Recent Trends in Foreign Direct Investment*

I. Introduction

Foreign direct investment (FDI) inflows and outflows to and from OECD countries showed continuing rapid growth last year. Inward investment into OECD countries grew by 35% and reached US dollars (USD) 684 billion, while outflows showed an increase of 22% and amounted to USD 768 billion (Table 1). Some OECD countries experienced an unprecedented level of inflows (*e.g.* Japan, Sweden and Germany) and others recorded historically high outflows (*e.g.* Denmark, France and Ireland).

The increase in greenfield investment was significant in 1999, but it was by far exceeded by the growth in mergers and acquisitions (M&A). As in previous years, M&A was the primary vehicle behind the increase in FDI.

Last year, Western Europe was the world's leading region for cross-border M&A. As for individual countries, the United Kingdom overtook the United States as the most active source of M&A investment. In terms of inflows, the United States has remained the most attractive location. The telecom industry is still the most important sector for M&A closely followed by the chemicals sector.

The 1990s brought considerable improvements in the investment climate, influenced in part by the recognition of the benefits of FDI. The change in attitudes, in turn, led to a removal of direct obstacles to FDI and to an increase in the use of FDI incentives. Continued removal of domestic impediments through deregulation and privatisation was also widespread. Deregulation and enhanced competition policy made M&A more viable in the telecommunications, electricity, other public utilities and financial services sectors, while privatisation pro-

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Table 1. **Direct investment flows, OECD countries, 1996-1999**
Million US dollars

	Inflows				Outflows			
	1996	1997	1998	1999p	1996	1997	1998	1999p
Australia	5 171	7 510	6 502	4 441	5 927	6 262	2 466	–3 192
Austria	4 429	2 656	4 902	2 952	1 935	1 948	2 948	2 703
Belgium-Luxembourg	14 061	12 093	22 724	15 868	8 065	7 273	28 453	24 937
Canada	94 07	11 470	16 499	24 268	12 879	22 054	26 575	17 362
Czech Republic	1 428	1 300	2 540	4 877	153	25	175	197
Denmark	7 76	2 801	6 722	7 450	2 518	4 210	3 962	8 207
Finland	1 109	2 116	12 141	3 024	3 596	5 292	18 643	4 194
France	21 942	23 174	28 955	37 416	30 395	35 586	41 913	88 324
Germany	6 577	11 092	21 271	52 403	50 841	40 716	91 183	98 853
Greece[1]	5 888	3 586	3 709	539	..	..	..	573
Hungary	2 275	2 173	2 036	1 944	–3	431	481	249
Iceland	82	149	112	90	62	51	99	70
Ireland[2]	1 888	1 676	3 904	5 422	..	..	8 569	18 326
Italy	3 535	3 698	2 611	5 019	6 465	10 619	12 078	3 038
Japan	228	3 224	3 193	12 378	23 424	25 991	24 159	20 730
Korea	2 325	2 844	5 416	8 798	4 670	4 449	4 799	4 044
Mexico	9 185	12 830	11 311	11 568	..	..	..	..
Netherlands	15 055	14 499	41 977	33 341	31 230	29 247	51 365	45 540
New Zealand[3]	3 697	1 832	2172	989	–1 260	–1 602	376	1 020
Norway	3 201	3 786	3 882	6 579	5 918	5 047	2 418	5 483
Poland	4 498	4 908	6 365	6 471	53	45	316	123
Portugal	1 368	2 278	2 802	570	776	1 668	2 901	2 679
Spain	6 820	6 387	11 797	9 357	5 590	12 547	18 935	35 421
Sweden	5 076	10 968	19 569	59 102	4 664	12 648	24 376	18 951
Switzerland	3 078	6 642	7 499	3 412	16 150	17 747	16 631	17 910
Turkey	722	805	940	783	110	251	367	645
United Kingdom	26 084	33 245	64 388	82 176	34 125	61 620	119 463	199 275
United States	88 977	109 264	193 375	282 507	92 694	109 955	132 829	152 152
TOTAL OECD	**248 882**	**299 004**	**509 313**	**683 744**	**340 977**	**414 079**	**636 480**	**767 814**

Note: Data are converted using the yearly average exchange rates.
p. provisional.
1. The above amounts include entrepreneurial capital net and real estate investment inflows.
2. The results shown are for net (inward and outward), direct investment capital flows. For 1999, balance of payments data.
3. Data are based on fiscal years ending 31 March.
Source: OECD /FDI database - Based on national sources.

grammes provided opportunities for international investment. The sale of state-owned companies to foreign investors represented a large share of the source of FDI, particularly among new members to the OECD and in some emerging economies.

In addition to the structural factors, the growth of FDI depends heavily on the business cycle in both home and host countries. The continuing expansion in the United States helped global FDI flows gain and maintain momentum. The quick recovery of Asian countries previously affected by financial crises contributed to this trend. Regional agreements to foster investment flows also paved the way for a higher level of FDI.

The investment strategies of multinational enterprises (MNEs) may provide important additional insights into FDI trends. Globalisation has become an integral part of corporate strategies in recent years, with FDI becoming an imperative rather than an opportunity. Moreover, the advent of new technology (*e.g.* the Internet) offers companies an increasingly effective strategy by which to penetrate overseas markets and to enhance the efficiency of their investments. The growth of FDI is to a certain extent self-perpetuating: competitors follow each other into a market, and FDI may induce other investments in the vertical chain, *e.g.* in suppliers or business service providers. The immediate outlook for investment flows therefore seems to be for continued growth.

This article's second section deals with the 1999 FDI trends in OECD countries. Section III deals specifically with M&A. In the last section, regional FDI trends in the 1990s are analysed and used to illustrate the role of the above-described factors in the growth of foreign investments in Asia, Latin America and selected other economies.

II. Recent trends in OECD countries[1]

The increase in FDI in the OECD area continued in 1999, both in absolute value and as a percentage of GDP. This took FDI activity to a remarkable peak, following almost a decade of continued growth.[2] In 1999, the increase of FDI inflows in Japan, Sweden and Germany were particularly notable. Compared with the previous year, they almost quadrupled in Japan, more than tripled in Sweden and more than doubled in Germany. Spectacular growth rates were also recorded in OECD outflows, with the outgoing FDI of Denmark, France, Ireland, New Zealand and Norway more than doubling compared with 1998.

The United States and United Kingdom witnessed record high FDI flows in 1999. These countries were the most prominent home and host countries, accounting for more than half of total OECD inflows and more than 45% of outflows. Investment inflows to the United States grew by almost 50% and by 28% to the United Kingdom. Outflows from these countries increased by 15% and 67% respectively. As discussed below, the driving force behind this trend was transatlantic M&A. Compared with last year, the United States strengthened its net capital importing position, while the United Kingdom's balance shows increasingly high net outflows.

Inflows into the United States came mainly from Europe. The most important investors were the United Kingdom, Germany and the Netherlands. In 1999, as in the previous year, the United Kingdom's share represented more than one third of total investments in the United States. As far as the sectoral distribution of invest-

Box 1. Foreign Direct Investment Statistics

OECD *International Investment Statistics Yearbook* provides detailed flow and stock statistics for inward and outward FDI based on reporting by the OECD Member countries. Data are presented for each category of FDI by geographical distribution, covering all partner countries in the world and by industrial sectors analysing the concentration by economic activity. The work is carried out by the OECD Secretariat under the auspices of the Working Party on Financial Statistics. The statistics of non-OECD countries relate to IMF balance of payments series and to UNCTAD statistics which supplements missing data with estimates. Some of the more detailed analysis for these countries also rely on the statistics disseminated by regional organisations such as ASEAN and ECLAC.

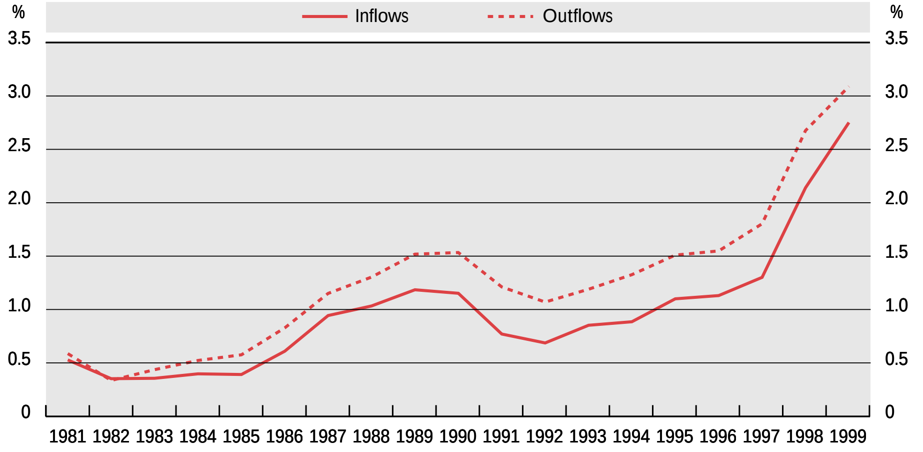
For methodological clarification, it is worth noting that, in general, the majority of foreign investment is composed of direct investment and portfolio investment. The dominant feature which determines the type of investment is the motivation of the investor. FDI is the expression of a lasting interest by a foreign investor in an enterprise where the investor can obtain an effective voice in the management of the enterprise. To achieve international harmonisation of the statistics, the lasting interest is identified with a numerical guideline of at least 10% ownership by the foreign investor (as opposed to portfolio investment for which the motivation of the investor is different). Although the 10% rule is the basic guideline for classifying the statistics, numerous other concepts are involved in the compilation of FDI statistics which have to be considered for a sound comparative analysis of FDI activity in the global market.

Methodological guidelines for compiling FDI statistics are indicated in the *OECD Benchmark Definition of Foreign Direct Investment, 3rd edition* and the *IMF Balance of Payments Manual, 5th edition*. With a view to assessing the extent of the implementation of methodological guidelines, OECD and IMF have conducted a joint survey which also includes information on data sources and dissemination policies. The results of this survey for around a hundred countries can be found in the *Report on the Survey of Implementation of Methodological Standards for Direct Investment* which is available both on the OECD and IMF web sites. Summary conclusions of the report were published in *Financial Market Trends* No 71, November 1998.

In the past decade or so, OECD countries, which constitute major players in FDI, have deployed significant resources and efforts to improve the methodology for measuring FDI activity as well as their overall balance of payments statistics. The comparability of FDI statistics in the region has improved notably although complementary efforts are planned to achieve further international consistency. It is worth noting that the statistical requirements of the European Union contributed substantially to these efforts.

ments is concerned, the manufacturing sector (especially the machinery industry) and telecommunications were the most prominent absorbers of investments, while the traditionally higher share of the petroleum industry declined over the year. On the outflow side, Europe is still the most important recipient of US FDI. However, between 1998 and 1999, its share decreased from 61% to 53%. Canada's, Latin America's and especially Asia's shares of outflows increased, with each representing around 15% of total FDI outflows.

Figure 1. ***OECD flows of FDI, 1981-99 (as percentage of GDP)***[1]



1. Based on the weighted average across all OECD countries.

Source: OECD/FDI database.

a) Mergers and acquisitions and other sources of FDI

Europe is an increasingly active player in the M&A market. For example, *France's* high inflows and record outflows (France's position as a net outward investor, with an amount of exceeding USD 50 billion, was more than double the amount of the previous year) were primarily due to large M&A activity. The largest project in the chemical industry accounted for more than 10% of total French outflows.

Germany was the target of a record USD 52 billion inflow last year, over twice the level of the previous year. The record was due to a merger in the chemical industry, in the course of which the newly established enterprise located its headquarters abroad and acquired the majority stake in the German company. German investments abroad remained on the record high level of the previous year, and were also led by M&A. The four largest mergers in which German investors participated accounted for more than half of total investments abroad. The most important host countries were the United States and the United Kingdom, accounting for 45% and 23% of German FDI outflows, respectively. As a result, Germany maintained its net investor position in 1999.

The *Netherlands* witnessed a decrease over the previous year's record high capital movements, though inflows and outflows were still high compared with the years before 1998. The country remained an important net outward investor.

While still experiencing high inflows, *Spain* became a large investor, mainly due to its increased activity in Latin America. Spanish participation in the privatisation of public utilities and banks in the region was considerable. M&A between companies in the private domain (the most important of which including an Argentinean company) contributed to the high level of flows. As a result, Spain was a net investor for the third consecutive year.

In 1999, while remaining a recipient of high gross inflows, *Ireland* doubled its investments abroad compared with 1998. This is related to the increasing importance of the country as a European platform for overseas companies.

Sweden became one of the largest recipients of FDI in the OECD area in 1999. The country absorbed almost the same amount of FDI inflows as in the previous decade put together. The record-high inflows (almost USD 60 billion) were due to an M&A deal in the chemical industry, which accounted for around two-thirds of the value of total inflows. As outflows were actually lower than in 1998, Sweden unusually became a net recipient.

The *Czech Republic* and *Poland* increased the level of FDI inflows due to large privatisation projects. Together with *Hungary*, they are still on the net receiving end of the FDI spectrum, as the companies in each country have been able to invest only negligible amounts abroad.

Greece, *Portugal* and *Turkey* continued to experience low inflows. On the other hand, Portugal has been playing an increasingly active role on the outflow side in the last few years, effectively becoming a net investor abroad.

As a new phenomenon, OECD members in Asia figured prominently as gross recipients of FDI. *Japan* received a historical record of inflows last year driven by the acquisition by Renault of an important stake in Nissan, as well as other M&A. Inflow into Japan was almost four times that of 1998, and almost half of the amount of the inflows of the entire decade, with European (especially French and Dutch) investors taking the leading role. However, even the record inflow did not come close to the traditionally high level of outflows, meaning that last year Japan was still a net investor abroad.

In *Korea*, in response to the financial crisis, regulatory changes favouring FDI continued last year, resulting in a further increase in the inflow of direct investments. After almost doubling the previous year, FDI grew by more than 60% in 1999. Inflows exceeded a generally unchanged level of outflows for the second consecutive year, changing the country's position to that of a net recipient of FDI.

The inflows were boosted by an ongoing process of corporate restructuring and privatisation.[3] The growth in direct investment from the EU and Japan was particularly pronounced.

The fact that the first three countries listed in Table 2 account for half of the cumulated inflows and outflows indicates the high concentration of OECD FDI in the nineties. Eight of the top ten recipients of FDI are also among the top ten outward investing countries, indicating that the larger OECD countries tend to be active in both undertaking and receiving FDI. Germany, the United Kingdom and Japan were the largest net investors in the nineties, and the United States is the largest net recipient.

Table 2. **Cumulative FDI flows in OECD countries, 1990-99**
Million US dollars

Inflows		Outflows		Net Outflows (+)	
United States	927 378	Unites States	876 705	Germany	305 988
United Kingdom	319 726	United Kingdom	566 400	United Kingdom	246 674
France	215 804	Germany	422 455	Japan	222 720
Netherlands	159 523	France	347 839	France	132 035
Sweden	127 633	Netherlands	250 860	Netherlands	91 337
Belgium-Luxembourg	123 206	Japan	248 729	Switzerland	84 506
Germany	116 467	Canada	120 113	Italy	33 451
Canada	99 000	Switzerland	119 187	Canada	21 113
Spain	97 780	Belgium-Luxembourg	109 350	Finland	17 919
Mexico	81 570	Sweden	102 114	Ireland	9 444
Australia	58 910	Spain	93 236	Korea	4 366
Italy	37 697	Italy	71 148	Norway	1 460
Switzerland	34 680	Finland	40 760	Denmark	782
Denmark	32 176	Denmark	32 958	Iceland	–96
Poland	30 616	Korea	29 018	Austria	–2 929
Greece	26 942	Norway	28 131	Spain	–4 544
Norway	26 670	Ireland	26 895	Turkey	–6 029
Japan	26 008	Australia	26 596	Portugal	–7 038
Korea	24 653	Austria	18 155	Belgium-Luxembourg	–13 856
Finland	22 841	Portugal	10 463	Czech Republic	–14 404
Austria	21 084	New Zealand	5 135	New Zealand	–15 620
New Zealand	20 754	Turkey	2 087	Hungary	–18 357
Hungary	19 618	Hungary	1 261	Sweden	–25 519
Portugal	17 501	Czech Republic	828	Greece	–26 369
Ireland	17 451	Poland	639	Poland	–29 977
Czech Republic	15 233	Greece	573	Australia	–32 314
Turkey	8 116	Iceland	380	Unites States	–50 673
Iceland	476	Mexico	na	Mexico	–81 570
TOTAL OECD	**2 709 512**	**TOTAL OECD**	**3 552 013**	**TOTAL OECD**	**842 501**

na: not available.
Source: OECD, International Direct Investment database.

III. Mergers and acquisitions in overview[4]

The value of international cross-border M&A activity rose by 47% to attain record levels in 1999. This reflects a continuation of the rapid growth in M&A activity in Europe and North America and the gradual emergence of the Asia Pacific region from a period of recession and restructuring.

In 1999 (like in previous years) the overwhelming majority of worldwide M&A was concluded among companies of OECD countries. Western Europe was the world's leading region for cross-border M&A in 1999, activity in the region increasing by 78% in value terms, representing some 73% of the world's cross-border deals. The region excelled as purchaser, while in the case of inward M&A it was closely followed by North America, indicating the continuing predominance of cross-Atlantic deals in the form of European acquisitions in the United States. The United Kingdom, fuelled by deals such as Vodafone-Airtouch and Zeneca-Astra, was the world's most acquisitive country for cross-border M&A in 1999, accounting for 30% of global M&A value. The United States was the leading country for inward deals in 1999 attracting 37% by total value, with major deals including Vodafone-Airtouch and Scottish Power-Pacificorp.

Because M&A deals are the most important driving factors behind overall FDI flows for most OECD countries, last year's M&A developments reflect those of FDI as described in the previous section. After the United States and the United Kingdom, Germany, France and Sweden were the most important host countries last year for inward M&A. Concerning outward M&A, the United Kingdom and the United States still lead, with Germany, France and the Netherlands as other important purchasing countries. Correspondingly, the list of the top ten worldwide M&A featured the companies of these countries and involved deals such as BP Amoco-Arco Atlantic Richfield, Mannesman-Orange, Hoechst-Aventis, Deutsche Telekom-One-2-One, Wal-Mart-Asda as well as those already mentioned.

Asia has started to catch up in the worldwide surge in M&A. The key buyer among Asian countries is Japan, followed by Singapore and Hong Kong (China) China. As far as inward M&A in Asia is concerned, the United States led investment with deals valued at USD 20 billion. Central and Eastern Europe remained out of favour for cross-border M&A in 1999. Poland was the most popular country in the region attracting USD 6 billion. Latin America fared better having USD 43 billion of inward investment during 1999 compared with USD 41 billion in 1998. Argentina was Latin America's leading country for inward investment attracting M&A totalling USD 21 billion, almost half of the region's total.

Over the past ten years cross-border M&A activity has risen fivefold. The rise of mega deals is demonstrated by the dramatic increase in the average deal value, climbing from USD 29 million in 1990 to USD 157 million in 1999. The 1999 average

Table 3. **International M&A deals in OECD countries**
Billion US dollars

	Inward				Outward			
	1996	1997	1998	1999	1996	1997	1998	1999
United States	70.6	64.3	190.8	293	65.5	80.8	132.8	145.7
United Kingdom	39.2	55.4	85.6	123	34.8	32.6	117.1	246.2
Sweden	2.6	3.8	6.1	59.7	1.5	6.3	14	10.8
Germany	6.7	19.3	37.9	42.4	27.4	15.7	60.4	93
France	11.4	13.7	24.3	35.6	11.5	21.6	36.5	83
Canada	10.4	12	15.4	29	22.1	24.7	42.3	16.3
Netherlands	3.6	8.8	18.4	26.9	20	20.7	39.1	52.1
Belgium	2	6.4	21.7	16.4	1.2	1.9	2.1	17.5
Japan	4.8	1.1	13.8	15.8	12.5	11.7	7.5	20.4
Italy	5.2	9.2	5.6	11.4	3	4	15.6	14.4
Korea	0.7	1.4	7.1	11	3.2	6.6	2.2	-
Switzerland	4.4	3.1	6.3	7.7	10.3	38.7	12.6	18.5
Australia	10	12.7	7.5	7.1	5.4	9.9	7.7	2.4
Denmark	0.4	4.5	0.5	6.2	3.8	1.3	1.3	5.3
Poland	1.2	2.1	1.8	5.8	–	–	–	–
Spain	1.8	6.2	5.9	5.4	6.3	13.2	11.8	25.4
Finland	1.2	0.4	5.4	4.5				
Norway	0.5	1.4	2	4.3	4.9	1.8	0.7	1.7
Ireland	0.6	1.6	1.2	4.3	3.9	3.3	4.1	3.5
Czech Republic	0.2	0.8	0.7	2.6	0.7	1	–	–
Mexico	2.8	8.2	1.4	2	0.7	0.7	0.7	2.9
Portugal	0.7	0.9	0.2	1	0.2	0.4	3.7	1.2
Luxembourg	0.1	0.9	2.9	0.9	0.2	2.7	1	2.6
New Zealand	3.5	1	3.4	0.9	1.1	0.4	0.3	0.3
Austria	0.9	1.3	3.1	0.7	0.1	0.8	0.6	1.5
Hungary	0.6	1.2	0.2	0.1	–	–	–	–
Greece	0	0.5	–	0.1	0	0.5	0.8	2.1
Turkey	0.5	1	0.2	–	0.6	0.3	0.5	0.5
Iceland	0	0	–	–	–	–	–	–
Total	**186.6**	**243.2**	**469.4**	**717.8**	**240.9**	**301.6**	**515.4**	**767.3**

Source: KPMG Corporate Finance, Dealwatch Database 2000

value of cross-border deals is up nearly 50% on the equivalent figure of USD 106 million for 1998, illustrating the increasing power of larger firms to close deals in the international M&A marketplace. For many, buying power is based on high-stock values in a buoyant equity capital market, leaving many unquoted corporations with a problem, namely how to finance a strategic acquisition.

In addition to the conventional driving forces behind M&A activity, such as internalisation benefits, operational synergies and strategic value, the current M&A explosion is fuelled by a number of other factors. The change in attitude in some countries towards take-overs, especially hostile ones, eased the barriers towards some large-scale M&A. The change in capital markets is also notable. Highly valued stocks provide an advantage for firms using them as the currency of take-overs. In Europe, the introduction of the euro reduced transaction costs and currency risks of M&A deals within the euro-zone. The reduction in transaction costs is particularly conducive to increasing the participation of small and medium-sized enterprises (SMEs) in the financial market. The deregulation of capital markets also enhances SMEs' participation in M&A activities. On the institutional side, the role played by 'agents' such as investment banks has grown significantly during the second half of the 1990s. These agents actively market acquisition opportunities and take initiatives in making deals. This new trend is in stark contrast to the traditional one in which the company itself initiated the deal.

Apart from global forces, industry-specific factors may have driven M&A activity. Advances in technology have made it possible to manage cross-border supply chains and centralised purchasing for more than one country. This has driven cross-border M&A in the retail sector. Large European retailers are racing to become bigger so as not to lose market share to large foreign competitors or new entrants, such as Walmart. M&A activities in the pharmaceutical and chemical industries are largely driven by increasing returns to scale in R&D. And the financial services industry in Europe offers a relatively fragmented market, which may prompt M&A motivated by consolidation.

The telecommunications industry was again the most active in the global M&A market, with deals representing 20% of the world's total in 1999. The chemical industry was second, and petroleum and gas exploitation came third. Banking and financial services and the production and distribution of electricity, gas and other forms of energy were the next most active sectors in 1999.

IV. Trends of FDI in the 1990s in selected emerging and recent OECD Member economies[5]

Taking a longer perspective, there has been an impressive growth of FDI in the 1990s. Global flows more than trebled, while investments in developing countries grew almost six-fold. Although OECD members continue to play a dominant role in international investment, increasing importance has been attached to emerging economies. This section reviews the trends in FDI in the 1990s in some of the major host countries among the emerging economies.

Asia

Asia has been attracting the lion's share of international investment in developing countries for some time. Inward investment into Asia in the 1990s experienced healthy, uninterrupted growth prior to the financial crisis. It recorded a decline in 1998 as the impact of the crisis took effect. Consequently, its share in the global investment flow declined and became almost on a par with that of Latin America.

The Asian financial crisis in the late 1990s had varying impacts in countries of the region, depending on the nature of investment and local economic conditions.

Investment in Asia in the 1990s was characterised by the rising prominence of China both as an FDI recipient and investor, and by the growth of intra-regional FDI. China emerged as a popular destination of FDI in the early 1990s, and became the second largest FDI recipient in the world after the United States by 1993. Other main destinations of international investment within Asia in the 1990s are Singapore, Malaysia, Thailand, Indonesia, Hong Kong (China), Chinese Taipei and Philippines. These eight countries together account for over 80% of investment into non-OECD Asian countries.

By 1997, the level of inward investment in newly industrialising economies [NIEs – Chinese Taipei, Singapore and Hong Kong (China)] had almost doubled compared with the beginning of the decade. Flows into Hong Kong (China) and Singapore have not been stable, while Chinese Taipei attracted a steady flow until the crisis. The volume of FDI in Chinese Taipei and Hong Kong (China) declined considerably in 1998, due to the slowdown of the regional economies. OECD investment into Hong Kong (China) turned negative, minus USD 1.1 billion in 1998, from USD 4.3 billion in 1997. Although it is suggested that China surpassed the United States and Japan to become the largest investor in Hong Kong (China) since the early 1990s, the decline of OECD investment provides a substantial explanation for the shrinking investment.

Since the latter part of 1980s, inward investment in ASEAN has grown at an impressive rate. The growth was largely led by Japanese investment, triggered by the appreciation of the yen, which pushed Japanese manufacturers out of the home country. The share of Japanese manufacturing investment in ASEAN4 (Malaysia, Indonesia, Philippines, and Thailand) grew from 8% in 1987 to 18% in 1992. Although it has not regained its peak, it has maintained a 16-17% share to date. Malaysia began to support export-oriented investments at an early stage. Since the late 1980s, Malaysia recorded a phenomenal growth of inward investment. After its peak in 1992, investment was maintained at the high level until the financial crisis, whereafter it dropped substantially. Indonesia owes its success in attracting investment principally to the oil and gas sector. The country recorded uninterrupted growth until 1997, but was hit hardest by the crisis. Thailand, successful in attracting both market-seeking and export-oriented investors during the 1990s, increased its FDI inflow by 47% in 1998. The conversion of the Philippines to investment promotion is more recent, since the mid-1990s. The country demonstrated its advantage as an export platform and increased export-oriented investment in the aftermath of the financial crisis.

The origin of inward investment differs considerably among the countries. The majority of inward investment in Singapore originates in OECD countries. The presence of European investment is also strong in Indonesia, while in the Philippines and Thailand the share of investors is evenly divided among the United States, Japan, Europe and NIEs. The increasing prominence of NIEs investment in Malaysia is notable.

It is worth noting the growth of intra-regional FDI in the 1990s, particularly from NIEs in the neighbouring countries. The role of Singapore may serve as an illustration. Today, a quarter of FDI in Malaysia comes from Singapore, which makes the country the largest investor in Malaysia. The share of Singaporean investment in Thailand, 12%, is also high. Chinese Taipei is also gaining importance in the region as an investor. The country was the second largest investor in Vietnam in 1997, which accounted for 17% of the total investment into Vietnam, although Singapore surpassed it in the following year. Chinese Taipei began to venture outside of the region in the 1990s. While 44% of investment went to ASEAN countries in the early 1990s its share has been shifting rapidly towards Latin America since the latter part of the 1990s. Perhaps the biggest beneficiaries of the growth of intra-regional FDI are less developed ASEAN members. In most of these countries, other ASEAN countries play a vital role as investors.

Hong Kong (China) has been the biggest investor into China since the inauguration of China's open policy in 1979, consistently accounting for roughly 60% of foreign investment. Contrary to its dynamism in China, Hong Kong (China) is much less active in other Asian countries. At the same time China has emerged as the biggest investor in Hong Kong (China) in the 1990s. In fact, China's outward investment expansion is another noteworthy phenomenon of the 1990s. Chinese investors – mostly state-owned enterprises – have demonstrated diversified interests: there is high concentration of investment in the trade and services sector in Hong Kong (China), whereas the availability of raw materials is seen as the main motive for their investments in Australia and Canada. Chinese investment in the United States is also active, in search of proprietary technology. Market-seeking investment from China can be found in a great variety of locations around the world.

Latin America

Most of the countries in Latin America have undergone drastic policy reformulation in the 1990s. Macroeconomic stabilisation, trade liberalisation, privatisation programmes, deregulation of policies regarding private investment, and regional integration all contributed to creating a favourable climate for foreign investments. As a result, the level of FDI inflows into the region has increased eightfold compared with the end of the 1980s[6]. The healthy growth of FDI in the region throughout the 1990s demonstrates that the confidence of foreign investors has recovered after going through the difficult decade of the post debt-crisis. In fact, the share of the region in global inward investment has at last recovered to the level prior to the debt crisis. The growth of FDI is largely influenced by privatisation programmes throughout the region.

The four largest economies of Latin America – Mexico, Argentina, Brazil and Chile – have been constantly receiving over 70% of the total inward FDI in Latin America since the 1970s. This trend remained unchanged in the 1990s. It should, however, be kept in mind that the amount of FDI attracted by some of the smaller countries in the region are quite significant when measured against the size of their economies.

Although the region as a whole demonstrates a steady growth in FDI flows in the 1990s, the country breakdown shows a rather different picture. Annual investment flows in individual countries depend largely on the completion of large-scale investment projects – be they privatisation, acquisition or a greenfield investment. As a result, most countries' FDI flow in the 1990s has shown large year-to-year fluctuations.

The change in the nature of FDI is even more striking. For example, the role of debt-equity swaps in attracting FDI has diminished. In the 1980s, the level of FDI flows to some countries, especially larger recipients were mainly sustained by such swaps. Argentina, Chile and Mexico owed their growth in FDI in the former half of the 1990s largely to their privatisation programmes. In the latter part of the 1990s Brazil has emerged as the largest FDI recipient in the region as a result of the sell-off of publicly owned entities. Over one-third of investment in the telecommunications and electricity industries – the two high profile industries that also in other countries usually attract foreign investors – was generated by privatisation.

The change in investment climate has also affected the sectoral distribution of FDI in the region. Prior to the wave of liberalisation, the majority of investment targeted the manufacturing sector and aimed at penetrating highly protected domestic markets. In the 1990s, however, privatisation and the opening up of industry previously closed to foreign investment induced a much higher growth of investment in the services sector, which is usually market oriented investment.

While the United States is by far the largest investor in the region, Spain has become very active since the mid-1990s, especially in Mercosur, Chile and the Andean countries. Latin America's share of Spain's total FDI soared from 29% to 72% between 1990-1998. A very large proportion of those FDI flows went to the services industry, through privatisation or M&A that became possible thanks to deregulation. Since 1996, Spain has overtaken the United Kingdom as main European investor.

Led by MNEs in the more mature economies in the region, outward investment in Latin America increased in the 1990s. The process of liberalisation, privatisation and deregulation forced some local MNEs into increased domestic competition, which made corporate restructuring inevitable.

There are signs that countries in the region may be able to sustain the level of FDI inflows once privatisation is completed. Experiences elsewhere indicate that as the privatisation process comes to an end, infusions of capital continue to occur in order to upgrade existing facilities that have been privatised. Mexico and some Caribbean countries have begun to attract a type of investment that is not related to privatisation but aimed at increasing the efficiency of MNEs' international production facilities. This type of investment is particularly concentrated in the automotive, computers, electronics and apparel industries.

Central and Eastern Europe and CIS economies

The history of FDI is relatively short for the formerly planned-economies, which opened up to capital inflows only at the end of the eighties and beginning of the nineties. Absolute values of FDI inflows have been growing during the last decade. However, compared with its contribution to world GDP or world imports, the region's share in total world FDI stock is still relatively low.

FDI performance can be differentiated by two groups of countries. The first group consists of countries aiming at EU accession. This group contains 10 countries[7], which have concluded association agreements with the EU and are currently negotiating accession. These countries, on average, performed better in the nineties than other countries in the region. The second group of countries attracted less FDI and includes countries belonging to the former Soviet Union (other than the Baltic republics) and the war-ridden economies of the Balkans.

In the first group of countries, according to balance of payments data from 1989 to 1999, Poland, Hungary and the Czech Republic attracted the largest FDI inflows, with the stocks of capital invested approaching or exceeding USD 20 billion in 1999.

As for FDI flows per capita, Estonia, Latvia and Slovenia can be added to the best performers with a more than USD 1500 per capita inflow. Countries in the second group had negligible inflows of FDI, with the notable exceptions of Russia, Kazakhstan and Azerbaijan.

On the one hand, the growth of FDI in these countries is determined by their progress in transition and macroeconomic stabilisation. Countries begin to receive significant inflows of FDI after their economies are more or less stabilised. Thus, in most of the countries in the first group, inflows increased to a significant level only in the second half of the nineties. Compared with the countries in the first group, distortions in factor markets and macroeconomic instabilities are still prevalent in most of the countries in the second group. Moreover, market institutions and the legal systems are often not in place or not working properly. These factors continue to act as a draw on FDI inflows in the second group. It must, however, be added that countries with a stable investment environment or with natural resources attracted more investment than would be expected on the basis of their progress in transition, in part because resource-seeking investments are traditionally less sensitive to economic policies and economic prospects of the home country.

The reliance on privatisation to attract FDI continues to cause annual fluctuations in the inflows into individual countries – and different methods and timing of privatisation may explain some level differences in FDI inflows. By the end of the nineties, only Hungary had shifted to post-privatisation FDI, with annual inflows standing at USD 1.5-2 billion without privatisation projects. Other countries in the first group still rely more on privatisation-related FDI inflows, while countries in the second group may be characterised by pre-privatisation FDI.

The most important countries investing in the region are the United States and Germany. The majority of these investments are made by large MNEs. Other large investors from Western Europe, like France, the United Kingdom and the Netherlands also have a relatively high share in the overall stock of investment. Some smaller companies have also taken part, notably companies located geographically close to the recipient countries (*e.g.* Germany, Austria, Italy and the Scandinavian countries). Asian investors, on the other hand, such as Japan and Korea are relatively underrepresented – especially when considering their otherwise global presence. They do, however, account for a few large projects, typically of the greenfield type.

The sectoral distribution of FDI depends on the privatisation process or on countries' endowments of natural and other production resources. Manufacturing companies are usually the first targets of privatisation, so in the early stages this sector's share is dominant in total FDI. The privatisation of services usually comes second, with the sale of state-owned companies in telecommunications, financial services and in retail trade[8]. Export-oriented investors attracted by the labour force – and, in some cases, by generous incentives – have in some cases undertaken greenfield investment in the vehicles and electronic industries.

Despite the relatively short history of the presence of foreign firms, companies with foreign participation already play a critical role in some economies of the first group. In Hungary, Estonia, Latvia and the Czech Republic, these companies' contribution to value added, foreign trade and GDP is exceedingly significant, even by international comparison. However, in some cases, the beneficial impact of companies with foreign participation on the host economy is arguably limited, on account of underdeveloped linkages with local companies.

Prospects of attracting FDI in the future seem to be relatively bright for the countries in the first group. Their aim to become EU members induces them to adapt policy and legal changes to make their economic environment more similar to that found inside the EU. Because of the self-perpetuating nature of FDI their relatively high existing FDI stock in itself attracts more foreign investment. The FDI, in turn, assists the transition process and, indeed, these countries' recovery from the transformation recession has been quicker than for those in the second group. FDI into the second group of countries could increase significantly as they make further progress toward structural reform.

Notes

1. Considerable progress has been made in enhancing the comparability of the FDI statistics (see text box). However, caution is called for, in that some discrepancies still remain in areas such as data collection methods, time of recording and coverage.
2. Starting from 0.5% of GDP at the beginning of the eighties, the share of the inflows came close to, and that of the outflows exceeded, 3% of GDP by the end of the nineties. The growth of FDI flows continued for the eighth consecutive year since 1992, when the recession in major OECD economies affected FDI flows adversely. Since then, every year has shown positive growth of both inflows and outflows for the OECD area, with an outstandingly high rate of growth in the last three years.
3. One of the biggest deals was Korea Telecom Freetel's strategic alliance, worth USD 600 million.
4. The definition of FDI applied by the IMF and the OECD is not fully comparable with M&A statistics. The KPMG Dealwatch database, cited in this article, collects cross-border M&A data through on-line financial databases, as well as the major financial print publications around the world. As several similar sources are available, the difference in figures is normally attributable to definitional discrepancy. While KPMG concentrates on cross-border activities and includes only the concluded deals, others may include both domestic activities as well as uncompleted deals in progress.
5. FDI data on emerging economies are drawn from IMF balance of payments statistics and UNCTAD. UNCTAD supplements IMF data for those countries for which balance of payments data are not available.
6. Different figures are reported due to the varying definition, methodology and coverage of statistics. For example, ECLAC and UNCTAD reported USD 76 billion for FDI in Latin America and the Caribbean in 1998, while IMF International Financial Statistics recorded USD 70 billion.
7. Bulgaria, the Czech Republic, Estonia, Hungary, Lithuania, Latvia, Poland, Romania, Slovakia, Slovenia.
8. However, there have been cases where privatisation of retail and wholesale trade has been carried out first, and quickly due to its attractiveness for investors and by the relatively quick and high revenues it provides to the public purse.

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