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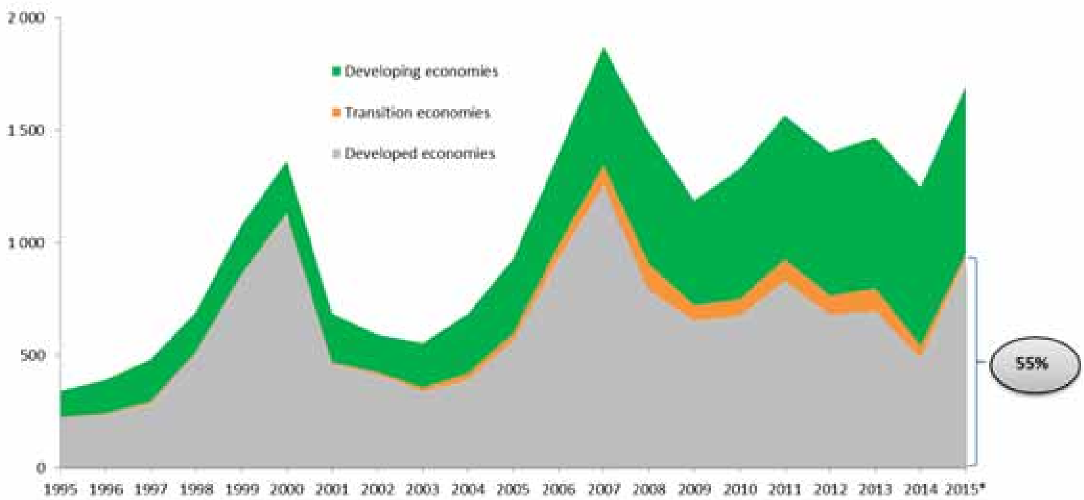
FDI RECOVERY IS UNEXPECTEDLY STRONG, BUT LACKS PRODUCTIVE IMPACT

HIGHLIGHTS

- *Global FDI flows jumped 36% in 2015 to an estimated US$1.7 trillion*, their highest level since the global economic and financial crisis of 2008-2009 (figure 1).

Figure 1. FDI inflows: global and by group of economies 1995-2015
(Billions of US dollars)



Source: ©UNCTAD.
*Preliminary estimates.
Note: Excluding Caribbean offshore financial centers.

- *A surge in FDI targeting developed economies (+90%) was the principal factor behind the global rebound.* Strong growth in flows was reported in the European Union (EU) as well as in the United States where FDI quadrupled, although from a historically low level in 2014. As a result, the pattern of FDI by economic grouping tilted in favor of developed countries which now account for 55% of global FDI inflows in 2015 (figure 1).

- *However, the growth was largely due to cross-border merger and acquisitions (M&As)*, with only a limited contribution from greenfield investment projects in productive assets. Moreover, a part of FDI flows was related to corporate reconfigurations involving large values in the financial account of the balance of payments but little movement in actual resources.

- *Developing economies saw their FDI reaching a new high of US$741 billion, 5% higher than in 2014.* Developing Asia, with its FDI flows surpassing half a trillion US dollars, remained the largest FDI recipient region in the world, accounting for one third of global FDI flows. Flows faltered in Africa and Latin America and the Caribbean (excluding offshore financial centers) reflecting the plummeting prices of their principal commodities exports.

- *Flows to transition economies continued to fall (-54%) as tumbling international commodities prices and regional conflicts undercut FDI.* Investment in the region's two largest host economies, the Russian Federation and Kazakhstan, fell sharply.

- *Cross-border M&As increased by 61% in 2015, while the overall value of announced greenfield investment projects registered little change from the previous year.* There was a decline in announced greenfield investments in developing economies, pointing to a growing weakness in MNEs' capital expenditures.

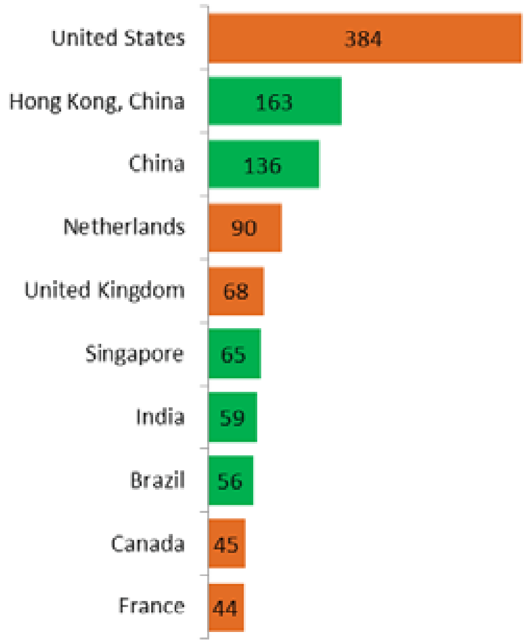
- *Barring another wave of M&A deals and corporate reconfigurations, FDI flows are expected to decline in 2016*, reflecting the fragility of the global economy, volatility of global financial markets, weak aggregate demand and a significant deceleration in some large emerging market economies. Elevated geopolitical risks and regional tensions could further amplify these economic challenges.

Global FDI flows rose in 2015 (+36%) to reach an estimated US$1.7 trillion, their highest level since 2007. A wave of cross-border mergers and acquisitions (M&As), which rose significantly in value, was largely responsible for the increase in FDI. Greenfield investment project announcements, in contrast, registered little change in value terms from 2014, with a rise in developed economies roughly compensating a pullback in MNEs' capital expenditures in developing economies.

The sharp increase of FDI inflows in developed economies changed the pattern of FDI by economic grouping in their favour. They now account for more than half of global FDI inflows. However at the regional level, developing Asia remained the largest host region for FDI inflows, surpassing EU and North America. Developing economies continue to make up half of the top 10 host economies in the year (figure 2).

The United States, with an estimated US$384 billion in inflows, vaulted back into first position among host economies in 2015, after exceptionally falling to third in 2014 (figure 2). FDI inflows to Hong Kong, China – the second largest recipient in the world – reached a record of $163 billion for the first time ever. The rise in both economies, however, was due in part to inversion deals and reconfiguration of corporate structures involving large values in the financial account of the balance of payments but little movement in actual resources.

Figure 2. Estimated FDI inflows: top 10 host economies, 2015
(Billions of US dollars)



Source: ©UNCTAD.
Note: FDI estimations in this Trends Monitor are based primarily on quarterly FDI data derived from the (extended) directional principle, though there are some countries for which the asset/liability data are used for estimation.

FDI flows to developed economies reached their second highest level

UNCTAD's preliminary estimates indicate that FDI flows to developed countries bounced back sharply in 2015, reaching their second highest level ever at US$936 billion, and accounting for the majority of the increase in global flows (figure 3). Buoyant cross-border M&A activities, most notably acquisitions of assets in the United States by foreign MNEs, boosted FDI flows. MNEs seeking growth, rushed to make acquisitions. The low interest environment and strong balance sheets facilitated such moves.

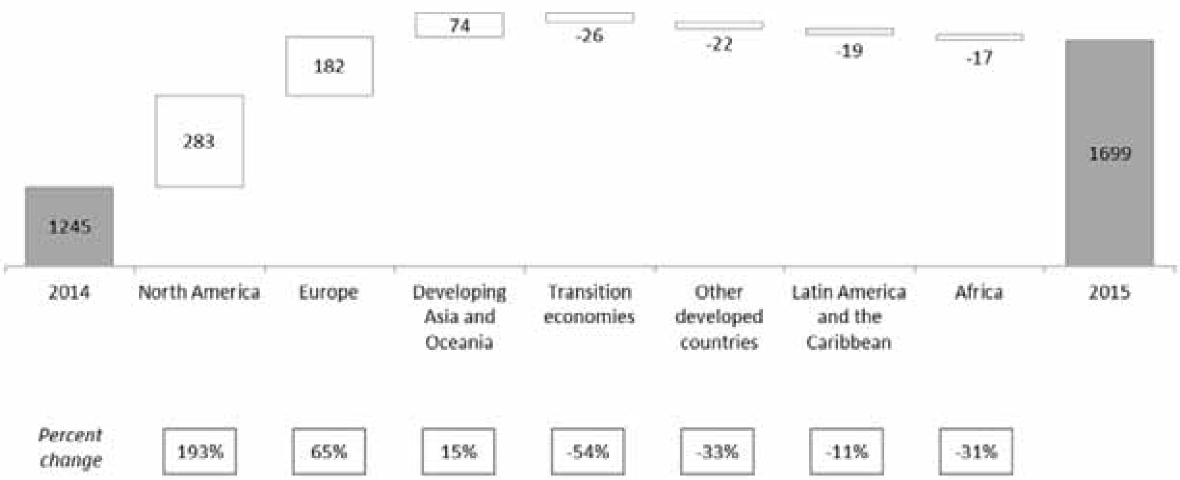
Therefore, the growth of FDI inflows did not translate into an equivalent expansion of productive capacity, as it was due in large part to cross-border M&As and with only a limited contribution from greenfield investment projects in productive assets. Furthermore, some deals were structured as inversions which usually involve little movement in resources.

FDI to the *EU* found traction rising to an estimated US$426 billion, after three successive years of decline. Inflows to the Netherlands (+146% to US$90 billion), Belgium (from –US$8.7 billion in 2014 to US$32.7 billion) and the United Kingdom (+29% to US$68 billion) rose strongly in 2015. The region's largest economies, Germany and France, also experienced an uptick in their flows. In Germany inward FDI returned to positive territory in 2015, after dipping into net divestment in 2014 (-US$6.2 billion to US$11 billion), thanks to a sharp reduction in net repayment of intra-company loans and a near doubling of reinvested earnings. FDI flows to France more than doubled (from US$15 billion in 2014 to US$44 billion in 2015), propelled by strong M&A sales including the acquisition of Lafarge SA by Holcim Ltd (Switzerland) for US$21 billion. While cross-border M&As to the region jumped (+68%), there was also an important increase in greenfield investment project announcements (+14%) signalling a potential rebound in capital expenditures in productive assets as macroeconomic and financial conditions improve.

The primary sector did not contribute to the rise in FDI or the doubling of M&A sales in developed countries. In Australia, where FDI fell markedly (-33%), significant divestments of mining assets reduced M&A sales and weighed down inflows. A large swing in intra-company loans (from a net inflow of US$13 billion in 2014 to a net repayment of $US4 billion in 2015) also caused flows to slump. The fall of FDI flows to Canada (-16%) was largely attributable to the primary sector as well, with a similar reduction in intra-company loans, especially for energy and mining MNEs.

For the United States, while the comparison with 2014 is skewed due to the exceptionally low level in that year caused by a single large divestment, the estimated US$384 billion FDI inflows in 2015 represent the highest level since 2000. The rise in flows was due largely to a surge in equity investments and a sharp increase in M&A sales. Acquisitions of assets in manufacturing and services more than compensated for the decline in the primary sector, with total M&A sales rising to $228 billion, the largest volume of cross-border acquisitions since 2000.

Figure 3. Regional contribution to FDI flows growth, 2014–2015
(Billions of US dollars)



Source: ©UNCTAD.
Note: Excluding Caribbean offshore financial centers. Percent changes are calculated for each region relative to 2014.

Record FDI flows to developing Asia offset sharp declines in other developing regions

In 2015, FDI inflows to *developing Asia* rose by 15% to an estimated US$548 billion, a new record. It continued to be the largest FDI recipient region in the world, accounting for one third of global FDI flows.

With FDI inflows jumping to an estimated US$163 billion, Hong Kong (China) became the largest recipient economy in the region and the second largest in the world (figure 3). The corporate reconfiguration of Cheung Kong Holdings and Hutchison Whampoa accounted for part of the increase. FDI inflows to mainland China rose by 6% to an estimated US$136 billion. While inward FDI flows in manufacturing declined, those in services kept momentum and drove total inflows to a new record level. FDI inflows to Singapore dropped slightly by 4% to an estimated US$65 billion contributing to an overall decline of 7% in ASEAN as a whole. FDI flows to India nearly doubled, reaching an estimated US$59 billion. Measures taken by the government to improve the investment climate have had an impact.

Table 1. FDI inflows, cross-border M&As and announced greenfield projects, by region and major economy, 2014–2015

(Billions of US dollars)

Region / economy	FDI inflows			Cross-border M&As			Announced greenfield project values		
	2014	2015[a]	*Growth rate (%)*	2014	2015	*Growth rate (%)*	2014	2015	*Growth rate (%)*
World	**1 245**	**1 699**	***36.5***	**398.9**	**643.7**	***61.4***	**714.3**	**720.7**	***0.9***
Developed economies	**493**	**936**	***89.9***	**274.5**	**566.8**	***106.4***	**229.6**	**247.5**	***7.8***
Europe Union	254	426	*67.6*	160.6	269.2	*67.6*	**122.4**	139.8	*14.2*
North America	146	429	*193.5*	44.1	242.3	*449.0*	77.7	76.6	*-1.4*
Developing economies	**703**	**741**	***5.3***	**120.1**	**67.6**	***-43.7***	**459.1**	**439.4**	***-4.3***
Africa	55	38	*-31.4*	5.1	20.4	*303.6*	88.0	71.1	*-19.2*
Latin America and the Caribbean	170	151	*-11.2*	25.5	10.1	*-60.2*	89.3	68.6	*-23.2*
Developing Asia	475	548	*15.5*	89.3	35.3	*-60.5*	280.6	299.3	*6.7*
Transition economies	**49**	**22**	***-54.1***	**4.2**	**9.3**	***120.8***	**25.7**	**33.8**	***31.8***

Source: ©UNCTAD.

[a] Preliminary estimates.

Note: World FDI inflows are projected on the basis of 150 economies for which data are available for part of 2015 or full year estimate, as of 15 January 2016. Annual figures are estimated based on available partial-year data, in most cases up to the third quarter of 2015. The proportion of inflows from these economies in total inflows to their respective region or subregion in 2014 is used to extrapolate 2015 regional data. Data exclude the financial centres in the Caribbean.

In 2015, *West Asia* saw its FDI flows increase by 5% to US$45 billion after six consecutive years of decline. However, the increase was driven largely by a rise of FDI flows in Turkey (+30% from US$12.4 billion to an estimated US$16 billion). Net M&As sales in the country nearly doubled, bolstered by the acquisition of Turkiye Garanti Bankasi AS by Banco Bilbao Vizcaya Argentaria SA (Spain) for US$2.5 billion.

FDI inflows to *Africa* fell by 31% in 2015 to an estimated US$38 billion, due largely to a decline of FDI in Sub-Saharan Africa. Flows to North Africa reversed their downward trend as Egypt saw a rebound of investment from US$4.3 billion in 2014 to an estimated US$6.7 billion in 2015. Central Africa and Southern Africa saw the largest declines in FDI. The end of the commodity “super-cycle” had an impact on resource-seeking FDI. Flows into Mozambique were down 21% but still notable at an estimated US$3.8 billion, while Nigeria saw its FDI decline by 27% to an estimated US$3.4 billion as the country was hit hard by the drop in oil prices. FDI into South Africa fell dramatically, down 74% to US$1.5 billion.

FDI flows to *Latin America* fell again in 2015 (-11%) reaching US$151 billion. Slowing domestic demand and a strong terms of trade shock caused by plummeting commodity prices hampered investment in South America. FDI flows to Brazil, the region’s principal recipient, fell 23% to US$56 billion. Inflows were also impacted by the divestment of GVT Participacoes S.A. – a telecommunications provider – by Vivendi S.A. (France) for US$9.8 billion to Telefonica Brasil S.A. (Brazil).

Falling profit margins in the extractive sector slowed new investments and crimped reinvestment in South America’s commodities exporters, with flows falling in Chile (-38%) and Colombia (-15%). This dynamic notwithstanding, FDI flows to Peru rose (+11%) with an increase in equity investments. In Argentina inflows increased, but only in comparison with a weak 2014 when the government compensated Repsol (Spain) for the nationalization of its majority-owned subsidiary YPF S.A., excluding this transaction 2015 FDI flows posted a moderate decline (-8.3%).

Economic growth and investment in Central America, in contrast, remained robust in 2015. Mexico registered a 14% increase in FDI to US$29 billion. This result was flattered by a surge in cross-border M&A sales (+33%) resulting from the completion of a number of megadeals, including the purchase of Grupo Iusacell SA de CV – a wireless telecommunications provider – by AT&T (United States) for US$ 2.5 billion and the acquisition of Vitro SAB de CV (Mexico) – a glass and plastic bottling manufacturer – by Owens-Illinois Inc (United States) for US$ 2.2 billion.

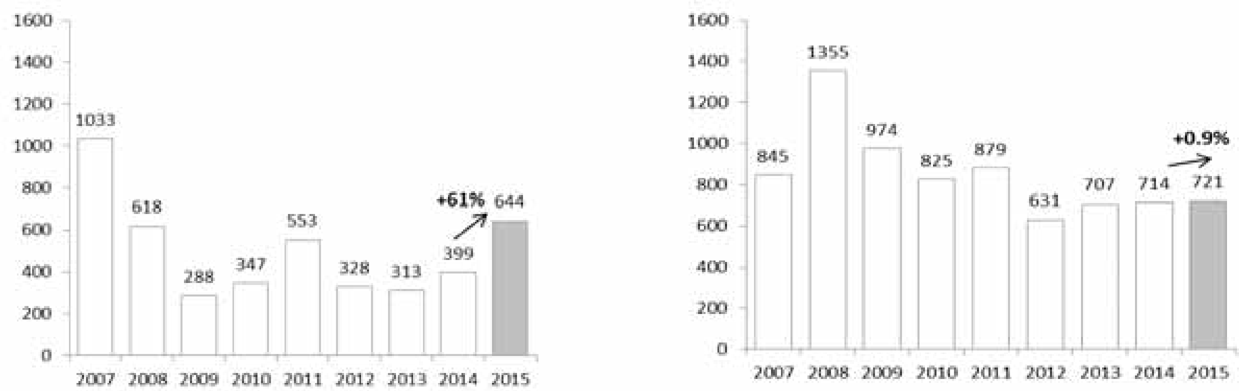
In *transition economies* the ongoing geopolitical situation and reduced market confidence led to a further decline of FDI flows by 54%, reaching an estimated US$22 billion. FDI flows in South-East Europe rose 3%. In the Russian Federation and Kazakhstan, the tumbling of international commodity prices weighed heavily on FDI flows, which declined by 92% and 66%, respectively. However, foreign investors continue to invest in the primary sector. For example Gaetano Ldt , a UK based private equity firm acquired Kumi Oil OOO in the Russian Federation and the Malaysian state-owned Petroliam Nasional Bhd acquired some stakes in Azerbaijan Gas Supply Co. for US$2.25 billion.

Surge in cross-border M&As, but signs of weakness in capital expenditures in developing economies

The year was marked by a pronounced upturn in cross-border M&As, which reached their highest level since 2007 (figure 4). MNEs took advantage of record cash positions, as well as exceptional global liquidity conditions, to make acquisitions with a view to boosting revenue growth and generating cost efficiencies. Net sales rose to US$644 billion, an increase of 61% over the previous year, spurred on by brisk deal making in the manufacturing sector (+132%, to US$339 billion). In particular, sales of assets related to the manufacturing of non-metallic mineral products, machinery and equipment, and electrical components rose sharply. Deal activity in the services sector was mixed, with slowing sales in financial services, but strong increases in real estate activities and transportation services. In contrast, sales in the extractive sector slid (-51%) as plummeting oil prices contributed to a significant retreat in the total value of deals in crude oil and natural gas activities (-68%).

Figure 4. The value of cross-border M&A sales and of announced greenfield investment projects, 2007–2015[a]
(Billions of US dollars)

(a) Cross-border M&As **(b) Announced greenfield FDI projects**



Source: ©UNCTAD, based on cross-border M&A database for M&As, and information from the Financial Times Ltd, fDi Markets (www.fDimarkets.com) for greenfield projects.
[a] Data for announced greenfield investment for 2015 are preliminary.
Note: Excluding Caribbean offshore financial centres.

Developed economies were largely the target of the upswing in cross-border M&As. Net sales in the EU rose 68% to US$269 billion, driven by strong increases in Ireland and the United Kingdom (together representing roughly three-quarters of the increase). Tax inversion deals, carried out by MNEs from the United States, were evident in both countries. Deal activity in the United States rose from US$11 billion in 2014 to US$228 billion in 2015 – with the jump in part reflecting the effect of the low 2014 value due to the divestment of Verizon Wireless (United States) by Vodafone (United Kingdom) in that year, but also a growing appetite for assets in the country. In contrast, the value of M&As in developing economies fell sharply (-44%) to US$68 billion. The above mentioned divestment in Brazil pulled Latin America and the Caribbean down (-60%), while sales in developing Asia retreated (-61%) from their exceptional levels, fuelled by large megadeals, of 2014.

Greenfield project announcements, which are indicative of MNEs' capital expenditure intentions, remained stagnant registering little dynamism in 2015 (+0.9%) (figure 4). Project announcements in developing economies declined sharply, particularly in Africa (-19%) and Latin America and the Caribbean (-23%).

FDI flows in 2016: a cloudy outlook

Barring another wave of M&A deals and corporate reconfigurations, FDI flows are expected to decline in 2016, reflecting the fragility of the global economy, volatility of global financial markets, weak aggregate demand and a significant deceleration in some large emerging market economies. Elevated geopolitical risks and regional tensions could further amplify these economic challenges.

Stagnant greenfield investment globally and outright declines in a number of developing regions suggests that the current upswing in global FDI flows is potentially fragile and exposed to the vagaries of the cross border M&A market.

However, improvement in macroeconomic conditions (with global growth projected to reach 2.9% in 2016 compared to 2.4% in 2015) due to modest recovery in developed economies, could strengthen the confidence of investors and induce them to make productive investments to cement their business plans. In addition, further depreciation of currencies in emerging markets and possible sales of assets to restructure corporate debt may also stimulate additional FDI.

The next issue of UNCTAD's Global Investment Trends Monitor will be released in mid-April 2016.

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For further information, please contact:

Mr James X. Zhan
Director
Investment and Enterprise Division
UNCTAD
Tel. +41 22 917 17 81
Email: diaeinfo@unctad.org