Indo-German Investments & Cooperation

Global FDI flows are projected to increase marginally, by about 5% in 2018, to USD 1.5 trillion

Global Foreign Direct Investment (FDI) flows fell sharply by 23%, in 2017, to USD 1.43 trillion from USD 1.87 trillion in 2016. The decline is in stark contrast to other macroeconomic variables, which saw substantial improvement in 2017.

"Downward pressure on FDI and the slowdown in global value chains, are a major concern for policymakers worldwide, and especially in developing countries," said Mukhisa Kituyi, Secretary-General, United Nations Conference on Trade and Development (UNCTAD). "Investment in productive assets will be needed to achieve sustainable development in the poorest countries," he further asserted.

The global fall was caused in part by a 22% decrease in the value of cross-border Mergers and Acquisitions (M&As). But even discounting the large one-off deals and corporate reconfigurations that inflated FDI in 2016, the 2017 decline remained significant. The value of announced greenfield investment – an indicator of future trends – also fell by 14%, to USD 720 billion.

Prospects for 2018 are therefore muted. Global flows are forecast to increase marginally, but remain well below the average over the past 10 years. An escalation and broadening of trade tensions could negatively affect investment in Global Value Chains (GVCs). Tax reforms in the USA are likely to significantly affect global investment patterns.

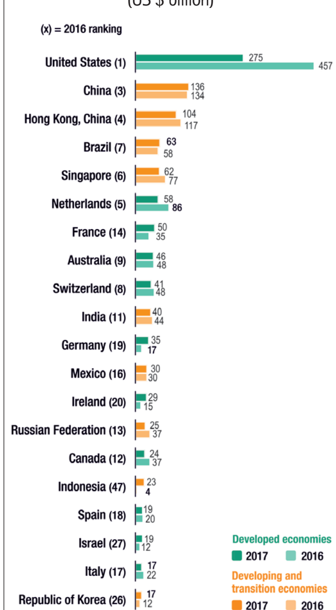
UNCTAD observed that the negative FDI trend is caused in large part by a decrease in rates of return. The global average return on foreign investment is now at 6.7%, down from 8.1% in 2012. Return on investment is in decline across all regions, with the sharpest drops in Africa and in Latin America and the Caribbean. The lower returns on foreign assets also affect longer-term FDI prospects.

As a result of the investment downturn, the rate of expansion of international production is slowing down. The modalities of international production and of cross-border exchanges of factors of production, are shifting from tangible to intangible forms. Sales of foreign affiliates continue to grow (up 6% in 2017) but productive assets and employees are increasing at a slower rate. This could negatively affect the prospects for developing countries to attract investment in productive capacity.

Growth of GVCs has also stagnated. GVC trade peaked in 2010–2012, after two decades of continuous increases. UNCTAD's data shows foreign value added in trade (the key GVC indicator) down 1 percentage point to 30% of trade, in 2017. The GVC slowdown shows a clear correlation with the FDI trend and confirms the impact of the FDI trend on global trade patterns.

FDI remains the largest external source of finance for developing economies. It makes up 39% of total incoming finance in developing economies as a group. It now accounts for less than a quarter in the Least Developed Countries (LDCs), with a declining trend since 2012. Over the past 10 years, at least 101 economies across the developed and developing world (accounting for more than 90% of global GDP), have adopted formal industrial development strategies. The last five years have seen an acceleration in the formulation of new strategies.

FDI inflows: top 20 host economies, 2016 and 2017
(US $ billion)



Source UNCTAD, FDI/MNE database (www.unctad.org/fdistatistics).

UNCTAD's survey shows that modern industrial policies are increasingly diverse and complex, addressing new imperatives, such as global value chain integration and upgrading, the knowledge economy, build-up of sectors linked to the Sustainable Development Goals and competitive positioning for the new industrial revolution. "The new industrial revolution is already affecting cross-border investment patterns. Investment policies must adapt as part of new industrial development strategies," said UNCTAD Secretary-General, Mukhisa Kituyi.

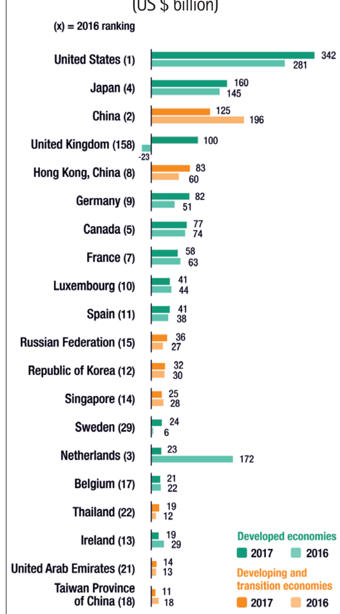
Outlook for 2018

The fragile growth of FDI flows expected for 2018 reflects an upswing in the global economy, strong aggregate demand, an acceleration in world trade and strong MNE (Multinational Enterprise) profits (total profits, which may not reflect the profitability of overseas operations). The improving macroeconomic outlook has a direct positive effect on the capacity of MNEs to invest; business survey data indicates optimism about short-term FDI prospects. Also, the expected increase in FDI inflows in 2018, is consistent with project data (M&As and announced greenfield projects) for the first quarter.

However, the expectation of an increase in global FDI is tempered by a series of risk factors. Geopolitical risks, growing trade tensions and concerns about a shift toward protectionist policies, could have a negative impact on FDI in 2018. In addition, tax reforms in the USA are likely to significantly affect investment decisions by USA MNEs in 2018, with consequences for global investment patterns. Moreover, longer-term forecasts for macroeconomic variables contain important downsides, including the prospect of interest rate rises in developed economies, with potentially serious implications for emerging market currencies and economic stability (IMF, 2018).

Projections indicate that FDI flows could increase in developed and transition economies, while remaining flat in developing economies as a group.

FDI outflows: top 20 home economies, 2016 and 2017
(US $ billion)



Source UNCTAD, FDI/MNE database (www.unctad.org/fdistatistics).

Sources

- http://unctad.org/en/pages/PressRelease.aspx?OriginalVersionID=458
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- UNCTAD World Investment Report 2018