Congressional Research Service
Informing the legislative debate since 1914

IN FOCUS

April 17, 2017

Foreign Direct Investment: Overview and Issues

Overview

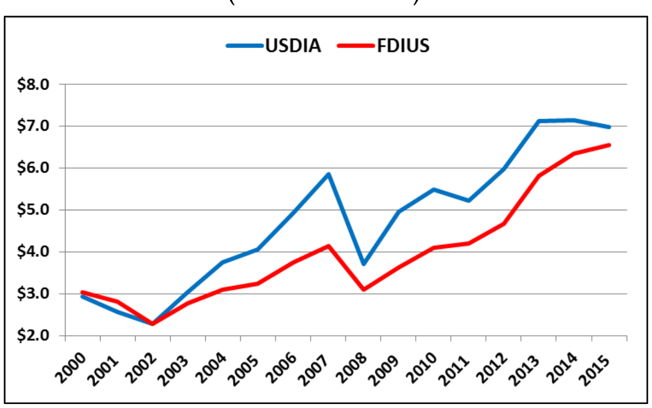
The growing prominence of foreign direct investment raises questions about its costs and benefits to the U.S. economy. Traditionally, the United States has supported a rules-based open and liberalized investment environment internationally as a key to promoting economic growth, including by negotiating investment provisions in free trade agreements (FTAs) and bilateral investment treaties (BITs). It also has included administering investment promotion programs. All of these efforts have been debated. For some policymakers, foreign investment expands markets abroad for U.S. firms and draws in capital and businesses that support local jobs. Others argue that U.S. direct investment abroad (USDIA) contributes to slow growth in U.S. jobs and wages and outsources U.S. jobs. Other policymakers argue that certain foreign direct investment in the United States (FDIUS), particularly by entities owned or controlled by a foreign government, compromises U.S. national security. In response, some policymakers argue that U.S. national security reviews of foreign investment transactions should be reformed, for example, to protect and promote certain industrial sectors in the economy.

FDI Trends and Recent Investments

With $7 trillion in total outward investment (USDIA), and $6.5 trillion in inward investment (FDIUS), the United States is the largest source and the largest recipient of FDI.

Figure 1. U.S. Direct Investment Position Abroad and Foreign Direct Investment Position in the United States at Market Value (Cumulative Amount)

(dollars in trillions)

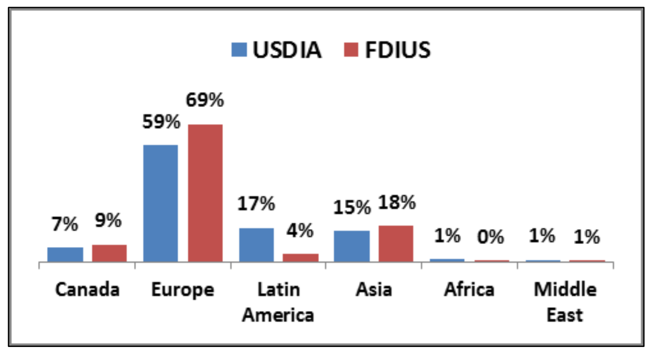


Source: Department of Commerce.

For U.S. multinational firms (combined U.S. parent companies and foreign affiliates), activities of the U.S parent company accounted for more than two-thirds of world-wide value added, capital expenditures, and research and development. By geographic area, about 74% of the U.S. direct investment position abroad is concentrated in high income developed countries where consumer tastes are similar to those in the United States: investments in Europe alone account for 60% of all USDIA, or $2.9 trillion. Similarly, direct investments by European firms account for 70% of FDIUS. U.S. firms have placed a slightly larger share of their investments in Latin America than in Asia, while Asian firms are investing more in the United States than are Latin American firms.

Figure 2. Share of U.S. Direct Investment Position Abroad and Foreign Direct Investment Position in the United States by Region, Historical Cost, 2015

(in percent)



Source: Department of Commerce

By sector, U.S. direct investment abroad is concentrated in high technology, finance, and services industries located in highly developed countries with advanced infrastructure and communications systems. The largest share of inward foreign investment (40%) is in the U.S. manufacturing sector, primarily in chemicals and transport industries.

Issues for Congress

Foreign Investment and Outsourcing

For some, USDIA contributes to slow growth in jobs and wages in the U.S. economy because U.S. firms are seen as outsourcing jobs, particularly manufacturing jobs, to lower wage countries. There are examples of U.S. firms closing a plant in the United States and opening a similar plant abroad, but there are no official sources that track such activities. Most USDIA, however, is in developed economies that are similar to the United States and most of this production is consumed where it is produced. Economists generally argue that the loss of jobs in the U.S. manufacturing sector can be traced to a number of factors, including two economic recessions (1999-2000, and 2008-2009) and improvements in productivity that have allowed the manufacturing sector to produce more goods with fewer workers: since 1980, employment in the U.S. manufacturing sector has fallen by one-third, while output has doubled. Also, foreign affiliates on average sell most of their output in the foreign country in which they are located or to neighboring countries; about 10% of foreign affiliate sales is to their U.S. parent companies.

Foreign Investment and National Security

Foreign investment, particularly by firms that are owned or controlled by a foreign government (state-owned enterprises, or SOEs), raise concerns about U.S. national security. Such national security-related issues are reviewed by the Committee on Foreign Investment in the United States (CFIUS), an interagency committee that serves the President. The Committee reviews foreign investment transactions to determine if: (1) they threaten to impair the national security; (2) the foreign investor is controlled by a foreign government; or (3) the transaction could affect homeland security or would result in control of any critical infrastructure that could impair national security. Presidents have rarely used this authority to block an investment transaction.

Some policymakers argue that the rise of SOEs and other factors require a more proactive approach that reviews foreign investments holistically, rather than on a case-by-case basis. Some policymakers also argue that the review process should be expanded to encompass the concept of national economic security and reviews should be reoriented toward restricting investments in certain economic sectors and to promote U.S. firms in a type of national industrial policy. Others argue, however, that the current system works well, although resource constraints are challenging the ability of the system to keep up with demands.

U.S. Investment Agreements

The United States is party to BITs or FTAs with investment chapters with over 50 countries. These agreements generally aim to reduce FDI restrictions and ensure nondiscriminatory treatment of investors and investment, subject to national security and other exceptions, while balancing other policy interests. They typically are enforced through binding arbitration under investor-state dispute settlement (ISDS). Some World Trade Organization (WTO) agreements address investment issues in a limited manner, but FTA investment chapters and BITs have been the primary tools for establishing investment rules internationally.

BITs require two-thirds Senate approval and FTAs require approval by both Chambers to enter into force in the United States. Congress sets U.S. investment negotiating objectives, most recently in the 2015 Trade Promotion Authority (TPA) (P.L. 114-26). One of the most important is to reduce or eliminate foreign investment barriers and ensure that foreign investors do not receive "greater substantive rights" for investment protections than US. investors in the United States. Recent investment negotiations have sharpened debates in Congress about the U.S. approach to investment, including on protections for investors and governments' regulatory ability, as well as other issues, such as the fairness and transparency of ISDS. In the global context, the possible need for additional rules, such as in the WTO, could be examined.

U.S. Investment Negotiations: State of Play

In January 2016, President Trump withdrew the United States from the Trans-Pacific Partnership (TPP). The TPP investment chapter, the most recent set of investment rules negotiated by the United States, built on prior U.S. investment agreements, including clarifying that TPP investment obligations apply to SOEs. Certain provisions, such as on ISDS, have been controversial. Congress could revisit TPP provisions in possibly renegotiating existing FTAs, or pursuing new FTAs. If the Administration resumes Transatlantic Trade and Investment Partnership (T-TIP) negotiations with the European Union (EU), questions could re-emerge over competing U.S. and EU approaches to ISDS. The United Stated previously also engaged in BIT discussions with China and India, which, if resumed, could lead to enhanced commercial relations but also raise questions about whether these countries would uphold their commitments.

Investment Promotion Programs

The United States promotes both USDIA and FDIUS. The **Overseas Private Investment Corporation (OPIC)** seeks to support economic growth in developing and emerging economies by providing political risk insurance, financing, and other services for qualifying U.S. private investments overseas. Operating under the Foreign Assistance Act of 1961, as amended, it aims to mitigate the political risks of investing overseas. Differing views in Congress about the role of the U.S. government, the effectiveness of trade promotion, and outsourcing concerns fuel debate over OPIC. This debate could intensify as Congress considers the President's FY2018 budget proposal, which proposes eliminating OPIC funding. **SelectUSA** is a Department of Commerce program established by a 2011 executive order to coordinate federal efforts to attract and retain investment in the United States, complementing state-level investment attraction programs. It aims to provide information on investment, help resolve investment issues involving federal programs and activities, and advocate for FDIUS. A permanent authorization for SelectUSA could affirm U.S. interest in competing for FDI; yet, overlap concerns may arise due to existing sub-federal investment attraction programs.

Outlook

The 115th Congress may be confronted with a range of FDI issues. It could examine the impacts on USDIA and FDIUS on the U.S. economy and jobs, potential changes to CFIUS, the U.S. approach to investment rules in trade negotiations, and the status of investment promotion and attraction programs.

James K. Jackson, Specialist in International Trade and Finance
Shayerah Ilias Akhtar, Specialist in International Trade and Finance

IF10636

Disclaimer