UN report underscores key role of foreign investment in global economic integration

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The latest World Investment Report (*WIR 2000*) published by the United Nations Conference on International Trade and Development (UNCTAD) highlights the further integration of global production as a result of the foreign direct investment (FDI) activities of the world's major transnational corporations.

According to *WIR 2000*, global foreign direct investment flows totaled $865 billion in 1999, an increase of 16 percent over the previous year, and are expected to top $1 trillion this year. This compares with only $58 billion in 1982.

"International production by transnational corporations (TNCs), now numbering some 63,000 parent firms with around 690,000 foreign affiliates and a plethora of inter-firm arrangements," the report notes, "spans virtually all countries and economic activities, rendering it a formidable force in today's world economy."

Underscoring the growing significance of foreign investment by TNCs in shaping the structure of the world economy, the report points out that gross product associated with international production and foreign affiliate sales worldwide has been rising faster than both global gross domestic product (GDP) and global exports. "Sales of foreign affiliates worldwide ($14 trillion in 1999, $3 trillion in 1980) are now nearly twice as high as global exports, and the gross product associated with international production is about one-tenth of global GDP, compared with one-twentieth in 1982. The ratio of world FDI inflows, which stood at $865 billion in 1999, to global gross domestic capital formation is now 14 percent, compared with 2 percent 20 years ago. Similarly, the ratio of world FDI stock to world GDP increased from 5 percent to 16 percent during the same period. And the number of transnational parent firms in 15 developed home countries increased from some 7,000 at the end of the 1960s to some 40,000 at the end of the 1990s."

Virtually all governments around the world are bringing in laws and regulations to facilitate the foreign investment activities of the TNCs. Over the period 1991-99, around 94 percent of the 1,035 changes worldwide in laws governing foreign direct investment created a more favourable environment for FDI.

One of the main components of the increase in FDI over the past decade has been the rise in cross-border mergers and acquisitions (M&As), which have increased from less than $100 billion in 1987 to $720 billion in 1999.

The total number of M&As, both cross-border and domestic, has grown at an annual rate of 42 percent between 1980 and 1999, while the value of M&As has increased as a share of world GDP from 0.3 percent in 1980 to 8 percent in 1999. There have been two M&A waves; the first in 1988-90 and the second from 1995 onwards.

Tremendous competitive pressures generated by technological changes, which can often transform market positions almost overnight, are driving the increase in merger activity. In the words of the report: "The crucial role of speed in today's business life is illustrated by such quotes from top executives as: 'In the new economy in which we live, a year has 50 days' or 'Speed is our friend—time is our enemy.'"

For many firms expansion through the merger with or acquisition of other firms is not a matter of choice but a question of survival in the increasingly ferocious struggle for sales and profits.

"Cross-border M&As," the report points out, "are growing so rapidly in importance precisely because they provide firms with the fastest way of acquiring

tangible and intangible assets in different countries, and because they allow firms to restructure existing operations nationally or globally to exploit synergies and obtain strategic advantages. In brief, cross-border M&As allow firms rapidly to acquire a portfolio of locational assets which has become a key source of strength in a globalised economy. In oligopolistic industries, furthermore, deals may be undertaken in response to the moves or anticipated moves of competitors. Even firms that would not want to jump on the bandwagon may feel they have to, for fear of becoming targets themselves."

The report draws a parallel between the current international M&A boom and that which took place in the US economy at the turn of the 19th century. Just as the earlier boom in the US contributed to the emergence of a national market for goods and services and a national production system, together with a national market for firms, "so is the current international boom reinforcing the emergence of a global market for goods and services and the emergence of an international production system, complemented by an increasingly global market for firms."

In recent months the world financial system has become increasingly unbalanced by the rise in the US dollar, relative to the euro. Last month the Group of Seven nations made their first major intervention in currency markets in five years in an endeavour to boost the European currency. But as many observers have pointed out, the intervention is likely to have little effect because the imbalance in currency values is being fueled not by speculation but by the inflow of capital into the US, as investors in Europe and the rest of the world seek the higher rates of return available in the American economy.

The *WIR 2000* provides figures that point to the growing importance of mergers and acquisitions in this foreign capital inflow. "The United States," it reports, "continued to be the single largest target country with M&A sales of $233 billion to foreign investors in 1999. More than a quarter of all M&A deals in the United States in 1999 were concluded by foreign acquirers ... compared with 7 percent in 1997."

On the other side of the Atlantic, TNCs based in the European Union invested $510 billion abroad in 1999, or nearly two-thirds of global FDI outflows. One of the factors at work in the EU has been the introduction of the euro, which has increased competition thereby exerting more pressure on firms to "restructure and consolidate their operations."

Figures in the report also indicate that the plunge in the value of the Australian dollar, which has lost around 20 percent against the US dollar since the start of the year, is bound up with shifting global investment flows. According to the *WIR 2000* the inward investment in Australia of $5.4 billion in 1999, down 14 percent on the previous year, was the lowest in four years and below the annual average for the decade to 1995.