Global capital flows - FDI trends

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From the ‘simple’ era of trade...

- B of P analysis used to be dominated by trade flows – capital flows small

- The exchange rate’s role was to maintain trade equilibrium (competitiveness)

- FDI a form of aid to poor countries

- Other flows needed to complete B of P

- Models simple - Mundell-Fleming linked ‘capital flow’ to interest rate differentials
## Global flows: trade and capital

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<tbody>
<tr>
<td>Goods trade (exports)</td>
<td></td>
<td>0.4</td>
<td>1.9</td>
<td>3.4</td>
<td>6.3</td>
<td>12+</td>
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<tr>
<td>Total</td>
<td></td>
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<td>Capital inflows</td>
<td>neglig.</td>
<td>0.1</td>
<td>0.5</td>
<td>4</td>
<td>10+</td>
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(sources: IMF, UNCTAD, OEF)
… to an era of capital flows

• Total global capital inflows rise from under $1trn to over $4trn pa from 1990 to 2000: big boost from boom in bilateral flows between OECD countries – eg US

• Developing country net inflows: up from under $25bn in late 1980s to $150-250bn pa (IMF WEO) – China $50-60bn pa

• More interest in type of flows and volatility: attempts to link this with risk profiles and exchange rates
Japanese YEN: US$ rate v 'equilibrium' rate?

Source: OEF

Trade based "equilibrium" estimate (cyclically adjusted)
World capital account inflows by type

Source: OEF
FDI accumulation led exports

China total goods export versus cumulative FDI

Source: National Statistics
FDI: explanatory factors

- Institutional issues such as market access, tariff and tax regimes, the rise of multinationals all have an influence

- Economies of scale and reductions in production costs – eg car plants, textiles

- Brands, delivery and quality assurance etc

- Organisational skills – centralise functions and gain from economies of scale here – eg R&D

- M&A affected by asset prices versus cost of ‘greenfield’ development - large part of FDI
## FDI largely M&A driven

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<th>1998</th>
<th>2000</th>
<th>2002</th>
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<tr>
<td>Total FDI</td>
<td>700</td>
<td>1400</td>
<td>650</td>
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<tr>
<td>Cross border M&amp;A</td>
<td>330</td>
<td>866</td>
<td>214</td>
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Total M&A deals over $1bn, source UNCTAD
Cross border deals 25-30% of total M&A deals