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RECENT DEVELOPMENTS IN INTERNATIONAL INVESTMENT AND TRANSNATIONAL CORPORATIONS

Trends in foreign direct investment

Report by the UNCTAD secretariat

SUMMARY

The increase of FDI outflows by 5 per cent in 1993 to $193 billion (and by an additional 6 per cent in 1994 to an estimated $204 billion) marked the end of the FDI recession. The global FDI stock stood at an estimated $2.1 trillion at the end of 1993 and the sales associated with some 207,000 foreign affiliates were around $5.8 trillion in 1992. The recovery of the economies of the developed countries -- though unevenly spread -- and the continuing strong growth of several major recipient developing countries were the principal factors for the turnaround in investment flows. Underlying these cyclical factors were, *inter alia*, the on-going liberalization of investment regimes (including the adoption of privatization programmes) and, the decline of majority foreign-owned cross-border mergers and acquisitions particularly among the developed countries.

Flows into developing countries, at a record $71 billion in 1993 (and an estimated $80 billion in 1994), continued to grow even as the economies of developed countries began to recover from the recession, thus boosting their share of total inflows to some 39 per cent. However, 80 per cent of the inflows were to 10 developing countries, in particular China. Outward FDI from several developing countries, including, in particular, inter-developing country FDI (and increasingly investments from developing to developed countries) is growing, especially from countries whose firms recognize the importance of investing abroad to remain competitive.

The levels of FDI flows and stocks are not indicative of the importance of other modalities of servicing markets and accessing assets internationally. The proliferation of modalities such as alliances, licensing agreements and subcontracting add more dimensions to the international transactions undertaken by TNCs, diminish the risks embedded in these transactions because of diversification, strengthen the relationship and multiply the links between producers and consumers in different countries.

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INTRODUCTION

1. At its twentieth session, the Commission on Transnational Corporations requested its secretariat to prepare a report on trends in foreign direct investment (FDI). The present report, prepared by the UNCTAD Division on Transnational Corporations and Investment, is in response to that request. The report begins with a review of recent trends in FDI stocks and flows at the global level, identifying the most important factors explaining these trends. The report continues with a discussion on FDI and transnational corporations (TNCs) originating from developing countries. The discussion then turns to other modalities of internationalization through which TNCs access foreign markets and factors of production.

I. RECENT TRENDS IN FOREIGN DIRECT INVESTMENT

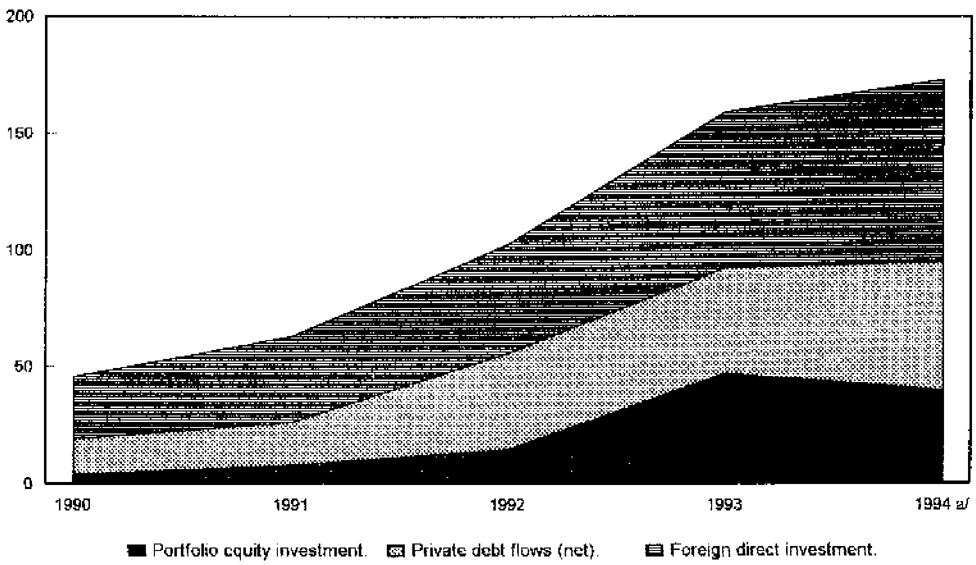
A. FDI stocks and flows: trends and interrelationships

2. Foreign direct investment is an increasingly important component of the international economy and, in the case of the developing countries, it is also an increasingly important form of net long-term resource flows. In developing countries, sustained FDI growth during the 1990s has taken place alongside a surge in portfolio equity investment flows, as well as an increase in private debt flows. Indeed, between 1990 and 1993, total private capital flows to developing countries almost quadrupled, with FDI constituting the largest single component of these flows (figure 1). The elimination of regulatory restrictions on portfolio equity investment, including with respect to foreign participation in developing-country stock markets, coupled with the privatization of State-owned enterprises through the issuance of international equity offerings (e.g., global depository receipts), have contributed to the surge in portfolio equity investments. The relaxation of the regulatory framework as regards foreign participation in domestic stock markets, in addition to expanding the options available to TNCs for raising capital or providing alternative modes for investment (e.g., the acquisition of firms listed in stock exchanges), also sends positive signals to potential foreign direct investors as regards a country’s overall investment climate and its stance towards the private sector. Nevertheless, the relationship between these two types of flows is not clear.

3. The diverging trends of portfolio equity and FDI flows in 1994 (figure 1) highlight the differences between these two types of flows in terms of their respective basic determinants and volatility. The decision of whether or not to undertake FDI is based on a match between long-term strategic considerations by TNCs and the location-specific advantages possessed by countries. By definition, FDI involves therefore a lasting commitment to the recipient economy, although some financial transactions associated with these investments may also be volatile. As a rule, however, FDI is less susceptible to transient financial shocks as long as they do not impinge upon the longer-term macroeconomic environment of the economy. In contrast, portfolio equity investment flows are typically of a more speculative nature and respond quickly to higher returns offered elsewhere and to higher risks in the host economy as perceived by foreign investors. As a result, portfolio equity investment tends to be more unstable than FDI and reacts faster to transient financial shocks, for instance, as the one experienced by Mexico in 1994/1995. However, to the extent that portfolio equity investment is transformed into FDI, the susceptibility of the latter to such shocks is also likely to increase.

4. In addition to being a financial flow, FDI also constitutes a flow of production assets and activities associated with TNCs. These activities are reflected in the global FDI stock -- attributable to some 207,000 foreign affiliates controlled by at least 38,000 parent firms[1/] -- which stood at an estimated $2.1 trillion at the end of 1993 (table 1). That stock generated sales by foreign affiliates worth $5.8 trillion in 1992,[2/] exceeding worldwide exports of goods and non-factor services worth $4.7 trillion in that year (one-third of which takes place on an intra-firm basis). Investment outflows were $193 billion in 1993, and an estimated $204 billion in 1994, while payments for royalties and fees (for licences, patents, use of brand names and trademarks,

Figure 1. FDI, portfolio equity investment and private debt flows to developing countries, 1990-1994
(Billions of dollars)



Source: World Bank, *World Debt Tables 1994/95, Volume 1* (Washington, D.C., The World Bank, 1995), table 1.1.

a/ Projected by the World Bank.

Note: The World Bank's classification of developing countries and hence the data on FDI presented here are different from those used elsewhere in this report.

services etc.) were some $37 billion in 1992, an estimated 80 per cent of which took place on an intra-firm basis. In 1993, the FDI stock grew twice as fast as worldwide exports of goods and non-factor services (table 1). As a result, the importance of FDI in international economic transactions increased further. The importance of FDI in relation to domestic investment in host countries has been growing in developing countries and the countries of Central and Eastern Europe over the 1990s while it declined in developed countries (table 2). Since 1991, the ratio of FDI to gross domestic capital formation in the former two groups of countries exceeded that in the developed countries.

5. Foreign-direct-investment stocks and flows are two indicators -- albeit very imperfect ones -- of the activities of TNCs, highlighting however different aspects. Developed countries taken as a group account for the largest share of global FDI stock, reflecting, among others, their much longer history and stronger performance as outward investors and recipients of inward FDI flows (table 3). Their dominant position is particularly significant with respect to outward FDI stock, of which they account for 97 per cent. They also account for the preponderant share (76 per cent in 1993) of global inward FDI stock. These shares, reflecting the geographic structure of TNC activities and the concentration of international production in developed economies, have been quite stable over the 1980s and 1990s, except for a slight reduction (in favour of developing countries) in 1992-1993. Within the developed countries, FDI stocks are concentrated in the Triad (Japan, European Union and the United States), with European Union countries accounting for the largest share of both inward and outward stock of FDI -- about 39 per cent and 44 per cent, respectively, in 1993.

Table 1. Selected FDI, economic and financial indicators in the world, 1981-1993

Indicator	Value at current prices, 1993 (Billions of dollars)	Average annual growth rates (per cent)			
		1981-1985	1986-1990	1991-1993	1992-1993
FDI outflows	193	-0.5	29.0	0.4	5.0
FDI outward stock	2 133	5.0	20.0	8.0	9.0
Sales of foreign affiliates of TNCs a/	5 800 b/	1.0 c/	17.0	20.0 d/	..
Current gross domestic product at factor cost	23 500	2.0	10.0	3.0	1.0
Gross domestic investment	4 465	0.8	11.0	2.0 d/	..
Exports of goods and non-factor services	4 721 b/	-0.7	15.0	5.0	1.0
Royalties and fees receipts	37 b/	-0.7	23.0	3.0 d/	..

Source: UNCTAD, Division on Transnational Corporations and Investment estimates, based on International Monetary Fund, balance-of-payments tape, retrieved on 5 January 1995; and unpublished data provided by the Organisation for Economic Co-operation and Development Secretariat and the World Bank, International Economics Department.

a/ Estimated by extrapolating the worldwide sales of foreign affiliates of TNCs from Germany, Japan and the United States on the basis of the relative importance of these countries in worldwide outward FDI stock.
b/ 1992.
c/ 1982-1985.
d/ 1991-1992.

Table 2. The ratio of FDI inflows to gross domestic capital formation, 1985-1992
(Percentage)

Region	1985	1986	1987	1988	1989	1990	1991	1992
Developed countries	2.3	3.0	4.2	4.3	5.2	4.8	3.3	2.6
Western Europe	3.3	3.2	4.2	5.2	7.2	7.3	5.6	5.3
North America	2.6	4.6	7.5	6.9	7.4	5.3	2.9	0.8
Other developed countries	0.6	0.7	0.7	0.9	0.9	1.0	0.7	0.8
Developing countries	2.1	2.0	2.9	3.4	3.2	3.4	4.2	4.9
Africa	4.2	2.6	3.6	3.6	6.7	3.1	4.3	4.5
Latin America and the Carribean	3.5	2.9	3.9	4.5	4.0	4.0	5.8	4.9
West Asia	0.4	0.3	0.2	0.6	0.4	0.3	0.7	0.6
East, South and South-East Asia	1.6	2.4	3.6	3.8	3.3	4.2	4.2	5.5
Oceania	15.6	12.8	13.6	16.7	21.4	17.8	7.3	4.7
Central and Eastern Europe	-	-	-	-	-	-	6.7	8.5
Memo item:								
Least developed countries	2.1	0.3	3.2	3.1	5.6	3.9	2.0	1.9

Source: UNCTAD, Division on Transnational Corporations and Investment estimates, based on United Nations, Department of Economic and Social Information and Policy Analysis, *Handbook of World Development Statistics* (New York, United Nations, 1993), mimeo., and World Bank, *World Debt Tables 1994/95* (Washington, D.C., The World Bank, 1994).

Table 3. FDI world stock, by country and region,a/ 1988-1993
(Billions of dollars)

Region/country	**1988**	**1989**	**1990**	**1991**	**1992**	**1993**
A. Outward stock						
Major home countries	799	937	1 131	1 244	1 315	1 429
France b/	51	75	110	130	161	182
Germany	104	121	152	173	179	194
Japan b/	113	157	205	236	253	257
United Kingdom	185	194	229	232	221	247
United States c/	346	390	435	473	501	549
World	1 149	1 363	1 655	1 830	1 948	2 133
B. Inward stock						
Developed countries	931	1 121	1 348	1 464	1 502	1 613
Western Europe	447	561	745	825	840	917
North America	407	472	504	532	544	570
Other developed	77	89	99	107	118	126
Developing economies	267	295	332	371	422	494
Africa	33	37	39	42	45	48
Latin America and the	97	105	116	131	148	168
East, South and South	107	123	146	167	198	245
West Asia	27	27	27	28	29	29
Oceania	2	2	2	2	2	2
Central and Eastern Europe	0.2	0.5	0.8	3	8	14
World	1 198	1 417	1 680	1 838	1 932	2 121

Source: UNCTAD, Division on Transnational Corporations and Investment FDI database.

a/ For most countries (except Germany, the United Kingdom and the United States), stocks are estimated as accumulated flows or as flow added to the stock reported in a particular year.

b/ Not including reinvested earnings.

c/ Excluding FDI stock in the finance (except banking), insurance and real estate industries of the Netherlands Antilles.

6. Data on FDI stock also throw light on the structure of international production in terms of its sectoral composition. Data on the outward FDI stock of the major home countries show that the services sector is the largest FDI sector, accounting for 46 per cent to 67 per cent of FDI stock in major home countries at the beginning of the 1990s, compared to between 35 per cent and 53 per cent in the mid-1980s.[3/] This structural change reflects a sustained shift in the composition of FDI flows from and to the major home countries towards service industries.

7. While, as mentioned above, the dominant share of developed countries in global FDI stock has remained largely unchanged in recent decades, it could well

change if recent trends with respect to FDI outflows from and inflows to developing countries continue, resulting in rapid growth in accumulated production capacity by TNCs in developing countries. Investment outflows from developing countries -- particularly to other developing countries -- have increased noticeably since the mid-1980s, and rose by a further 21 per cent in 1993, to reach $12 billion. But it is with respect to inward FDI flows that the recent performance of developing countries has been particularly striking, in the broader framework of international FDI flows.

8. The year 1993 was characterized by the end of the FDI recession that had prevailed in 1991 and 1992. In 1993, the decline in FDI flows came to a halt, with global outflows increasing by 5 per cent, to reach $193 billion (table 4). However, only a handful of countries (notably, the United States and the United Kingdom) recovered strongly from the FDI recession; outflows from other developed countries (mostly in Western Europe and Japan) continued to decline in 1993. And although the decline of investment inflows to developed countries also reversed in 1993, their growth rate of 7 per cent, as well as that of outflows (4 per cent), was well below that during the 1980s. As a result, the share of developed countries in worldwide inflows decreased from 64 to 58 per cent between 1992 and 1993, even though, as discussed earlier, these countries dominate the global inward stock, accounting for almost four-fifths of it. Outflows from the five major home countries increased by 7 per cent in 1993, to $133 billion (for a share of worldwide outflows of 69 per cent); preliminary estimates for 1994 show continuing recovery, to a level of $142 billion (table 5).

9. In contrast to the low growth of FDI flows to developed countries, developing countries enjoyed, with $71 billion in 1993,[4/] a new record level of FDI inflows, which was further improved to an estimated $80 billion in 1994 (an increase of 36 per cent between 1992 and 1993 and 13 per cent between 1993 and 1994), for an estimated stock of nearly $500 billion in 1993 (tables 3 and 4). More than 80 per cent of the *increase* in FDI flows to developing countries in 1993 was accounted for by one developing country, China. Excluding China, FDI flows into developing countries increased by 6 per cent in 1993 (comparable to the increase registered by developed countries) and by 15 per cent in 1994. Overall, the total inflows into developing countries in 1993 alone were higher than the level of inflows to developed countries in 1986. In fact, between 1986 (the beginning of the most important FDI upswing so far) and 1993, flows into developing countries (including China) increased fivefold. Developing countries are thus becoming increasingly significant hosts for FDI, accounting for a historic high of 39 per cent of worldwide inflows in 1993, a development (if maintained) that, over time, would change the structure of global TNC activities. Clearly, developing countries as a whole are becoming more attractive host countries, largely in response to their good growth performance combined with on-going liberalizations of FDI policies,[5/] the continuing implementation of privatization programmes open to foreign participation and the continuous search for new dynamic markets and cost-efficient production locations by TNCs. The highlights, by geographical region, are as follows (for a more detailed discussion of regional trends outside the developed countries, see TD/B/ITNC/3)[6/]:

- Asia and the Pacific. Investment inflows increased by 51 per cent in 1993, reaching some $48 billion in that year and an estimated $53 billion in 1994. Asia and the Pacific accounted for 68 per cent of total inflows to developing countries in 1993. With nearly $28 billion,[7/] China emerged as the largest recipient of investment inflows *worldwide* in 1993 (accounting for 15 per cent of these flows), a position which it probably lost to the United States in 1994 (an estimated $30 billion in inflows for China versus $41 billion in inflows for the United States, based on data for the first three quarters of 1994 for the latter).

- Latin America and the Caribbean. Investment inflows increased by 16 per cent in 1993, reaching some $19 billion in that year and an estimated $22 billion in 1994. Latin America and the Caribbean accounted for 27 per cent of total inflows to developing countries in 1993. Argentina, with over $6 billion in inflows in 1993, was the largest recipient.

Table 4. FDI inflows and outflows, 1982-1994
(Billions of dollars and percentage)

Country	1982-1986 Annual average	1987-1991 Annual average	1989	1990	1991	1992	1993	1994 a/	1982-1986 Annual average	1987-1991 Annual average	1992	1993	1994 a/	1982-1986 Annual average	1987-1991 Annual average	1992	1993	1994 a/
	(Billions of dollars)								Share in total b/ (percentage)					Growth rate b/ (percentage)				
Developed countries																		
Inflows	42	143	171	177	120	100	107	117	77	82	64	58	57	24	1	-16	7	9
Outflows	53	184	215	228	184	174	181	192	98	96	95	94	94	25	9	- 6	4	6
Developing countries																		
Inflows	13	30	29	32	39	52	71	80	23	17	33	39	39	-0.4	13	32	36	13
Outflows	1	7	11	10	7	10	12	12	2	4	5	6	6	11	28	47	21	3
Central and Eastern Europe																		
Inflows	0.02	0.6	0.3	0.3	2	5	6	7	0.03	0.4	3	3	3	3	278	91	22	23
Outflows	0.008	0.02	0.02	0.04	0.01	0.04	0.04	0.06	0.01	0.01	0.02	0.02	0.03	53	7	336	-2	36
All countries																		
Inflows	55	174	200	209	162	157	183	204	100	100	100	100	100	17	4	-3	17	11
Outflows	55	192	226	239	191	184	193	204	100	100	100	100	100	25	9	-4	5	6

Source: UNCTAD, Division on Transnational Corporations and Investment estimates, based on International Monetary Fund, balance-of-payments tape, retrieved on 5 January 1995, and data from the Organisation for Economic Co-operation and Development Secretariat.

a/ Based on preliminary estimates.

b/ Calculated on the basis of FDI flows expressed in millions of dollars.

Note: Here and in other tables, the levels of worldwide inward and outward FDI flows and stocks should balance; however, in practice, they do not. The causes for the discrepancy, include differences between countries in the definition and valuation of FDI; the treatment of unremitted branch profits in inward and outward FDI; treatment of unrealized capital gains and losses; the recording of transactions of "offshore" enterprises; the recording of reinvested earnings in inward and outward FDI; the treatment of real estate and construction investment; and the share-in-equity threshold in inward and outward FDI.

Table 5. FDI outflows from the five major home countries, 1982-1994
(Billions of dollars and percentage)

Country	1982-1986 Annual average	1987-1991 Annual average	1990	1991	1992	1993	1994 a/	1982-1986 Annual average	1987-1991 Annual average	1992	1993	1994 a/	1982-1986 Annual average	1987-1991 Annual average	1992	1993	1994 a/
	(Billions of dollars)							Share in total d/ (percentage)					Growth rate d/ (percentage)				
France b/	3	20	35	24	31	21	25	5	11	17	11	12	17	27	31	-34	21
Germany	6	18	29	23	16	15	15	10	10	8	8	9	35	26	-32	- 3	-1
Japan b/	7	35	48	31	17	14	18	13	18	9	7	8	34	12	-44	-20	32
United Kingdom	10	28	19	16	19	26	27	19	15	11	13	13	24	-16	21	33	5
United States c/	11	28	30	31	41	58	56	20	15	22	31	28	7	5	31	41	-3
Total (5 countries)	37	130	161	125	124	133	142	67	68	68	69	70	22	7	-0.3	7	6
All countries	55	192	239	191	194	193	204	100	100	100	100	100	25	9	-4	5	6

Source: UNCTAD, Division on Transnational Corporations and Investment estimates, based on International Monetary Fund, balance-of-payments tape, retrieved on 5 January 1995, and official national sources.

a/ Based on preliminary estimates.

b/ Not including reinvested earnings. In the case of France, reinvested earnings are not reported after 1982.

c/ Excluding outflows to the finance (except banking), insurance and real estate industries of the Netherlands Antilles. Also excludes currency-translation adjustments.

d/ Calculated on the basis of FDI flows expressed in millions of dollars.

- Africa. At about $3 billion, FDI flows into Africa remained stagnant in 1993, despite the on-going liberalization of investment regimes by a number of countries. As a result, Africa's share in all inflows to developing countries declined to 5 per cent in 1993, compared with 11 per cent during 1986-1990. Although North Africa has fared better than Sub-Saharan Africa overall, FDI inflows to North Africa increased only marginally in 1993, to $1,430 million (compared with $1,413 million in 1992).

10. Disparities in distribution continue to be a notable feature of FDI in developing countries.[8/] The ten largest host developing economies have consistently absorbed between 66 and some 80 per cent of total flows to developing countries over the past ten years (81 per cent in 1993) (table 6). On the other hand, investment flows to the 47 least developed countries have remained consistently small: only some $500 million in 1993 (about the size of inflows to Morocco), and their share of total inflows to developing countries was minuscule, at 0.7 per cent that year.

11. The composition of the ten largest developing-country FDI recipients ranked in terms of flows is largely similar to that in terms of stocks (table 6). But FDI is less concentrated in the ten largest host economies in terms of stocks than in terms of flows. For the most part, these countries have attracted large investment flows over the past ten years, and the resulting additions to their stocks are reflected in their ranking in terms of the size of their investment stock. The two major exceptions to the similarity of their rankings

Table 6. The ten largest host developing economies to FDI flows and stock, 1993
(Millions of dollars)

Host economy	Flows	Host economy	Stocks
All developing economies	70 812	All developing economies	494 418
Total, ten largest developing host economies a/	57 105	Total, ten largest host economies a/	336 996
Percentage share of the ten largest developing host economies in total inflows to developing economies	81	Percentage share of the ten largest host economies in total inward stock of developing economies	68
China	27 515	China	57 172
Singapore	6 830	Singapore	50 802
Argentina	6 305	Indonesia	44 146
Mexico	4 901	Mexico	41 912
Malaysia	4 351	Brazil	40 371
Indonesia	2 004	Malaysia	26 936
Thailand	1 715	Saudi Arabia	22 463
Hong Kong	1 667	Argentina	21 701
Taiwan Province of China	917	Hong Kong	17 669
Nigeria	900 b/	Thailand	13 824
Memorandum:			
Percentage share of the nine largest host economies, excluding China	42	Percentage share of the nine largest host economies, excluding China	57

Source: UNCTAD, Division on Transnational Corporations and Investment estimates, based on International Monetary Fund, balance-of-payments tape, retrieved on 5 January 1995; data from the Organisation for Economic Co-operation and Development Secretariat; and national official sources.

a/ Excluding tax havens.

b/ Estimated.

are Brazil and Saudi Arabia, whose large stocks were accumulated in earlier years and which do not appear in the list of the largest recipients in terms of flows for 1993.

12. Central and Eastern Europe. Investment inflows to the countries of Central and Eastern Europe increased by 22 per cent in 1993, reaching some $6 billion in that year, for a stock of $14 billion at the end of 1993, attributable to some 50,000 foreign affiliates in operation. The growth of inflows, however, has slowed due to the lingering economic recession in some countries of Western Europe (the main source of investment inflows), combined with the slow or negative growth in these countries during their transition towards a market economy. Central and Eastern Europe accounted for 3 per cent of worldwide inflows in 1993; these continue to be unevenly distributed within the region, with the Czech Republic, Hungary and Poland accounting for the majority of investments.

13. The developed countries were the principal source of, as well as beneficiaries from, the recovery of FDI flows. Investment outflows from them rose by 4 per cent in 1993, after declining by 19 per cent in 1991 and 6 per cent in 1992 (table 4). The reversal of the downward trend in developed countries in the 1990s is mostly a consequence of the recovery from the recent downswing in economic activity, albeit at different speeds. The highlights for the developed countries are:

- United States. After experiencing a large decline in 1992 (to a level of $3 billion), mostly due to sluggish economic growth and the low profitability of foreign affiliates, FDI inflows to the United States recovered to reach some $21 billion in 1993. Despite the strong and rapid recovery of inflows, their level is only 30 per cent of the level attained in the peak year 1989, when inflows reached $69 billion. On the other hand, outflows increased considerably throughout the 1990s (by 41 per cent in 1993 for a new historic high of $58 billion).

- Western Europe. Overall, investment inflows decreased by 10 per cent in 1993, reaching around $73 billion in that year. Western Europe accounted for 40 per cent of worldwide inflows in 1993. From a peak of $110 billion in 1990, investment flows into the European Union fell by 15 per cent in 1993 (compared with 1992), to $66 billion. That decline was widespread throughout the European Union; by contrast, other Western European countries experienced a near-doubling of inflows in 1993. Outflows also declined by 10 per cent to $100 billion in 1993; the 33 per cent increase for the United Kingdom and the 32 per cent increase for the non European-Union countries (to $26 billion and $13 billion, respectively) in 1993 were not sufficient to compensate for large declines of outflows from France, Belgium, Luxembourg and other members of the European Union.

- Japan and other developed countries. After a record level of nearly $3 billion in 1992, investment inflows to Japan fell to $100 million in 1993 (about the same as inflows to Gabon in that year). Outflows fell by another 20 per cent (for the third consecutive year), to $14 billion, reaching a trough in 1993, with, however, signs of recovery in 1994. Investment inflows to other developed countries declined by 37 per cent, reaching nearly $7 billion in 1993. Australia (like Japan) saw a sharp drop in investment inflows. Other developed countries accounted for 4 per cent of worldwide inflows in 1993.

14. Although investment flows recovered in 1993, their rebound was neither robust nor widespread. Moreover, only a few developed and developing countries registered sizeable increases in investment inflows. Developing countries as a whole fared better than developed countries in terms of the size of the increase in investment inflows, with these increases being concentrated in Asia and the Pacific and Latin America and the Caribbean. The least developed countries, especially those in Africa, continue to be less favoured by foreign investors (with a few exceptions), but these investments continue to be important in relation to the size of domestic capital formation in comparison with other, more advanced developing economies.

B. Major factors behind recent trends

15. Improved economic conditions in a number of major home countries as they began to emerge from the economic recession of the early 1990s, combined with continuing robust growth in many developing countries, produced the setting that marked the end of the FDI recession in 1993. And all this took place against the backdrop of the on-going relaxation of investment restrictions in developing countries, including the continuing implementation of privatization programmes open to foreign participation, and the progressive realization of TNC strategies aimed at penetrating new markets and rationalizing their operations in the face of international competition. That the recovery in worldwide investment flows in 1993 was slow can be attributed partly to the uneven recovery from the economic recession in the major home and host countries. In fact, slow growth lingered in many developed economies in 1993, and the robustness of the recovery was not the same across all developed countries. Japan and several countries in Western Europe (France, Germany, Italy and Spain), for example, grew in 1993 at substantially lower rates than the United States and the United Kingdom which emerged from the recession earlier. Indeed, it was the increase in investments by the latter two countries that was principally responsible for the end of the FDI recession in the developed countries. The flows of other developed countries were still affected by their slow recovery and the time lag that is usually observed between the end of a recession and the subsequent growth of investment flows. Thus, despite the recovery of worldwide FDI outflows in 1993, their level in that year exceeded only slightly the level attained in 1991 -- itself 20 per cent below the peak level in 1990.[9/]

16. The unfavourable economic conditions in the early 1990s also had a dampening effect on cross-border mergers and acquisitions -- a strategy for investing abroad that had become especially important in the late 1980s. In addition, greater attention paid by TNCs to their core business has led to divestments from activities not related to the core and to a decline in cross-border mergers and acquisitions. Greater focus on core activities resulted from the experiences of a number of TNCs with unsuccessful diversifications into new lines of business and product areas.[10/] Thus, the failure of majority foreign-owned cross-border mergers and acquisitions to recover affected the related FDI inflows which remained weak for the developed countries in 1993 (table 7).[11/] However, the value of minority foreign-owned cross-border mergers and acquisitions increased considerably in 1993, pointing to an increasing use by TNCs of alliance-type low-equity associations as a modality of penetrating foreign markets (table 7 and figure 2), as discussed further below. A notable exception from this trend is the United States, where the large increase in investment inflows in 1993 concurred with the increase (by 80 per cent) in the value of all cross-border mergers and acquisitions, including the increase of both majority and minority foreign-owned mergers and acquisitions.

17. The on-going relaxation of investment restrictions, including the continuing implementation of privatization programmes, has created new opportunities for FDI in developing countries and Central and Eastern Europe. Nevertheless, the value of FDI from privatization remained stagnant in 1993 compared with the previous year, accounting for nearly 8 per cent of total investment inflows to developing countries in 1993 (table 8). In Latin America and the Caribbean FDI from privatization more than halved in 1993 while total FDI flows continued to grow strongly. Privatization-related FDI increased more than tenfold in Sub-Saharan Africa between 1992 and 1993; but over 90 per cent of that investment consisted of one privatization (in Nigeria). East Asia and the Pacific saw a doubling of FDI from privatization in 1993, although the share of these investments in total inflows remained constant. It should be noted that, in many cases, additional post-privatization investments have followed the initial investment: contrary to conventional perception, privatization need not represent a one-time factor in influencing FDI flows. [12/]

18. Direct investment from developing countries has become an increasingly important source of foreign capital, especially for other developing countries. In terms of stocks, FDI from developing countries, at $70 billion at the end of 1993, constituted 3 per cent of the global outward stock. In 1990, the share of developing countries in the inward FDI stock of 58 host countries was, on

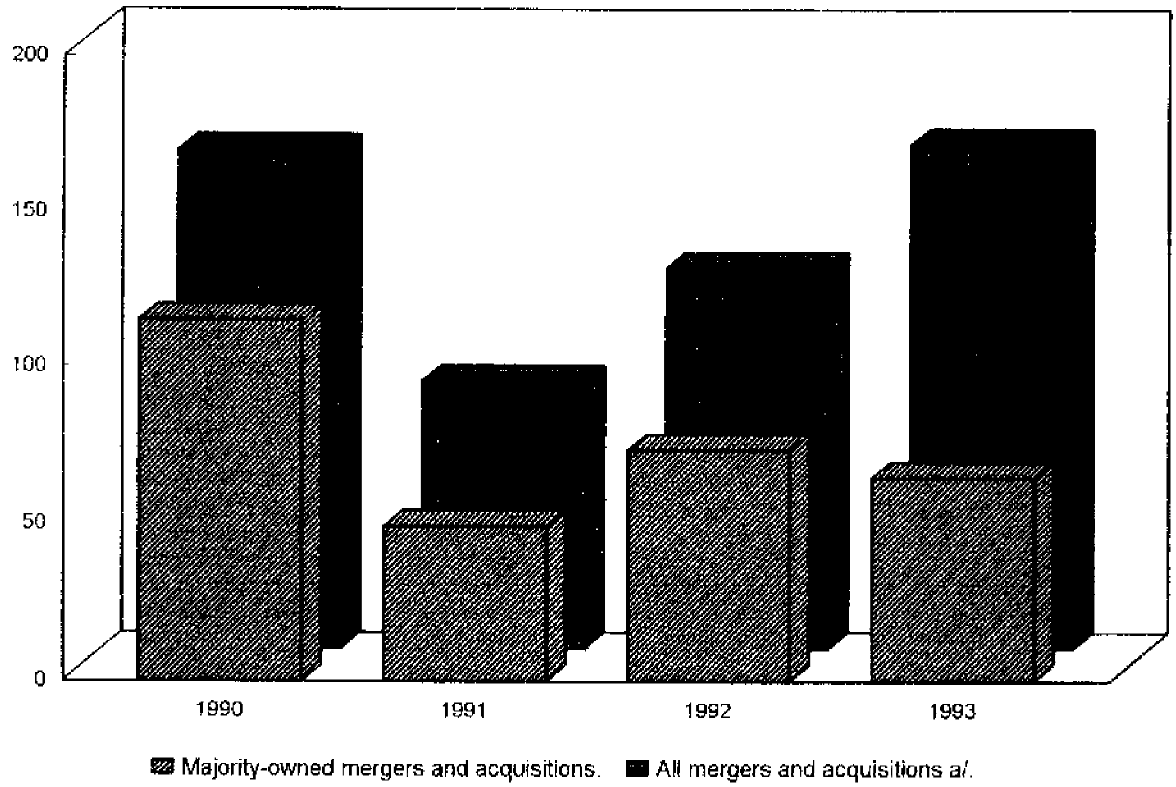
Table 7. The value of worldwide cross-border mergers and acquisitions and FDI inflows to developed countries, 1987-1993
(Billions of dollars)

Item	1987	1988	1989	1990	1991	1992	1993
Worldwide (majority foreign-owned) cross-border mergers and acquisitions	71	113	123	115	49	74	65
FDI inflows to developed countries	113	134	171	177	120	100	107
Cross-border mergers and acquisitions as a ratio of FDI inflows to developed countries (%)	63	84	72	65	41	74	61

Source: UNCTAD, Division on Transnational Corporations and Investment estimates, based on KPMG, *Dealwatch* (Amsterdam, KPMG, various issues) and unpublished data.

Figure 2. Cross-border mergers and acquisitions, 1990-1993
(Billions of dollars)

Source: KPMG, *Dealwatch* and unpublished data.



a/ Through majority and minority foreign-equity participation and joint ventures that also include mergers. Data include portfolio investment.

Table 8. FDI from privatization in developing countries, 1989-1993 a/
(Millions of dollars and percentage)

Region	1989	1990	1991	1992	1993	1989-1993
North Africa and Middle East						
FDI from privatization	1.0	-	3.2	19.2	302.0	325.4
Share of region's FDI inflows	0.06	-	0.4	1.4	22.3	5.5
Sub-Saharan Africa						
FDI privatization	13.8	38.2	11.1	49.8	544.7	657.6
Share of region's FDI inflows	0.6	4.3	1.2	4.6	52.1	10.8
East Asia and the Pacific						
FDI from privatization	-	0.7	77.1	522.7	1076.4	1676.9
Share of region's FDI inflows	-	0.01	0.6	2.6	2.9	1.9
South Asia						
FDI privatization	0.1	10.6	4.2	41.8	16.2	72.9
Share of region's FDI inflows	0.02	2.0	0.9	6.9	2.0	2.5
Latin America and the Caribbean						
FDI from privatization	183.3	2461.5	3264.3	2414.5	1107.4	9430.5
Share of region's FDI inflows	2.3	32.5	27.8	18.4	7.2	16.9
All developing regions						
FDI from privatization	198.2	2511	3359.9	3048	3047	12164.1
Share of region's FDI inflows	0.9	12.3	12.2	8.4	5.5	7.6
Memo item:						
Central and Eastern Europe						
FDI from privatization	461.5	475.5	1868.2	2697.9	2979.8	7545.9c/
Share of region's FDI inflows	..	..	76.3	58.5	53.3	59.7

Source: based on Frank Sader, "Privatization techniques and foreign investment in developing countries, 1988-93" (Washington, D.C., Foreign Investment Advisory Service, 1994), mimeo..

a/ The World Bank's developing-country classification used in this table differs from that used elsewhere in this report.
b/ Foreign direct investment from privatization is larger than the recorded FDI inflows reported by the IMF in the balance-of-payments data.
c/ 1991-1993.

Note: For the purposes of this table, each region comprises only those countries that have received FDI in connection with privatizations.

average, about 6 per cent, ranging from 1 per cent in Denmark, Norway and Sweden to 40 per cent in Thailand, 41 per cent in Malaysia, 49 per cent in Sri Lanka and 65 per cent in China. [13/]

II. FOREIGN DIRECT INVESTMENT AND TRANSNATIONAL CORPORATIONS FROM DEVELOPING COUNTRIES

19. Investment outflows from developing countries increased by 21 per cent in 1993, reaching $12 billion. The rapid growth of outflows from developing countries in recent years more than doubled their share of global outflows between the periods 1980-1984 and 1990-1993 (table 9).[14/] Still, the share of outflows from developing countries in worldwide outflows is significantly lower than the share of exports from developing countries in global exports: 6 per cent compared with 23 per cent, respectively, in 1993. Investment outflows are highly concentrated, with 74 per cent of outflows (and 74 per cent of the outward stock) originating in the four Asian newly industrializing economies (Hong Kong,[15/] Republic of Korea, Singapore and Taiwan Province of China) and China in 1993, but the number of developing countries that have joined the ranks of outward investors is increasing. Traditionally, outflows of capital from developing countries have been restricted, but the relaxation of foreign - exchange restrictions in several countries (e.g., the Republic of Korea and India [16/]) has fostered the growth of outward investments.

20. East and South-East Asia is an important FDI source for a number of developing countries in the same region. Nearly 70 per cent (or $22 billion) of FDI implemented in China during the period 1985-1992 originated in Hong Kong, Singapore and Taiwan Province of China. In Indonesia, Malaysia, Philippines and Thailand, one quarter of FDI inflows during the period 1985-1992 ($20 billion) was also from these economies.[17/] While investment from the newly

Table 9. Average annual FDI outflows from developing economies and world, 1970-1993
(Millions of dollars)

Home region/economy	1970-1979	1980-1984	1985-1989	1990-1993
Developing region/economy, total	224	763	4 459	9 464
Africa	36	78	112	162
Latin America and the Caribbean, of which:	97	260	400	1 278
Brazil	90	236	212	730
East, South and South-East Asia, a/ of which:	72	283	3 595	7 461
China	-	90b/	671	2 536
Republic of Korea	10	73	157	1 070
Singapore	..	106	325	882
Taiwan Province of China	2	45	2 384	2 802
Thailand	1	2	49	169
West Asia	18	142	352	563
World	27 625	48 277	133 831	201 446
Developing economies as percentage of world	0.8	1.6	3.3	4.7

Source: UNCTAD, Division on Transnational Corporations and Investment estimates, based on International Monetary Fund, balance-of-payments tape, retrieved on 5 January 1995; data from the Organisation for Economic Co-operation and Development Secretariat; and national official sources.

a/ Includes the Pacific. The total for the subregion is less than the sum of economies listed below due to negative outflows.

b/ Annual average for 1982-1984.

industrializing economies still flows mainly to the above-mentioned Asian countries, the destinations of such investments have diversified to include new host countries in the region, as well as in other regions. Taiwan Province of China and Hong Kong are, respectively, the largest and second largest home countries for FDI in Viet Nam; together, all the Asian newly industrializing economies accounted for 52 per cent of the total approved FDI inflows in that country during the period 1988-October 1994. [18/] Singapore became the largest investor in Myanmar with about one quarter of the total approved FDI ($1 billion) during the period 1988-March 1994. [19/] As an example of inter-regional investments among developing countries, China has become the third largest source country (after the United States and Panama) in Peru, with large investments in the mining and petroleum industries. [20/]

21. On average, the FDI share from developing countries is higher in host *developing* countries (19 per cent in 1990) than in host *developed* countries (4 per cent in the same year); in the former group, that share has increased from 16 per cent in 1980. More recently, however, the share of developing-country investments in total FDI received by developed countries (as reported by the latter) has been rising, but from a small initial base. For example, Asia’s share in the total inward stock of the United States increased from 0.8 per cent in 1988 to 1.2 per cent in 1993, while, in comparison, the share of imports into the United States from Asia remained relatively stable between these two years (table 10). The increasing importance of developed countries as hosts to FDI from developing countries is confirmed by the outward investments reported by the major developing home economies: the share of investments from the Republic of Korea into developed countries increased from one third of its total outward investment in 1980 to more than one half in the early 1990s. And the share of developed countries in the total outward investment stock of Taiwan Province of China increased from 43 per cent to more than one half during the same period. An illustration of TNCs from the major developing home economies investing in developed countries is provided by Samsung, a conglomerate from the Republic of Korea which has recently announced plans to invest over $700 million in an automobile manufacturing plant in the United Kingdom and by Cemex (Mexico) investments in the United States and Spain.[21/] Furthermore, TNCs from the Asian newly industrializing economies have also been engaging in strategic alliances with firms from developed countries.[22/]

22. Intra-regional FDI in Latin America has been boosted foremost by improvements in the economic conditions of countries that have adopted more liberal policies, such as Mexico and Chile, and by the lowering of investment and trade barriers that hindered outward investments. The North American Free Trade Agreement and its envisaged expansion to Chile (and, potentially, other countries in that region) and MERCOSUR (which came into effect in January 1995) are also expected to play a role in the regional restructuring of TNC operations based in -- or operating in -- the member countries. Some Latin American companies have already begun to pay closer attention to other countries in the region, with MERCOSUR becoming a testing ground for the ability of these companies to compete outside the boundaries of their home countries (although they still remain shielded from international competition within the borders of MERCOSUR). Most of these investments are market-driven (as opposed to efficiency seeking). For example, Brahma, a large brewing company from Brazil, is expanding its production facilities within the region through investments in Argentina (and Venezuela); in its decision to invest abroad, MERCOSUR played more of a facilitating role by helping to reduce administrative procedures and costs.[23/] Investment from Brazil in Latin America is currently concentrated in other MERCOSUR members: Argentina (automobile parts and components, foodstuffs), Paraguay (alloyed steel) and Uruguay (finance). In turn, FDI from Uruguay in Brazil nearly tripled between 1991 ($5 million) and 1992 ($14 million). The number of strategic alliances between Argentinean and Brazilian firms is also increasing.[24/] There are also some signs that FDI between Colombia, Ecuador and Venezuela, members of the Andean Common Market, has been growing in response to the negotiations for a free trade agreement, as well as the liberalization of investment regimes.[25/] Venezuela has become a sizeable outward investor (indeed, a net outward investor), with investments especially

Table 10. The share of FDI inward stock and imports attributed to developing economies and to the developing economies of Asia, as reported by selected developed countries, 1988 and 1993
(Percentage)

Host economy	FDI stock from				Imports from			
	All developing countries		Asia		All developing countries		Asia	
	1988	1993	1988	1993	1988	1993	1988	1993
United	6.4	6.7	0.8	1.2	36.8	40.5	20.6	23.3
United	3.8	2.7a/	1.1	1.7a/	12.1	13.9a/	7.1	8.8a/
Japan b/	13.4c/	14.1c/	3.0d/	2.7d/	46.9	49.1	31.4	35.9
Germany	2.3	2.1a/	0.6	0.6a/	14.4	13.8a/	6.7	7.6a/
France	2.1e/	2.0f/	0.2e/	0.3f/	13.8e/	15.7f/	4.7e/	6.2f/

Source: UNCTAD, Division on Transnational Corporations and Investment estimates, based on the Division's FDI database; OECD, *International Direct Investment Yearbook 1994* (Paris, OECD, 1994) and International Monetary Fund, *Direction of Trade Statistics Yearbook*, various years.

a/ 1992.
b/ Based on cumulative FDI approvals for fiscal years.
c/ Includes Australia and New Zealand, not separately available.
d/ Comprises only Hong Kong.
e/ 1989.
f/ 1991.

in Colombia and Ecuador; similarly, investment outflows from Colombia to Venezuela doubled between 1990 and 1993 to $50 million.[26/] Finally, an estimated 65-70 per cent of Chile's approved outward investments (more than $400 million in 1993) is in Argentina.[27/]

23. Like TNCs based in developed countries, developing-country TNCs in the manufacturing sector undertake international production to minimize costs and improve efficiency, access large and growing markets, acquire natural resources, technology and expertise and improve their export performances. In services, TNCs from developing countries seek to supply markets which the non-tradability of most services prevents them from reaching otherwise. For the most part, however, it appears that a smaller proportion of firms from developing countries (as opposed to those from developed countries) possesses the ownership-specific advantages (e.g., advanced proprietary technology, established brand names, special marketing and organizational skills) that are typically required to invest successfully abroad. Manufacturing investments consist normally of relatively labour-intensive, low-skill and low-technology activities, and the output is usually in the form of undifferentiated products whose competitiveness is based more on price rather than on the sophistication of the product design, quality or performance. Such firms invest typically in other developing economies. Examples include firms from Taiwan Province of China that invest in China,[28/] Thailand and Viet Nam in labour-intensive, low-skill operations. Similar investments by the Republic of Korea in China's northern provinces aim at reducing the cost of producing traditional exports, such as textiles and shoes, and improving efficiency. Geographical proximity and cultural affinity also can play a role regarding the location of such investments, as exemplified by the investments of ethnic Chinese in Asia.

24. On the other hand, a number of TNCs from such developing countries as Brazil, India, the Republic of Korea, Mexico and Taiwan Province of China have developed significant technological and innovation capabilities and production experiences, making their ownership-specific advantages comparable to those of

firms from developed countries. These advantages are further enhanced through a gradual accumulation of skills, information and technology [29/] and through access to resources and exposure to international competition by investing abroad. Foreign direct investment from Mexico in the United States in the glass industry and similar investments from the Republic of Korea and Taiwan Province of China in the automobiles, semiconductors and computers industries in the United States are examples of such investment.

25. Foreign direct investment from a number of developing countries is likely to continue to grow fairly rapidly in the future, especially to other developing but also increasingly to developed countries. The need to remain competitive internationally while confronting rising cost pressures at home, coupled with the desire to service prosperous markets elsewhere, is likely to push firms from such countries, especially those from the newly industrializing economies, to initiate or expand outward investment. As a greater number of these firms acquires ownership-specific advantages that enable them to compete abroad and to acquire additional resources and assets (including created assets) in order to enhance further their competitiveness, investments from developing to developed countries can also be expected to increase. The growing awareness by the governments of the ways in which outward investments can strengthen the competitiveness of their indigenous firms is beginning to initiate a process of gradually removing the legal obstacles to such investments. Finally, the investment-development path, whereby the "outward and inward investment position of a country is systematically related to its level of economic development relative to the rest of the world",[30/] implies that, as per capita incomes increase, the gap between inward and outward FDI will diminish and that some developing countries will progressively become net outward investors.[31/] While firms from East and South-East Asia are currently the leading outward investors, the growth of intra-regional investments in Latin America and the Caribbean, strengthened by regional trading schemes, are likely to bolster the importance of that region as an outward investor.

III. MODALITIES OF INTERNATIONALIZATION

26. The growth of FDI, including the increasing participation of developing countries in it, is part of a broader process of internationalization through which firms seek access to markets and (natural and created) assets and, more broadly, organize international production.

A. Market access

27. Firms can use various modalities to deliver goods and services to foreign markets: exports (including exports within the transnational network of firms); FDI; cross-border, cooperative inter-firm agreements (such as strategic alliances); non-equity forms of TNC involvement (e.g., licensing, turnkey agreements, franchising, management contracts); and subcontracting. For firms, these various modalities are partly interchangeable (e.g., subcontracting can be a substitute for FDI), partly complementary to each other (e.g., exports and FDI can be complementary since intra-firm exports between parent firms and foreign affiliates constitute a large part of total exports), and they are, in any event, tightly interwoven with each other, in a quest to maintain or expand market positions.

28. The magnitude and hence the changing importance of different modalities of delivering goods and services to foreign markets is difficult to assess, given the lack of appropriate and comparable data. Worldwide sales of foreign affiliates -- as a measure of the importance of FDI -- exceed exports of goods and non-factor services, despite the recent slow-down in the growth of these sales as a result of the economic recession in the major developed countries (table 11). Given the lack of satisfactory data, this and the subsequent calculations in this section are based on rough estimates only and therefore need to be interpreted with caution. In the case of the United States, sales of foreign affiliates in 1992 amounted to around two-and-a-half times the export volume of goods and non-factor services (table 12). Licensing agreements typically entail an important element of continuous control as they involve the

Table 11. Modalities of international transactions, 1984-1992
(Billions of dollars)

Year	Sales of foreign affiliates	Sales associated with licensing with unaffiliated firms a/	Estimated intra-firm exports b/	Exports of goods and non-factor services	Exports of goods and non-factor services excluding estimates of intra-firm exports
1984	2,500	30	770	2,310	1,540
1985	2,500	40	780	2,340	1,560
1986	2,900	50	860	2,580	1,720
1987	3,500	60	1,020	3,050	2,030
1988	4,200	80	1,090	3,270	2,180
1989	4,400	80	1,180	3,540	2,370
1990	5,500	110	1,370	4,110	2,750
1991	4,800	120	1,450	4,350	2,900
1992	5,800	120	1,570	4,720	3,150

Source: UNCTAD, Division on Transnational Corporations and Investment estimates.

a/ The share for unaffiliated firms' receipts of royalties and fees worldwide is based on the share of unaffiliated firms in the total receipts of royalties and fees for the United States. Sales are estimated using the assumption that royalties and fees, as a proxy for licensing, are 7.5 per cent of total sales associated with them.

b/ Estimated on the basis of the assumption, based on United States data, that intra-firm trade accounts for about one third of total trade. Some intra-firm exports may be included in the sales of foreign affiliates.

Note: Some figures have been rounded.

Table 12. United States: modalities of international transactions, 1986-1993
(Billions of dollars)

Year	Sales of foreign affiliates	Sales associated with licensing with unaffiliated firms a/	Sales associated with franchising b/	Intra-firm exports of goods and non-factor private services c/	Goods and non-factor private services exports d/	Goods and non-factor private services exports excluding intra-firm exports d/
1986	929	25 e/	..	66	288	221
1987	1,053	29	1.5	72	330	259
1988	1,195	37	2.3	86	410	324
1989	1,285	35	2.7	98	468	370
1990	1,493	42	3.2	100	513	413
1991	1,542	45	4.4	107	555	448
1992	1,579	49	4.5	115	593	478
1993	..	54	5.4	..	617	..

Source: UNCTAD, Division on Transnational Corporations and Investment estimates, based on United States, Department of Commerce, *Survey of Current Business*, various issues; and unpublished data.

a/ Estimated for unaffiliated firms on the basis of the assumption that receipts of royalties and fees, as a proxy for licensing, are 7.5 per cent of total sales associated with them.
b/ Estimated on the basis that franchising fees are 7.5 per cent of total sales associated with them.
c/ Exports of non-bank parent firms shipped to their foreign affiliates.
d/ Exports of services exclude royalties and licence fees.
e/ Includes sales associated with franchising.
Note: All figures have been rounded.

use of the parent firms' technology by the firms purchasing the licence. Assuming that royalties and fees represent an estimated 5-10 per cent of sales, then goods and services delivered to foreign markets by way of licensing agreements appear to have doubled between 1987 and 1992 (table 11). Data on the importance of other non-equity forms of TNC involvement are not available; but the number of cross border strategic alliances increased substantially over the past two decades, suggesting that this form of internationalization has increased as well.[32/] As a result, worldwide sales by foreign affiliates plus sales associated with worldwide licensing to unaffiliated firms as a percentage of world exports of goods and non-factor services increased from an estimated 110 per cent in 1984 to 125 per cent in 1992; if one assumes (on the basis of data for the United States) that intra-firm trade accounts for about one third of total exports and adds estimated intra-firm trade to these transactions (subtracting it from exports), the ratios of sales associated with TNC activity to the value of arm's length exports increase to 215 per cent and 238 per cent, respectively in the two years. In other words, only about one third of international transactions are not associated with TNC activity. In the case of the United States, whose firms are among the leaders in the internationalization process (and for which better data are available), such transactions account for about one quarter of all international transactions (table 12). In other words, the lion's share of the international transactions of the United States are linked to the activities of the country's TNCs.

29. Thus, the relative importance of various modalities in terms of bringing goods and services to foreign markets is changing, with modalities involving transactions within TNCs or by TNC affiliates having surpassed arm's length trade in importance -- for some countries, in fact, to a considerable extent. This means that a larger share of international transactions has shifted into a different kind of market: they no longer take place between independent agents governed by market forces but rather involve related agents, often under a common corporate governance. One of the policy implications of this shift is that discussions -- and, for that matter, negotiations among policy-makers -- dealing with market access ought to be broad enough to capture all market-access modalities -- and not only trade -- of importance to firms in terms of delivering goods and services to foreign markets. This also raises issues for developing countries regarding competition policies and intra-firm pricing.

B. Access to factors of production

30. Access to markets is only one feature of these modalities. An equally important -- if not more important -- feature of some of them is that they also provide access to the various factors of production, defined broadly to include such tangible and intangible assets as capital, labour, technology, skills and entrepreneurship. This is particularly the case for FDI which, by its very nature, combines the ownership advantages of firms with the locational advantages of countries in the interest of improving the efficiency -- and, in any event -- the profitability of the production process for the firm as a whole. More broadly, the very rationale of a good part of FDI is precisely to gain access to factors of production abroad.

31. As discussed earlier, the importance of various modalities of accessing markets and factors of production has changed over time, driven by international competition in the framework of corporate strategies that need to take into account the possibilities offered by advances in technology and the liberalization of international economic transactions. Heightened international competition and the constant struggle to maintain or enhance the competitive position of the firm have put a premium on innovation and the introduction of new and improved products, leading to shorter product cycles, with the time lag between development of new products and their commercialization being constantly reduced; these factors also put a premium on access (especially through FDI and strategic alliances) to created assets wherever they are located, with one implication being that the production cycle can begin in any part of a corporate network. New technologies (especially information, communication and transport technologies) and liberalization greatly increase the ability to decompose the value chain of production of goods and (increasingly) services into discrete activities and to locate them wherever they can be undertaken best from the

perspective of the firm, while, at the same time, integrating them through a mix of the most appropriate modalities in the interest of an international production and sales effort. Better intellectual property protection, patent and copyright laws further facilitate this process by making it safer --and hence easier -- to license patents, technology, trademarks and designs. At the same time, more and more countries are now in a position to provide a network of domestic suppliers that can support the operations of the foreign affiliates located there or that can enter into non-equity arrangements directly with parent firms. Indeed, a domestic (or regional) network of suppliers that can effectively complement TNC activities has become an increasingly important location-specific advantage.

32. Thus, what matters in today's world economy from a firm's perspective is not only market access (broadly defined) but also access to factors of production. One of the policy implications of this is that even a broadly defined market-access concept is still only a partial concept because it does not capture all features of the various modalities of international transactions that are important for a firm's competitiveness. "Access to markets and factors of production" rather than "market access" alone captures more adequately the essential characteristics of the internationalization process. To the extent that the organization and management of factors of production takes place under the common governance of TNCs, it defines the scope of international production.

* * *

33. Transnational corporations have a wide range of options for accessing international markets and assets, and they can choose those modalities that fit their overall strategies and core competencies best. A firm that engages in international transactions using more than one modality is likely to expose itself to a wider number of potential business-related risks; but such diversification can also reduce its vulnerability to risks associated with any single modality. As markets and the organization of production increasingly become global in nature, and created assets become more important in the production process, what matters to firms is, more and more, not only access to markets but access to markets <u>and</u> factors of production.

34. This has implications for countries as well. As TNCs help to expand the range and depth of their international transactions, they help countries to participate more fully and in a more sophisticated manner in a deeper international division of labour. This is particularly important for the majority of developing countries that currently participates in the international division of labour primarily through trade and inward foreign direct investment.

Notes

1/ UNCTAD, Division on Transnational Corporations and Investment, FDI database.

2/ Sales of foreign affiliates had declined in 1991 from the 1990 level, in spite of the growing FDI stock. This reflected the recession which manifested itself first in declines of sales.

3/ UNCTAD, Division on Transnational Corporations and Investment, FDI database for France, Germany, Japan, the United Kingdom and the United States.

4/ This figure differs from the estimate for 1993 reported in the UNCTAD, Division on Transnational Corporations and Investment, *World Investment Report 1994: Transnational Corporations, Employment and the Workplace* (United Nations publication, Sales No. E.94.II.A.14) due to data revisions.

5/ For a discussion of the liberalization of FDI policies, *ibid.*, chapter 7.

6/ See also UNCTAD, Division on Transnational Corporations and Investment and World Bank, *Assessing the Sustainability of Regional Foreign Direct Investment Flows* (Geneva and New York, United Nations, forthcoming).

7/ *China Trade Report*, 32 (May 1994), p. 15. That figure is somewhat inflated by "roundtripping" of investments (estimated at about $3 billion in 1993) originating in China and routed back to China via Hong Kong to benefit from fiscal and other incentives awarded to foreign investors and an overvaluation of capital equipment whose value is included in the FDI statistics. See "’Cheating in China ventures", *Financial Times*, 5-6 November 1994.

8/ See UNCTAD, Division on Transnational Corporations and Investment, *World Investment Report 1994*, *op. cit.*.

9/ The decline of worldwide outflows between 1991 and 1992, at 4 per cent, is much lower compared to the 34 per cent decline between 1981 and 1982. However, the recovery of outflows was much more robust in 1983 than in 1993: in 1983, outflows increased by 18 per cent whereas in 1993 outflows rose by 5 per cent.

10/ For example, Unilever sold 12 companies in non-core business; as a result, in 1992, core product groups accounted for 96 per cent of total sales. See Unilever, *Annual Report*, 1993.

11/ Data on cross-border acquisitions reported here include all investments that result in the investor, located in one country, to hold more than 50 per cent of the outstanding voting securities of a business located in another country. Only imperfect comparisons can be made between cross-border acquisitions and FDI flows because the data are not strictly comparable. For further explanations, see UNCTAD, Division on Transnational Corporations and Investment, *World Investment Report 1994*, *op. cit.*, chap. I.

12/ See John H. Dunning and Matija Rojec, "Foreign privatization in Central and Eastern Europe", Central and Eastern European Privatization Network Technical Paper Series, No. 2, Ljubljana, Slovenia.

13/ United Nations, Transnational Corporations and Management Division, *Transnational Corporations from Developing Countries: Impact on Their Home Countries* (United Nations publication, Sales No. E.93.II.A.8), table II.1, pp. 24-25.

14/ Such well-known outward investor economies as India, Indonesia, Hong Kong, Malaysia, Saudi Arabia and the United Arab Emirates do not report FDI outflows and, therefore, are not included in the investment data reported here. In the cases of Hong Kong and Singapore, a large part of these investments is not by indigenous firms.

15/ Although outward FDI data are not reported by Hong Kong, estimates based on host-country information indicate that Hong Kong is probably the largest foreign investor among developing countries, accounting for more than 20 per cent of the outward stock from developing countries (excluding tax-haven countries) in 1990. See *Transnational Corporations from Developing Countries: Impact on Their Home Countries*, *op. cit.*, table II.1 and II.3, pp. 24-25 and 27-29.

16/ John Burton, "South Korea plans to relax limits on foreign exchange", *Financial Times*, 6 December 1994; see also International Monetary Fund, *Exchange Arrangements and Exchange Restrictions, Annual Report 1994* (Washington, D.C., International Monetary Fund, 1994).

17/ JETRO, *JETRO Hakusho: Toshi-hen 1994* (Tokyo, 1994), pp. 10-15.

18/ Viet Nam State Committee for Co-operation and Investment, unpublished data.

19/ *Asiaweek*, 25 May 1994, p. 44.

20/ Examples include the acquisition of a privatized iron ore company, Hierro Peru (renamed Shougang Hierro Peru after the acquisition), for $120 million in 1992 by Metropolitan Steel Inc. and an oil exploration contract with Petro Peru in 1993 by China State Development Peru Inc., the first exploration investment in that region by China, with investments of $43 million over the first five years. The sales price of Hierro Peru will eventually reach $312 million as China has a debt of $54 million and has the obligation to invest $150 million in the three years following the acquisition. This acquisition is regarded as a successful privatization case as Hierro Peru’s production more than doubled in 1993. See JETRO, *JETRO Hakusho: Toshi-hen 1994*, *op. cit.*, pp. 150-151.

21/ "Samsung to invest $723 million in new UK manufacturing plant", *Financial Times*, 18 October 1994; "The children with the magic powder", *The Economist*, 21 May 1994.

22/ For example, Rover (an affiliate of BMW, Germany) and Kia (Republic of Korea) have agreed to develop together a new range of automobile engines. See, Kevin Done, "Korean group in engines deal with Rover", *Financial Times*, 17 October 1994.

23/ Angus Foster, "Latin American rediscover their neighbours’ markets", *Financial Times*, 1994.

24/ There were 53 strategic alliances by mid-1993. Examples include a joint venture of Malteria Pampa between Londrina (Argentina) and Brahama (Brazil) and a complementary exchange arrangement of parts and components in agricultural machinery between Deuts Argentina and Angrale (Brazil). JETRO, *JETRO Hakusho: Toshi-hen 1994*, *op. cit.*, p. 161.

25/ JETRO, *JETRO Hakusho: Toshi-hen 1994*, *op. cit.*.

26/ *Ibid*.

27/ "Latin American finance" (survey), *Financial Times*, 11 April 1994.

28/ It has been reported that more than 20,000 companies have moved productive assets valued at an estimated $20 billion into China. See "The tigers face a challenge", *Financial Times*, 17 October 1994.

29/ John Cantwell and Paz Estrella Tolentino, "Technological accumulation and third world multinationals". Discussion Papers in International Investment and Business, University of Reading, No. 139 (1990), mimeo..

30/ John H. Dunning, "The investment development path revisited: some emerging issues". Draft paper prepared for the workshop on "Revisiting the investment development path", Rotterdam, the Netherlands, 15-16 December 1994.

31/ In recent years, the Republic of Korea and Taiwan Province of China have become net outward investors. In 1993, FDI outflows exceeded inflows also for Brazil, Mauritius and Venezuela.

32/ John Hagedoorn and M. Schakenraad, "The role of interfirm cooperation agreements in the globalisation of economy and technology" (Brussels, Commission of the European Communities, November 1991), mimeo.; and John Hagedoorn and Geert Duysters, "Strategic groups and networks of strategic partnering in international high-tech industries", paper presented at the annual meeting of the Academy of International Business, 3-6 November 1994, mimeo..