



Foreign Direct Investment in the United States: An Economic Analysis

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Summary

Foreign direct investment in the United States has rebounded slowly after falling from the \$310 billion recorded in 2008, a record surpassed only by the \$320 billion invested in 2000 in U.S. businesses and real estate. (Note: The United States defines foreign direct investment as the ownership or control, directly or indirectly, by one foreign person [individual, branch, partnership, association, government, etc.] of 10% or more of the voting securities of an incorporated U.S. business enterprise or an equivalent interest in an unincorporated U.S. business enterprise (15 CFR §806.15 [a][1]). In 2011, according to U.S. Department of Commerce data, foreigners invested \$234 billion in U.S. businesses and real estate. Foreign direct investments are highly sought after by many state and local governments that are struggling to create additional jobs in their localities. While some in Congress encourage such investment to offset the perceived negative economic effects of U.S. firms investing abroad, others are concerned about foreign acquisitions of U.S. firms that are considered essential to U.S. national and economic security.

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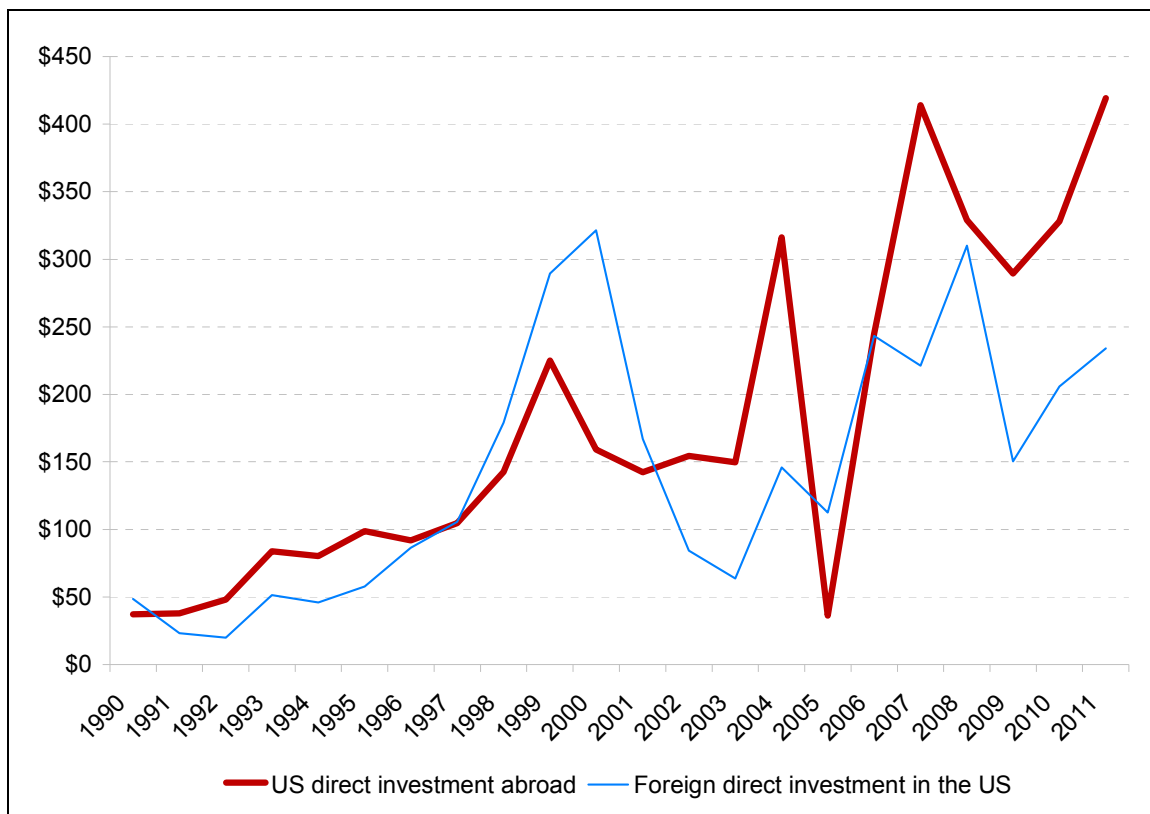
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Recent Investments

Foreigners invested \$234 billion in nominal terms in U.S. businesses and real estate in 2011, according to data published by the Department of Commerce.¹ As **Figure 1** shows, this represents a 14% increase over the \$155 billion invested in 2010. Investments abroad by U.S. parent firms increased by 28% in 2011 to \$419 billion, up from the \$328 billion they invested abroad in 2010. The increase in foreign direct investment flows mirrors a rebound in global flows following the sharp drop in direct investment flows in 2009 and 2010. According to the United Nations' *World Investment Report*, global foreign direct investment inflows decreased by 38% in 2009 compared with the amount invested in 2008. Such investment rose by 13% in 2010 and by 16% in 2011 to reach \$1.5 trillion, short of the \$2.0 trillion invested globally in 2007.

Figure 1. Foreign Direct Investment in the United States and U.S. Direct Investment Abroad, Annual Flows, 1990-2011

(in billions of dollars)



Source: U.S. Department of Commerce.

The cumulative amount, or stock, of foreign direct investment in the United States on a historical cost basis² rose from \$2.26 trillion in 2010 to about \$2.55 trillion in 2011. This marked an

¹ Scott, Sarah P., U.S. International Transactions: First Quarter of 2012. *Survey of Current Business*, July 2012, p. 59. Direct investment data reported in the balance of payments differ from capital flow data reported elsewhere, because the balance of payments data have not been adjusted for current cost adjustments to earnings.

² The position, or stock, is the net book value of foreign direct investors' equity in, and outstanding loans to, their (continued...)

increase of 12.5%.³ The Department of Commerce does not attempt to deflate the annual nominal amounts for direct investment with a specific price deflator. Instead, the department publishes alternative estimates based on current cost and market value to provide other measures of the value of direct investment.

As a share of the total amount of nonresidential investment spending in the U.S. economy, investment spending by foreign firms was equivalent to 11% in 2011, far below the 20% reached in 2009. Better credit conditions and a slight rise in the rate of growth in the U.S. economy tended to push up such mainstays of foreign direct investment activity as mergers and acquisitions. The rise in the value of foreign direct investment includes increases in equity capital, reinvested earnings, and a smaller increase in intercompany debt. Equity values, which accounted for 40% of the total amount of foreign direct investment in 2011, fell by nearly one-third from that recorded in 2010. Reinvested earnings rose by nearly 30% to account for 37% of total foreign direct investment, as U.S. affiliates relied more on their own earnings than on funds borrowed from their foreign parent companies. Intercompany debt accounted for the rest of the total amount of foreign direct investment, or about 23%. In comparison, U.S. direct investment abroad in 2011 was comprised almost entirely of reinvested earnings.

Foreign direct investments in the U.S. manufacturing sector as a whole in 2011 were higher than in 2010 and accounted for nearly half of the overall increase in foreign direct investment in 2011. Foreign direct investment in the banking, finance, retail trade, and professional services all increased in 2011, compared with investments in 2010. In comparison, investments were down in the wholesale trade, real estate, and information sectors. Data for the first two quarters of 2012 indicate that foreign direct investment in the United States is down about 41% from the amount recorded in the comparable period in 2011. Such investments may well continue to lag behind similar investment in 2010 in the second half of the year if the rate of economic growth stalls.

With over \$441 billion invested in the United States, the United Kingdom is the largest foreign direct investor, as is indicated in **Table 1**. Japan is the second-largest foreign direct investor in the U.S. economy with about \$289 billion in investments. Following the Japanese are the Dutch (\$240 billion), the Germans (\$215 billion), the Swiss (\$212), the Canadians (\$211 billion), the French (\$199 billion) and Luxembourg (\$190).

In some cases, investments by one or two countries dominate certain industrial sectors, suggesting that there is a rough form of international specialization present in the investment patterns of foreign multinational firms. At year end 2011, the cumulative amount of investment, or the investment position measured at historical cost, indicates that the Netherlands and the United Kingdom accounted for the bulk of foreign investments in the U.S. petroleum sector, reflecting investments by two giant companies: Royal Dutch Shell and British Petroleum. Japanese investments in the U.S. wholesale trade sector are also substantial, followed by British

(...continued)

affiliates in the United States. A change in the position in a given year consists of three components: equity and intercompany inflows, reinvested earnings of incorporated affiliates, and valuation adjustments to account for changes in the value of financial assets. The Department of Commerce also publishes data on the foreign direct investment position valued on a current-cost and market value bases. These estimates indicate that in 2011 foreign direct investment increased by \$311 billion measured at current cost to a cumulative value of \$2.9 trillion, while the market value measure rose by \$112 billion in to reach a cumulative value of \$3.5 trillion.

³ Barefoot, Kevin B., and Marilyn Ibarra-Caton, *Direct Investment Positions for 2011: Country and Industry Detail, Survey of Current Business*, July 2012. p. 20.

investments, and European investors account for the bulk of foreign investments in the retail trade sector. German investors are the largest investors in the information sector as a result of a number of large media company acquisitions. French, German, and British investments dominate other foreign investments in the banking sector, while Dutch, Canadian, British, and French investments account for over half of the investments in the finance sector. Britain's \$87 billion investment in the U.S. finance and insurance sectors surpasses the more than approximately \$74 billion invested in the finance sector alone by British firms (data for banking have been suppressed by the Department of Commerce), followed by Japan (\$35 billion) and Canada (\$34 billion), although investments in the U.S. banking sector by Germany and France likely are larger than investments by either Japan or Canada. Foreign direct investment in the U.S. manufacturing sector is dominated by a number of countries, each with substantial investments: investments by the United Kingdom (\$140 billion), Switzerland (\$106 billion), the Netherlands (\$101 billion), Japan (\$83), Luxembourg (\$69), Germany (\$64 billion), and France (\$60 billion) account for nearly three-fourths of the total amount of foreign direct investment in this sector.

Investment spending by developed economies accounts for 95% of all foreign direct investment in the United States. These investments are predominately in the manufacturing sector, which accounts for about 33% of foreign direct investment in the United States, a decline from periods when such investment accounted for a majority share of the total. Another 21% of foreign direct investment is in the banking and finance sectors, and 14% is in the retail and wholesale trade sectors, reflecting purchases of department stores and other investments to assist foreign firms in marketing and distributing their products. The fast-growing information sector accounts for 5.8%, while real estate and services account for modest shares of 1.9% and 3.5%, respectively. All other industries account for the remaining 21%.

Table 1. Foreign Direct Investment Position in the United States on a Historical-Cost Basis at Year-End 2011
(in billions of U.S. dollars)

All	All industries	Manufacturing	Wholesale trade	Retail trade	Information	Banking	Finance	Real estate	Services	Other industries
All countries	\$2,547.8	\$838.3	\$310.0	\$50.6	\$147.1	\$153.1	\$376.8	\$48.4	\$88.1	535.6
Canada	210.9	32.3	6.8	(D)	0.8	34.3	62.9	2.2	(D)	64.9
Europe	1,811.9	676.1	163.1	38.9	134.3	71.1	298.2	23.3	56.1	350.8
Austria	4.8	2.3	0.4	(D)	0.0	(D)	0.0	0.0	(D)	0.1
Belgium	86.0	50.3	19.6	7.1	(D)	(D)	(D)	0.0	0.0	6.2
France	198.7	60.2	31.3	(D)	13.8	9.3	(D)	0.5	6.8	39.6
Germany	215.9	64.0	24.0	3.7	48.9	11.4	42.7	8.2	0.1	12.8
Ireland	25.0	11.8	0.9	0.0	(D)	0.2	4.2	0.0	(D)	2.3
Italy	23.0	7.5	1.4	3.0	(D)	(D)	(D)	0.1	(D)	(D)
Luxembourg	190.4	69.2	5.3	(D)	16.8	0.0	45.9	1.8	(D)	49.4
Netherlands	240.3	100.9	27.4	2.4	8.2	(D)	37.4	3.1	32.1	(D)
Sweden	42.3	29.6	6.6	(D)	0.5	(D)	0.1	0.9	(D)	1.4
Switzerland	211.7	106.0	9.4	6.3	(D)	(D)	44.8	0.6	0.4	44.7
UK	442.2	139.9	25.8	3.5	26.3	(D)	87.2	4.9	(D)	(D)
L. America	85.7	(D)	7.3	(D)	0.9	4.2	-14.1	12.2	(D)	48.2
Africa	4.3	(D)	0.6	(D)	0.0	(D)	(D)	(D)	(D)	(D)
Mid. East	25.4	(D)	6.9	(D)	0.8	(D)	(D)	(D)	(D)	(D)
Asia	409.7	111.9	125.3	5.1	10.2	42.0	29.5	8.9	11.8	65.1
Australia	55.9	5.2	0.2	(D)	(D)	2.9	4.1	2.0	0.4	40.7
Japan	289.5	82.7	103.2	4.8	9.9	35.0	22.1	6.3	8.6	16.9
Korea	18.4	3.1	14.0	0.0	0.0	0.1	0.2	(D)	0.0	(D)
OPEC	14.4	(D)	(D)	(D)	0.0	0.9	(D)	(D)	0.0	2.9

Source: Lowe, Jeffrey H., Direct Investment Positions for 2009-2011: Detailed Historical-Cost Positions and Related Financial and Income Flows, Survey of Current Business, September 2012, p. 80.

Notes: The position is the stock, or cumulative, book value of foreign direct investors' equity in, and net outstanding loans to, their U.S. affiliates. A negative position may result as U.S. affiliates repay debts to their foreign parents, and as foreign parents borrow funds from their U.S. affiliates. "D" indicates that data have been suppressed by the Department of Commerce to avoid the disclosure of data of individual companies.

Acquisitions and Establishments

Another way of looking at foreign direct investment is by distinguishing between transactions in which foreigners acquire existing U.S. firms and those in which foreigners establish new firms—termed “greenfield” investments. New investments are often preferred at the local level because they are thought to add to local employment, whereas a foreign acquisition itself may add little, if any, new employment. In 2008, outlays for new investments, which include investments made directly by foreign investors and those made by existing U.S. affiliates, were \$260 billion, a 3.0% increase over the \$252 billion invested in 2007. According to the Department of Commerce, the increase in new investments reflected several large transactions.⁴ These transactions include the acquisition of Anheuser-Busch Cos. Inc., by Stichting Interbrew SA for \$52 billion; the acquisition of Alcon Inc., by Novartis AG for \$10.8 billion; and large investments in Commerce Bancorp, New Jersey, Morgan Stanley, and Citigroup. Acquisitions of existing U.S. firms accounted for 93% of the new investments by value. Investments by the existing U.S. affiliates of foreign firms accounted for 82% of the total transactions by investor, while other foreign direct investors accounted for the remaining 18% of transactions. Investment outlays by foreign firms increased from 2007 to 2008 in all major sectors, except wholesale trade, retail trade, and real estate. Investment in information, manufacturing, and services all posted increases. The Department of Commerce halted publication of the annual report on foreign acquisitions after the June 2008 edition. Instead, it is developing a separate report that it expects will better capture the construction of new plants by foreign-owned firms that are operating in the United States.

Economic Performance

By year-end 2010, the latest year for which detailed data are available, foreign firms employed almost 6 million Americans, less than 4% of the U.S. civilian labor force, and owned over 33,000 individual business establishments.⁵ Foreign firms have a direct investment presence in every state. Employment of these firms ranges from over 636,000 in California, to about 7,700 in South Dakota. Following California, New York (459,600), Texas (455,200), Pennsylvania (285,300), Illinois (263,800), New Jersey (256,700), and Florida (239,500) have the largest numbers of residents employed by foreign firms. In 2010, 36% of the foreign firms’ employment was in the manufacturing sector, more than twice the share of manufacturing employment in the U.S. economy as a whole, with average annual compensation (wages and benefits) per worker of about \$76,000.

Retail and wholesale trade accounted for another 21% of total affiliate employment. Dutch-affiliated firms are the largest single employers in the retail trade sector and account for nearly one-third of total affiliate employment in this sector, while Japanese and German firms account for over half of the employment in the wholesale trade sector. Canadian, French, and Japanese firms account for the largest share of affiliate employment in the services sector, which accounted for about 20% of total affiliate employment. Employment in the information, finance, and real

⁴ Anderson, Thomas, *Foreign Direct Investment in the United States: New Investment in 2008. Survey of Current Business*, June 2009. p. 34.

⁵ *Foreign Direct Investment in the United States: Operations of U.S. Affiliates of Foreign Companies, Preliminary 2010 Estimates*. Bureau of Economic Analysis, September 2012, Table 1A-1.

estate services sectors accounts for another 14% of total affiliate employment. Average employee compensation is highest in the finance sector—\$159,000—where British, Canadian, Swiss, French, and Dutch firms account for three-fourths of the employment. The rest of the affiliate employment is spread among a large number of other industries.

The affiliates of foreign firms spent \$163 billion in the United States in 2010 on new plants and equipment, imported \$542 billion in goods and exported \$250 billion in goods. Since 1980, the total amount of foreign direct investment in the economy has increased eight-fold and nearly doubled as a share of U.S. gross domestic product (GDP) from 3.4% to 6.4%. It is important to note, however, that these data do not imply anything in particular about the role foreign direct investment has played in the rate of growth of U.S. GDP.

The performance of foreign-owned establishments, on average, compared with their U.S.-owned counterparts presents a mixed picture. Historically, foreign-owned firms operating in the United States have had lower rates of return, as measured by return on assets, than U.S.-owned firms, although the gap between the two groups appears to have narrowed over time. According to the Bureau of Economic Analysis, this narrowing of the gap in the rate of return appears to be related to age effects, or the costs associated with acquiring or establishing a new business that can entail startup costs that disappear over time and market share.⁶ By other measures, foreign-owned manufacturing firms appear to be outperforming their U.S. counterparts.⁷ Although foreign-owned firms account for less than 3% of all U.S. manufacturing establishments, they have had six times more value added on average and seven times higher value of shipments than other manufacturing establishments. The average plant size for foreign-owned firms is much larger—six times—than for other U.S. firms, on average, in similar industries. This difference in plant size apparently rises from an absence of small plants among those that are foreign-owned. As a result of the larger plant scale and newer plant age, foreign-owned firms paid wages on average that were 60% higher than other U.S. manufacturing firms, had 40% higher productivity per worker, and 58% greater output per worker than the average of comparable U.S.-owned manufacturing plants. Foreign-owned firms also display higher capital intensity in a larger number of industries than all U.S. establishments.

These differences between foreign-owned firms and all U.S. firms should be viewed with some caution. First, the two groups of firms are not strictly comparable: the group of foreign-owned firms comprises a subset of all foreign firms, which includes primarily very large firms; the group of U.S. firms includes all firms, spanning a broader range of sizes. Secondly, the differences reflect a range of additional factors, including the prospect that foreign firms that invest in the United States likely are large firms with proven technologies or techniques they have successfully transferred to the United States. Small foreign ventures, experimenting with unproven technologies, are unlikely to want the added risk of investing overseas. Foreign investors also tend to opt for larger scale and higher capital-intensity plants than the average U.S. firm to offset the risks inherent in investing abroad and to generate higher profits to make it economical to manage an operation far removed from the parent firm.

⁶ Mataloni, Raymond J. Jr., An Examination of the Low Rates of Return of Foreign-Owned U.S. Companies, *Survey of Current Business*, March 2000, p. 55.

⁷ *Foreign Direct Investment in the United States, Establishment Data for 2002*, Bureau of Economic Analysis, June 2007.

Conclusions

Foreign direct investment in the United States in 2010 rose sharply over the amount invested in 2009, but did not rise to the record levels of such investment recorded in previous years. Other countries have experienced a similar turnaround in foreign direct investment inflows, especially some of the less developed economies where there is a great potential for investment. As the rate of growth of the U.S. economy improves relative to other advanced economies, interest rates stay low, and the rate of price inflation stays in check, foreign direct investment in the United States likely will continue to increase. Of particular importance will be public concerns over foreign direct investment in the economy as a whole and on the overall phenomenon referred to as “globalization,” with its impact on jobs in the economy. Concerns over foreign direct investment, where they exist, stem not so much from the perceived potential losses of international competitiveness that characterized similar concerns in the 1980s, but from potential job losses that could result from mergers and acquisitions, although such losses could occur whether the acquiring company is foreign- or U.S.-owned. Such concerns are offset, at least in part, by the benefits that are perceived to be derived from the inflow of capital and the potential for new jobs being created in local areas.

Although job security is an important public issue, opposition to some types of foreign direct investment stems from concerns about the impact of such investment on U.S. economic and security interests, particularly in light of the terrorist attacks of September 11, 2001. The U.S. economy, however, remains a prime destination for foreign direct investment. As the pace of economic growth in the nation increases relative to that of foreign economies, foreign direct investment likely will increase as new investments are attracted to the United States and existing firms are encouraged to reinvest profits in their U.S. operations.

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