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Foreign Direct Investment: Overview and Issues

Overview

The growing prominence of foreign direct investment (FDI) raises questions about its costs and benefits to the U.S. economy. Traditionally, the United States has supported a rules-based and open investment environment internationally in order to promote economic growth and advance other policy objectives. U.S. investment policy includes negotiating rules, disciplines, and market access commitments concerning FDI in trade agreements and Bilateral Investment Treaties (BITs) and administering investment promotion programs. It also involves reviewing certain proposed inbound FDI transactions for U.S. national security implications. FDI is a part of U.S. trade policy, given that it is a major driver of trade and plays a role in facilitating global supply chains.

These policy components have been the subject of longstanding debate. For some policymakers, foreign investment expands markets abroad for U.S. firms and draws in capital and businesses that support local jobs. Some policymakers also assert that FDI can advance U.S. foreign policy and other strategic objectives. Others argue that U.S. direct investment abroad (USDIA) may contribute to slow growth in U.S. jobs and wages and outsources U.S. jobs. Some policymakers argue that certain foreign direct investment in the United States (FDIUS), particularly by entities owned or controlled by a foreign government, may compromise U.S. national security.

During the Trump Administration, the U.S. investment policy landscape experienced notable changes. In response to various policy debates, as well as concerns raised by China's FDI activity, in 2018, Congress updated laws governing reviews of foreign investment in the United States for national security concerns with the Foreign Investment Risk Review Modernization Act (FIRRMA, P.L. 115-232). It also consolidated and expanded U.S. authorities to support private investment overseas for foreign policy and strategic economic aims, with the Better Utilization of Investments Leading to Development Act (BUILD Act, P.L. 115-254). Other developments included the enactment of legislation to implement the U.S.-Mexico-Canada Agreement (USMCA, P.L. 116-113), which contained investor protections that varied in key respects from existing U.S. trade agreements.

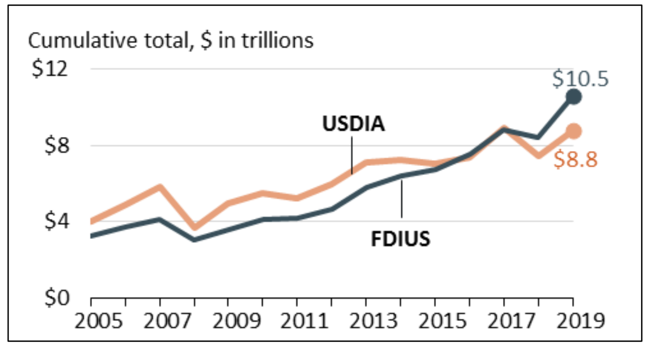
FDI Trends and Recent Investments

With $8.8 trillion in total USDIA, and $10.5 trillion in total FDIUS in 2019—at market value—the United States is the world's largest source and recipient of FDI.

During 2005 through 2019, USDIA more than tripled, and FDIUS more than doubled (**Figure 1**), but both levels are expected to dip in 2020 amid the Coronavirus Disease 2019 (COVID-19) pandemic.

For U.S. multinational firms (combined U.S. parent companies and foreign affiliates), activities of the U.S parent companies accounted for more than two-thirds of world-wide value added, capital expenditures, and research and development.

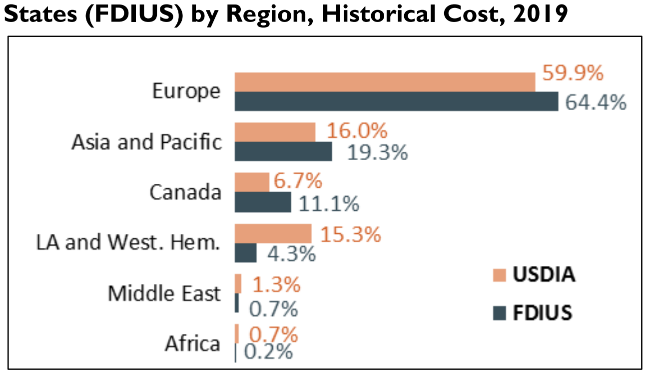
Figure 1. U.S. Outward and Inward FDI Position, at Market Value, 2019



Source: Department of Commerce, Bureau of Economic Analysis.

By geographic area, about 75% of the U.S. direct investment position abroad (cumulative amount) 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 USFDI, or $3.6 trillion. Similarly, direct investments by European firms account for 64% of the FDIUS position. U.S. firms have placed a slightly larger share of their investments in Latin America (LA) than in Asia, while Asian firms have invested more in the United States than have Latin American firms. (See **Figure 2**.)

Figure 2. Share of U.S. Direct Investment Position Abroad (USDIA) and FDI Position in the United States (FDIUS) by Region, Historical Cost, 2019



Source: Department of Commerce, Bureau of Economic Analysis.

By sector, USDIA is concentrated in high technology, finance, and services industries located in highly developed countries with advanced infrastructure and communications systems. The largest share of FDIUS (40%) is in the U.S.

manufacturing sector, primarily in chemicals and other manufacturing.

Issues for Congress

Foreign Investment and Outsourcing

For some observers, 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 U.S. plant and opening a similar plant abroad, but there are no official sources that track such activities. Most USFDI, however, is in developed economies that are similar to the United States and most of this production by foreign affiliates is consumed where it is produced and is part of accessing markets abroad. 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. Economists generally attribute the loss of U.S. manufacturing jobs to broader factors, including economic recessions (1999-2000, and 2008-2009) and improvements in productivity (automation and other advances in technology) that have allowed the manufacturing sector to produce more goods with fewer workers.

Foreign Investment and National Security

Some 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 U.S. 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 used this authority to block at least six transactions.

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. FIRRMA aimed to address these and other concerns by expanding the ability of CFIUS to review transactions, including non-controlling investments, some real estate transactions, and acquisitions that involve critical technologies, critical infrastructure, and personal data.

U.S. International Investment Agreements

While some World Trade Organization (WTO) agreements address investment issues in a limited manner, investment provisions in bilateral investment treaties (BITs) and bilateral and regional free trade agreements (FTAs) serve as the primary tools for establishing investment rules internationally. 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). 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), which expires on July 1, 2021. These negotiating objectives seek to reduce or eliminate foreign investment barriers and ensure that foreign investors do not receive "greater substantive rights" for investment protections than U.S. investors domestically. The USMCA contains the most recent set of U.S. investment commitments. It limits some core investor protections, including eliminating ISDS with Canada, and curtailing ISDS use with Mexico.

Congress may revisit U.S. investment policy objectives in a potential debate over TPA renewal, as well as in shaping and overseeing potential future FTA or BIT negotiations. Congress also may examine investor protection issues with respect to emerging markets, given that the most recent U.S. BIT talks with China and India stalled. Another potential issue is the possible need for multilateral investment rules, such as in the WTO and the potential EU-China investment agreement under negotiation.

Investment Promotion Programs

The U.S. International Development Finance Corporation (DFC), a new, consolidated U.S. government agency authorized by the BUILD Act, promotes private investment in developing countries to support U.S. global development, foreign policy, and economic interests. It provides political risk insurance, financing, direct equity investments, and technical assistance. As the successor to the Overseas Private Investment Corporation (OPIC, now terminated), the DFC followed longstanding debate about the role of the U.S. government in trade promotion, and outsourcing concerns. Congress may examine the DFC's effectiveness in supporting U.S. commercial and broader strategic interests, including the extent to which DFC-supported projects allow U.S. firms to gain critical footholds in overseas markets.

SelectUSA, a Department of Commerce program established by a 2011 executive order, aims to coordinate federal efforts to attract and retain investment in the United States, complementing state-level investment attraction efforts. It provides information on investment, and aims to help resolve investment issues involving federal programs and activities and to advocate for FDI in the United States. Codification of authorization could affirm U.S. interest in competing for FDI; yet, overlap concerns may arise due to existing sub-federal investment attraction programs.

Outlook

U.S. investment policy may evolve under a Biden Administration. The 117th Congress could examine the impacts of FDI on the U.S. economy and jobs, including the effects of the pandemic, additional potential changes to CFIUS, U.S. investment policy objectives and commitments in FTAs and BITs, and the effectiveness of investment promotion programs.

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