Ukrainian industrial groups continue advance into Europe," *Kyiv Post*, January 25, 2007; "Mapa investytsiy," *Ukrainsky Tyzhden*, No. 17 (26), 25 kvitnya – 1 travnya 2008 roku.

[a] 2009 consolidated revenue data. Available statistical data and media list Metinvest Group often separately. In fact, it is controlled by SCM. Amount of company's OFDI unknown.
[b] Turnover by the end of 2005.
[c] Total assets (Ukrainian and foreign).
[d] Turnover by the end of 2008.
[e] Greenfield projects in 2007.
[f] Investments in Huta Stali Czestochowa (Poland) and Dunaferr (Hungary).
[g] Turnover for alcoholic beverages produced in 2005.
[h] Financial data are not available; however, Pryvat Group has a stake in Highlanders Alloys (US), Feral CA (Romania) and Ghana Manganese (Ghana). The company also controls Palmary Enterprises Ltd.
[i] Financial data are not available; the company has a stake in Skopski Legury (FYROM), Vorskla Steel Denmark (Denmark) and plans to bid for a stake in Kremikovtzi plant (Bulgaria).
[j] DF Group owns foreign affiliates in Austria, Estonia, Germany, Hungary, Italy, Russia, Switzerland, and Tajikistan. Financial data are not available.

Annex table 6. Ukraine: main M&A deals, by outward investing firm, 2007–2009

Year	Acquiring company	Target company	Target industry	Target economy	Shares acquired (%)	Transaction value (US$ million)
2009	Ciklum	Mondo A/S-Activities	Information retrieval services	Denmark	100	n.a.
2009	Gruppa EastOne	Rossiya	Life insurance	Russia	100	n.a.
2009	Metinvest Holding (affiliated with SCM)	United Coal Co	Bituminous coal and lignite surface mining	United States	100	n.a.
2009	Industrialni Dystrybutsiyni Systemy (IDS)	Akva Star LLC	Beverages	Russia	100	n.a.
2008	Palmary Enterprises Ltd	Consolidated Minerals Ltd	Ferroalloy ores	Australia	88	1,008
2008	Maximum Exploration Corp	Extraordinary Vacation USA Inc	Advertizing	United States	100	13.3
2008	ZAT RUR Group SA	ZAO Intekom	Crude petroleum and natural gas	Russia	100	n.a.
2008	Volya Cable	Oisiw Ltd	Investment	Cyprus	100	n.a.
2008	Metinvest Holding (affiliated with SCM)	Trametal SpA	Metallurgy	Italy	100	n.a.
2008	Milkiland BV	Ostankino Dairy	Dairy products	Russia	75	n.a.
2007	Nemiroff	Legro Sp z.o.	Beverages	Poland	100	n.a.
2007	Sevastopolenergo	Neva Metal Trans	Transportation	Russia	100	n.a.
2007	Motordetal-Konotop	Fumel Technologies SAS	Gray and ductile iron foundries	France	100	n.a.
2007	Bank Delta	Atom Bank	Banking	Belarus	100	n.a.
2007	Pryvat Group	JKX Oil & Gas PLC	Crude petroleum and natural gas	UK	13	80
2007	Pryvat Group	TaoBank	Banking	Georgia	75	25

Source: Thomson ONE Banker, Thompson Reuters.

Annex table 7. Ukraine: main greenfield projects, by outward investing firm,[a] 2007-2009

Year	Investing company	Target industry	Target economy	Estimated/ announced transaction value (US$ million)
2009	Vorskla Steel	Metallurgy	Hungary	926.6
2009	Roshen	Food	Russia	235
2009	Motor Sich	Manufacturing	Russia	144.5
2009	Gerc Investment & Construction	Real estate	Iraq	40.7
2009	UPEC	Metallurgy	Russia	40.0
2009	Pivdennyi Bank	Financial services	Bulgaria	35.9
2009	Credit Rating Agency	Financial services	Russia	35.9
2009	Credit Rating Agency	Financial services	Belarus	35.9
2009	PryvatBank	Financial services	Italy	32.4
2009	PryvatBank	Financial services	Germany	32.4
2009	Kviza Trade	Retail trade	Moldova	27.3
2009	AvtoKraZ	Automotive	Azerbaijan	24.4
2009	Antonov ASTC	Aerospace	Russia	15.2
2008	UTTECH	Automotive	Russia	600.0
2008	Yoakside Trading	Real estate	Vietnam	400.0
2008	Erlan	Beverages	Russia	318.0
2008	Konti	Food	Russia	252.3
2008	AutoKraZ	Automotive	Cuba	232.0
2008	AutoKraZ	Automotive	Russia	204.4
2008	Metinvest (SCM)	Metallurgy	Italy	169.9
2008	Metinvest (SCM)	Metallurgy	Russia	40.5
2008	Image Holding	Food	Russia	39.3
2008	Metinvest (SCM)	Metallurgy	UK	36.4
2008	Concorde Capital	Financial services	Russia	35.8
2008	Pivdennyi Bank	Financial services	Bulgaria	35.8
2008	Sokrat	Financial services	Uzbekistan	32.6
2007	Ukrprominvest	Automotive	Russia	700.0
2007	Naftogaz	Oil and natural gas	Egypt	281.3
2007	Pryvat Group	Financial services	China	58.4
2007	Naftogaz	Oil and natural gas	Libya	57.5
2007	Avec & Co	Real estate	UK	40.7

Source: fDi Intelligence. Financial Times.

[a] Data on shares acquired and joint venture partners (if any) are not available.

ANNEX

TEMPLATE

Template

Columbia FDI Profiles
Country profiles of inward and outward foreign direct investment
issued by the Vale Columbia Center on Sustainable International Investment

Outward FDI from [name of country] and its policy context, 2011

Or

Inward FDI in [name of country] and its policy context, 2011

Guidelines for Authors

The purpose of the *Columbia FDI Profiles* is to provide, in a concise format, the salient features of the outward or inward FDI of a country, with special attention to policy and regulatory issues.

There will be separate *Profiles* for inward FDI (IFDI) and outward FDI (OFDI).

As *Profiles* will be assembled in an e-book at the end of the calendar year; therefore, it is essential that they all follow a fully consistent style.

The information in the *Profiles* will be sent to FDI experts, policy makers (including from investment promotion agencies), corporate executives, journalists, and students interested in current developments in FDI inflows and outflows at the country level and in policies that impact these flows, along with interesting developments of a specific sort that the authors wish to address.

The *Profiles*, written by country experts, should be no more than 1,200 words in length. The first Profile for a country could have around 1,800 words (5-6 pages of text plus "additional readings" and the annex tables). Authors (and, as the case may be, co-authors) will thus need to be selective as to the extent to which they address in detail points raised in the guidelines below. We realize that the template is rather ambitious and reflects an ideal data situation and that, for many countries, much of the information may not yet be available. Moreover, the data quality is likely to vary and hence may require the assessment of the authors as to its reliability or usability. Where a problem is encountered in preparing a table as a result of a genuine data problem, this should be explained in a footnote immediately after the table concerned.

The text is to be followed, as a rule, by seven standardized tables as laid out in the generic tables and in the sequence laid out below. (Authors may choose to add additional tables, but no graphs please). It would be very useful to have a general introductory note to describe the data situation and any issues related to it. The standardized tables should show US-Dollar figures for consistency reasons as it is planned to publish the Profiles at the end of the year in a volume (see the explanations with regard to the conversion of national currencies into US-Dollar below). In the text, authors should use US-Dollar values, again for consistency reasons and to allow comparison with other countries. Having the tables also implies that there is no need for their verbalization in the text. (In the text, the tables should be referred to in the standard sequence; for example, table 6 should not be referred to before tables 1-5 have been referred to.) Ideally, the text should contain a consistent and well-founded "story" of recent trends and their drivers as well as their policy framework, and it should not only present data. A short list of references and data sources through which readers may obtain additional information should also be appended; this list of references should not contain references to literature already mentioned in the text.

Beginning with the second Profile, the sector on "Interesting developments" will become more important; it could draw, for example, on recent research undertaken (including by the author of a Profile) on an FDI-related issue.

The peer-reviewed *Profiles* will be published on the web site of the Vale Columbia Center on Sustainable International Investment (VCC) and distributed through various channels to the international FDI community; they will also be consolidated in the e-book mentioned earlier.. Views expressed in the *Profiles* will be those of the authors and not necessarily those of the Vale Columbia Center.

To ensure comparability, the *Profiles* should all have the same structure and cover the same basic variables, as outlined below.

Introductory paragraph

The first paragraph of the *Profile* should present the essential findings of the paper in a manner that entices the reader to read on. It should strive to be no longer than 100 words and will appear as the abstract of the *Profile* when it is listed on the VCC web site. This paragraph will also be used in the email through which the *Profiles* are being sent to the international FDI community and the media.

Trends and developments[654]

Please use the latest available "hard" (actual published) data (for authors preparing updates of reports already published, it would be desirable to issue the update as soon as possible after the release of new annual data). Concerning the quality of data

[654] The subtitles refer to inward or outward FDI, as the case may be**.** Please note that each *Profile* deals only with **either** inward or outward FDI.

the authors are encouraged to use the OECD/IMF Benchmark for FDI Statistics or if they are not able to do so explain the reasons. When hard data are not available, please indicate to us what you judge the quality of the estimates to be and how they were derived. Similarly, please indicate when "hard" data are of limited reliability, coverage, etc. To repeat, it is understood that not all the data mentioned below may be available for your country. In most cases, authors should use US dollar values instead of national currencies. National data should be converted in US-Dollar using the average dollar exchange rate published by the IMF against the national currency of the respective period. Dollar figures in the text should be written as follows: e.g. US$ 8 billion. Figures should be rounded and should not have more than one decimal.

In all cases, please indicate your data sources and give full reference to academic literature, press articles and reports in your analysis and tables in the text part. Full references have to be made in footnotes. (Full references are also needed as the list of additional readings at the end is not a list of references contained in the text and the annex tables. The recommended additional readings at the end of the article should be limited to a maximum of 5 – 7 readings, and they should not contain readings already mentioned in the text. With regard to the style of the references, please see the examples below.) The list of data sources can, however, repeat sources already used in the text. When the text mentions data that are contained in annex tables, you should cite the table as the source (which in turn reports your actual source; in the annex tables, full reference to the sources are necessary). The *Profile* itself should not contain any tables or charts; tables should be appended as annexes (unfortunately, we cannot publish graphs). To the extent possible, the text should be specific; for example, a sentence like "nearly 60% of FDI went into services, with insurance and construction accounting for half of it" is preferable to a sentence like "FDI went mainly into services".

Country-level developments

1. FDI stock (annex table 1) and flows (annex table 2), preferably covering the ten most recent years of hard data, including recent changes, especially noting when there seems to be a break in trend. Comparison with some (three to five) comparable countries. Flows by component (equity, reinvestment, other). Repatriated earnings.

2. Estimated FDI flows in the current year and short-term outlook; in other words, please characterize prospective developments.

3. Sectoral distribution of FDI stock (or, if not available, flows), discussing notable changes over the past five years in sectors and industries, or a striking contrast to earlier years if relevant (annex table 3).

4. Geographical distribution of FDI stock (or, if not available, flows), and notable changes over the past five years, if any, or a striking contrast to earlier years if relevant (annex table 4).

5. Operational data of foreign affiliates (e.g., employment, sales of foreign affiliates, value-added, exports/imports, profitability, etc.). (We realize that, in many cases, not all of this information will be available.)

6. Distinctive or surprising quantitative or qualitative features of FDI, if any.

7. Drivers of OFDI/IFDI.

The corporate players

1. Names of large foreign affiliates in the country (or, in the case of OFDI, parent companies). ("Foreign affiliates" refers to any company in which the parent firm has at least 10% equity; "Subsidiary" refers to a company in which the parent firm has 51% or more of the equity.)

2. Company-level data: principal foreign affiliates in the country (for IFDI) or MNEs headquartered in the country (for OFDI) and available central characteristics (annex table 5 – see the materials issued in the Emerging Markets Global Players project, available at www.vcc.columbia.edu for variables that could be covered in text or table); note if SOEs are active in FDI. *Total* number in the country of foreign affiliates (for inward FDI) or multinationals headquartered (for outward FDI)). Degree of concentration of IFDI/OFDI.

3. Describe any pattern in the ten biggest cross-border M&As (annex table 6) and greenfield deals (annex table 7) within the past three years, or longer if current developments are more noteworthy seen against previous years' data. In the definition of M&As and greenfield investment we follow the methodology of UNCTAD's World Investment Reports. Therefore, we define expansion projects as greenfield investments.

Effects of the global economic and financial crisis in 2008/09

1. For reports on 2009-10, please consider the effects of the global economic crisis on FDI, e.g., effect of the credit crunch and recession on FDI, deteriorating prices of assets facilitating M&A, any major divestments of affiliates, postponement of projects, and decline in reinvested earnings that are outcomes of the crisis.
2. Most recent developments in 2010. Possible end of or recovery from the sharp downturn of FDI during 2010 in your country? (depending on availability of data for 2010) or continuing decline in FDI flows and reasons for this.

The policy scene

Significant policy and other developments (in-country or internationally) that affect the FDI picture:

1. The first Profiles for every country should start with a snapshot of the policy situation to establish a baseline. Subsequent Profiles can then update. (E.g. the overall policy stance of the respective country with respect to outward and inward FDI could be outlined in short). Special attention should be given to policies relating to sustainable FDI (i.e., FDI that makes a clear contribution to economic, social and environmental development and takes place in the context of governance mechanisms that allow for a fair sharing of benefits associated with a given investment).
2. Information and analysis of policies to ensure the sustainability of investment, including environment, social and economic development and governance.

3. Major FDI policy developments (any new protectionism or liberalization of investment policies/measures and how these are implemented; sources of political pressure for/against them).

4. For both inward and outward investment: new BITs or FTAs with investment chapters (or their regional equivalents), as well as double taxation agreements, signed or under negotiation.

5. If possible, the broad policy environment that is the backdrop to the new developments just noted (open or controlled access/or outflow policy; which sectors if any are restricted and why (national security concerns, competition, infant industry, other); capital account opened or closed.

6. Significant new international investment arbitration cases, if any, involving foreign direct investors.

7. FDI laws and policies.

8. Applicable tax laws and their implications.

9. Main legal developments relevant to the investment environment.

10. Special promotional activities (and overall evaluation).

11. For OFDI: reinvestment insurance scheme, existence of development finance corporations taking equity participation in developing countries.

12. Contact points for the interested reader: national and sub-national investment agencies, dedicated governmental services/divisions (addresses etc. for more information).

Interesting developments (an optional section)

Anything interesting that you may want to flag that does not belong to any of the earlier categories, e.g., special developments in a sector, interesting industry-level consequences of inward or outward FDI, if any, including changes in these (more competition or less, impact on organized labor in the sector, environmental impact, linkages to other producing sectors, etc), a special case.

Conclusions and outlook

A very short summary and an outlook (economic outlook and possible change in the policy context) should round out the Profile. Please do not repeat the introductory paragraph.

Additional readings

Not more than 5-7 key writings on the subject, not referred to in the text itself. Below are examples of how different readings should be listed (style):

Almunia, Joaquin, "Statement by the European Commissioner on the Santiago Principles," *IWG Press Release* No. 08/08, October 11, 2008, available at: www.iwg-swf.org.

Benito, Gabriel G., "Divestment of foreign production operations," *Applied Economics*, vol. 29 (1997), pp. 1365-1377.

Federal Reserve Bank of San Francisco, "Recent Japanese and Chinese investments in U.S. and European financial institutions," *Asia Focus*, vol. 10 (2009), pp. 1-32.

UNCTAD, *World Investment Report 2008: Transnational Corporations and the Infrastructure Challenge* (New York and Geneva: United Nations, 2008).

Dunning, John H. and Sarianna M. Lundan, *Multinational Enterprises and the Global Economy* (Cheltenham: Edward Elgar, 2008).

Useful websites

For FDI policy and regulation: Government of India, Ministry of Commerce and Industry, available at: www.dipp.nic.in.

For FDI statistics: Secretariat of Industrial Approvals, Ministry of Commerce and Industry, available at: www.dipp.nic.in/fdi_statistics/india_fdi_index.htm.

Statistical annex

- The statistical annex should begin with a short discussion of the data situation in relation to the country, to alert readers to any problems.
- Ideally, all Profiles should contain the 7 annex tables listed below, and in this order, as it is planned to publish the Profiles in a volume in January 2011, to be updated thereafter. Therefore, the Profile format should be as consistent as possible. In addition, authors can provide additional tables to annex tables 1 to 7 that are numbered 1a, 2a, etc. All figures in the annex tables 1 to 7 (but not necessary in all of the additional material) should be converted into US-Dollar using IMF exchange rate data (e.g. IMF's "International Financial Statistics"). Authors who do not have access to IFS-statistics could be provided with annual average Dollar exchange rates (for FDI flows) and end of year exchange rates (usually for FDI stocks) by the Columbia team. If the official statistical institutions or central banks publish the official FDI data for the respective country in US-Dollar, in addition to the figures in national currencies, the authors could use these Dollar figures instead of calculating the US-Dollar figures with IMF exchange rates. Unfortunately, we cannot publish graphs in the Profiles as it is very difficult to get a standardized format from the different authors.
- Concerning methodological issues relating to the quality of data, authors are encouraged to use the OECD/IMF Benchmark for FDI Statistics or if they are not able to do so explain the reasons.
- Please add an explanation of the method of statistical recording of the data use for each annex table in the form of a note immediately below the table (see examples of possible explanations below).

Annex table 1. [Name of country]: outward/inward FDI stock, 2000-2010 (US$ billion)
[For mostly large figures please give only US$ billion without the decimal]

Economy	**2000**	**2010[a]**
[Your country]		
Memorandum: comparator economies (e.g. 5 economies, listed by size of the economies in descending order)		

Source: [full reference]
[a] First nine months only.
[b] …

Note: Authors should explain the main characteristics of the FDI stock statistics of their country, including:

- Degree of compatibility with the OECD Benchmark Definition of FDI
- Method of collecting the stock data (compulsory surveys of firms, simple addition of FDI flows, etc.
- Institution which is responsible for the stock data (national central bank, statistical offices or national authorities, …)
- FDI stock based on book value or historic cost?
- Reliability of the data, limitations of the data
- Please indicate the currency conversion rate/date where possible.

Annex table 2. [Name of country]: outward/inward FDI flows, 2000-2010

(US$ billion)

Economy	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
[Your country]										
Memorandum: comparator economies (listed by size of the economies in descending order)										

Source:
[a] …
[b] …
Note: Explanation of the main characteristics of the FDI flows statistics (institution which collects the data; for some economies different institutions supply FDI flow data: in this case a judgement of the reliability of the different data should be given; quality of the FDI flow data, etc.)

Annex table 3. [Name of country]: sectoral distribution of outward/inward FDI stock, 2000, 2010

(US$ billion or US$ million depending on the size of the figure)

Sector / industry	2000	2009
All sectors / industries		
Primary		
Agriculture, forestry, and fishing		
Mining, quarrying and petroleum		
Mining and quarrying		
Petroleum		
Secondary		
[Relevant detail]		
Services		
[Relevant detail]		
Unspecified other sectors/industries		

Source:
[a]
[b]

This table will be very much driven by the data available in terms of coverage of investments, industry detail and years of data available on a comparable basis. In many cases, stock data will not be available and flow data may have to suffice, averaging flows over selected three-year periods, especially when data of individual years are "lumpy". In some cases, data may only be available for M&A activity, which may be used with the caveat that such investments cover only a part of total investment. Table could cover only two years, unless authors want to draw distinction with previous decade.
Note: Pls explain in a note the data problems and the quality of the data (if there are any problems like those mentioned above).

Annex table 4. [Name of country]: geographical distribution of outward/inward of FDI stock, 2000-2010 (US$ million)

Region / economy	**2000**	**2010**
World		
Developed economies		
Europe		
European Union		
[Relevant country detail listed alphabetically]		
North America		
Canada		
United States		
Other developed countries		
Australia		
Japan		
Developing economies		
Africa		
[Relevant country detail listed alphabetically]		
Asia and Oceania		
[Relevant country detail listed alphabetically]		
Latin America and Caribbean		
[Relevant country detail listed alphabetically]		
Transition economies		
[Relevant country detail listed alphabetically]		
Unspecified destination		

Source:
a
b

The same comment applies to table 4 as to table 3. Again, additional years could be covered if pertinent to a point in the text. For a classification of the countries, please see the classification in UNCTAD's *World Investment Report*.

***Note*: see comments to annex table 3**

Annex table 5. [Name of country]: principal foreign affiliates/MNEs headquartered in country, ranked by [criterion], [year]

Rank	Name	Industry	Foreign assets (US$ billion or US$ million depending on the size of the figures)
1	XYZ Corp.	Oil and gas operations	5,222
2	ABC Inc.	Conglomerate	4,560
3	Etc.	Etc.	Etc.
4			
5			
6			
Etc.			

Source: [Full source]

[a]

[b]

In cases in which countries have been participants in the Emerging Market Global Players (EMGP) project, rankings and data reporting in that exercise are the preferred source of data for table 5. In general, the preferred indicator of size for the ranking is foreign assets in US dollars. If not available, sales or turnover may be used. List of top 10-20 firms if possible. Please indicate data limitations in the table footnote(s). Ranking covers firms that responded to a [specified] survey or for which reliable public information could be found, and thus the data may be incomplete. Each firm has management control over at least one foreign affiliate.

Note: Please explain in a short note the characteristics of the data source(s) and its/their quality.

Annex table 6. [Name of country]: main M&A deals, by outward/inward investing firm, 2008-2010 [latest three years]

Year	Acquiring company	Home economy	Target company	Target industry	Target economy (OFDI) or source economy (IFDI)	Shares acquired (%)	Estimated/ announced transaction value (US million)
2009							
2009							
2008							
2008							

Source: Thomson ONE Banker, Thomson Reuters.
a
b

[Data from Thomson Reuters will be supplied to the authors by VCC]

Annex table 7. [Name of economy]: main greenfield projects, by outward/inward investing firm, 2008-2010 [latest three years]

Year	Investing company	Home economy	Joint venture partner (if any)	Industry	Host economy (OFDI) or source economy (IFDI)	Shares owned (%)	Estimated/ announced investment value (US$ million)
2009							
2009							
2008							
2008							

Source: fDi Intelligence, a service from the Financial Times Ltd.
a
b

Data from the Financial Times will be supplied to the author by VCC

For annex tables 6 and 7 pls take the main M&A deals and Greenfield projects and limit the tables to a maximum of one page each.

If you are using the data provided by us, please note proper citations below.

For M&A data:
Source: Thomson ONE Banker. Thomson Reuters.

For greenfield data:
Source: fDi Intelligence, a service from the Financial Times Ltd.

For further information, please visit our website:

http://www.vcc.columbia.edu