

**United Nations Conference on Trade and Development**

**WORLD INVESTMENT  
PROSPECTS SURVEY  
2007–2009**



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## NOTE

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The following symbols have been used in the tables:

Two dots (..) indicate that data are not available or are not separately reported.

Rows in tables have been omitted in those cases where no data are available for any of the elements in the row.

A hyphen (-) indicates that the item is equal to zero or its value is negligible.

A blank in a table indicates that the item is not applicable.

A slash (/) between dates representing years (e.g. 1994/1995) indicates a financial year.

Use of a dash (–) between dates representing years (e.g. 1994–1995) signifies the full period involved, including the beginning and end years.

References to “dollars” (\$) are to United States dollars, unless otherwise indicated.

Annual rates of growth or change, unless otherwise stated, refer to annual compound rates.

Because of rounding, details and percentages in tables do not necessarily add up to totals.

The material contained in this study may be freely quoted with appropriate acknowledgement.

## PREFACE AND ACKNOWLEDGMENTS

The UNCTAD World Investment Prospects survey 2007–2009 aims at providing an outlook on future trends on FDI by the largest TNCs. The present publication is the last issue in a series of similar surveys that have been carried out regularly by UNCTAD since 1995 as part of the background work for its *World Investment Reports*. The series has included, for instance, studies on "International Investment: towards the year 2001" and "International Investment: towards the year 2002" (United Nations, 1997; United Nations, 1998), which were joint publications of Arthur Andersen, Invest in France Mission and UNCTAD, as well as two UNCTAD publications entitled "Prospects for foreign direct investment and the strategies of transnational corporations" for the years 2004-2007 and 2005-2008 respectively (UNCTAD, 2004a; UNCTAD, 2005a).

Research collaboration for the present survey and analysis of the results were conducted principally by Fabrice Hatem (Invest in France Agency and Ecole de Management de Normandie) and by an UNCTAD team comprising Justin Fisher, Masataka Fujita, Devianee Keetharuth and Jean-François Outreville, under the overall guidance of Anne Miroux.

Assistance was provided at various stages by the following: Emin Akcaoglu, Sarah Dunbar, Kumi Endo, Darya Gerasimenko, Niron Hashai, Niels Heystek, Jovan Licina, Lizanne Martinez, Hafiz Mirza, Alexander Mohr, Shin Ohinata, Rajah Rasiah, Aslak Solumsmoen, Tadelle Taye, Laurent Trupin, Kee Hwee Wee and Dong Wu. The text benefited from comments and feedback by Torbjörn Fredriksson, Gyoyong Liang, and Padma Mallampallay. Katia Vieu provided secretarial assistance and desktop publishing was done by Teresita Ventura. It was edited by Praveen Bhalla.

A panel of location experts was set up to provide qualitative analysis on FDI trends and to contribute to assessing the results of the survey. We would like to thank the participants of this panel: Ash Ahmad, Massaki Amma, David Bridgman, René Buck, Kai Hammerich, Christina Knutsson, Peter Lemagnen, Marc Lhermitte, Paid McMenamin, Charles-Albert Michalet, Mark O'Connell, Robert Pilous, Roel Spee and Mario Ste-Marie.

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## EXECUTIVE SUMMARY

How is foreign direct investment (FDI) likely to evolve over the period 2007–2009? Will its present upswing continue? What are the major driving forces behind this growth, and what risks could hinder it? What are the main locational advantages and disadvantages of potential host countries in attracting FDI and where are the preferred investment locations? What are the most striking patterns of these future FDI flows in terms of host and home countries, activities and modes of entry? To provide answers to these questions, UNCTAD conducted a worldwide survey of decision-makers of some of the world's largest transnational corporations (TNCs) between March and June 2007 (box 1).

### **Box 1. The UNCTAD Survey on World Investment Prospects: objectives and methodology**

The survey<sup>1</sup> aims at providing an understanding of the outlook for future trends in FDI by the largest TNCs for the period 2007 to end 2009, on the basis of the responses of a sample of companies regarding their investment strategies. Such surveys have been carried out by UNCTAD regularly since 1995 (see references and annex 1).

To conduct the survey, a questionnaire was sent in March 2007 to chief executive officers or investor relations office of a representative sample of 1,500 non-financial companies, chosen among the world's 5,000 largest TNCs on the basis of foreign assets. Responses were collected by mail and by e-mail between April and June 2007. Some face-to-face and phone interviews were also carried out in order to gain more in-depth insights into companies' internationalization strategies.

A total of 191 responses were received, representing a response rate of about 13%. Although the distribution of respondents by home region does not necessarily mirror that of the top 5,000 TNCs (e.g. Japanese companies are more represented than firms from other countries – annex tables 6 and 9), it was found that the survey results were not biased by nationality after controlling for the number of responses by home region. The statistical results were submitted to a group of 14 location experts (consultants, academics and members of investment promotion agencies) for comments and analysis on medium-term opportunities, risks and uncertainties affecting FDI.

The main findings from the survey (table 1) can be summarized as follows:

- An expansion of FDI flows and projects by TNCs is anticipated over the period 2007–2009. More than two thirds of respondent companies reported that they planned to increase their FDI expenditures in each of the years of this period. The steady world economic growth expected over the next few years and the availability of internal and external finance will favour an increase in investment flows.

**Table 1. Summary of survey results**  
(Per cent of responses)

<b>A. Global prospects</b>			
<b>FDI growth prospects</b>	<b>Decrease</b>	<b>Remain the same</b>	<b>Increase</b>
Prospects for FDI flows in 2007 compared with 2006	13	19	68
Prospects for FDI flows in 2008 compared with 2007	11	23	66
Prospects for FDI flows in 2009 compared with 2008	9	27	64
Prospects for FDI flows in 2009 compared with 2006	10	19	71
<b>Corporate functions most likely to be relocated or expanded overseas in 2007-2009</b>	<b>No</b>	<b>A little</b>	<b>A lot</b>
1. Production of goods and services	27	27	46
2. Distribution/sales office	32	43	25
3. Logistics/supporting services	42	49	10
4. Research & development	53	30	17
5. Regional headquarters	63	31	7
6. Finance	66	30	4
<b>Major threats to global FDI flows in 2007-2009</b>	<b>Not important</b>	<b>Important</b>	<b>Very important</b>
1. Financial instability	12	60	27
2. War and political instability	13	32	55
3. Change in investment regime	15	57	28
4. Global economic downturn	22	50	27
5. Perceived corruption	24	52	24
<b>Top 6 destinations for FDI in 2007-2009 (per cent of respondent companies that listed each of the countries as one of the top 5 FDI locations)</b>			
1. China		52	
2. India		41	
3. United States		35	
4. Russian Federation		21	
5. Brazil		13	
6. Viet Nam		12	
<b>Greenfield projects and M&amp;As as FDI entry modes into a specific country for the period 2007-2009</b>	Greenfield investments: 66; M&As: 34		
<b>Most important factors influencing location of companies in 2007-2009 (by per cent of TNC responses)</b>			
1. Size of market		21	
2. Growth of local market		20	
3. Access to international/regional markets		10	
4. Stable investment environment		10	
5. Availability of skilled labour force		9	
<b>Most important location criteria by sector, 2007-2009</b>			
<b>Primary sector</b>	<b>Manufacturing sector</b>	<b>Services sector</b>	
1. Access to natural resources	1. Size of local market	1. Size of local market	
2. Stable investment environment	2. Growth of local market	2. Growth of local market	
3. Government effectiveness, incentives	3. Government effectiveness, incentives	3. Stable investment environment	
4. Access to international/regional markets	4. Cheap labour	4. Access to international /regional markets	

Source: UNCTAD survey.

Table 1. Summary of survey results (continued)

	Africa		Asia			Developed regions					
	North Africa	Sub-Saharan Africa	West Asia	South, East and South-East Asia	Latin America and the Caribbean	United States and Canada	EU-15	New EU-12	Other Europe (non-EU-Europe)	Other developed countries	South-East Europe and CIS
Companies that have FDI stocks in the relevant regions in 2006	18	18	24	65	41	70	66	49	27	46	25
Expected change in FDI stocks by region, 2007-2009											
Decrease	3%	5%	3%	2%	2%	6%	8%	2%	4%	5%	0%
No change	75%	78%	66%	24%	50%	37%	35%	36%	61%	55%	61%
Increase	23%	17%	32%	74%	47%	57%	57%	61%	35%	41%	39%
Most attractive business locations in the relevant regions, 2007-2009											
First choice	Egypt (2%)	South Africa (3%)	Turkey (3%)	China (52%)	Brazil (13%)	United States (35%)	United Kingdom (9%)	Poland (6%)	Norway (1%)	Australia (9%)	Russian Federation (21%)
Second choice	Morocco (2%)	Nigeria (2%)	United Arab Emirates (2%)	India (41%)	Mexico (7%)	Canada (4%)	Germany (6%)	Czech Republic (2%)	Switzerland (1%)	Japan (4%)	Ukraine (7%)
Level of priority for each region as an FDI location (0 = not at all important and 4 = very important) 2007-2009	1.08	0.83	1.54	2.95	1.89	2.77	2.66	2.43	1.74	1.98	1.64
Expected modes of entry of FDI by region in 2007-2009 (per cent of respondents indicating greenfield FDI)	69	88	65	76	70	57	50	54	75	50	61

Source: UNCTAD survey.

- The major motives behind the growth of FDI remain market-seeking and, to a smaller but growing extent, resource-seeking (mainly skilled labour, but also raw materials and finance). Efficiency-seeking relocation to countries with low labour costs was also mentioned by respondents, but to a lesser extent

than other factors. Companies are also very responsive to a stable investment environment and to government effectiveness.

- Despite their optimistic views regarding opportunities for international expansion, company executives are sensitive to global risk factors that could potentially hinder the pursuit of their investment strategies. Such risks include geopolitical instability, protectionist policies or uncertainties about world economic growth.
- Regarding host regions, the UNCTAD survey leads to three major findings for the period 2007–2009: (i) companies' preference for South, East and South-East Asia and the new EU-12 as investment locations will increase; (ii) Western Europe (EU-15 and "Other Europe") and North America will continue to attract the largest share of FDI flows; and (iii) a relatively lower degree of preference will be given to other regions overall, notably Africa and West Asia.
- In the view of investors, locational advantages vary widely in the different host regions: North America and Western Europe are seen as offering a stable investment environment and government effectiveness, while South, East and South-East Asia and the new EU-12 offer low-cost labour and markets with growth potential.
- While companies will maintain a preference for their home regions in their forthcoming international investment strategies, they will also give greater priority to other regions of the world. Globalization strategies are thus continuing to gain momentum as compared to regional expansion strategies.
- Overall, greenfield projects<sup>2</sup> are likely to be the preferred mode of entry into a country, but with noticeable differences among host regions. Indeed, most of the projects in developing economies will take the form of greenfield investments. In contrast, the propensity for M&As will be higher for FDI in the main developed economies where there are greater takeover opportunities.
- Regarding the internationalization of corporate functions, investment strategies will involve not only production and distribution, but also administrative functions, call and shared services centres, headquarters and R&D activities.
- In terms of sectoral patterns, new waves of FDI projects can be expected in the primary sector and in many service industries such as utilities and trade. In the manufacturing sector, opportunities should develop at a steady pace in

fields such as those related to the environment and renewable energies, as well as information and communication technologies (ICT), health care and biotechnology.

- The rise in investment flows will emanate not only from the largest TNCs in developed countries, but also, increasingly, from TNCs in emerging economies.
- While companies from all regions are expected to increase their FDI, those from developing Asia show a particularly dynamic potential.

The full report on the survey findings is divided into three chapters: chapter I highlights global trends in FDI and determinants of future FDI flows; chapter II describes the prospective trends by host regions and countries; and finally, chapter III analyses FDI patterns by activities, home countries, modes of entry and the respective roles of globalization and regional integration.

## Notes

- <sup>1</sup> Hereafter referred to as the "UNCTAD survey".
- <sup>2</sup> This refers to the number of projects; in terms of value, mergers and acquisitions (M&As) account for the largest share of FDI flows.

## CHAPTER I

### GLOBAL PROSPECTS: FDI SET TO RISE FURTHER

Responses to the survey suggest a persistent rise in FDI for the period 2007–2009. Factors such as the quest for markets, resources and efficiency, will continue to drive the internationalization of firms. In addition, favourable world economic growth prospects and the availability of financial resources will stimulate investment in the short to medium term. However, companies also display a high degree of sensitivity to global risks, ranging from geopolitical and macroeconomic ones to those linked to a possible rise of protectionist tensions.

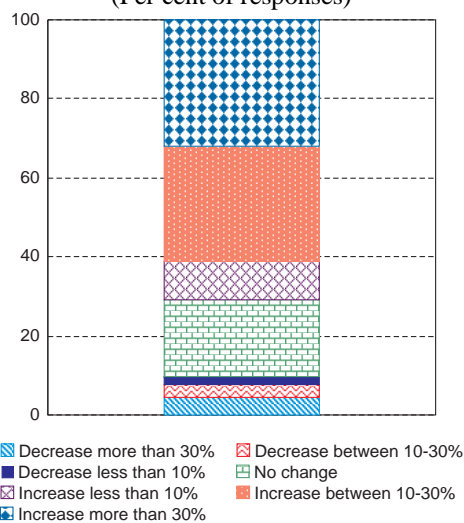
#### 1. Foreseeable rise in FDI flows

According to the UNCTAD survey, the majority of TNCs plan to increase their FDI expenditures over the next few years. The worldwide upturn observed since 2003 should thus continue at least until end 2009.

After a decline in the early 2000s, FDI flows have been rising continuously since 2003, with an acceleration of this trend in 2006. This increase is reflected in various indicators such as cross-border M&As, greenfield projects and the number of jobs created abroad. FDI flows reached more than \$1.3 trillion<sup>3</sup> in 2006, approaching levels similar to the record level observed in 2000 of \$1.4 trillion.<sup>4</sup> The rise in FDI flows has largely taken place through an increase in the number and value of cross-border M&As. The number of greenfield projects has also grown.<sup>5</sup>

According to the UNCTAD survey, this trend should continue up to 2009. Most of the responding companies (70%) expected to increase in their FDI expenditures between 2006 and 2009 (figure 1). For about 32% of companies, this increase should be quite large (i.e. more than 30%). On the other hand, only 9% of the companies anticipate a decrease in their investment flows. The overall positive trend is confirmed by the

**Figure 1. Expected change in FDI flows between 2006 and 2009**  
(Per cent of responses)

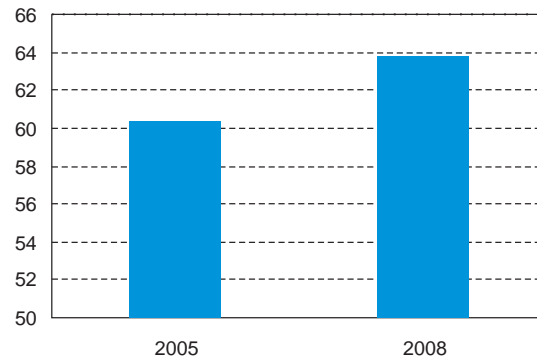


Source: UNCTAD survey.

views of location experts, most of whom anticipate growing FDI flows till end 2009.

This can be attributed to two facts: a global increase in total investment expenditures by companies, and a growing share of investments abroad in total investment. For the companies responding to the survey, this share could rise from 60% to 64% between 2005 and 2008 (figure 2).

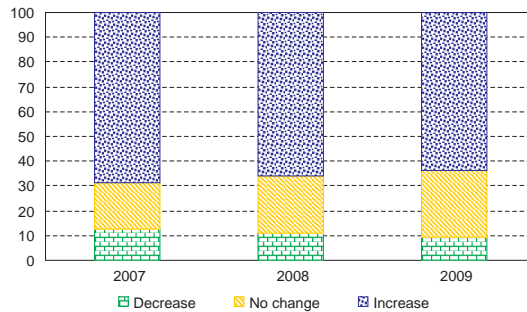
**Figure 2. Share of FDI in total investment, 2005, 2008**  
Average ratio of FDI of companies to their total investment (%)



Source: UNCTAD survey

There could be consistent growth in FDI flows until end 2009, as a large proportion of companies expect to increase their investments abroad over this period:

**Figure 3. Annual changes in FDI flows, 2007–2009<sup>a</sup>**  
(Per cent of responses)



Source: UNCTAD survey.

<sup>a</sup> Changes in relation to the preceding year.

68% of them plan to do so in 2007, 66% in 2008 and 64% in 2009 (figure 3). On the other hand, only 13% envisage a reduction of their investments abroad in 2007, 11% in 2008 and 9% in 2009. The percentage of companies that anticipate stable levels of investment from one year to the next increases over time, from 19% in 2007 to 23% in 2008 and 27% in 2009.



## 2. Structural and short-term conditions favour FDI growth

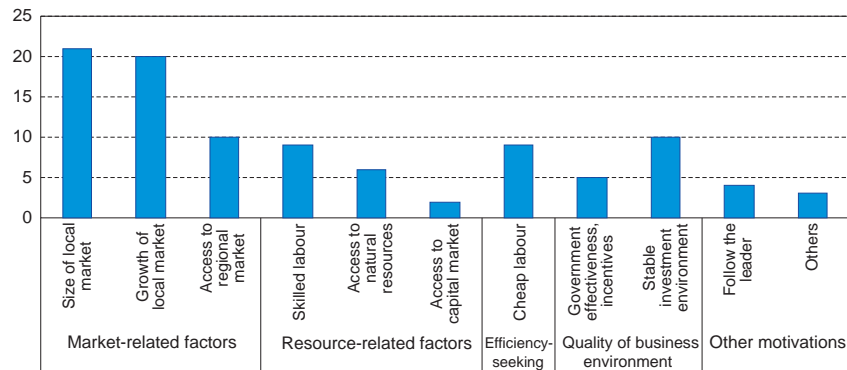
The possible rise in FDI flows for the period 2007–2009 (both in absolute terms and compared to total investment) can be explained by three major factors: a continuation of the prevailing long-term trends that are conducive to the internationalization of companies; a short- to medium-term economic outlook, characterized by sustained growth and availability of financial resources; and the emergence of new sources of and opportunities for investment (discussed in chapter III).

### *a. An ongoing quest for markets, resources and efficiency*

Access to markets will remain by far the most significant driving force for FDI, followed by resource-seeking strategies and cost-control.

There are three main motives for companies to internationalize their production activities: market-seeking, resource-seeking and efficiency-seeking. In addition, the existence of open, pro-business and stable investment environments in a growing number of locations encourages foreign investment. Results of the UNCTAD survey show that all of these factors will continue to be at work in the coming years, albeit with varying degrees of importance (figure 4).

**Figure 4. Location criteria in order of importance, 2007–2009**  
(Per cent of responses)



Source: UNCTAD survey.

**Market-related factors.** Most TNCs, including the biggest ones, are still very concentrated on their home market in terms of sales (Rugman and Verbeke, 2004). They intend to keep expanding their sales abroad to take advantage of the opportunities offered by the world market. Responses to the UNCTAD survey confirm that access to large and fast growing markets will remain the major driving force behind FDI growth in different ways:

- *Size of the local market* was mentioned as a major location determinant in 21% of responses (figure 4). Predictably enough, large economies such as China, the Russian Federation and the United States seem to be especially favoured by this criterion (see also tables 5 and 6);
- *Growth of the local market* was mentioned in 20% of responses, with a special focus on emerging economies such as Brazil, China and India;
- *Access to the regional market* was the third most important criterion, mentioned by 10% of the companies. It was cited as especially important for locating in countries that could provide export bases for sales to large markets, such as Poland as a base for the markets of Western Europe.

The fact that the three most cited factors are all market-related helps explain why developed countries remain the most attractive to FDI: together they account for about three quarters of world GDP (World Bank, 2007b). However, investors' interest in growing markets largely explains the willingness of companies to increase their presence in developing countries, as these countries' share in world GDP could rise to 33% by 2030 (World Bank, 2007b).<sup>6</sup>

**Resource-related factors.** The quest for resources is becoming an increasingly important motive for companies' internationalization. Overall, access to various kinds of resources – skills, natural resources or financial markets – was mentioned as a major location criterion by about 17% of the respondents.

- *Access to skilled labour* was the most frequently mentioned among the various types of resource-seeking motivations, with 9% of responses. Survey responses and interviews with location experts suggest that an increasing number of companies now consider access to qualified and creative manpower as an important determinant of competitiveness. Consequently, a large share of FDI is influenced by (or even dedicated to) the search for qualified manpower. The most striking example is the ongoing internationalization of corporate R&D through the establishment or acquisition of research centres abroad (chapter III).

- Access to *natural resources* was cited as a major location criterion by 6% of respondents. It is a major feature of the attractiveness of sub-Saharan African countries, Australia, Latin America and West Asia. This result can be put in perspective along with another finding of this survey: the buoyant growth prospects for FDI in the primary sector over the next few years (UNCTAD, forthcoming). As pointed out by a number of experts who provided comments and analysis for the UNCTAD survey, increasing demand for natural resources – especially oil and gas, and metallic minerals – should trigger a new wave of investments in those fields.
- Finally, *access to capital markets and financial services* was considered a major location criterion in 2% of cases, with a special focus on the United Kingdom the United States, and developed economies more generally.

**Efficiency-seeking.** The search for low-cost labour, a major consideration for maintaining cost-efficiency in certain industries, remains an important location determinant, quoted by almost 9% of respondents. Unsurprisingly, survey respondents identified low-cost labour as a factor favouring investments in such regions as East, South and South-East Asia, the new EU-12, North Africa, and, to a lesser extent, Latin America and sub-Saharan Africa. It was not mentioned as a favourable factor for investment in Western Europe and North America (chapter II).

Location experts suggested that relocation of labour-intensive manufacturing activities from developed countries to low-cost regions would remain at the top of companies' agendas. The latest survey of Japanese manufacturing companies by the Japan Bank for International Cooperation (JBIC, 2007) shows, for instance, that developing Asian countries and, to a lesser extent, South-East Europe and the CIS, as well as some new EU-12 members, could remain major destinations for efficiency-seeking Japanese investment abroad in the immediate future. As wage increases are taking place in many countries that experienced waves of relocation (for example, the Czech Republic), labour-intensive activities might migrate once again to countries with lower wages that have more recently opened up to FDI.

Apart from the three main motives analysed above, companies consider **the overall quality of the business environment** as an important location determinant. Stability of the investment environment and government effectiveness<sup>7</sup> were quoted as relevant criteria in 10% and 5% of the responses respectively. Western Europe and North America were stated as the most attractive regions by these criteria, although the new EU-12 countries are also increasingly recognized for their improvement in the quality of their business environment (chapter II).

Many analyses converge on the diagnosis that the climate for foreign investment has consistently improved in all regions in recent years, partly due to the policy reforms implemented by governments. The number of new regulations more favourable to foreign investment has consistently exceeded that of more restrictive ones over the past few years, although restrictive tendencies have been slightly on the rise since 2001 (table 2). The internal business climate of countries has improved as well. A yearly report issued by the World Bank points to a number of recent improvements in the regulatory and administrative environment in many countries (World Bank, 2006). The growing competition for international projects is one trigger for additional reforms aimed at further improving the attractiveness of host countries. All these factors may lead to a greater sense of safety among companies regarding foreign locations, and it may reduce companies' perception of risks with respect to FDI.

Table 2. Regulatory changes regarding FDI, 1992-2005

Item	Average 1992-2000	2001	2002	2003	2004	2005
Number of countries that introduced changes in their investment regimes	61	71	70	82	102	93
Number of regulatory changes	122	207	246	242	270	205
More favourable to FDI <sup>a</sup>	115	193	234	218	234	164
Less favourable to FDI <sup>b</sup>	7	14	12	24	36	41

Source: UNCTAD 2006.

<sup>a</sup> Includes liberalizing changes or changes aimed at strengthening market functioning, as well as increased incentives.

<sup>b</sup> Includes changes aimed at increasing control, as well as reducing incentives

Finally, **competitive pressure** is also an important factor in the internationalization of production. With the international integration of markets, companies seek to become or remain significant players on the world stage by taking steps to enter or expand their activities in promising foreign market and/or acquiring strategic assets through takeovers or mergers. This triggers internationalization, restructuring and concentration in many industries, largely through M&A operations (chapter III). It also leads a substantial number of companies to follow their industry leader whenever it decides to set up operations in a foreign location. This last strategy was quoted as a major location determinant in 4% of responses to the UNCTAD survey.

*b. A favourable short-term macroeconomic outlook*

The world economy is going through a period of growth and financial abundance, prompting positive expectations among business executives and creating conditions favourable to new international projects.

Global economic growth has been sustained at relatively high levels over the past five years, a trend confirmed by growth in 2006 as well (table 3). According to the latest forecasts issued by various international institutions such as the International Monetary Fund (IMF, 2007), the World Bank (2007b), and the OECD (2007), and despite recent turmoil on the financial markets, the world economy still looks well set for continued growth in 2007-2008. While the projected annual growth rates for developing countries are expected to be above 6%, in developed economies they are expected to reach levels of over 2.5% (table 3).

**Table 3. World economic growth and growth prospects, 2005-2008**

Source	Region	GDP (annual growth rate %)			
		2005	2006	2007	2008
IMF	<b>World</b>	4.9	5.4	4.9	4.9
	<i>of which:</i>				
	Developed economies	2.5	3.1	2.5	2.7
	Developing economies	7.5	7.9	7.5	7.1
	<i>Memorandum item:</i>				
	<b>World trade volume</b>	7.4	9.2	7.0	7.4
World Bank	<b>World</b>	4.7	5.1	4.5	4.6
	<i>of which:</i>				
	High-income economies	2.7	3.1	2.4	2.8
	Developing economies	6.6	7.0	6.4	6.1
OECD	<b>OECD countries</b>	2.6	3.2	2.7	2.7

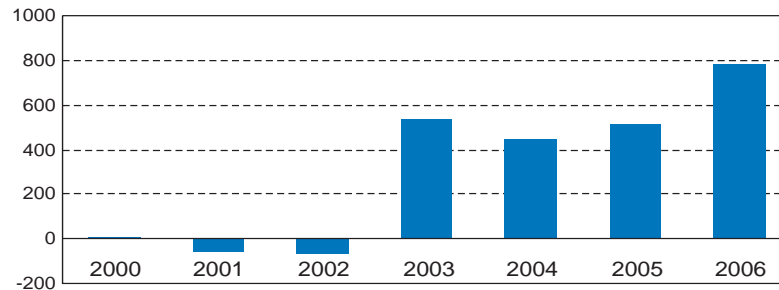
Source: IMF 2007, World Bank 2007b and OECD 2007.

This favourable macroeconomic outlook is consistent with the optimistic views among business circles, with regard to the present economic situation and prospects, as shown by various surveys published by international consulting companies (CESifo, 2007; PricewaterhouseCoopers, 2006; McKinsey, 2007). These positive prospects will

encourage companies to invest all the more, given the availability of financial resources, both externally and internally:

- *Self-financing.* Taking advantage of the dynamism of the market, many companies today enjoy a sound financial situation: net income and profits have been on the rise in recent years, boosted by increased sales. In the United States, for example, profits of the 500 largest corporations rose from a mere \$8 billion in 2000 to reach \$785 billion in 2006 (figure 5).

**Figure 5. Profits of top 500 United States companies, 2000–2006**  
(Billions of dollars)



Source: *Fortune* (various years): "America's largest corporations".

- *External financing.* The low cost of capital and its ample availability at both the domestic and international levels facilitate the external financing of investment programmes. Interest rates should remain relatively low for the 2007-2008 period (IMF, 2007). Equity markets are close to record levels, long-term bond yields have remained below long-term trends and risk spreads have narrowed in most markets. The multitude of fund-raising techniques (e.g. hedge funds, mutual funds, private equity funds)<sup>8</sup> facilitates the financing of all types of investments – greenfield and M&As – even if they also entail new risks (see also below).

Consequently, sustained growth is expected in worldwide investment expenditures. According to the World Bank (2007b), the annual growth rate of fixed capital formation could reach 5.4% in the newly industrializing Asian economies for the period 2007–2008 (more than 2% higher than the 2005–2006 average) and 2.7% in the developed economies (1.5% below the 2005–2006 average).<sup>9</sup>

### 3. Does the perception of potential risks influence international investment strategies?

The high level of risk awareness expressed by companies does not hinder their investment plans for the foreseeable future.

Respondents to the UNCTAD survey anticipate a sustained growth in FDI flows until 2009. But the question arises as to whether a major event – or a combination of events – might undermine such optimism, as was the case in previous periods of FDI recession (such as in 2001–2002). The UNCTAD survey attempted to examine the major potential risks, grouped into three categories: geopolitical (e.g. war or terrorism), macroeconomic (e.g. impact of volatile oil prices and financial instability), and institutional (e.g. changes in investment regimes and government effectiveness). Company executives were asked to indicate whether or not each of these risks could be an important hindrance in their investment decisions for the three years ahead. Location experts interviewed for the survey were also asked the same question.

Although company executives perceived a rather high degree of potential risk in all three categories, geopolitical risks were considered the most significant, followed by those linked to financial instability and changes in investment regimes. These concerns, however, seemed unlikely to dissuade them from increasing their investment efforts, but could lead them to focus more on risk management strategies. Some of those risks are explored below in further detail.

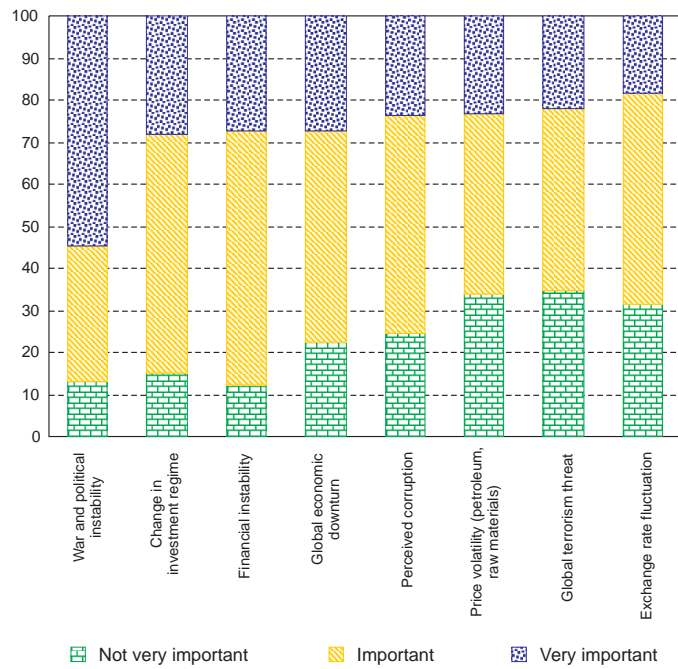
#### *Considerable awareness of geopolitical and financial risks among companies*

Responses by companies to the UNCTAD survey question on risks (figure 6) highlight the following points:

- There appears to be a high level of awareness regarding a wide range of risks that could potentially hinder companies' investments and business: all the risk factors listed in the survey were considered "important" or "very important" by a large majority of companies (figure 6). Four risk factors considered

“important” or “very important” by more than three quarters of the companies are: financial instability, global economic downturn, changes in investment regimes, and war and political instability. Even for the less frequently mentioned risks, such as global terrorism threats and exchange rate fluctuations, more than 60% of companies considered them “important” or “very important”.

**Figure 6. Importance of risk factors for FDI decisions, 2007–2009**  
(Per cent of responses)



Source: UNCTAD survey.



- On the other hand, a sense of emergency was relatively limited among the respondents. In the majority of responses, risks were qualified as only “important” (in a range of 40% to 60% of answers, depending on the question), rather than “very important”. The only exception was “war and political risks”, rated “very important” by over 50% of respondents.

Location experts expressed relatively optimistic views regarding the level of the global risks that could affect FDI flows over the next three years. While several of them recognized that the risks of terrorism and war are far from negligible, especially in West Asia, the majority considered that investment in the short term is unlikely to be adversely affected by those risks. In particular, they believed the probability of a protectionist backlash affecting FDI in the short to medium term, to be relatively low despite growing concerns on this issue.

Some insights are provided below on two of the major risks mentioned by companies: changes in investment regimes and macroeconomic/financial instability.

*Is there a risk of a protectionist wave against FDI in the short term?*

Respondents to the UNCTAD survey expressed some concern regarding the possible rise of protectionist tensions in both host and home countries. More than 80% of companies mentioned that the risk of negative changes in investment regimes is “important” or even “very important” for the short term. According to location experts interviewed for the survey, this risk is not negligible, mainly due to the following four factors: a general climate of fear against globalization in some quarters, fuelled by social and political concerns; rising hostility against the acquisition of local companies by foreign interests, especially private equity and hedge funds, which are accused of short-term profit-seeking strategies detrimental to job preservation and long-term development; in many developing countries (notably in Latin America), growing sensitivity over the conservation and national control of natural resources; and finally, in developed countries, hostile reactions linked to the fear of offshoring to developing countries and its impact on employment at home.

Such concerns have fuelled some negative reactions towards FDI, as illustrated by recent events such as the public opposition in the United States to the proposed takeover of the management of six United States port terminals by DP World (United Arab Emirates) (UNCTAD, 2006), or the renegotiation of contracts with TNCs in the extractive industries in Latin America and the Russian Federation. Although these events are limited to a small number of highly publicized and emblematic cases, and do

not impair the global increase of FDI flows, they may send negative signals to investors.

Nevertheless, the evidence on regulatory measures shows no reason for concern. While it is noted that some changes in 2005 were less favourable to FDI, many of which were related to the extractive industries and concentrated in a few countries, the majority of changes were in the direction of favourable to FDI (table 2).

*How robust is the present world economic growth?*

A relatively high percentage of respondents pointed out the existence of macroeconomic and financial risks: more than three quarters of them considered a global economic downturn as a major risk in the years ahead, and about 90% expressed concerns about the potential impact of financial instability on FDI flows (figure 6).

Various recent economic outlook reports confirm the existence of these risks. According to the IMF (2007), at present the major sources of risk for world economic growth are (in order of importance): a sharper slowdown in the United States if that country's housing sector continues to deteriorate;<sup>10</sup> a revival of inflationary pressures, particularly in the event of another spike in oil prices in connection with geopolitical tensions in West Asia; reducing risky assets if financial market volatility were to increase from historically low levels; and a disorderly unwinding of large global imbalances (especially related to the United States external trade deficits and Chinese surpluses and possible adjustments in currency exchange rates). In addition to these risk factors, the location experts cited a possible overheating and slowdown of both the Chinese and Indian economies.

However, international experts generally see the potential short-term impact of those risks as rather limited.<sup>11</sup> Even in the worst-case scenario considered by the IMF, annual world growth would remain at around 4%. This optimistic point of view is shared by most of the location experts for the UNCTAD survey.

## Notes

- <sup>3</sup> All figures are in United States dollars unless otherwise stated.
- <sup>4</sup> For a detailed discussion and final data for 2006, see UNCTAD, forthcoming.
- <sup>5</sup> According to the Locomonitor database compiled by OCO Consulting, the number of international greenfield projects announced in the world was around 12,000 in 2006 – an increase of 13% over 2005.
- <sup>6</sup> For a detailed analysis by host regions and countries, see chapter II
- <sup>7</sup> Government effectiveness combines the perception of the quality of public service provision, the quality of the bureaucracy, the competence of civil servants, the independence of the civil service from political pressures, and the credibility of the government's commitment to policies.
- <sup>8</sup> For a more in-depth analysis on this issue, see UNCTAD, 2006 and UNCTAD, forthcoming.
- <sup>9</sup> Other studies confirm the increase in gross domestic capital formation (IMF, 2007; OECD, 2007)
- <sup>10</sup> As illustrated by the recapitalization crisis in the United States financial market in mid-2007.
- <sup>11</sup> According to the IMF, “overall risks to the outlook seem less threatening than six months ago but remain oriented towards the down side, with concern about financial risks” (IMF, 2007).



## CHAPTER II

### FDI PROSPECTS BY HOST REGION <sup>12</sup>

Regarding FDI prospects by host region, the survey points to three major findings: first, companies will increase their level of preference for South, East and South-East Asia as well as for the new EU-12 countries as investment locations; second, Western Europe and North America will continue to be the leading destinations for investment flows; and, finally, other regions, notably Africa and West Asia, will be given a lower degree of preference. Following an examination of overall trends and prospects by region, this chapter presents details of the specific situation in each of the regions of the world.

#### 1. Overall results of the survey

##### a. Current trends: evolving patterns in the international division of labour

Regionalization and new patterns in the international division of labour between developed and developing countries have been the driving forces behind the recent rise in FDI flows.

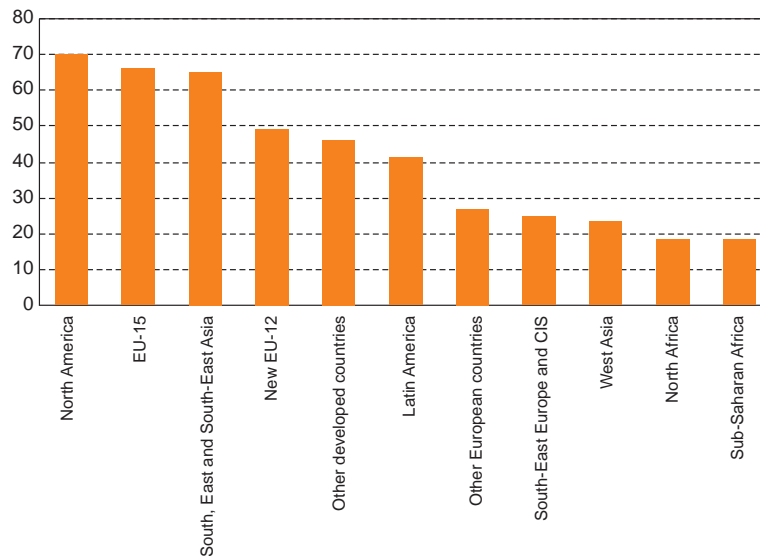
In recent years, the regional distribution of inward FDI has been characterized by a rapid growth in FDI flows and stocks in the fast-growing economies in Asia and the new EU-12, while Western Europe and North America still rank among the top destination regions. Responses to the UNCTAD survey largely confirm that pattern and throw further light on it:

- Of the responding TNCs, 65% had already invested in South, East and South-East Asia in 2006, a percentage not far from that observed for the EU-15 and North America (figure 7). Their presence in Africa – both North and sub-Saharan – South-East Europe and the CIS and West Asia was considerably smaller, with less than 25% of respondents having already invested there.<sup>13</sup>
- Results of the survey show a high concentration of TNCs in their respective home regions. For instance, companies from European countries are more present in other European countries than are other companies. Similarly, North American companies are better represented in North America (through cross-border investments between the United States and Canada) than their European and Asian counterparts (table 4).

FDI in labour-intensive manufacturing activities is generally concentrated in low-wage developing countries and transition economies, while Western Europe and North America remain attractive for market-oriented activities, knowledge-intensive manufacturing industries and high-value-added service activities.<sup>14</sup> In Europe, for instance, Western European countries host a large proportion of projects in biotechnology, software, health products and the

services sector as a whole, while the new EU-12 countries have achieved a better performance in textiles and garments, household electronics, automotive and other consumer goods (annex figure 1).

**Figure 7. Proportion of companies with FDI in different regions, 2006**  
(Per cent of respondents)



Source: UNCTAD survey.

As newcomers, such as Viet Nam, Ukraine and members of the CIS countries, are beginning to attract FDI, location opportunities available to companies are increasing rapidly. Competition between host countries is thus becoming fiercer, notably in three fields: first, in labour-intensive manufacturing, where the “flying-geese pattern”<sup>15</sup> is evident in various parts of the world; second, in service industries and some corporate functions, such as shared services and customer support centres, which are resorting to offshoring; and finally, in knowledge-based activities, where the attractiveness of some emerging economies is gaining momentum, challenging the former monopoly of North America and Western Europe as preferred investment locations. For instance, in Europe, the share of the new EU-12 countries in projects in high-value-added industries is growing rapidly (annex figure 2).

Table 4. Companies with FDI stocks in the host regions, by home regions, 2006  
(Per cent of respondents)

Host region	All respondents	Home region of the respondent:			
		Developing countries	Europe	North America	Other developed countries
<b>Developed countries</b>					
North America	70	40	72	84	83
EU-15	66	20	85	74	71
New EU-12	49	17	69	47	46
Other European countries	27	9	39	21	23
Other developed countries	46	31	45	37	69
<b>Developing countries</b>					
North Africa	18	9	32	21	8
Sub-Saharan Africa	18	14	27	16	12
West Asia	24	14	31	26	23
South, East and South-East Asia	65	51	59	63	83
Latin America	41	14	43	53	52
<b>South-East Europe and CIS</b>	25	11	32	21	23

Source: UNCTAD survey.

**b. Future trends: FDI in South, East and South-East Asia on the rise, but developed economies remain attractive**

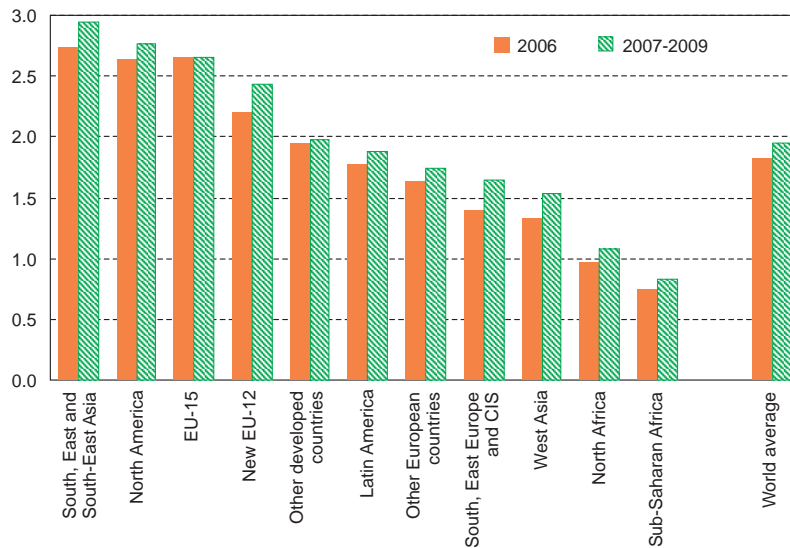
Investors' strategic priorities indicate a growing preference for South, East and South-East Asia, the new EU-12 and the transition economies, while Western Europe and North America remain very attractive. On the other hand, Africa as a whole continues to be a marginal destination.

Will there be any major shifts in the geographical orientation of investment in the next three years? Will Africa, the CIS and West Asia be relatively less marginalized as FDI destinations? Is the attractiveness of South, East and South-East Asia (and especially China) sustainable? Will developed countries in Europe and North America continue to be the most favoured destinations for FDI? Three questions were asked in the survey to throw light on these points: the first one focused on the strategic regional preferences of companies, the second on the prospects for FDI by host regions, and the

third on the attractiveness of individual countries. The following were the main findings from the responses:

- Globally, the hierarchy of preferences by region should remain practically unchanged during the 2007–2009 period as compared to 2006 (figure 8): South, East and South-East Asia top the list, followed by North America and the EU-15, while West Asia, North Africa and sub-Saharan Africa continue to feature lowest among companies' preferences (figure 8).

**Figure 8. Investment preferences by host region, 2006 and 2007–2009**  
(Average score)<sup>a</sup>



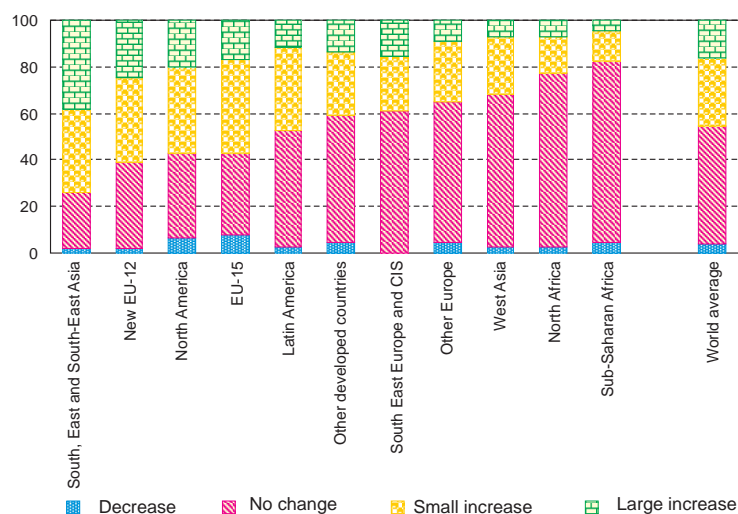
Source: UNCTAD survey.

<sup>a</sup>Note: (0=Not at all important, 4=Very important)



- FDI prospects are especially bright in regions such as South, East and South-East Asia, as well as the new EU-12. These are the regions for which TNCs indicated the largest increase in preferences for the coming period (figure 8). Their attractiveness is also confirmed by the fact that the largest proportion of companies reported considering an increase in their investments there (figure 9).
- Prospects for Latin America and West Asia are less favourable. The rise in preference for West Asia indicated by the survey (figure 8) is not confirmed in terms of expected increase in companies' investments (figure 9). As for Latin America, there are moderate improvements in terms of both preferences and TNCs' investment plans.

**Figure 9. FDI prospects by host region, 2007–2009**  
(Per cent of responses)



Source: UNCTAD survey.

- Similarly, indicators are not uniform for North America and the EU-15, despite an overall increase in preference for the region. For instance, a relatively large percentage of respondents reporting they propose to increase their investments in these two regions is accompanied by a somewhat larger than average share of companies that are considering reducing their investments there (figure 9).
- Finally, the increase in both preferences and actual investments in other developed countries and regions such as North Africa and sub-Saharan Africa are below average. Those regions might thus remain marginal in terms of FDI inflows.

## 2. Detailed results by host region

### a. Prospects for developing countries: South, East and South-East Asia is the most preferred regional location

South, East and South-East Asia, which offers major locational advantages such as market growth and size, cost and quality of labour, is consolidating its position as the most preferred region of international investors.

*South, East and South-East Asia* is increasingly considered a preferred location, with 65% of company respondents already investing there (figure 7). The region is set to maintain its leading position among host regions for TNC investments until end 2009, and could even reinforce its lead over the next preferred regions: the EU-15 and North America. This is borne out by the fact that the highest percentages of companies (39%) are considering substantially increasing their investment expenditures in this region (figure 9). Growth of domestic markets is the most significant locational asset of this region, followed by the size of those markets, access to the regional market and low labour costs (table 5). On the other hand, the stability of the investment environment and government efficiency are not regarded as major factors of attraction for investors.

South, East and South-East Asia include the two leading host countries for FDI location until 2009: China and India (figure 10). In fact, almost two thirds of the companies that participated in the survey stated that they had plans to invest in either or both of these two economies. While, in the view of investors, they share the same advantages in terms of labour costs and size/growth of market, India ranks higher in terms of skilled labour (table 6). Location experts for the UNCTAD survey also expressed optimism for investment prospects in these countries, stressing the fact that

India and China are among the few developing countries in the world where it is possible to find three major kinds of locational advantages (low costs, markets and technological capabilities). The experts thus consider an increase in FDI projects as the most probable scenario, including in medium-technology manufacturing in China and in high-value-added services in India. Moreover, these projects could be increasingly oriented towards new regions in these countries (e.g. Central China, mid-sized towns in India), as costs are rising in established locations such as Bangalore (India) and Shenzhen or Shanghai (China). On the other hand, according to investors, these countries still present constraints in terms of their investment environment, government effectiveness and access to capital markets (table 6). Location experts confirmed the existence of some negative elements, such as the lack of protection of intellectual rights in China or the high turnover of manpower in some areas in India.

**Table 5. Factors attracting investment by region, 2007-2009**  
(Per cent of the total number of responses for all factors in the region)

Host region / Location criteria	Follow the leader	Skilled labour	Low-cost labour	Size of local market	Access to capital market	Access to natural resources	Access to regional market	Growth of local market	Government effectiveness, incentives	Stable investment environment	All Others	100 factors
<b>Developed</b>												
North America	2	11	-	24	7	6	10	12	7	20	2	100
EU-15 and other European countries	3	11	-	20	6	4	11	12	11	19	4	100
New EU-12	3	12	12	12	2	8	13	19	6	12	1	100
Other developed countries	2	9	-	17	2	15	7	13	7	22	6	100
<b>Developing</b>												
North Africa	-	4	17	17	-	25	13	21	-	4	-	100
Sub-Saharan Africa	6	-	6	15	-	23	9	18	12	12	-	100
West Asia	3	3	3	27	7	15	5	25	5	7	-	100
South, East and South-East Asia	6	4	8	25	1	5	12	31	1	3	4	100
Latin America	4	12	6	16	1	10	11	21	7	7	5	100
South-East Europe and CIS	6	4	8	25	1	5	12	31	1	3	4	100
<b>World average</b>	<b>4</b>	<b>9</b>	<b>9</b>	<b>21</b>	<b>2</b>	<b>6</b>	<b>10</b>	<b>20</b>	<b>5</b>	<b>10</b>	<b>3</b>	<b>100</b>

Source: UNCTAD survey.

Investors also identified other attractive destinations in Asia: Malaysia, Thailand and, in particular, Viet Nam. Ranked sixth in the countries preferred by investors (figure 10), Viet Nam has a very good reputation in terms of quality and cost of labour (table 6).

**Table 6. Ten most attractive countries for FDI by factors favouring investment, 2007–2009**  
(Per cent of responses for a given country)

Host country / Location criteria	Follow the leader	Skilled labour	Low-cost labour	Size of local market	Access to capital market	Access to natural resources	Access to regional market	Growth of local market	Government effectiveness, incentives	Stable investment environment	Others	All factors
China	6	8	14	26	1	3	7	28	2	4	1	100
India	5	13	14	24	-	1	7	29	1	4	1	100
United States	2	11	-	25	7	6	10	12	6	19	2	100
Russian Federation	7	4	5	29	1	4	8	36	-	3	4	100
Brazil	3	10	5	24	-	7	8	29	5	3	5	100
Viet Nam	8	14	27	14	-	2	8	17	3	3	3	100
United Kingdom	2	8	-	20	8	6	9	9	13	20	5	100
Australia	-	11	-	8	3	19	8	11	8	25	6	100
Mexico	5	19	12	9	-	2	14	12	12	12	4	100
Poland <sup>a</sup>	7	14	11	14	4	4	9	16	7	14	-	100
Germany <sup>a</sup>	9	18	-	21	6	-	9	12	3	23	-	100
<b>World average</b>	<b>4</b>	<b>9</b>	<b>9</b>	<b>21</b>	<b>2</b>	<b>6</b>	<b>10</b>	<b>20</b>	<b>5</b>	<b>10</b>	<b>3</b>	<b>100</b>

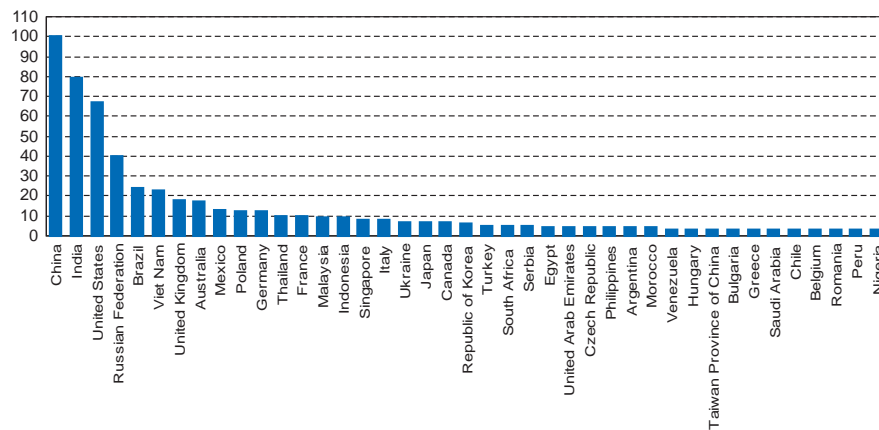
Source: UNCTAD survey.

<sup>a</sup> Poland and Germany are both ranked 10th.

For Latin America and the Caribbean, the investment outlook is less promising. Its ranking, as compared to other regions, is intermediate for practically all the responses to the survey. The percentage of company respondents declaring they had already invested there (40%) is close to the world average (figure 7), as is the level of preference of companies for this region (figure 8) and the percentage of TNCs intending to increase their investments (47% as against 45% for the average of all regions, figure 9). As in the case of South, East and South-East Asia, the size and growth of domestic markets were the most frequently cited reasons for investing in Latin American countries, but skilled labour and access to natural resources were also considered positive factors, although by a relatively lower proportion of respondents (table 5). On the other hand, the stability of the investment climate and access to low-cost labour were not considered major locational assets for the region. More than 20 companies included Brazil in the list of the most attractive locations for future investment, ranking it among the top five destinations; but Mexico was the only other

Latin American country mentioned among the 20 most attractive locations in the world (figure 10).

**Figure 10. Most attractive economies for the location of FDI, 2007–2009**  
(Total number of responses)



Source: UNCTAD survey.

Indicators for West Asia are more mixed, but overall they point to a relatively reserved forecast for the three years ahead. This region is characterized by a rather low level of FDI: of the companies surveyed, only 24% of respondents stated they had already invested there (figure 7). The priority given to this region is also rather low, as it is ranked only ninth (out of 11 regions listed) in the hierarchy of preference for 2006 (figure 8) – a ranking which is not expected to improve by 2009. Consequently, the percentage of companies considering an increase in their investments in the region is relatively low: only 32% as compared to the average of 45% (figure 9). Growth and size of the local market and access to natural resources were the most frequently cited reasons for investing in the region, but low labour costs, availability of skilled manpower and a stable investment environment were the least cited. The table shows access to the regional market and government effectiveness as even less cited than a stable investment environment. Turkey and the United Arab Emirates are the countries most favoured by investors in West Asia, but with a rather modest world ranking (figure 10).

Africa as a whole (including North and sub-Saharan Africa) remains at the bottom of the list for all indicators: percentage of companies that have already set up operations in the region (figure 7), present and future levels of preference (figure 8), and anticipated increase in investment flows (figure 9). Access to natural resources and markets, and, for Northern Africa only, access to low-cost labour and international markets, were among the most frequently cited reasons for investing in these regions, but with a low number of responses; and skilled labour was practically never mentioned (table 5). South Africa, Egypt, Morocco and Nigeria are, in that order, the most attractive countries in the region (figure 10), but with a modest ranking in the world as a whole. Nevertheless, there are important FDI opportunities in the region, as illustrated by the recent increase in investment flows into North Africa. This is largely due to the re-channelling of Gulf countries' investment outflows from the United States to new destinations in the Arab world (such as Morocco) for the financing of real estate and infrastructure projects, to ongoing privatization processes – especially in the services and financial industries – and, to a lesser extent, to the development by TNCs of export-oriented activities in countries such as Egypt, Morocco and Tunisia to supply the European and West Asian markets (UNCTAD, 2006; UNCTAD, forthcoming).

**b. FDI in the new EU-12, South-East Europe and the CIS is on the rise**

The regions registering the most marked increase in investors' preferences for FDI locations in the near future will be the new EU-12 and South-East Europe and the CIS.

The *new EU-12 countries*<sup>16</sup> have already begun to attract large international projects. Nearly half of the respondents had already invested there (figure 7), and the region ranks fourth in the world as a preferred investment location for TNCs (figure 8). A large proportion of the companies (about 61%) indicated that they were considering increasing their investments there over the period 2007–2009 (figure 9). In the investors' views, the greatest locational assets of the region are growth of local markets, access to international markets (e.g. Western Europe), government effectiveness, access to skilled and cheap labour, size of local markets and a stable investment environment. Poland ranks tenth among the most attractive investment destinations worldwide (figure 10), while Hungary, the Czech Republic, Romania and Bulgaria were also mentioned by some companies as attractive investment locations.

So far, *South-East Europe and the CIS* region has not attracted large amounts of investments: only 25% of respondents reported having already set up operations there (figure 7). The region ranks eighth (out of 11) in the preference list of investors. However TNCs intend to increase substantially their preference for this region in the

next few years (figure 8). Growth and size of local markets, access to regional markets and cheap labour were stated as the most significant locational advantages of countries in the region, while the investment climate and government efficiency still lag far behind (table 5). The Russian Federation is ranked fourth among the most preferred countries worldwide, while some respondents also mentioned Ukraine and Serbia as attractive locations (figure 10). The ongoing improvement of the investment climate in the latter countries (World Bank, 2006) could enhance interest among foreign investors for these upcoming locations.

### c. The main developed regions still remain very attractive

Market size, quality of resources and a stable investment climate ensure that the EU-15 and North America will remain among the most preferred locations for FDI.

The main developed regions all present very similar profiles in terms of locational assets and handicaps. Foreign companies continue to invest there to take advantage of the size of the domestic markets, the quality of the labour force, facility of access to financial markets, effectiveness of the governments and stability of the business climate. On the other hand, these regions are handicapped by their relatively high labour costs and moderate growth prospects, compared to some of the other regions. All developed countries thus face constant relocation pressures on labour-intensive activities, and the need to make up for lost jobs in traditional manufacturing by shifting to innovative and high-value-added activities and services. But the overall investment prospects for the period 2007–2009 vary significantly from one developed region to another.

North America is already a preferred location for investors, with 70% of the respondents having activities there (figure 7), and the region should continue to occupy the second place worldwide as a preferred investment location for the period 2007–2009 (figure 8). Of all the respondents, 57% stated they intended to increase their investments in this region – a larger percentage than the world average (figure 9). The United States is ranked the third most attractive location for FDI in the world, after China and India (figure 10). Canada was also singled out as a fairly attractive location for FDI. However, this positive outlook is weakened somewhat by the fact that a fairly significant percentage of companies (6%) also stated their intention to reduce their investments there.

The EU-15 has a similar profile: a high percentage of companies have already set up activities in the region (figure 7); investors rank it as the third most preferred location in the world, despite a rising gap with the two regions ranked higher: South, East and South-East Asia and North America (figure 8). While a large majority of



companies mentioned that they intended to increase their FDI in the region over the period 2007–2009, a non-negligible number of them (8%) were considering reducing their investments there (figure 9). Respondents listed the United Kingdom, Germany and France among the 12 most attractive countries worldwide, but none of them was listed among the top five (figure 10).

Other Europe, a group which includes European countries that are not part of the EU, of which Switzerland and Norway are the most important as FDI locations, was given a rather low level of preference by respondents (figure 8), possibly due to its small size. It should be noted, however, that Western Europe as a whole is the region of the world where the largest share of respondents (70%) already have a presence.

*Other developed countries* (Australia, Israël, Japan and New Zealand) are not major preferred locations for companies: only 46% of respondents declared having already invested there (figure 7). The level of preference given to this diverse group of countries (fifth most preferred in the world) is likely to remain moderate, with a relative decline as compared to the rest of the world (figure 8). The percentage of companies intending to increase their investments there is lower than the average for the world (figure 9). As opposed to other country groups within the developed regions, local market size was not considered an important locational asset, the only large economy of the group being Japan (table 6). Finally, from this group of countries, only Australia features among the world's 10 most attractive countries for investment according to the percentage of responses received (figure 10), notably due to the availability of natural resources in the country (table 6), while Japan ranks 19th (figure 10).

### Notes

- <sup>12</sup> For details on the regional classification used in this survey, see annex 5.
- <sup>13</sup> For detailed data on actual FDI flows and stocks, see UNCTAD, forthcoming.
- <sup>14</sup> At the same time, there is a growing discrepancy between the geographical pattern of FDI inflows and that of job creation linked to international projects. Data on inward FDI flows show a greater orientation towards developed countries, notably through a high volume of purchases of companies hosted in these regions (UNCTAD, forthcoming). Data on international projects show that FDI leads to job creation in developing Asia, and to a lesser extent, the new EU-12, where large, labour-intensive projects are being located (Hatem, 2007).
- <sup>15</sup> The “flying geese” pattern, a concept originally developed in the 1930s by Japanese economist Kaname Akamatsu, was revived 30 years later to describe the regional development process that began in East and South-East Asia in the 1960s (Ozawa, 2005). In this model, enterprises from the most advanced country in a specific region (e.g. Japan in Asia) begin to invest abroad in a first set of host economies (e.g. Taiwan Province of China, Republic of Korea), relocating some labour-intensive activities there. As these host countries develop, assisted by the inward FDI, they are characterized both by an increase in their value-added activities and a rise in their internal costs, which diminishes their initial competitive advantage for the location of labour-intensive activities. The domestic companies of these countries thus begin to invest abroad in a second set of host countries (e.g. China, Malaysia), replicating there the initial relocation model initiated by the first movers (e.g. Japanese firms). Step by step, a growing number of countries are involved in this regional integration and development process. A similar pattern is presently unfolding in Europe, including not only the EU-15 and EU-12 countries, but also South-East Europe and the CIS, and perhaps North Africa as well.
- <sup>16</sup> For analytical purposes, this discussion combines the new EU-12 countries and South-East Europe and the CIS, as both regions share many similar characteristics and issues relating to the attraction of FDI.





## CHAPTER III

### PATTERNS OF FDI BY ACTIVITY, INVESTOR AND ENTRY MODE

The UNCTAD survey throws light on five major findings regarding the evolving patterns of FDI. First, FDI is expected to grow rapidly in a large number of activities, such as those in the primary sector, intermediate goods manufacture, food processing, light manufacturing, trade and network services, a list which ranges well beyond the usually mentioned high-value-added manufacturing and service industries. Second, the ongoing internationalization of corporate functions that were formerly concentrated in home countries, such as internal administrative services, decision-making centres and R&D, is expected to continue. Third, the growing international ambitions of TNCs from developing countries (especially from Asia) could have an impact on the home-country pattern of FDI. Fourth, many companies are likely to expand their strategic scope beyond their home regions. Finally, the responses show that, while greenfield projects will be the most commonly used mode of establishing operations into a specific host country, the propensity for M&As will be higher in developed countries, due to the existence of more takeover opportunities there than in the developing world.

#### 1. Sectoral prospects

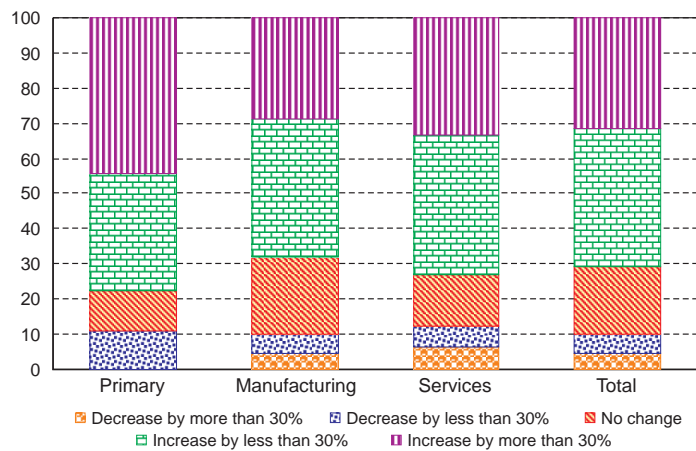
FDI flows are likely to grow in most industries. This can be attributed to various factors, including a general trend towards the internationalization of companies' activities, the existence of a large number of innovative segments spread over various economic activities, rapidly rising demand for many goods and services, and the existence of international restructuring opportunities.

The UNCTAD survey shows that most industries will share in the global dynamism of international investment.<sup>17</sup> In practically all industries, more than 60% of respondents stated they planned to increase their FDI expenditures during the 2006–2009 period (figure 11). The primary sector, electrical and electronic equipment and some service industries (e.g. trade and public utilities) were identified as those most likely to experience the highest growth in FDI (table 7).

- **Primary sector.** The growing demand for raw materials and energy resources has prompted a new wave of FDI in extractive industries (oil and gas, metal minerals) (UNCTAD, forthcoming). Indeed, 78% of the respondents in the primary sector anticipated an increase in their FDI expenditures (figure 11). Expansion strategies of companies from emerging countries such as China are expected to play an important role in this trend.
- **Manufacturing sector.** Prospects for FDI are bright in most industries, including those considered the most traditional, due to a combination of factors. These include the general trend towards the internationalization of companies, the setting up of larger scale international production and

distribution networks, and the existence of promising new products and segments of activity in all industries.<sup>18</sup>

**Figure 11. Changes in FDI by sector, 2006–2009**  
(Per cent of responses)



Source: UNCTAD survey.

- Services sector.** This sector has been characterized in recent years by the rapid internationalization of companies<sup>19</sup> which had lagged behind manufacturing companies in the 1970s and 1980s in terms of presence abroad. Consequently, the degree of internationalization of the top companies in services, other than financial services,<sup>20</sup> is now close to that observed for the manufacturing sector (annex table 4). Three major drivers are behind this trend: the desire of companies to gain access to local markets, the opening up of those markets to foreign investors through deregulation and privatization processes, including in infrastructure industries, and the increasing tradability of many services (UNCTAD, 2004b). Around a third of responding companies in the services sector mentioned that they anticipated an increase of over 30% in their FDI expenditures over the period 2006–2009. The most significant increases in FDI (by over 30%) are expected to occur in the trade (by 50%) and electricity, water and gas industries (by 40%) (table 7).

Many of the developments in markets and products are difficult to categorize in the usual industry classifications, in the sense that they may affect a large range of activities all along the value chain: from the production of raw material to final delivery and consumer support services. Consequently, they may have implications for FDI projects in a range of industries. This is typically the case for the new activities connected with environmental and energy concerns, which rank among the most powerful drivers of FDI for the coming years (box 2).

The geographical patterns of investment and location criteria differ by industry (tables 8 and 9):

- In the *primary sector*, the low representation of such companies in the sample does not permit a detailed analysis (annex table 7). However, for this sector, access to natural resources is by definition an important criterion, and companies are likely to prefer investing in regions well endowed in such resources, in particular sub-Saharan Africa and Latin America.

**Table 7. Changes in investment by industry, <sup>a</sup> 2006–2009**  
(Per cent of responses)

Sector/industry	Decrease by more than 30%	Decrease of 10-30%	Decrease by less than 10%	No change	Increase by less than 10%	Increase of 10- 30%	Increase by more than 30%	Total
<b>Primary</b>	-	-	11	11	-	33	44	100
<b>Manufacturing</b>	4	3	3	22	10	29	29	100
<i>of which:</i>								
Food products, beverages and tobacco	-	-	-	-	-	78	22	100
Textiles, clothing and leather	-	-	-	-	40	40	20	100
Pharmaceuticals, chemicals and plastics	11	-	-	17	17	22	33	100
Metals and non-metallic products	-	5	5	35	10	20	25	100
Electrical and electronic equipment	7	14	-	21	-	14	43	100
Professional equipment goods	4	-	4	25	13	29	25	100
Motor vehicles and transportation	10	-	10	20	-	50	10	100
Other manufacturing	-	-	-	33	8	17	42	100
<b>Services</b>	6	6	-	15	8	31	33	100
<i>of which:</i>								
Electricity, gas and water	10	-	-	20	10	20	40	100
Trade	-	14	-	14	7	14	50	100
Transport and telecommunications	14	-	-	29	-	43	14	100
Other services	6	6	-	6	11	44	28	100
<b>Total</b>	4	3	2	20	9	29	32	100

Source: UNCTAD survey.

### **Box 2. Waste management, clean technologies and renewable energies: major areas of future FDI**

Rising environmental concerns, together with growing demands for energy and potential shortages of fossil fuels, might trigger a major wave of international investment projects in a large number of activities, as shown by the following examples:

**In the primary sector**, wide opportunities have opened up for the use of agricultural products in the production of biopolymers, biosolvents, biolubricants and bioenergy. For instance, Acciona and Abengoa (both from Spain) have invested in new projects in France for the production of bio-diesels in 2006; Grupo Activos (Spain) plans to build new bio-diesel production units in Portugal, Brazil and Uruguay; INEOS Enterprises (United Kingdom) plans to build a large bio-diesel production facility in the port of Antwerp in Belgium; and Martifer (Portugal) plans to construct a bio-diesel production facility, based on sunflower processing, in Romania.



**Box 2. Waste management, clean technologies and renewable energies: major areas of future FDI (concluded)**

**In energy**, activities relating to alternative energies (solar, wind, biomass) are on the rise. Worldwide investment in renewable energies rose from \$7 billion in 1995 to \$37 billion in 2005 (Lemagnen, 2007). Further growth of FDI projects in this field is expected, especially in Europe where prospects for solar and wind energy are bright.<sup>a</sup> For instance, in 2006, wind power facilities were set up, among many others, by DONG Energy (Denmark) and E.ON (Germany) in the United Kingdom, by Iberdrola (Spain) in Poland, Hungary and Estonia, by Enel (Italy) in Romania, and by Siemens (Germany) in Sweden. Acciona (Spain) has decided to set up a large photovoltaic plant for power generation in Portugal. This implies increasing demand for new kinds of equipments such as photovoltaic cells or specialized electrical equipment. Silpro (Netherlands), for example, has set up a new factory for the production of components for photovoltaic cells in southern France in 2006. In the same year, SCHOTT (Germany) decided to set up a second factory in Spain for the production of components for solar cells. Saint-Gobain (France) and Royal Dutch/Shell Group (United Kingdom/Netherlands) have set up a joint venture for the production of solar cells in Germany, and Suzlon Energy (India) plans to develop its R&D and production capabilities for wind power solutions in Lommel, Belgium.

**In manufacturing as a whole**, massive investments can be expected for the implementation of new environment-friendly products and processes. For instance, companies operating in the pulp and paper industry are expected to make greater efforts to recycle their wastes as bio-products, implying a major revamping of their existing processes. In the automotive industry, a large proportion of R&D programmes are presently geared towards the design of efficient, energy-saving vehicles, as exemplified by the R&D projects presently under development in the Mov'eo competitiveness cluster in the Normandy valley of France. Globally, new technologies aimed at minimizing carbon dioxide emissions are being used or are under development in many industries.

**In environment-related industries and services**, large investments are under way in Europe in reverse logistics (collection of waste products), recycling and water treatment, in response to the tightening of the European Union regulations. For instance the new Citron factory (a Swiss company specialized in recycling facilities) in the French City of Le Havre has developed an advanced technology for the recycling of small power batteries. In 2006, Brother Industries (Japan) launched a recycling facility in Krupina, Slovakia and Coca-Cola (United States) has set up a recycling plant as a joint-venture with four Austrian companies in Austria. Veolia Environnement (France) is building a waste incinerator at Rufford Colliery in the United Kingdom, Brazilian TSL Engenharia Ambiental is to open a carton recycling packing plant in Spain; Losonoco (United States) plans to create a bio-ethanol plant based on the recycling of biodegradable waste in Billingham (United Kingdom).

*Source:* UNCTAD based on Lemagnen, 2007; Invest in France Agency, 2007; and Hatem, 2007.

<sup>a</sup> According to Lemagnen (2007), two million people could be employed in Europe in renewable energy industries by 2020. Prospects are also bright in emerging economies where economic growth is boosting energy demand: for example, China accounted for 78% of new world capacity in solar water heating in 2005.

**Table 8. Location criteria, by sector, 2007–2009** •  
(Per cent of responses)

Location criteria	Primary	Manufacturing	Services
Follow the leader	5	4	5
Skilled labour	10	10	8
Cheap labour	1	11	5
Size of local market	6	22	22
Access to capital market	1	1	6
Access to natural resources	22	5	3
Access to regional market	13	11	10
Growth of local market	7	22	20
Government effectiveness, incentives	15	4	8
Stable investment environment	20	8	13
Others	-	3	2
<b>All factors</b>	<b>100</b>	<b>100</b>	<b>100</b>

Source: UNCTAD survey.

- In the *services sector*, where the size of the local market and a stable investment climate are considered particularly important factors for attracting FDI, a large percentage of investors expressed again a preference for South, East and South-East Asia, but also for countries in developed regions, especially Western Europe (26% of respondents) (table 9).

In the *manufacturing sector*, where access to low-cost labour remains one of the major determinants of FDI in many industries, companies expressed a more marked preference for South, East and South-East Asia, with 50% of respondents mentioning an interest in that region (table 9).

**Table 9. Attractiveness of regions for FDI in the manufacturing and services sector, 2007–2009**  
(Per cent of responses)

Host region	Manufacturing	Services
South, East and South-East Asia	50	28
New EU-12	4	7
Latin America	10	2
North Africa	2	1
North America	12	11
Other developed countries	3	7
South-East Europe and CIS	10	12
Sub-Saharan Africa	2	4
West Asia	3	3
Western Europe	5	26
<b>World</b>	<b>100</b>	<b>100</b>

Source: UNCTAD survey.

## 2. Growing internationalization of corporate functions

Production and distribution will remain the most internationalized functions, but presence abroad will increase in other business functions, such as administrative support centres, finance and regional headquarters.

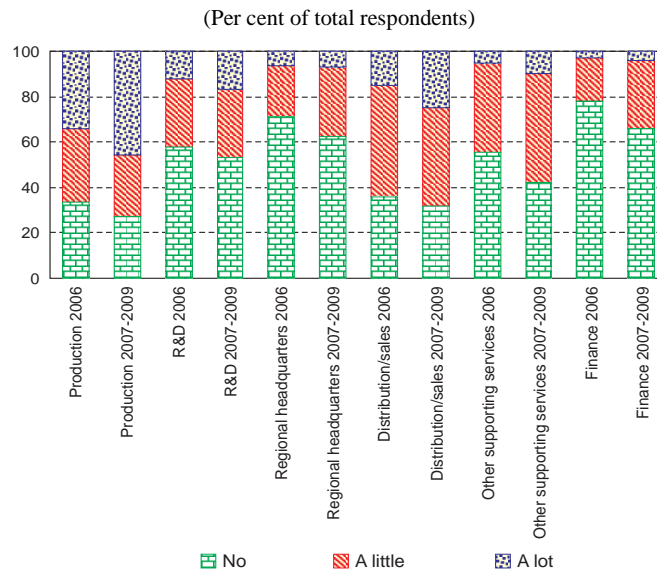
An analysis of past and current trends shows that large TNCs have so far implemented very different internationalization strategies for the various corporate functions (UNCTAD, 2002). While production and sales functions have already been widely internationalized, R&D, finance and decision-making centres have remained more centralized in the home country, even in the recent past; and other business support functions have been characterized by a moderate degree of internationalization.

Responses by companies to the UNCTAD survey point to a sharp increase in the international expansion of all business functions, including those which in the recent past have still been mainly located in the home country of the company (figure 12). In logistics, shared services and call centres (classified under "other supporting services"), for instance, 59% of the respondent companies indicated that they intended to expand or relocate abroad in the near future, compared with 44% in 2006 for regional headquarters, this percentage is 38% (as against 29% in 2006), while in finance activities, 34% of the companies reported their intention to expand abroad (as against 22% in 2006).

Many corporate functions (especially logistics, distribution, shared services and call centres) could be affected by a major re-engineering process, characterized by three main features: *first*, a growth in outsourcing, favouring the development of specialized business service providers; *second*, the implementation by companies of an integrated international network of support functions, relying upon specialized sites located in various countries; and *third*, growing competition among potential host countries in attracting projects related to business services, which will provide companies with a larger range of locational options, including the offshoring of some activities (e.g. support and call centres) to low-cost countries such as India or Morocco. All three elements are likely to provide a new impetus for international investment in those activities.

In R&D activities also, respondents seem eager to internationalize: 47% of companies mentioned they were likely to relocate or expand projects abroad in the three years, to end 2009, as against only 42% in 2006. This is because an increasing number of companies consider access to talent and innovation capabilities as a major aspect of competitiveness and seek to secure access throughout the world. In R&D activities, companies use several means to implement their global sourcing strategies, such as contracts with universities and research centres, investment of venture capital in promising projects, acquisition of start-up and innovative companies, acquisition of patents and licences, and setting up R&D centres abroad (UNCTAD, 2005a and b). These developments open up new areas for FDI flows: in Europe alone, about 130 new international projects in R&D centres were announced each year between 2002 and 2006 (Hatem, 2007). Nevertheless, the bulk of internationalization is likely to take place in production and distribution/sales, with 73% and 68% of respondent companies respectively intending to expand or relocate these functions abroad by 2009 (figure 12).

**Figure 12. Expansion or relocation abroad by corporate function, 2006 and 2007–2009**



Source: UNCTAD survey.

### 3. Investment patterns by home country and size of companies

An analysis by size and home country of the TNCs surveyed shows that all categories of firms plan to increase FDI expenditure, in particular companies from developing countries or those of a smaller size than the sample average.

#### a. Does the home region matter for the internationalization of companies?

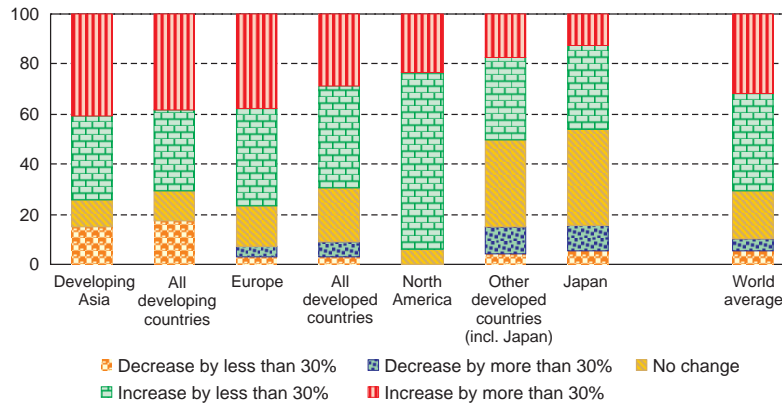
While companies from all regions plan to increase their FDI, firms from developing Asia might be particularly dynamic.

In practically all home regions – with the exception of Japan – a majority of companies reported that they intended to increase their investments abroad in the three years up to and including 2009 (figure 13).<sup>21</sup> Consistent with this, the percentage of firms intending to reduce their investments is very low in all home regions – never more than 20%. Companies from all over the world will thus take part in the internationalization process.

However, some interesting geographical differences by home region are worth mentioning (figure 14 and annex 2):

- TNCs from European countries<sup>22</sup> are slightly more internationalized than the world average, both in terms of their share of foreign assets (annex table 6) and in terms of the geographical diversification of their FDI stocks (figure 14). Moreover, they are likely to increase their investment at a pace close to the world average (figure 13).
- TNCs from North America are less internationalized than the average in terms of their share of foreign assets to total assets (annex table 6).<sup>23</sup> Their presence abroad is also slightly less diversified regionally than that of European companies (figure 14). However, responses to the survey show that this group has the highest percentage of companies intending to increase their investments abroad (figure 13).

**Figure 13. Expected change in FDI expenditures by home region, 2006–2009**  
(Per cent of responses)



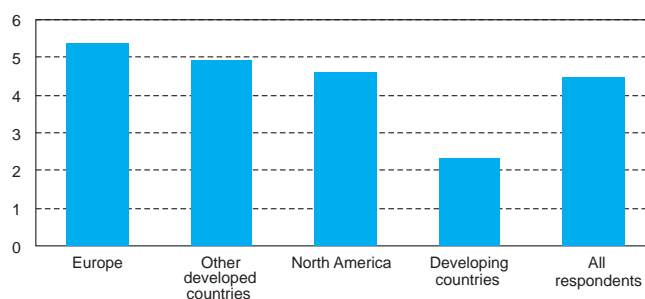
Source: UNCTAD survey.

Note: For a definition of the various home regions, see annex table 10.

- Companies from Japan are less internationalized than average in terms of foreign assets (annex table 6). According to the UNCTAD survey, their FDI abroad is expected to increase in the years to come.<sup>24</sup> Nevertheless, this country has the lowest percentage of companies that intend to increase their investments abroad (figure 13).
- Finally, companies from developing countries (especially from Asia) show a number of interesting features (annex 2). First, their number is already very high, as they account for practically one quarter of the top 5,000 TNCs by size of foreign assets. Second, they have already reached a very high internationalization ratio in terms of assets, especially companies from Singapore, Taiwan Province of China and Hong Kong (China). With rapid development taking place in their home countries, these companies are increasingly becoming active international investors (UNCTAD, 2006). Third, these companies still, however, appear less diversified geographically than the average TNC in the sample (figure 14), due to the fact that a large share of their investments abroad is concentrated in a limited number of countries such as China. Fourth, their FDI is likely to develop at a steady pace: 41% of respondents from developing Asia mentioned that they intended to increase

their investments abroad sharply (e.g. by more than 30%) over the period 2007–2009.

**Figure 14. Indicators<sup>a</sup> of geographical diversification of FDI by home region of the company, 2006**  
(Number of host regions)



Source: UNCTAD survey.

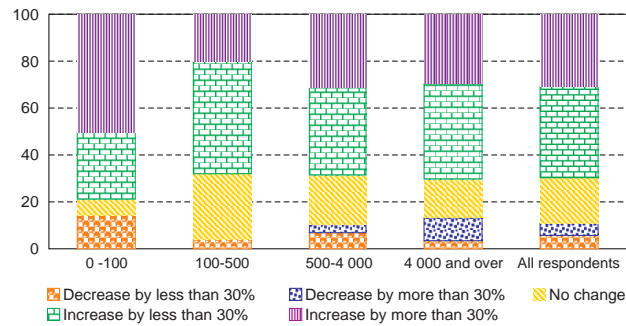
<sup>a</sup> Measured as the average number of the 11 host regions where the respondent companies from a given home region declared they had already invested.

#### b. Does company size matter for their internationalization?

FDI prospects are positive for companies of all sizes, but some of the smallest firms among the top 5,000 TNCs – many of them from developing countries – could rank among the most dynamic investors abroad in the period 2007–2009.

A large majority of respondents, whatever the size of the company, reported that they intended to increase their FDI over the period 2006–2009 (figure 15), especially the smallest companies in the sample (with home assets of less than \$100 million). Half of these small companies said they intended to sharply increase their investments abroad, compared to an average of 30% of all companies. While these companies are already the most internationalized (in terms of foreign to total assets) of the top 5,000 TNCs (annex 2), their level of geographical diversification remains lower than the average for this group (figure 16). Some smaller TNCs, already widely internationalized, but mainly on a regional level, could thus rank among the most dynamic investors abroad in the coming years.<sup>25</sup> A significant proportion of companies of this kind are from the developing world (mainly Asia).<sup>26</sup>

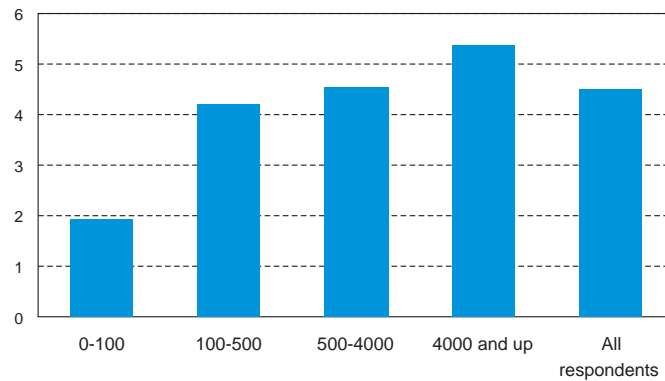
**Figure 15. Expected change in FDI expenditures by company size,<sup>a</sup> 2006–2009**  
(Per cent of responses)



Source: UNCTAD survey.

<sup>a</sup> Measured by the home-country assets of the parent company in millions of dollars.

**Figure 16. Indicator<sup>a</sup> of geographical diversification of FDI by size of the company, 2006**  
(Number of host regions)



Source: UNCTAD survey.

<sup>a</sup> Measured as the average number of host regions (out of a total of 11) where companies of each given range of size (in terms of home-country assets of the parent company in millions of dollars) had already set up activities.



#### 4. FDI still prefers its home region, but its geographical scope is expected to expand

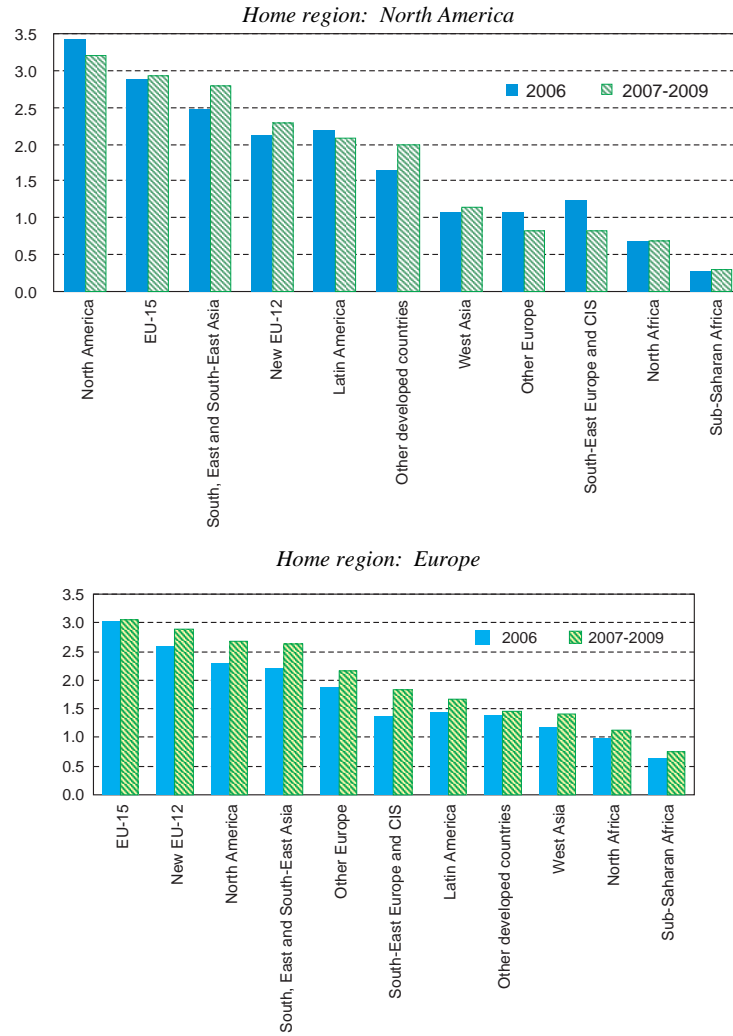
While companies are expected to continue giving preference to their home regions in their FDI strategies, they will also pay increasing attention to other potential locations in the world.

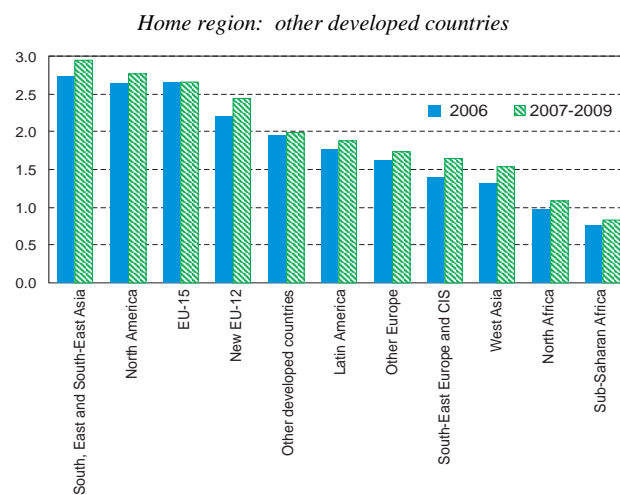
As noted in chapter II, companies have continued to give a high level of preference to their home regions<sup>27</sup> in their international investment strategies in the recent past. Responses to the survey showed that there will be a slow but striking evolution of this pattern for the three years up to end 2009, characterized by the progressive expansion of the strategic scope of companies outside their home regions, where they will nevertheless continue to invest a large share of their FDI.

Overall, the home regions will remain the preferred locations of companies, whatever their origin (figure 17). Consistently, the home region is always the one where the companies plan the largest increase in their investments abroad (figure 18). Regional expansion will thus remain a major driving force behind the international growth of companies.

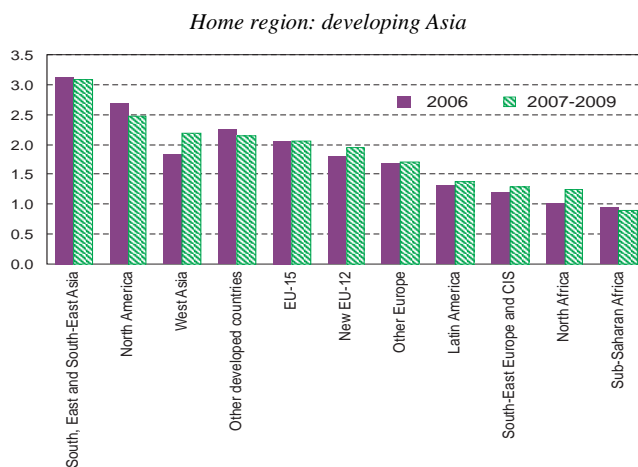
On the other hand, companies are set to increase, sometimes significantly, the level of preference given to many locations outside their own home regions; for instance, North American companies are likely to increase their preference for developing Asia, Europe and other developed countries. European companies are expected to increase significantly their level of preference for all regions of the world, with the exception of Western Europe. Japanese companies (which account for the largest share of firms from “other developed countries”) expressed no change in their preference given to South, East and South-Asia (which so far has been their main region of investment), while increasing their interest in the Americas, the EU-12, and South-East Europe and the CIS (figure 17). Finally, it should be noted that companies from developing Asia (mainly from South, East and South-East Asia) are likely to increase their preference for the EU-12, West Asia, South-East Europe and the CIS, and North Africa, which might lead to growing South-South investment flows.

**Figure 17. Regional preferences for investment, by home region of respondent firms, 2006 and 2007–2009 (average score)**



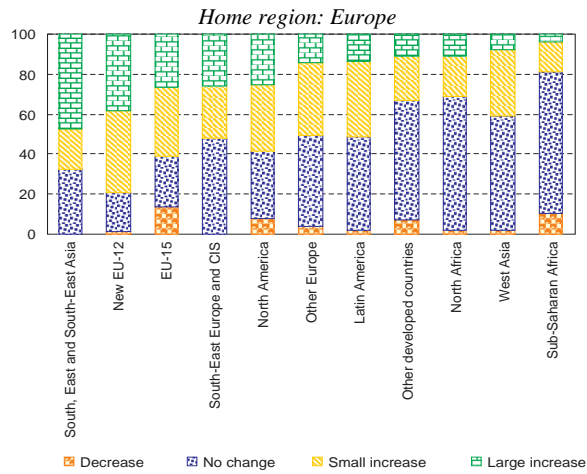
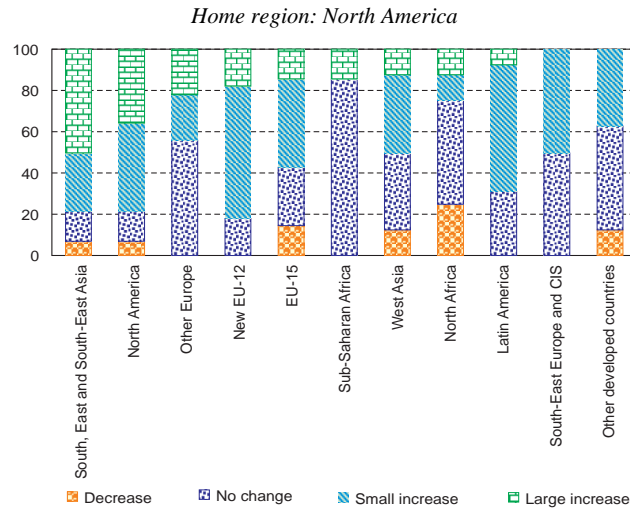


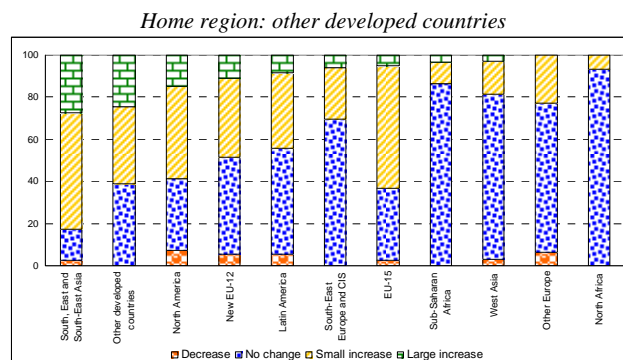
*Note:* Japan is classified in this study in the category of “other developed countries” but as analysed in the figure above, the home region is considered to be South, East and South-East as the latter countries are Japan’s neighbours (see also footnote 27).



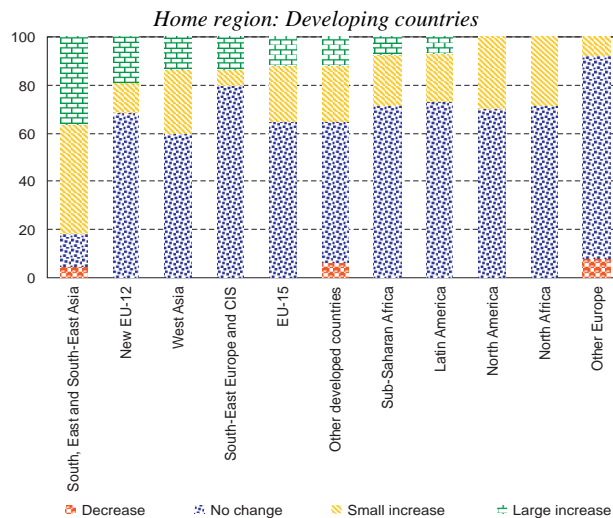
*Source:* UNCTAD survey.  
*Note:* 0=Not at all important, 4=Very important

**Figure 18. Expected increase in FDI in host region, by home region of respondent firm, 2007–2009**  
(Per cent of responses)





Note: Japan is treated under the category of “other developed countries”, as explained in note to table 17.



Source: UNCTAD survey.

Note: 0 = Not at all important, 4 = Very important

### 5. Specific modes of entry by host region, industry and home region

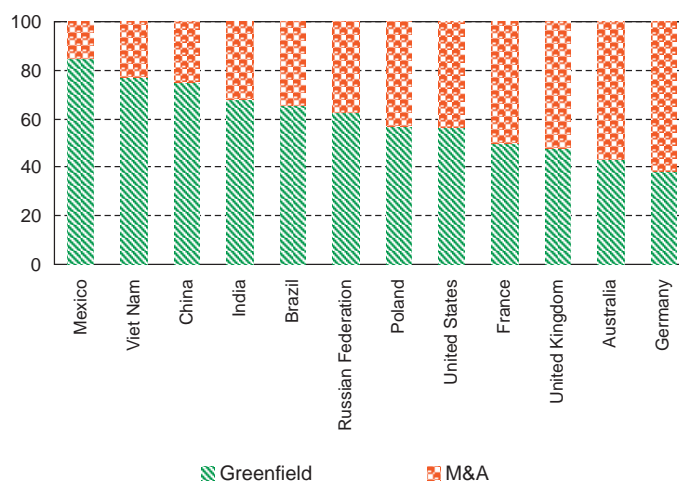
While greenfield investments are more commonly used overall than M&As as a mode of entry into a foreign country, the propensity to use M&As is notably higher for FDI in developed economies.

To carry out their internationalization strategies, TNCs use various tools, such as sub-contracting agreements, M&As, greenfield investments or partnerships. It is well known that M&As have been gaining momentum in recent years as a preferred mode of internationalization, as highlighted by previous UNCTAD surveys (UNCTAD, 2004b; UNCTAD, 2005b), among others.

However, until this survey, no specific analysis had been carried out by UNCTAD on the preferred mode of entry of companies into a specific country. While cross-border M&As are commonly used for large international restructuring aimed at increasing the company's market power at the global level, it is questionable whether this tool will be as commonly used for more limited operations focused on only one country's market and business culture. The UNCTAD survey thus tried to gain insights on this specific issue by asking the companies to indicate, for each of the countries they considered the most attractive, whether they would rely on M&As or greenfield investments as a mode of entry. The results are as follows:

- Overall, greenfield investments were much more frequently cited as an entry mode into a specific country than M&As. This result is also confirmed by examining the data on the number of cross-border M&As and greenfield FDI projects. For example, in 2005 there were about 6,100 M&As, compared with 9,500 greenfield projects (UNCTAD, 2006).
- While the propensity to use M&As is higher when investing in a developed economy, greenfield investments are more frequently used for entry into developing countries and transition economies (figure 19). This is mainly due to the existence of more takeover opportunities in developed countries (with a larger number of attractive companies to target, and openness and liquidity of the stock-exchange markets).

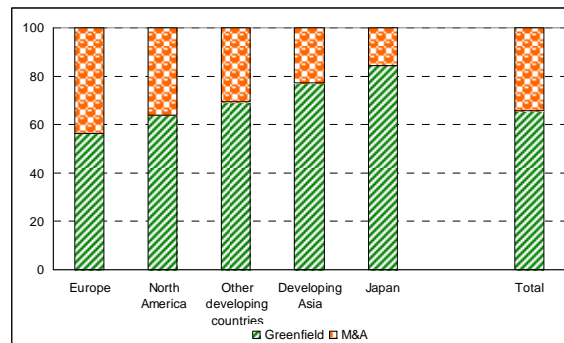
**Figure 19. Use of M&As and greenfield investments as an entry mode into selected host countries, 2007–2009**  
(Per cent of responses)



Source: UNCTAD survey.

- Western European and North American companies are more likely than others to use M&As as an entry mode, while companies from Japan and developing economies tend to rely more on greenfield investments (figure 20).<sup>28</sup> Two major factors behind the choice of mode are: the regional destination of operations, with North American and European companies channelling a larger share of their investment in the main developed countries; and the business culture, as Western companies are more inclined to use M&As, other things being equal, than Japanese ones.
- TNCs in the services sector are more likely to use M&As than the average of all sectors (figure 21). One explanation is that in many service industries, the purchase of an existing distribution network or trademark is a much quicker and more efficient mode of entry than the creation of a new one (e.g. in electricity supply, telecommunication networks and retailing).

**Figure 20. Use of M&A and greenfield investments as an entry mode into a specific country, by home region, 2007–2009**  
(Per cent of responses by home region of respondent firm)



Source: UNCTAD survey.

**Figure 21. Use of M&As and greenfield investments as entry modes into a specific country, by sector, 2007–2009**  
(Per cent of responses by sector of respondent firm)



Source: UNCTAD survey.



## Notes

- <sup>17</sup> For more details on the industry classification used in this survey, see annex 5.
- <sup>18</sup> For a full discussion of potential new products in various industries, see Hatem, 2006.
- <sup>19</sup> Besides financial and trading services, in which firms have been expanding internationally for some time.
- <sup>20</sup> Financial services are excluded from the UNCTAD survey (see annex table 5).
- <sup>21</sup> For more details on the home region classification used in this study, see annex 5.
- <sup>22</sup> Europe as a home region includes the EU-15, new EU-12 and other European countries including Norway and Switzerland.
- <sup>23</sup> This is true only for United States companies, as Canadian companies already show a rather high internationalization ratio, largely due to their investments in the United States.
- <sup>24</sup> Based on statistics of the Ministry of Finance, Japan, the total amount of outward FDI from January to May 2007 was \$36 billion, already 77% of the total amount for 2006, boosted by a large number of M&As.
- <sup>25</sup> Although these companies are not small and medium-sized enterprises (SMEs), but already rather large TNCs, this finding confirms that of various studies and statistical sources that suggest the existence of an ongoing trend of internationalization by SMEs that have considerably increased their FDI flows in recent years (Fujita, 2007). Nevertheless, SMEs still remain much less internationalized on average than larger firms. There thus remains a potential for further internationalization of SMEs willing to take greater advantage than in the past of the opportunities offered by foreign markets and resources.
- <sup>26</sup> This trend should nevertheless be considered as distinct from the one analysed earlier regarding the dynamism of TNCs from developing countries, as responses by “small” TNCs from developed countries concerning FDI prospects were quite similar to those of their Asian counterparts.
- <sup>27</sup> The term “home region” refers to a group of countries located in the same contiguous geographic area as the country of the TNC in question, rather than to the strict classification shown in annex table 10.
- <sup>28</sup> Despite a recent rise in M&As by developing-country firms, illustrated by some spectacular deals, the vast majority of M&As, including cross-border M&As, are still undertaken by European and North American purchasers (UNCTAD, forthcoming).



## CONCLUSIONS AND POLICY IMPLICATIONS: ADAPTING TO THREATS AND OPPORTUNITIES

The UNCTAD survey points to a series of future FDI trends and prospects that hold opportunities as well as threats for national economies and their governments.

Among the major opportunities highlighted by the survey are an overall foreseeable increase in FDI flows and rapid development of new investments in activities such as new energies, environment-related industries and business-support functions (e.g. shared service centres).

Among the major risk factors pointed out by the survey, some are of a global nature, such as financial or geopolitical instability. Others only affect specific regions, such as the trend towards offshoring labour-intensive activities that affects the main developed countries. To compensate for the loss of such activities, this last group will therefore need to take advantage of new development opportunities in innovative industries and high-value-added services.

Several aspects of the analysis of the survey results also point to the existence of growing competition among host countries for attracting FDI. An increasing share of world investment will be made in the form of FDI. Companies will have a wider choice among a growing number of new and attractive host countries, such as Viet Nam and Ukraine, for the location of their projects. Each host country will thus have to make the most of its locational advantages to maximize its share in global FDI.

But locational advantages tend to change. Many open questions remain for the long term (box 3) and local and national authorities need to pursue policies that prepare their economies for a competitive environment for FDI in the long term.

### **Box 3. Some issues related to FDI in the long term**

Some issues and uncertainties pointed out by the UNCTAD survey and the panel of experts have not yet had major consequences for FDI flows, but might have an impact on them in the longer term. Among the most frequently mentioned are the following:

*The environment.* Beyond its foreseeable medium-term impact on projects in new energy or waste management, environmental concerns might have more widespread impacts on the geographical and sectoral structure of economies. For instance, growing negative externalities linked to “mega cities” might lead to a growing attractiveness of medium-sized towns for investment projects. Moreover, the gradual exhaustion of oil resources might affect many activities directly based on them, such as those related to automobiles and transportation, basic chemicals and plastics, and even pharmaceuticals. All this will involve significant changes in sectoral investment patterns.

**Box 3. Some issues related to FDI in the long term** (concluded)

*Social responsibility issues.* Companies are increasingly facing various ethical and social issues connected with their activities abroad (e.g. the impact of their FDI activities on particular groups in the host and home economies, environmental issues and work ethics). Factors such as respect for social standards in host countries and a growing sense of eco-responsibility among companies involving a growing focus of investments on environment-friendly processes may have an impact on FDI trends and structure.

*Impact of technological innovation.* The further development of information and communication technologies (ICTs) might have a major impact on the role of proximity in work organization, and thus on business networks and investment patterns. On the one hand, it could open up new fields for relocation of services, such as call centres or shared service centres, thus increasing investment flows in these fields. On the other hand, it could also favour an increased reliance of companies on strategic alliances with remote partners, thus reducing the need to set up wholly-owned businesses in foreign countries.

*The future of organizations.* Corporations are affected by a series of internal transformation processes, which could have an impact on the way they are managed as well as on their international investment patterns. Among the most frequently raised issues relating to this are: first, the management of multicultural organizations, where participants are of diverse cultural origins and might differ in their specific values and ways of doing business; second, the notion of collaborative work and leveraging of knowledge, which can affect the way international innovation and R&D networks will be set up and managed; third, the management of risks and volatile markets, which could have consequences on the risk/profitability trade-off in the investment decision-making process.

*Impact of demographic changes.* Will the ageing of populations in Western countries induce companies to locate in regions endowed with a younger population? Will advanced countries set up large-scale immigration policies aimed at attracting young qualified workers, thus developing new kinds of promotional activities in addition to those presently focused on FDI?

*Source:* UNCTAD survey, based on interviews with the location experts.

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## ANNEX 1. METHODOLOGY OF THE UNCTAD SURVEY

**Objective.** The aim of the UNCTAD survey was to project future trends in FDI flows by the largest TNCs. Questions were addressed to capture, among others, projected changes in FDI expenditures over the next three years until 2009 as compared with 2006; the most attractive locations for FDI in the future; the most important location criteria, and the major risk factors.

**Frame creation.** First of all, the largest 5,000 TNCs ranked by foreign assets were selected as the basic frame for the survey. The Thomson One Banker database was consulted to identify these companies (annex 2). A sample of 1,500 companies was then selected at random, not because it would provide a certain level of precision, as is often done, but more out of necessity to avoid an undue burden on administration, implementation and follow-up procedures (Cochran, 1977). After sorting the list of companies by foreign assets (FAs), a probability proportional to size (PPS) sample was drawn without replacement, using FAs as the measure of size. PPS was employed in order to make use of implicit stratification, to ensure that companies of all sizes would be selected in the sample and also to ensure that a significant percentage of the largest 100 TNCs<sup>29</sup> would definitely be selected and surveyed.

**Questionnaire creation.** A draft questionnaire was tested among a handful of executives. Based on their comments, as well as an internal review, a questionnaire was finalized and sent to the companies in March 2007.

**Data collection.** A mixed-mode approach for data collection was adopted, using the post, e-mail and telephone follow-up. The questionnaire was also available for completion online. Between April and June 2007, 191 responses were collected, resulting in an answer rate of 13% approximately (annex 3).

**Annex table 2. Comparing the representation of the frame, sample and survey responses by sector**  
(Per cent of respondent companies)

Sector	Frame	Sample	Survey responses
Primary	7	7	5
Manufacturing	56	60	62
Services	37	34	27
Unknown	..	..	6
<b>Total</b>	<b>100</b>	<b>100</b>	<b>100</b>

**Annex table 1. Comparing the representation of the frame, sample and survey responses by region**  
(Per cent of respondent companies)

Region	Frame	Sample	Survey responses
<b>All developed regions</b>	74	83	76
Europe	28	35	39
North America	30	31	10
Other developed countries	16	33	27
Japan	11	15	23
<b>All developing regions</b>	26	17	18
Developing Asia	24	14	15
<b>Unknown</b>	..	..	6
<b>Total</b>	<b>100</b>	<b>100</b>	<b>100</b>

**Reliability of the sample.** A quarter of the 5,000 TNCs are from developing economies and 24% from developing Asia. Considering the geographical distribution of the frame of 5,000 companies, the sample of 1,500 and the 191 responses, it can be inferred that the responses match the distribution in the sample, with the exception of the United States, which is underrepresented and Japan which is overrepresented, reflecting different attitudes to completing questionnaires in the two countries. In the case of Japan, wherever the overrepresentation

could be a potential source of bias, the results were normalized and analysed with and without Japan in the sample before any analysis was done.

The sectoral distribution is fairly uniform across the frame, the sample and the responses (annex table 2).

**Location experts for the UNCTAD survey.** In addition to the survey carried out among companies, a group of location experts was established for the purpose of collecting qualitative information on FDI trends and to review the drafts of this study (see list of experts in annex table 3).

Annex table 3. List of location experts associated with the survey

Title	Last name	First name	Title	Institution
Mr	Amma	Massaki	Director General	JBIC Institute
Mr	Ash	Ahmad	Senior Economist	Invest in Canada Agency
Mr	Bridgman	David	Head, Africa Region	Multilateral Investment Guarantee Agency
Mr	Buck	René	President	Buck Consultants International
Mr	Hammerich	Kai	President and Director-General	Invest In Sweden Agency
Mrs	Knutsson	Christina	Director	GDP Global development
Mr	Lemagnen	Peter	Director	Oxford Intelligence
Mr	Lhermitte	Marc	Partner	Ernst and Young
Mr	McMenamin	Paid	Chairman	Deerac Fluidics
Mr	Michalet	Charles-Albert	Professeur honoraire	Université Paris-Dauphine
Mr	O'Connell	Mark	Chief Executive Officer	OCO Consulting
Mr	Pilous	Robert	Director, Investment Development Department	Czech Invest
Mr	Spee	Roel	Partner	PLI – Global location Strategies
Mr	Ste-Marie	Mario	Director General	Invest in Canada Agency



## ANNEX 2. CHARACTERISTICS OF THE FRAME FOR THE SURVEY

The survey frame was compiled from the 5,000 largest companies listed in the Thomson database (ranked by foreign assets).

**Annex table 4. Top 5,000 companies by sector and industry, ranked by foreign assets**

Sector/Industry	Number of companies (% of total)	Foreign assets (% of total)	Internationalization ratio <sup>a</sup>
<b>Primary</b>	<b>6.5</b>	<b>5.3</b>	<b>0.45</b>
<b>Manufacturing</b>	<b>55.6</b>	<b>62.4</b>	<b>0.33</b>
Food products, beverages and tobacco	3.8	5.2	0.38
Textiles, clothing, leather	2.8	0.6	0.40
Chemicals, petrochemicals, plastics, and rubber	9.6	19.3	0.32
Metals and non-metallic products	4.4	4.5	0.36
Electrical and electronic equipment	10.9	5.9	0.34
Professional equipment goods	15.2	11.1	0.29
Motor vehicles and transportation	3.5	12.3	0.33
Other manufacturing	5.5	3.6	0.36
<b>Services</b>	<b>37.4</b>	<b>32.0</b>	<b>0.33</b>
Electricity, gas and water	1.9	7.2	0.31
Trade	12.3	8.5	0.33
Transport and telecommunications	5.1	10.9	0.36
Business and other services	18.1	5.4	0.32
<b>Unspecified</b>	<b>0.5</b>	<b>0.3</b>	<b>0.47</b>
<b>Total</b>	<b>100</b>	<b>100</b>	<b>0.34</b>

Source: UNCTAD, based on Thomson ONE Banker.

<sup>a</sup> Ratio of foreign assets to total assets.

Annex table 5. Top 5,000 companies by size<sup>a</sup>

Size <sup>a</sup>	Number of companies (% of total)	Foreign assets (% of total)	Internationalization ratio <sup>b</sup>
<b>0-100</b>	<b>29.6</b>	<b>1.7</b>	<b>0.45</b>
0-10	5.5	0.2	0.6
10-100	24.0	105.0	0.42
<b>100+</b>	<b>68.1</b>	<b>94.2</b>	<b>0.27</b>
100-500	28.8	4.8	0.3
500-4 000	28.7	19.8	0.25
4000 and over	10.6	69.6	0.23
<b>Unspecified</b>	<b>2.4</b>	<b>4.2</b>	<b>0.91</b>
<b>Total</b>	<b>100</b>	<b>100</b>	<b>0.34</b>

Source: UNCTAD, based on Thomson ONE Banker.

<sup>a</sup> Classified according to magnitude (in millions of dollars) of assets of the home-country parent company.

<sup>b</sup> Ratio of foreign assets to total assets.

Annex table 6. Top 5,000 companies by home country of the parent company

Region	Number of companies (% of total)	Foreign assets (% of total)	Internationalization ratio <sup>a</sup>
<b>All developed regions</b>	<b>74.0</b>	<b>90.3</b>	<b>31.0</b>
Europe	27.7	47.7	40.0
North America	30.1	28.9	24.8
Other developed countries <sup>b</sup>	5.2	1.8	37.1
Japan	11.0	11.9	22.6
<b>All developing regions</b>	<b>26.0</b>	<b>9.7</b>	<b>41.6</b>
Developing Asia	24.1	7.2	42.0
<b>Total</b>	<b>100</b>	<b>100</b>	<b>33.8</b>

Source: UNCTAD, based on Thomson ONE Banker.

<sup>a</sup> Ratio of foreign assets to total assets.

<sup>b</sup> Excluding Japan.

### ANNEX 3. SURVEY RESULTS: DETAILED STATISTICAL TABLES

Annex table 7. Respondents by sector and industry

Sector/industry	Number	Share in total (%)
<b>Primary</b>	<b>10</b>	<b>5</b>
<b>Manufacturing</b>	<b>118</b>	<b>62</b>
Food products, beverages and tobacco	9	5
Textiles, clothing and leather	5	3
Chemicals, petrochemicals, plastics and rubber	19	10
Metals and non-metallic products	20	10
Electrical and electronic equipment	15	8
Professional equipment goods	27	14
Motor vehicles and transportation	11	6
Other manufacturing	12	6
<b>Services</b>	<b>53</b>	<b>28</b>
Electricity, gas and water	13	7
Trade	14	7
Transport and telecommunications	7	4
Business and other services	19	10
<b>Unspecified</b>	<b>11</b>	<b>6</b>
<b>Total</b>	<b>191</b>	<b>100</b>

Source: UNCTAD survey.

Note: Financial services are excluded from this survey as they are not covered in the list of the 5,000 top companies from which the representative sample was constructed.

Annex table 8. Respondents by company size<sup>a</sup>

Size <sup>a</sup>	Number	Share in total (%)
<b>0-100</b>	<b>15</b>	<b>8</b>
0-10	7	4
10-100	8	4
<b>100+</b>	<b>165</b>	<b>86</b>
100-500	25	13
500-4 000	80	42
4 000 and over	60	31
<b>Unspecified</b>	<b>11</b>	<b>6</b>
<b>Total</b>	<b>191</b>	<b>100</b>

Source: UNCTAD survey.

<sup>a</sup> Classified according to magnitude (in millions of dollars) of the assets of the home-country parent company.

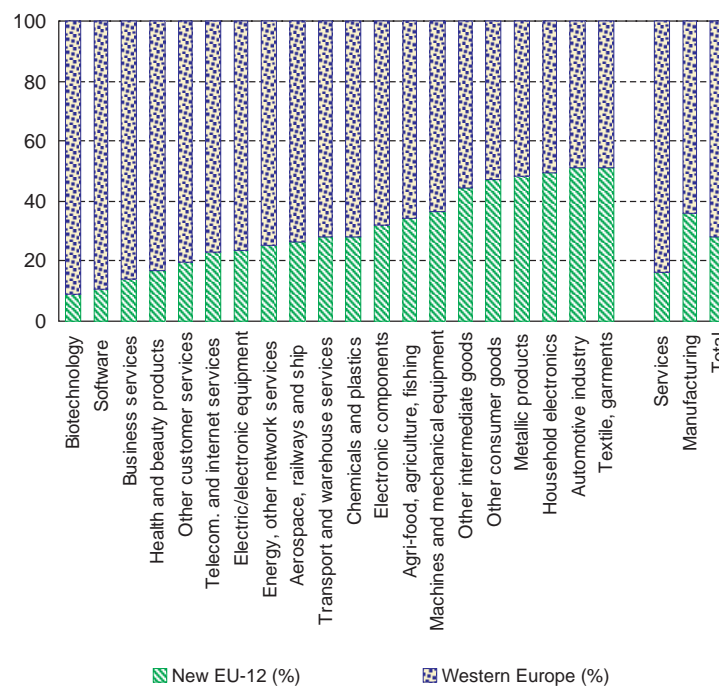
Annex table 9. Respondents by home region

Region	Number	% of total
<b>All developed regions</b>	<b>145</b>	<b>76</b>
Europe	74	39
North America	19	10
Other developed countries	52	27
Japan	44	23
<b>All developing regions</b>	<b>35</b>	<b>18</b>
Developing Asia	28	15
<b>Unspecified</b>	<b>11</b>	<b>6</b>
<b>Total</b>	<b>191</b>	<b>100</b>

Source: UNCTAD survey.

### ANNEX 4. GEOGRAPHICAL BREAKDOWN OF INTERNATIONAL INVESTMENT PROJECTS IN EUROPE, BY SELECTED INDUSTRY

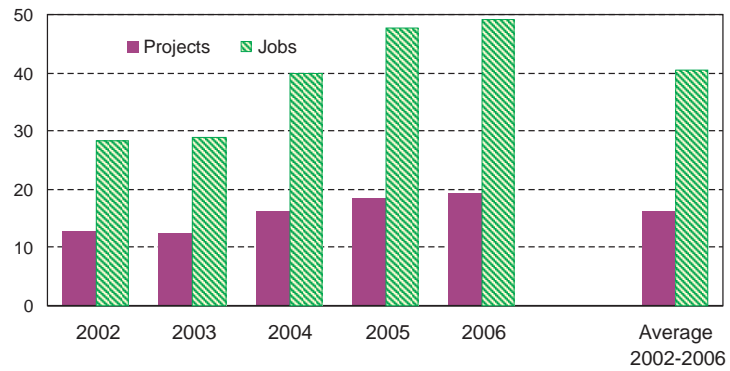
Annex figure 1. Distribution of international projects in Europe's host regions, by industry, 2002–2006  
(Per cent of projects)



Source: UNCTAD, based on Invest in France Agency database on *International Investment in Europe*.

Note: In this annex, the new EU-12 does not include Cyprus and Malta and Western Europe is defined as EU-15 plus other Europe, Cyprus and Malta.

**Annex figure 2. Market share of international projects and jobs heading to the new EU-12 countries in selected high value added industries,<sup>a</sup> 2002–2006**  
(Per cent of all international projects heading to whole of Europe in these industries)



Source : Invest in France Agency Data Base on International Investment in Europe.

<sup>a</sup> Aerospace, electronic components, biotechnology, health products, other business services and software.

## ANNEX 5. INDUSTRY CLASSIFICATIONS USED IN THE SURVEY

The industry classification used in this survey, while generally the same as those used in UNCTAD's *World Investment Reports*, are slightly different. The following tables (annex tables 10 and 11) show the correspondence between the survey classification and the usual UNCTAD ones.

**Annex table 10. Classification by home regions**

UNCTAD survey	
Europe	EU-15, new EU-12, other Europe
North America	Canada and United States
Other developed economies	Australia, Israel, Japan, New Zealand
Developing economies	All other countries

**Annex table 11. Classification by host regions**

Selected regions referred to in the UNCTAD survey	Countries
North America	Canada and United States
EU-15	Austria, Belgium, Denmark, Finland, France, Germany, Greece, Ireland, Italy, Luxembourg, Netherlands, Portugal, Spain, Sweden and United Kingdom.
New EU-12	Bulgaria, Cyprus, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, Romania, Slovakia and Slovenia
Other Europe	Norway and Switzerland
Western Europe	EU-15, Other Europe, Cyprus and Malta.
Other developed countries	Australia, Israel, Japan and New Zealand

*Note:* For the other regions not listed above, the standard United Nations classification is used.

Annex table 12. Classification by sector and industry

UNCTAD World Investment Prospects Survey	<i>World Investment Report</i>
<b>Primary</b>	Agriculture, hunting, forestry and fisheries, mining, quarrying and petroleum
<b>Manufacturing</b>	<b>Manufacturing</b>
<i>of which:</i>	<i>of which:</i>
Food products, beverages and tobacco	Food, beverages and tobacco
Textiles, clothing and leather	Textiles, clothing and leather
Pharmaceuticals, chemicals and plastics	Chemicals and chemical products
Metals and non-metallic products	Metals and metal products, non-metallic mineral products
Electrical and electronic equipment	Electrical and electronic equipment
Professional equipment goods	Machinery and equipment
Motor vehicles and transportation	Motor vehicles and other transport equipment
Other manufacturing	Wood and wood products, publishing, printing and reproduction of recorded media, coke, petroleum products and nuclear fuel, other manufacturing
<b>Services</b>	<b>Services</b>
<i>of which:</i>	<i>of which:</i>
Electricity, gas and water	Electricity, gas and water
Trade	Trade
Transport and telecommunications	Transport, storage and communications
	Business activities, construction, hotels and restaurants, finance, public administration and defence, education, health and social services, community, social and personal service activities, other services
Business and other services	

#### Note

The list of the 100 largest TNCs in the world, ranked by foreign assets can be found in UNCTAD's annual *World Investment Report*.



## QUESTIONNAIRE

### *World Investment Prospects Survey 2007-2009*

In order to improve the quality and relevance of the work of the UNCTAD Division on Investment, Technology and Enterprise Development, it would be useful to receive the views of readers on this publication. It would therefore be greatly appreciated if you could complete the following questionnaire and return it to:

Readership Survey  
UNCTAD Division on Investment, Technology and Enterprise Development  
United Nations Office in Geneva  
Palais des Nations, Room E-9123  
CH-1211 Geneva 10, Switzerland  
Fax: 41-22-917-0194

1. Name and address of respondent (optional):

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2. Which of the following best describes your area of work?

Government	<input type="checkbox"/>	Public enterprise	<input type="checkbox"/>
Private enterprise	<input type="checkbox"/>	Academic or research Institution	<input type="checkbox"/>
International organisation	<input type="checkbox"/>	Media	<input type="checkbox"/>
Not-for-profit organisation	<input type="checkbox"/>	Other (specify) _____	

3. In which country do you work? \_\_\_\_\_

4. What is your assessment of the contents of this publication?

Excellent	<input type="checkbox"/>	Adequate	<input type="checkbox"/>
Good	<input type="checkbox"/>	Poor	<input type="checkbox"/>

5. How useful is this publication to your work?
- Very useful     Somewhat useful     Irrelevant
6. Please indicate the three things you liked best about this publication:
- \_\_\_\_\_
- \_\_\_\_\_
- \_\_\_\_\_
7. Please indicate the three things you liked least about this publication:
- \_\_\_\_\_
- \_\_\_\_\_
- \_\_\_\_\_
8. If you have read other publications of the UNCTD Division on Investment, Enterprise Development and Technology, what is your overall assessment of them?
- |                    |                          |  |                          |
|--------------------|--------------------------|--|--------------------------|
| Consistently good  | <input type="checkbox"/> | Usually good, but with some exceptions | <input type="checkbox"/> |
| Generally mediocre | <input type="checkbox"/> | Poor                                   | <input type="checkbox"/> |
9. On the average, how useful are those publications to you in your work?
- Very useful     Somewhat useful     Irrelevant
10. Are you a regular recipient of Transnational Corporations (formerly The CTC Reporter), UNCTAD-DITE's tri-annual refereed journal?
- Yes     No
- If not, please check here if you would like to receive a sample copy sent to the name and address you have given above