

Assessing the impact of the current financial and economic crisis on global FDI flows

by

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Executive summary

The year 2008 will mark the end of a growth cycle in international investment that started in 2004 and saw world foreign direct investment (FDI) flows reach a historic record of \$1.8 trillion in 2007. Due to the impact of the ongoing worldwide financial and economic crisis, FDI flows could decline by more than 20 per cent in 2008. A further decrease in FDI flows can be expected in 2009, as the full consequences of the crisis on transnational corporations' (TNCs)' investment expenditures will continue to unfold.

The fall in global FDI in 2008–2009 is the result of two major factors affecting domestic as well as international investment. First, the *capability* of firms to invest has been reduced by a fall in access to financial resources, both internally – due to a decline in corporate profits – and externally – due to lower availability and higher cost of finance. Second, the *propensity* to invest has been affected negatively by economic prospects, especially in developed countries that are hit by severe recession. The impact of both factors is compounded by the fact that, as of early 2009, a very high level of risk perception is leading companies to extensively curtail their costs and investment programmes in order to become more resilient to any further deterioration of their business environment. All of the three major types of FDI (market-seeking, efficiency-seeking, and resources-seeking) will be impacted by these factors, though with different magnitudes and consequences on location patterns.

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The setback in FDI has particularly affected cross-border mergers and acquisitions (M&As), the value of which was in sharp decline in 2008 as compared to the previous year's historic high. It has also taken the form of a rising wave of divestments and restructurings. International greenfield investments have been less impacted to this point, but could be increasingly affected in 2009 as a large number of projects are presently being cancelled or postponed.

However, the impact on FDI is different, depending on region and sector. Developed countries have so far been the most affected, with a decline in FDI inflows in 2008, due mainly to sluggish market prospects. Flows into developing economies continued to grow in 2008, but at a much lower rate than the year before. An outright decline in FDI inflows to those countries is possible in 2009, due to a pull-back both in efficiency and resource-seeking FDI aimed at exporting to advanced economies that are currently depressed, and in market-seeking FDI aimed at servicing local markets with growth prospects that, although still positive, have receded.

Among industries, FDI flows to financial services, automotive industries, building materials, intermediate goods and some consumption goods have been the most significantly affected to date. But the consequences of the crisis are now quickly expanding to FDI in other activities, ranging from the primary sector to non-financial services.

In the short term, the negative impact of the present economic recession on global FDI prospects should be the dominant one. Medium-term FDI prospects are more difficult to assess, due to the exceptional magnitude of the present crisis and to the fact that it could lead to major structural changes in the world economy. Nevertheless, some favourable factors for FDI growth are still at work, some of which are even a consequence of the crisis itself. Driving forces such as investment opportunities triggered by cheap asset prices and industry restructuring, large amounts of financial resources available in emerging countries, quick expansion of new activities such as new energies and environment-related industries, and a resilient trend in the internationalization of companies will presumably trigger, sooner or later, a new pickup in FDI flows.

The exact date of this upward switch will, however, depend on a series of uncertain factors such as the speed of economic and financial recovery, the efficiency of public policy in addressing the causes of the present crisis, the return of investor confidence and the ability to prevent protectionist tendencies. To illustrate those uncertainties and provide a framework for further discussion and analysis, this paper presents a set of three scenarios: V (quick recovery of FDI as soon as 2010), U (slow recovery beginning in 2011), and L (no recovery before 2012).

Public policies will obviously play a major role in the implementation of favourable conditions for a quick recovery in FDI flows. Structural reforms aimed at ensuring more stability in the world financial system, renewed commitment to an open environment for FDI, the implementation of policies aimed at favouring investment and innovation are key issues in this respect. For effectively dealing with the crisis and its economic aftermath, it is important for policymakers to resist the temptation of quick-fix solutions or protectionism, and to maintain an overall favourable business and investment climate.

Introduction

The unusual magnitude of the on-going crisis is raising major concerns about the future of the world economic outlook, especially as it relates to international investment. In this context, UNCTAD has complemented its estimates of foreign direct investment (FDI) inflows¹ for the past year with the present note on the impact of the crisis on international investment.²

This note is organized as follows. Chapter I provides a quantitative analysis/picture of FDI flows in 2008, in the light of the evolution of the overall economic environment, including the instability in the financial sector and the global economic slowdown. It also shows the uneven magnitude of the setback in international investment among regions and industries. Chapter II analyzes the channels of transmission of the present crisis to FDI, and assesses its impact by type of FDI. Chapter III explores various scenarios for the medium term, ranging from quick recovery to persistent stagnation of FDI flows. Finally, chapter IV deals with the implications of the present crisis for public policies.

I. The end of an FDI growth cycle: worldwide FDI down by more than 20% in 2008

A record year for FDI in 2007. During 2003–2007, FDI flows followed an upward trend, fuelled by steady world economic growth, ongoing liberalization in investment regimes and the implementation of large-scale internationalization strategies by a growing number of transnational corporations (TNCs). This led to an unprecedented level in FDI flows in 2007, with flows reaching a historic record of \$1.8 trillion.

The crisis leaves its first marks on FDI in early 2008. The financial instability triggered by the United States subprime crisis which began in summer 2007 has led to a progressive deterioration of the investment situation. Various indicators during the first half of 2008 already suggested a decline in world growth prospects as well as in investors' confidence. This deteriorating climate began to leave its first negative marks in investment programmes, including FDI, in early 2008. According to UNCTAD's 2008-2010 *World Investment Prospects Survey*, conducted April–June 2008, 40 per cent of the respondent companies already mentioned at that time that the financial instability had a "negative" or "very negative" impact on their investment expenditures and programmes. The same study showed that, on average, TNCs' views on their medium-term investment prospects were already significantly less optimistic than in the previous year's survey (UNCTAD, 2008a). Data available during summer 2008 already showed a downward trend for the first semester of 2008, both for cross-

¹ See UNCTAD Press Release, "Global foreign direct investment now in decline – and estimated to have fallen during 2008", UNCTAD/PRESS/PR/2009/001.

² In view of the quickly evolving consequences of the crisis on economic growth in developed and developing countries, and on international investment, updates will be released during the course of 2009.

border mergers and acquisitions (M&As) and FDI flows, as compared to the same period of the previous year (UNCTAD, 2008b).

A brutal shock in October 2008. During the first eight months of 2008, the world financial system went through a period of relative relief, leading to some optimism regarding the outcome of the on-going crisis. But subsequently, a brutal crisis erupted again, when first, major United States financial firms, such as Lehman Brothers and AIG and then European financial institutions, such as Fortis, Dexia, and a number of Icelandic banks showed signs of insolvency. It then became clear that this crash was a symptom of a wider underlying malaise in the global financial services industry, reflecting in particular serious lacunae in the regulatory system.³ The crisis then expanded in magnitude, and full-scale turmoil ensued in financial markets, buffeting many developed and emerging economies. A number of emerging economies such as Hungary, Latvia and Ukraine, as well as Iceland, had then to turn to the International Monetary Fund (IMF) for assistance.

The crisis then quickly spread far beyond the financial sector, with serious repercussions for the “real economy”. Much tighter credit conditions unavoidably affected firms’ ability to spend on factories and equipment as well as on acquisitions. Consumer confidence fell sharply in many parts of the world, reaching historical lows first in the case of the United States and later on in the European Union.⁴ And large companies in many industries were seriously affected by the decline in sales. Starting with financial services, which have been directly affected by the crisis, the shock waves have hit many other industries, ranging from extractive industries and manufacturing to infrastructure services.

A global economic slowdown is now projected⁵ and recession is already gripping a number of major developed economies. Industries likely to be especially affected are a number of manufacturing industries, including automobiles, aircraft, building materials, consumer goods, steel, and services such as transport services (airlines, logistics) (box 2).

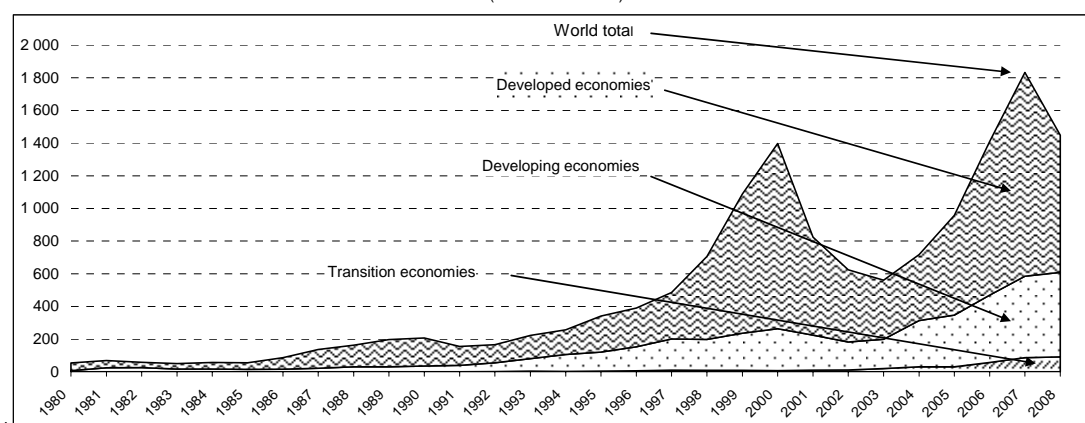
³ For UNCTAD’s view on the financial crisis, see, for example, “The crisis of a century”; *UNCTAD Policy Briefs*, October 2008; and “Follow-up International Conference on Financing for Development to Review the Implementation of the Monterrey Consensus”, Issues note by the UNCTAD secretariat, Trade and Development Board, Forty-fifth executive session, Geneva, 13 November 2008 (TD/B/EX(45)/2).

⁴ The United States consumer confidence index, for example, plummeted in October 2008 to an all-time low since records began in 1978 (“US consumer confidence hits record low”. *Financial Times*, 28 October 2008). The Economic Confidence Index in the Eurozone has fallen to its lowest level since its creation in 1995. (Source: Bloomberg in *Le Monde*, 10 January 2009.)

⁵ According to the most recent IMF forecast in November 2008 (see also table 2), world output is projected to expand by 2.2 per cent in 2009, down by .75 per cent compared to the October projection and down by 1.5 per cent as compared to the projection in April. (Source: IMF, “Rapidly weakening prospects call for new policy stimulus”, *World Economic Outlook Update*, 6 November 2008.) United Nations forecasts are even more pessimistic, with a meager 1 per cent growth projected for the world economy by the most recent *World Economic Situation and Prospects* (United Nations, January 2009).

FDI to decline by more than 20 per cent in 2008. In the face of the global economic slowdown (and recession in a number of major economies), tighter credit conditions and falling corporate profits, many companies have announced plans to curtail production, lay off workers and cut capital expenditure, all of which has implications for FDI. According to a preliminary estimate by UNCTAD, world FDI flows are expected to have declined in 2008 by 21 per cent (figure 1 and table 1), due among other things to a sharp step-back of flows during the last quarter of the year.

Figure 1. FDI inflows, global and by group of economies, 1980-2008
(Billions of dollars)



Source: UNCTAD, based on FDI/TNC database (www.unctad.org/fdi statistics) and UNCTAD own estimates.

However, the impact of the crisis varies widely, depending on region and country, with consequences for the geographic pattern of FDI flows. One has to keep in mind that the present situation is very different from that of the most recent previous financial crisis, which originated in developing countries (such as the 1997 Asian crisis, see UNCTAD, 1998a) and had a significant negative influence on FDI inflows in a number of them (such as Indonesia).⁶ In contrast, the current crisis began in the developed world, though it is rapidly spreading to developing and transition economies. Developed countries have thus been directly hit by the financial crisis, while its effects on developing economies have so far been indirect in most cases, with varying degrees of severity among regions and countries. This has direct consequences on the geographical patterns of FDI inflows.

Developed countries were the most affected in 2008. In many developed countries, preliminary data suggest that in 2008, as a result of the protracted and deepening problems affecting financial institutions, as well as the liquidity crisis in the money and debt markets, FDI flows have fallen, leading to a decline estimated at about 33 per cent for this group as whole. Inward flows might be particularly low in Finland, Germany, Hungary and Italy, even compared with 2006 levels, while flows to the United Kingdom, France⁷ and the United States are estimated to have declined

⁶ In other countries, the crisis speeded up liberalization and actually led to an increase in FDI inflows (as in the Republic of Korea).

⁷ According to a survey of the French affiliates of United States TNCs released in October 2008, 83 per cent of respondents said that their groups as a whole had been affected by the worldwide economic slowdown, and 60 per cent said that their French affiliates had been affected. (Source: American Chamber of Commerce in France and Bain & Co., *2008 Amcham-Bain Barometer*, 23 October 2008.)

– by a significant margin in the case of France and the United Kingdom compared to their 2007 historical high levels. Decreased earnings of developed-country TNCs and a decline of syndicated bank loans have particularly limited financing for investment. A decline in leveraged buyout transactions also dampened cross-border M&As, further depressing FDI flows. Cross-border M&A sales in developed countries fell by a similar magnitude (33 per cent) in 2008 (table 1).

Table 1. FDI inflows and cross-border M&As, by region and major economy, 2007-2008 (Billions of dollars)

Region/economy	FDI inflows			Cross-border M&As		
	2007	2008 ^a	Growth rate (%)	2007	2008 ^a	Growth rate (%)
World	1,833.3	1,449.1	- 21.0	1,637.1	1,183.7	-27.7
Developed economies	1,247.6	840.1	- 32.7	1,454.1	981.8	-32.5
Europe	848.5	562.3	- 33.7	825.0	548.7	-33.5
United States	232.8	220.0	- 5.5	379.4	314.9	-17.0
Japan	22.5	17.4	- 22.6	21.4	19.1	-10.8
Developing economies	499.7	517.7	3.6	152.9	177.0	15.7
Africa	53.0	61.9	16.8	10.2	26.3	157.0
Latin America and the Caribbean	126.3	142.3	12.7	30.7	29.5	-3.8
Asia and Oceania	320.5	313.5	- 2.2	112.0	121.2	8.2
West Asia	71.5	56.3	- 21.3	30.3	31.5	4.0
South, East and South-East Asia	247.8	256.1	3.3	81.5	89.4	9.7
Transition economies	85.9	91.3	6.2	30.1	25.0	-17.0

Source: UNCTAD.

^a Preliminary estimates.

Note: World FDI inflows in 2008 are projected on the basis of data for 103 economies for which data were available for part of 2008 as of 19 December 2008. Data for 2008 are estimated by annualizing the data available, in most cases for 6–10 months of 2008, except for France, Germany, Greece, the Netherlands, Poland, Romania, Spain, Sweden, Canada, United States, Australia, Japan, Pakistan, Kazakhstan and Ukraine where FDI flows in last few months of 2008 are assumed to be negligible. The proportion of inflows to these economies in total inflows to their respective region or subregion in 2007 is used to extrapolate the 2008 data. For cross-border M&As, estimates were made on the basis of data available as of 5 January 2009.

In developing and transition economies, FDI inflows have so far remained more resilient. The growth rate of FDI inflows to developing countries, while lower than in 2007 (when it exceeded 20 per cent) should still reach an estimated 4 per cent. Flows to *Africa* are expected to grow further to more than \$60 billion, despite the slowdown in global economic growth and its negative consequences for the region. Flows to East, South and South-East Asia (the largest recipient of FDI among developing economies, accounting for almost half of all flows to developing countries) might rise, but by a slower rate compared with 2007. West Asia is projected to see flows decline significantly (more than 20 per cent), following the record level registered last year, due to slower growth in oil demand, rising costs and lower funds from export proceeds (due to lower prices of oil). By contrast, FDI flows to Latin America and the Caribbean are expected to show significant resilience to the world economic slowdown, with an estimated 13 per cent increase, partly as a result of a strong rise in FDI flows to South America. However, Central America and the Caribbean – which are traditionally highly dependent on the United States economy – are most likely to register a decline. FDI flows to the transition economies of South-East Europe and the Commonwealth of Independent States should maintain their upward trend despite the financial crisis and regional conflicts, registering an increase of about 6 per cent. In contrast to developed countries, M&As in developing countries rose by 16 per cent in 2008, particularly in Africa and Asia (table 1), although from a

generally low level (with the exception of Asia, where M&A values are already significant).

While the decrease in FDI inflows has hit developed countries the hardest, some developing economies with open but weak financial systems are also very vulnerable to external shocks. They face unprecedented challenges from the possible drying up of financial flows from both official and private sources. For example, FDI inflows are expected to have declined sharply in such countries as Indonesia, the Republic of Korea, Pakistan, Singapore and Turkey, due to fallout from the financial crisis.

II. Channels of transmission of the crisis to FDI flows

The current global financial and economic crisis influences firms' *capacity* to invest as a result of reduced availability of finance and their *propensity* to invest due to gloomy economic and markets prospects.

Reduced access to finance. Financial factors have negatively affected TNCs' *capacity* to invest, both internally and externally, as tighter credit conditions and lower corporate profits curtail TNCs' financial resources for overseas investment projects (as well as domestic ones). On the one hand, credit has become less abundant and more expensive. The external funding environment for non-financial companies has deteriorated markedly since mid-2008, making it more difficult for them to invest in foreign operations or to make cross-border M&A deals. For instance, spreads in corporate bonds soared dramatically in the last months of 2008 (IMF, 2008). On the other hand, poor earnings of large companies in a broad range of industries in the United States, Europe and Japan, as evidenced by declared or projected profits from the third quarter of 2008 onwards, reduce the companies' self-financing capabilities. For example, operating earnings of S&P 500 companies are projected to decline by 22 per cent in 2008.⁸ At the same time, a more than 40 per cent decline in stock markets worldwide has reduced TNCs' ability to turn to stock markets for financing purposes and to leverage their M&A activities using stock shares.

Gloomy prospects. The gloomy evolution of markets, including the looming sharp economic recession worldwide (and even recession in a number of developed countries) and a heightened appreciation of risk, has also reduced firms' *propensity* to invest for further expansion both domestically and internationally of production capacity. As indicated above, according to the latest IMF forecasts, world output is predicted to expand by only 2.2 per cent in 2009, a decline of almost three percentage points compared to 2007. Total output in advanced economies as a whole would contract on a full-year basis in 2009, the first such fall in the post-war period, from 1.4 per cent in 2008 to -0.3 per cent in 2009, while emerging and developing economies would maintain a positive though reduced growth rate (+ 5.1 per cent). The United Nations and the World Bank point to similar declines (table 2).

⁸ Source: Morgan Stanley, "Corporate profits: global recession intensifies downside risks", *Global Economic Forum*, 6 November 2008. Similarly, 541 Japanese manufacturing companies listed in stock markets are projected to lose their profits by more than 20 per cent in 2008 (*Nikkei*, 2 November 2008).

Table 2. World GDP growth and growth prospects, 2007-2008
(Yearly GDP growth rate according to various sources)

Sources/regions	2007	2008	2009	2010
IMF: world	5	3.7	2.2	-
Advanced economies	2.6	1.4	-0.3	-
Emerging and developing economies	8.0	6.6	5.1	-
World Bank: world	3.7	2.5	0.9	3.0
high income countries	2.6	1.3	-0.1	2.0
developing countries	7.9	6.3	4.5	6.1
United Nations: world	3.8	2.5	1.0 (baseline)	-
Developed economies	2.5	1.2	-0.5 (baseline)	-
Economies in transition	8.3	6.9	4.8 (baseline)	-
Developing economies	7.2	5.9	4.6 (baseline)	-

Source: IMF (2008), World Bank (2009), and United Nations (2009).

Risk aversion. Companies' investment plans may also be scaled back due to a high level of perceived risks and uncertainties, in order to develop resilience to possible "worst-case" scenarios regarding financial and economic conditions. As many available confidence indicators have fallen to historical lows – as indicated, for example, by the fall in the Ifo World Economic Climate index,⁹ the consumer confidence index of the Conference Board¹⁰ or the Euro Zone Economic Confidence Index – a large percentage of companies might implement cost-cutting programmes (including divestments, layoffs, postponing or cancellation of investment projects) beyond what would be justified by the grim scenarios regarding business prospects.

As show in box 1, the impact of these negative factors may vary significantly depending of the type of investment as defined by their main motives: market-seeking, efficiency-seeking and resources-seeking.

Box 1. Various types of investment motives are affected unequally by the crisis

International investment theory usually distinguishes between types of FDI according to three major motives for investing abroad (see UNCTAD 1998b: 91): market-seeking, efficiency-seeking, and resource-seeking. All three are impacted by the ongoing financial and economic crisis, but with differences in magnitude and location pattern of impact.

The most directly affected types of investment so far have been *market-seeking* projects, especially those aimed at developed countries. As advanced economies might experience a negative growth in 2009, companies are restraining the launching of new projects aimed at increasing their market-oriented production capabilities there (see examples in box 2), while they remain more committed to capacity expansion in emerging and developing economies (see examples in box 3). But this commitment might weaken in 2009 as growth slows in the latter group of economies, due – among other reasons – to a decline in the value of their exports as a result of weakening external demand from the developed countries and a fall in commodity and energy prices.

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⁹ According to the latest issue of the *World Economic Survey*, published quarterly by the German Ifo Institute for Economic Research since 1987, the Ifo World Economic Climate index fell to its lowest historical level in the fourth quarter of 2008.

¹⁰ "US consumer confidence hits record low", *Financial Times*, 28 October 2008.

The impact of the crisis on *efficiency-seeking* projects is more difficult to assess. On the one hand, these projects will suffer globally from the decline in the companies' financial capabilities. On the other hand, many companies might be compelled by the ongoing crisis to restructure their international activities to cut cost and boost overall efficiency. This means above all closing or downsizing obsolete or non-cost-competitive facilities (often located in advanced economies), but also opening some new cost-efficient facilities, especially in emerging economies.

Finally, *resource-seeking* FDI projects could suffer, at least in the short-term, from the decline in world demand and consequently in prices, with particularly negative effects on resource-rich developing countries. It should be noted, however, that this setback in resource-seeking investment closely follows a period of euphoria, when quickly-rising world demand triggered imbalances in commodity markets, boosting prices and leading companies to launch many new projects. It is highly probable that these imbalances will quickly arise again once the present recession is over, putting resource-seeking FDI back on the road to growth.

The decline in the propensity to invest abroad can take various forms (including divestment and restructuring), and differ according to entry modes (e.g. M&As, greenfield investment):

There has been a recent rise in *divestments and restructuring of operations* (see examples in box 2). Companies indeed undertake divestments and make cuts in existing production capacity – either by shutting down plants or factory lines, or by selling some of their assets to other companies¹¹ – to restructure foreign operations, save costs, or improve their balance-sheet situation, especially through lowering the debt-equity ratio.¹²

There is also evidence that *cross-border M&As* have already been sharply affected as a direct consequence of the crisis, with a 17 per cent decline in cross-border M&As in the first 10 months of 2008 as compared to the same period of 2007 (table 1). This decline was due, among other factors, to the fact that leveraged buyouts, a common transaction method in M&As, have fallen considerably due to weakened world stock markets. For some countries, the difficulties emerging in M&A deals have brought large privatization projects to a halt (table 3).¹³ The decline in cross-border M&As is of utmost importance for FDI flows, which are strongly correlated with cross-border M&A amounts.

¹¹ In the last-mentioned case, recording FDI flows in the balance-of-payments based statistics may vary depending on the location of the asset sold and the country of residence of the selling and buying companies.

¹² See e.g. Mehrdad Baghai, Sven Smit, and S. Patrick Viguerie, "M&A strategies in a down market", *The McKinsey Quarterly*, September 2008.

¹³ For example, the global financial crisis will bring the Swedish Government's \$26 billion privatization programme to a halt two years before it is due to be completed. The French Government is also to postpone the privatization of State-owned company La Poste due to the financial crisis. (Source: *Financial Times*, 4 November 2008.) In Mexico, the Government has pushed back the deadline of bidding for Punta Colonet, a \$6 billion port project. The privatization of Kuwait Airways Corporation might also be postponed due to the present global financial crisis. (Source: Kuwait News Agency, 23 October 2008.)

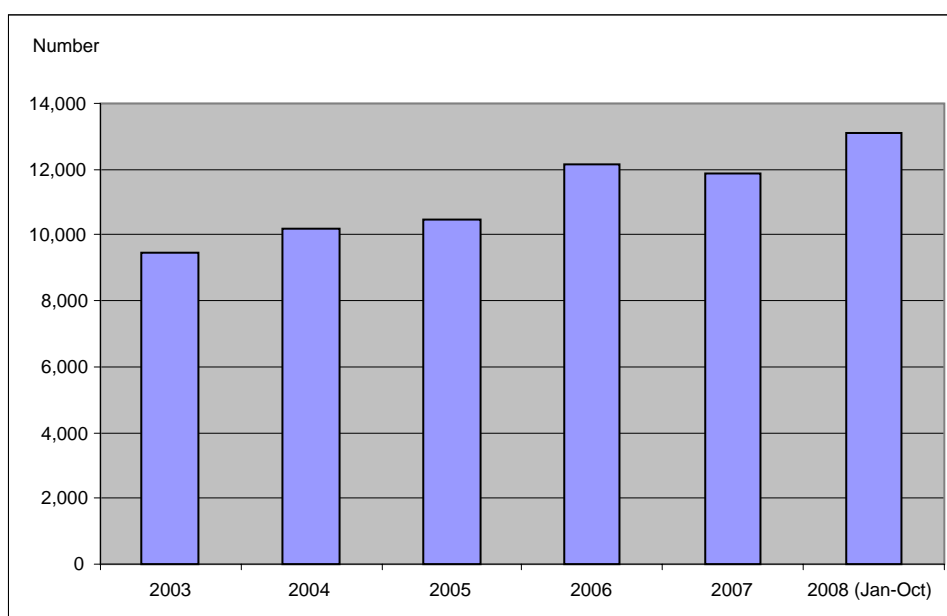
Table 3. Selected cross-border M&As and privatization programmes dropped or halted due to the global financial crisis, 2008-2009

Acquiring company (country)/privatization	Target company (country)	Value	Industry
Samsung Electronics (Rep. of Korea)	SanDisk (United States)	\$5.9 billion	Electronics
Xstrata (United Kingdom and Switzerland)	Lonmin (United States)	\$10 billion	Mining
AT&T, Vodafone, Blackstone	Huawei mobile handset business (China)	\$2 billion	Electronics
Ping An Insurance (China)	Fortis (Belgium)	Euro 2.2 billion	Finance
Privatization	Punta Colonet (Mexico)	\$6 billion	Port
Privatization	Kuwait Airways (Kuwait)	-	Airlines
Privatization	La Poste (France)	-	Postal services
Privatization	TeliaSonera (Sweden)	-	Telecom
Privatization	Nordea (Sweden)	-	Finance
Privatization	Oman Telecommunication Company (25%)	-	Telecom
Privatization	SBAB (Sweden)	-	Finance

Source: UNCTAD, based on various newspaper accounts.

Greenfield investments (new investments and expansion of existing facilities) seem to have so far been quite resilient to the crisis. At the end of October, the number of such investments since the beginning of 2008 was already over 13,000, exceeding the level registered for the whole year 2007 (figure 2). But many recent announcements in various industries point to the cancellation or postponement of many projects, the consequences of which will be fully felt in 2009. For example, Hutchison Whampoa (Hong Kong, China), the largest TNC from the developing world and a leading conglomerate in infrastructure industries globally (UNCTAD, 2008b), has announced that it will suspend all new investments in its global operations.¹⁴ (For other examples, see box 2).

Figure 2. Number of worldwide greenfield FDI cases, 2003-2008 October



Source: UNCTAD, based on data from FDI Markets, FDI Intelligence (www.fdimarkets.com).

¹⁴ Source: *Ming Pao News*, 24 October. 2008.

Box 2. Concrete examples of decreases in FDI

A number of developments indicate the negative impact of the crisis on FDI in specific industries and on specific companies. They include the following:

- Financial services are experiencing a wave of restructuring in most affected countries. AIG of the United States, for example, is selling off its Japanese and Philippines insurance affiliates. In Iceland, where nearly half of inward FDI stock is in financial services, FDI inflows are expected to turn negative to the order of \$0.4 billion in 2008. Inflows to the Netherlands, another financial centre, could also fall by more than 70 per cent (annex table).^a
- In the mining industry, Rio Tinto (United Kingdom and Australia) and Anglo American (United Kingdom) have indicated that they will reconsider their global expansion plans in the light of waning business confidence and the worsening economic outlook. British Petroleum announced in October 2008 that it will cut 5,000 jobs worldwide in 2009, mainly in developed markets.
- In the automotive industry, leading United States automobile maker General Motors announced in November 2008 – even before the bailout granted by the United States Federal Government – plans to cut costs and capital spending while raising funds through the sale of assets. Daewoo, a subsidiary of General Motors, announced that it would temporarily close Republic of Korea factories in the same month. Similarly in Argentina, General Motors plans to cut jobs just a few months after record production in the country in September. The company also planned to halt production in Thailand in December 2008 and January 2009, and to cut jobs in its Gliwice plant in Poland. Opel, a subsidiary of General Motors, has asked for more public support from the German Government. Ford is to shut down its operations in Berdoux, France, due to poor sales, from October 2008 to at least mid-January 2009. French automaker PSA has already halted its car production for a while in China, and it intends to temporarily close factories in Spain and France. Another French automaker, Renault, also plans to reduce jobs significantly in Europe.
- In the aircraft industry, orders for new aircrafts are falling, as illustrated by the order cancellations announced by EADS (France) and Boeing (United States).
- In building materials, Lafarge SA (France), the world's largest cement producer, will scale back international expansion and sell assets to reduce its debt ratio. The company is committed to completing only 60 per cent of previously-planned investments in new plants amid a global slump in cement demand. Lafarge also sold its cement and aggregates units in Italy to local group Sacci.^b The world's second largest cement maker Cemex (Mexico) will sell its assets in the Canary Islands in order to cut debts. Cemex is also facing slumping sales in Europe.
- In consumer goods, GlaxoSmithKline (United Kingdom), the world's second largest drug maker by revenue, is cutting its operations in the United States. Following the lead of many of its competitors, the company is reducing its United States sales force and will close its affiliate in Philadelphia. French cosmetics group L'Oréal, faced with a sales slump, announced in November that it would close two factories in Europe, one in Monaco and one in Wales (United Kingdom).
- In the steel industry, a number of companies including ArcelorMittal (Luxembourg) and POSCO (Republic of Korea) have started to revise their growth plans.^c For example, ArcelorMittal, the world's largest steelmaker, is reviewing its global expansion programme released in 2007 due to bleak sales prospects. One potential change being considered is to postpone its ambitious project in India, which includes two new steel plants with total investment of \$20 billion. Steelmakers in the United Kingdom, the Russian Federation and Japan have also decided to curtail production. This happened only two months after steel prices rose to a record high.

- In transport services, the logistics giant Deutsche Post (Germany) is restructuring its United States operations and substantially reducing its work force in the country.

Source: UNCTAD, based on reports in newspapers and other media.

^a FDI flows in 2008 into these countries as well as others mentioned in this note are estimates by UNCTAD.

^b Source: *Bloomberg*, 4 November 2008.

^c Peter Marsh, "Mittal reviews \$35bn growth plans", *Financial Times*, 23 October 2008.

III. What next? Scenarios for the medium term

While the negative impacts of the financial and economic crisis on FDI will presumably remain dominant in 2009, various positive factors are still at work and will trigger, sooner or later, a recovery of international investment flows. The date of this recovery is, however, dependant on many factors that are uncertain. Three different scenarios (V, U and L) are considered to depict these uncertainties, as well as the complex nature of the recovery mechanisms at work. These alternative scenarios are outlined below, following a discussion of the specific features of the current crisis, of their negative implications for FDI and of the various positive factors still at work.

The current financial and economic crisis is different in nature and magnitude from those of the last 20 years, for at least three reasons: (a) originating in the developed countries, it has rapidly impacted the world economy as a whole due both to its unusual scale and to the existence of large diffusion channels related to globalization; (b) it is not a "usual" business cycle incident, but is of a more profound nature – it reveals structural weaknesses and shortcomings in the regulation of the world financial system, such as lack of transparency and control mechanisms and the incapacity to prevent hazardous behaviours excessively focused on the search for short-term profitability; (c) it might also reflect changes in economic power between the advanced economies – considerably affected by the crisis, including for inward FDI flows – and emerging and cash-rich developing countries, the position of which in the world economic and financial system is presently strengthening.¹⁵

This situation has two major consequences for FDI in 2009 and onwards. First, it could have a lasting negative effect on the dynamics of FDI flows, due to its forceful impacts on market growth and financial resources. Second, it creates a situation of widespread uncertainty regarding the future evolution of FDI and notably the date and conditions of a future pick-up of flows.

However, positive driving forces remain at work. There are a number of reasons why TNCs might remain committed to FDI, even in the midst of the crisis.

First, a number of large emerging economies, such as Brazil, China, India and the Russian Federation, have remained attractive to FDI, particularly to market-seeking FDI. They maintained relatively high economic growth rates (compared to

¹⁵ UNCTAD Policy Brief, "Rebuilding financial multilateralism", No.4, October 2008.

advanced economies) in 2008.¹⁶ As prospects continue to deteriorate in developed countries (more markedly than in developing ones), investors will favour the relatively more profitable options available in developing countries.¹⁷ Examples of FDI in developing and transition economies arising from continuing market opportunities in those countries, or the longer-time horizons of investing TNCs include:

- PepsiCo announced in early November that it would invest an additional \$1 billion to expand its production in China in the next four years, while at the same time shutting down six factories and laying off 3,300 workers in the United States in order to cut costs.¹⁸
- Italian automaker Fiat Group and OJSC Sollers signed a letter of intent in November to expand production of Fiat cars in the Russian Federation, where demand remains strong, despite the slowdown in the automobile industry in Europe and the United States. This is part of the shift of production towards emerging economies. For example, in 2008, the total number of car sales in the “BRIC” countries (Brazil, the Russian Federation, India and China) was expected to exceed that in the United States.¹⁹

Second, financial crises and tough economic periods also offer opportunities to companies to buy assets at “bargain prices” and take advantage of large-scale industry consolidation in some activities. For aggressive, cash-rich TNCs – or those from cash-rich countries – the acquisition of undervalued assets may boost their investment in both developed and developing countries, depending on the circumstance and opportunities. Dramatic exchange rate and share price falls may lead to a round of acquisitions targeting bargain assets in a number of countries, and a possible wave of consolidations in certain industries, such as oil and gas, metal mining,²⁰ automotive industry and financial services. A number of companies have already taken advantage of such opportunities (box 3).

Box 3. Concrete examples of increases in FDI through cross-border M&As

- Japanese financial companies have recently acquired several United States financial companies affected by the financial crisis (e.g. the acquisition of Asian and European operations of Lehman Brothers by Nomura Holdings and of a stake in Morgan Stanley by Mitsubishi UFJ Financial Group).
- Financial companies established abroad by Icelandic firms were also bought up: Glitnir AB (a branch of Glitnir in Sweden), and DLG Ltd. and Kaupthing Singer & Friedland Premium Finance Ltd. in the United Kingdom, both of which were owned

¹⁶ According to the November estimates by IMF, projected economic growth rate of BRICs in 2008 is as follows: 5.2 per cent for Brazil, 6.8 per cent for the Russian Federation, 7.8 per cent for India, and 9.7 per cent for China.

¹⁷ On the importance of the substitution effect between investment abroad and home, see for instance the study by E. L. Yeyati, U. Panizza and E. Stein (2007), which supports the view that the substitution effect dominates the income effect (unexpected earnings and losses) during expansions and recessions.

¹⁸ Source: www.dwnnews.com.

¹⁹ “A global love affair: a special report on cars in emerging markets”, *The Economist*, 15 November 2008.

²⁰ Australia provides an example: the slump in share prices of mining companies in Australia and the sharp depreciation of the Australian dollar have created good acquisition opportunities for resource-hungry investors from developing Asia.

by Kaupthing Bank, were acquired by HQ AB (Sweden), DM Plc (United Kingdom) and Close Brothers Group Plc (United Kingdom), respectively, in 2008.

- Examples abound of investments by sovereign wealth funds (SWFs), which have particularly targeted financial services in developed countries since 2007.^a While some of these investments are portfolio investments, SWFs today are increasingly involved in direct investments. Cross-border M&As by these funds reached \$15 billion in the 10 months to October 2008, which was already 50 per cent larger than the amount for the whole of 2007. Significant M&A deals in non-financial industries have also taken place as illustrated by the acquisition of Labroy Marine Ltd. of Singapore, a shipbuilding company, by Dubai Drydocks World LLC.
- Several mega M&A deals (those with an acquisition value of over \$1 billion) have occurred in manufacturing industries (such as computer equipment, aircraft and pharmaceuticals) in the United States since September 2008.^b

Source: UNCTAD, based on newspaper accounts.

^a For instance, CIC invested in Morgan Stanley (United States); Abu Dhabi Investment Authority acquired a stake in Citigroup (United States); KIC (Republic of Korea) – together with Kuwait Investment Authority – bought a stake in Merrill Lynch (United States); and GIC fund purchased a stake in UBS (Switzerland). Temasek Holdings (Pte) Ltd (Singapore) also bought a stake in Merrill Lynch; and Dubai International Financial Centre purchased OMS (Sweden).

^b Examples of such significant deals include the purchase of IKON Office Solutions Inc, a computer and peripheral equipment and software company, by Ricoh (Japan); of DRS Technologies Inc by the Italian aircraft firm Finmeccanica SpA and of APP Pharmaceuticals Inc and Sciele Pharma Inc by Fresenius SE (Germany) and Shionogi & Co Ltd (Japan).

Third, companies are still committed to increasing their level of internationalization in the medium term, a finding which constitutes a significant indicator for a future upturn in FDI flows. As shown in the *World Investment Prospects Survey, 2008–2011* (UNCTAD, 2008a), large TNCs around the world still seem to be eager to pursue internationalization strategies (and thus increase FDI expenditures in the medium-to-long term). It should also be stressed that, despite a decline in FDI *flows*, there is so far no perceptible sign that the crisis has had a negative impact in the relative size of FDI *stocks*, as compared to the overall value of productive assets. In other terms, the crisis has not so far resulted, to our knowledge, in a specific setback in the internationalization level of companies in terms of assets and, presumably, in other internationalization indicators.

Fourth, new sources of FDI have emerged, especially from the South. Emerging economies and countries well-endowed with natural resources are becoming a growing source of FDI, either through the internationalization strategies carried out by their TNCs, or through the investment activities of their SWFs. TNCs from the South, in particular, are likely to continue to be active international investors. This will help boost FDI to developing countries, such as Viet Nam (where most FDI is from other developing countries), which is expected to register record FDI levels in 2008.²¹ China's outward FDI will remain oriented upwards, as indicated in late 2008 by Chen Jian, its Vice Minister of Commerce.²² SWFs, most of which are based in developing countries, will also be increasingly involved in FDI. Given the sheer size

²¹ The three largest investment cases in Viet Nam in 2008 are two in steel and one in oil refinery. Companies from Malaysia, Taiwan Province of China and Kuwait are involved, respectively, in these cases. In addition, in November 2008, Formosa Plastics (Taiwan Province of China) announced its intention to invest up to \$15 billion in a large-scale petrochemical complex in central Viet Nam.

²² "Commerce Ministry: foreign investment strategy unchanged", *China Daily*, 21 October 2008.

of assets under their management (between \$3 trillion and \$5 trillion, and expected to reach about \$10 trillion by 2015²³), their FDI potential is high (UNCTAD, 2008b). The adoption of the Santiago Principles in October 2008 to enhance the transparency of such funds might contribute to a defusing of protectionist tendencies that their rapid international expansion provoked.

Fifth, many quickly-growing industries are presently characterized, even in the midst of the present crisis, by very promising FDI prospects. Among these, one could mention the following examples, sorted by type of industries (UNCTAD, 2008a): (a) in *life sciences*: equipment and services for medical diagnosis (notably in vitro), clinical tests, biotechnologies, bio-cosmetics, oncology and bio-production; (b) in *agro-food industries*: intermediate food products, special ingredients (colourings, emulsifiers, preservatives), processed seafood, aquaculture products and high value added products (e.g. pastries, pre-cooked food, health food); (c) in *transport equipment*: automotive and aerospace electronics, hybrid motors, automotive logistics and innovative materials; (d) in *business services*: customer service centres, providers of outsourced logistics and business services, regional headquarters, R&D centres, technical engineering and financial services; (e) in *personal services*: retail, care of senior citizens, health care (e.g. medical care at home and remote diagnosis), financial services; (f) in *information and communication technologies*: micro and nano electronics, software for video games, interactive and virtual image technologies, Internet technologies and embedded technologies for wireless telecommunication systems; (g) in *energy, chemistry, and environmental conservation*: nano materials, improvements in existing materials, photovoltaic energy, wind power, water processing, recycling of wastes and non-food use of agricultural products (e.g. bio-fuels, bio-polymers, bio-solvents, bio-materials); (h) in *other industries*: technical textiles (e.g. textiles with particular qualities in terms of robustness, suppleness, or adaptability), robotics.

Whether these positive factors will offset the impact of the financial constraints facing firms and the reduced demand and slower economic growth in many parts of the world remains an open question. Different answers can be considered depending on the time horizon. The key factors at work in the short to medium term are summarized in table 4.

²³ Source: Deutsche Bank Research, "SWFs and foreign investment policies - an update", 22 October 2008.

Table 4. Summary of the possible implications of the crisis for FDI in the short-to-medium term

Variable affected by the crisis	Present evolution	Impact on FDI flows in 2009	Uncertainties in the medium term
Availability of financial resources	Intensive credit squeeze (less availability and higher costs) Decreased company profits Necessity to repatriate capital to compensate for losses	Growing financial constraints on investments, though some companies and institutions still have large amounts of cash	Speed of the recovery in the financial sector and end of the credit squeeze Capacity of new types of investors (companies from emerging countries, SWFs), to act as a major engine of FDI growth
Asset prices	Large decrease in the value of stocks	Reduced M&A activity including leveraged buy-outs At the same time, some M&A operations are encouraged by companies well-endowed with cash, but at a lower value by definition	Recovery patterns of the stock exchange market (with an impact on the value of international M&As)
Market growth	Slowed world economic growth at least until 2009	Reduced incentives for market-oriented FDI, especially in developed countries	Time schedule and geographic patterns of the economic recovery
Perception of uncertainty	Very negative evolution of all available business confidence indices	Companies to restrain further investment plans and cut extensively in existing costs and assets, especially in hard-hit advanced countries	A progressive return of confidence is a prerequisite for a new pickup in investment
Public policies	Monetary and fiscal stimulus policies carried out in various countries in the world; the reform to the financial system has not yet begun; no specific impact of the crisis on FDI policies, but existence of some protectionist tensions	Impact of macroeconomic policies on business environment will affect demand and business environment, and FDI flow as a result.	Capacity of public policies to ensure stability of the financial system, to renew commitment to an open attitude to FDI, to encourage investment and innovation, and to foster confidence of economic actors
Sector-specific crisis and restructuring	The financial sector, automotive, construction and intermediate goods have been especially hit, but the crisis rapidly extends to other industries and services	Divestments, sales of assets and M&As for restructuring in hardest-hit industries	Speed and scope of the restructurings and shifts in market power triggered by the crisis (increased role of companies from emerging and developing countries?)
Location patterns of FDI	Market-seeking FDI projects in developed countries are the most affected due to the looming recession there	Export-oriented FDI projects in developing and emerging economies (both efficiency- and resource-seeking) could be increasingly affected due to the low dynamism of advanced country markets	Rising attractiveness of the South for both market-oriented and efficiency-seeking FDI?
New sources of FDI	Growing role of SWFs and companies from emerging countries (but financial resources somewhat squeezed in the short term)	Growing share of emerging and developing countries in FDI outflows	Will FDI from the newer sources compensate for the decline in FDI from advanced countries?

Source: UNCTAD.

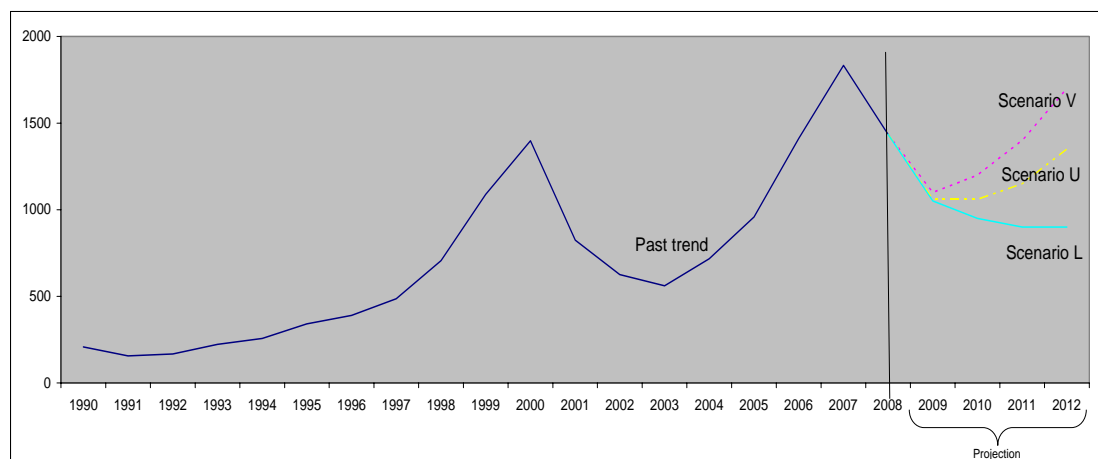
In the very short term (2009), various factors (such as the severity of the crisis, the fact that it is affecting a significant number of large TNCs in the United States and

Europe, and that both the financial and non-financial sectors have been seriously disrupted), lead to anticipate that the offsetting factors will have much less impact than the downward forces. Companies are more likely to undertake divestments than to seize investment opportunities during this initial phase of the downturn.²⁴ This is why a further decline in FDI in 2009 can be expected. It is also very likely that FDI flows to developing countries – which up to now have exhibited resilience overall – will slow down more markedly than has been observed to date.

In the short-to-medium term (2010-2012), there are three scenarios for a pickup in FDI. Prospects on how the balance between negative and positive factors for FDI will evolve are very open for 2010 and onward, due to the variety of uncertainties and their complex potential interactions. As shown in table 4, these uncertainties relate to a large range of factors, such as the severity or duration of the slowdown in global growth, the efficiency of global policy responses to the crisis by Governments (especially of initiatives aimed at stimulating investment), the stabilization and recovery of the financial system, and the capacities of emerging countries' TNCs to become a major engine of FDI growth. One of the key uncertainties is when the cross-border M&A flows will pick up again, as they are one of the major components of FDI flows. It should also be stressed that the impact of the crisis on FDI is likely to differ widely in magnitude, depending on industries, home and host countries, as well as on investment modalities.

To give a structured vision of these uncertainties, three scenarios could be drawn up for FDI evolution up to 2012 (figure 3). The underlying hypotheses of these scenarios are as follows.

Figure 3. Worldwide FDI inflows with three different trajectories, 1990-2012
(Billions of dollars)



Source: UNCTAD, based on FDI/TNC database (www.unctad.org/fdi statistics) and UNCTAD own estimates.
Note: the shapes of V, U and L scenarios are for illustrative purposes only and not based on any statistical methods.

V scenario (optimistic): Quick upturn in FDI flows, beginning end 2009.

Underlying assumptions are: (a) end of the recession as early as the second half of 2009; (b) quick return of investors' confidence due, among others reasons, to efficient government policies; (c) no protectionist setback; (d) fresh wave of cross-border M&As due to industry restructurings and availability of cash in some companies and

²⁴ See Baghai, Smit and Viguerie, op. cit., *The McKinsey Quarterly*, September 2008.

financial institutions. Based on a combination of very optimistic assumptions, this scenario seems rather unlikely as seen from today.

U scenario (base case). FDI flows begin to pick up only in 2011. Major underlying assumptions are: (a) global recession is worse than in the V scenario, lasting at least till the first semester of 2010; (b) the global value of cross-border M&As remains limited due to the low price of stocks; (c) the trend towards the internationalization of companies is still at work in the medium term. To date, this scenario appears as the most probable one.

L scenario (pessimistic). FDI flows do not pick up before 2012. Underlying assumptions are: (a) a longer and worse-than-expected economic depression results, among others, in protectionist tensions affecting the overall trend in globalization; (b) due to the accumulation of negative factors, companies remain extremely cautious about investments, especially those aimed at financing their international development.

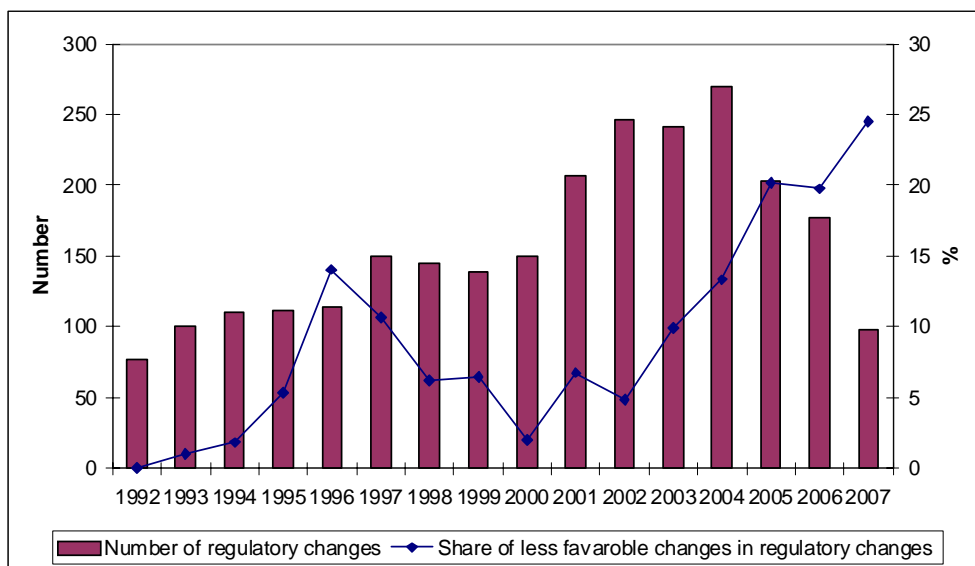
Appropriate policy responses are required to limit the probability of this pessimistic scenario and favour a quicker recovery in FDI flows. The policy implications of the ongoing economic crisis as regards international investment will thus be examined in the following section.

IV. Policy implications

The effectiveness of government policy responses at both the national and international levels in addressing the financial crisis and its economic aftermath will play a crucial role for creating favourable conditions for a new pickup in FDI. The challenge is to restore the credibility and stability of the international financial system, to provide stimulus to economic growth in order to prevent the risk of a spiraling depression, to renew a pragmatic commitment to an open economy, potentially put at risk by rising protectionist tensions, and to encourage investment and innovation. So far, however, it is hard to say that the crisis has led to a clear set of measures either favourable or not to FDI. But, as it has revealed some structural shortcomings in the way the global economy is operated, it can also pave the way for the implementation of public policies aimed at maximizing the positive impact of FDI on development.

Before the crisis erupted, there were already signs of some more restrictive attitudes towards FDI (for instance, in extractive industries and as regards acquisitions by SWFs). Although remaining at a low level, the percentage of negative regulatory changes as compared to positive ones has significantly increased since 2003 (figure 4). The situation, however, is different between regions. In Latin America, for instance, as much as 60 per cent of policy measures taken in 2007 were less favourable to FDI (UNCTAD, 2008b).

Figure 4. Number of national regulatory changes and the share of less favourable changes in the total, 1992-2007



Source: UNCTAD 2008, p. 13.

Up to now, no signs of a significant direct impact of the crisis on FDI policies have been observed. This is understandable, given the fact that FDI is not at the root of the current crisis. Therefore, specific FDI policies would not offer per se a promising avenue to tackle the existing problems. However, as will be explained below, some national policy reactions of a more general scope (e.g. stricter regulation of the financial sector, more infrastructure investment, state aids for individual economic sectors, tax reductions) are likely to indirectly impact FDI, negatively or positively. A number of measures have already been introduced to prevent a further deterioration of the global economy; and these will influence FDI flows both in the financial and non-financial sectors.

On the one hand, a number of policy initiatives at the national level could stimulate FDI. Three categories of policy measures can be distinguished. First, many developed countries have adopted large-scale bailout plans and rescue packages for the *financial sector*. Providing State guarantees to financial institutions could have a crowding-in effect on FDI, as these companies might be considered as “safe” investments by foreign investors. Moreover, some countries have even actively sought the participation of foreign investors in individual rescue deals.²⁵ Second, several countries – such as the United States, France, Germany and Spain – have announced large *public investment programmes*, mainly aimed at infrastructure investments, which not only builds confidence in economy but also opens up investment opportunities by TNCs. Third, a number of countries have *adopted fiscal or monetary stimulus* measures which might also have a positive impact on FDI flows. For example, the United Kingdom Government has announced a value added tax cut, and the German Government decided to launch a financial package to help small and medium-sized enterprises (SMEs) in difficulty get access to credit. Also, the French Government announced measures to make credit more easily available for SMEs. The United States Federal Reserve Board has cut interests rates to a level close to zero, and the bailout programme has been extended to cover the three major automotive

²⁵ For instance, Belgium has been negotiating with the French BNP Paribas concerning the takeover of the Belgian bank Fortis.

manufacturers. The Japanese Government lowered the corporate tax rate for SMEs. For large Japanese TNCs, it decided to allow loans by the Japan Bank for International Cooperation, which are excluded from loan businesses under normal circumstances, to be extended to them in order to support activities of their foreign affiliates operating in developing countries.²⁶

Some developing countries are also introducing public support measures. Facing the negative impact of the global financial crisis, for example, the Chinese Government announced in November 2008 a RMB 4 trillion (about \$600 billion) public investment plan to boost economic growth. It will last three years – until the end of 2010 – and may help keep the annual gross domestic product growth rate of China at 8–9 per cent during the period. By enhancing growth prospects and increasing investor confidence, the plan may help attract or maintain FDI inflows to China. Though on a smaller scale, the following countries have similar packages – the Republic of Korea (35 trillion won or \$32 billion), India (200 billion rupees or \$4 billion), Thailand (300 billion Baht, or \$8.6 billion), Malaysia (7 billion ringgits or \$2 billion), Philippines (300 billion pesos or \$6.3 billion), and Viet Nam (up to \$6 billion). Furthermore, the corporate tax rate was lowered in the Republic of Korea (from 13–25 per cent to 10–20 per cent) and the Philippines (from 35 per cent to 30 per cent). Special measures are also provided for SMEs in such countries as Singapore and Viet Nam.

At the international level, various initiatives can be mentioned. At the Group of Twenty Summit on Financial Markets and the World Economy, held on 14 November 2008, leaders renewed a political commitment to an open global economy, stating in their declaration that “...within the next 12 months, we will refrain from raising new barriers to investment or to trade in goods and services, imposing new export restrictions, or implementing World Trade Organization (WTO) inconsistent measures to stimulate exports...”.²⁷ Another measure in response to the financial crisis includes a new regional initiative by nine Asian countries (including Australia, Japan and the Republic of Korea) which agreed in November 2008 to offer reinsurance for exports by foreign companies already insured by local authorities.²⁸ This additional insurance further reduces the trade risks that have been aggravated by the current crisis, which should help exports by foreign companies from this region.

On the other hand, some national responses to the crisis might also have a potentially negative impact on FDI flows. This could be the case, for instance, of some of the measures aimed at helping the *financial sector* – which alone accounts for the largest share of global FDI, i.e. one fifth of global FDI stock in 2006. For example, several countries – such as Belgium, Germany, Iceland, Luxembourg, the Netherlands, United Kingdom and the United States – have acquired shares in domestic banks or insurance companies. A partial or even total nationalization of these firms means that opportunities for private investment, including FDI, have been reduced. In other cases, some new operative conditions imposed on financial institutions in exchange for State assistance – such as restrictions on the payments of dividends – are likely to reduce the attractiveness of such companies to investors. Concerns that States increasingly interfere with business operations, and that considerations to protect the public

²⁶ *Nikkei*, 24 December 2008.

²⁷ Paragraph 13 of the Declaration of Summit on Financial Markets and the World Economy.

²⁸ *Nikkei*, 18 November 2008.

interest may prevail over investors' interests, are also likely to dampen the attractiveness of FDI to potential investors, in particular in the financial sector. In addition, State aid outside the financial sector may have a negative impact on outward FDI. For instance, the French support programme for the domestic automobile industry is conditioned on the requirement that French car makers do not locate production abroad.

Conclusion

The present crisis may be a source of both threats and opportunities for public policies on FDI. Among the dangers looming for the years ahead, one can mention the risk of shifting efforts away from achieving a pro-investment and pro-business environment and the emergence of protectionist tensions.

The crisis, however, also opens a chance to implement efficient global policy responses to enhance the stability of the financial system and stimulate economic growth. Various voices – such as that of Joseph Stiglitz (Stiglitz, 2008) and UNCTAD itself (UNCTAD, 2008c) – advocate the necessity to go beyond the mere short-term management of the ongoing crisis and to set up the bases of sounder economic regulations, especially in banking, with more control and restriction on the activities of commercial banks, hedge funds and other financial institutions. This requires action at a coordinated international level to rebuild financial multilateralism, foster the stability and equity of the worldwide financial system, promote stronger transparency or disclosure standards, create guarantee funds to help emerging and developing countries to secure the debt of their corporations, and to reassess the importance of public policies and regulations.

In addition, at the country level, measures specifically aimed at stimulating investment could also be more extensively implemented. Investment promotion agencies could also play a key role in fostering after-care policies aimed at retaining existing activities by TNCs and in implementing targeted investment promotion programmes on promising activities.

To conclude, beyond its immediate negative impact on FDI flows in 2008 and presumably 2009, the ongoing crisis opens a period of major uncertainty. For effectively dealing with the crisis and its economic aftermath, it is important that policymakers maintain an overall favourable business and investment climate (including for FDI) and refrain from protectionist tendencies.

Annex table. FDI inflows and cross-border M&As, by region and major economy, 2007-2008

(Billions of dollars)

Region/economy	FDI inflows			Cross-border M&As		
	2007	2008 ^a	Growth rate	2007	2008	Growth rate
			(%)			(%)
World	1,833.3	1,449.1	- 21.0	1,637.1	1,183.7	- 27.7
Developed economies	1,247.6	840.1	- 32.7	1,454.1	981.8	- 32.5
Europe	848.5	562.3	- 33.7	825.0	548.7	- 33.5
European Union	804.3	557.4	- 30.7	782.0	506.4	- 35.2
Austria	30.7	12.9	- 57.9	9.0	3.0	- 66.6
Belgium	40.6	17.1	- 58.0	5.4	28.3	420.6
Czech Republic	9.1	11.4	24.8	0.4	5.1	1 353.3
Denmark	11.2	14.7	31.3	11.2	6.4	- 42.8
Finland	8.5	- 6.3	- 173.9	11.8	4.2	- 64.2
France	158.0	114.3	- 27.6	62.4	37.2	- 40.4
Germany	50.9	26.0	- 48.9	101.0	42.9	- 57.5
Hungary	5.6	3.4	- 39.5	0.7	1.6	122.1
Ireland	30.6	- 6.1	- 120.1	5.4	4.9	- 9.8
Italy	40.2	2.3	- 94.3	31.4	27.4	- 12.8
Netherlands	99.4	29.5	- 70.4	209.8	25.4	- 87.9
Poland	17.6	16.2	- 7.7	1.3	1.2	- 7.4
Romania	9.8	10.6	8.6	1.8	1.0	- 41.4
Spain	53.4	57.3	7.3	66.0	71.6	8.4
Sweden	21.0	36.5	74.3	12.4	25.3	104.8
United Kingdom	224.0	109.4	- 51.1	231.0	206.2	- 10.7
United States	232.8	220.0	- 5.5	379.4	314.9	- 17.0
Japan	22.5	17.4	- 22.6	21.4	19.1	- 10.8
Developing economies	499.7	517.7	3.6	152.9	177.0	15.7
Africa	53.0	61.9	16.8	10.2	26.3	157.0
Egypt	11.6	10.9	- 5.6	1.9	15.9	732.7
Morocco	2.6	2.4	- 7.0	0.3	0.1	- 64.7
South Africa	5.7	12.0	111.2	6.7	8.2	22.9
Latin America and the Caribbean	126.3	142.3	12.7	30.7	29.5	- 3.8
Argentina	5.7	7.3	27.9	1.4	0.6	- 54.0
Brazil	34.6	41.7	20.6	8.6	9.7	13.6
Chile	14.5	17.8	23.2	2.7	3.3	24.6
Colombia	9.0	10.9	20.3	4.4	0.6	- 86.0
Mexico	24.7	20.7	- 16.0	6.0	3.7	- 38.8
Peru	5.3	7.4	38.9	1.2	0.4	- 64.7
Asia and Oceania	320.5	313.5	- 2.2	112.0	121.2	8.2
West Asia	71.5	56.3	- 21.3	30.3	31.5	4.0
Turkey	22.0	16.4	- 25.5	15.5	11.9	- 23.4
South, East and South-East Asia	247.8	256.1	3.3	81.5	89.4	9.7
China	83.5	92.4	10.6	15.5	20.3	30.6
Hong Kong, China	59.9	60.7	1.3	26.8	18.2	- 32.3
India	23.0	36.7	59.9	5.6	11.2	100.8
Indonesia	6.9	5.5	- 21.3	2.7	2.7	- 0.3
Malaysia	8.4	12.9	53.4	4.5	5.5	22.4
Singapore	24.1	10.3	- 57.2	8.8	17.0	91.6
Thailand	9.6	9.2	- 4.4	2.9	0.6	- 78.2
South-East Europe and the CIS (Transition economies)	85.9	91.3	6.2	30.1	25.0	- 17.0
Russian Federation	52.5	61.7	17.6	23.5	17.7	- 24.9
Ukraine	9.9	9.7	- 1.5	1.7	6.0	260.5

Source: UNCTAD.

^a Preliminary estimates.

Note: World FDI inflows in 2008 are projected on the basis of data for 103 economies for which data were available for part of 2008 as of 19 December 2008. Data for 2008 are estimated by annualizing the data available, in most cases for 6-10 months of 2008, except for France, Germany, Greece, the Netherlands, Poland, Romania, Spain, Sweden, Canada, the United States, Australia, Japan, Pakistan, Kazakhstan and Ukraine, where FDI flows in the last few months of 2008 were assumed to be negligible. The proportion of inflows to these economies in total inflows to their respective region or subregion in 2007 is used to extrapolate the 2008 data. For cross-border M&As, estimates were made on the basis of data available as of 5 January 2009.

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