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UNITED NATIONS CONFERENCE ON TRADE AND DEVELOPMENT

BOPCOM 07/05

World Investment Report 2007

Transnational Corporations, Extractive Industries and Development

20th Meeting for the IMF Committee on Balance of Payments Statistics, October 29, 2007

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UNCTAD
16 October 2007

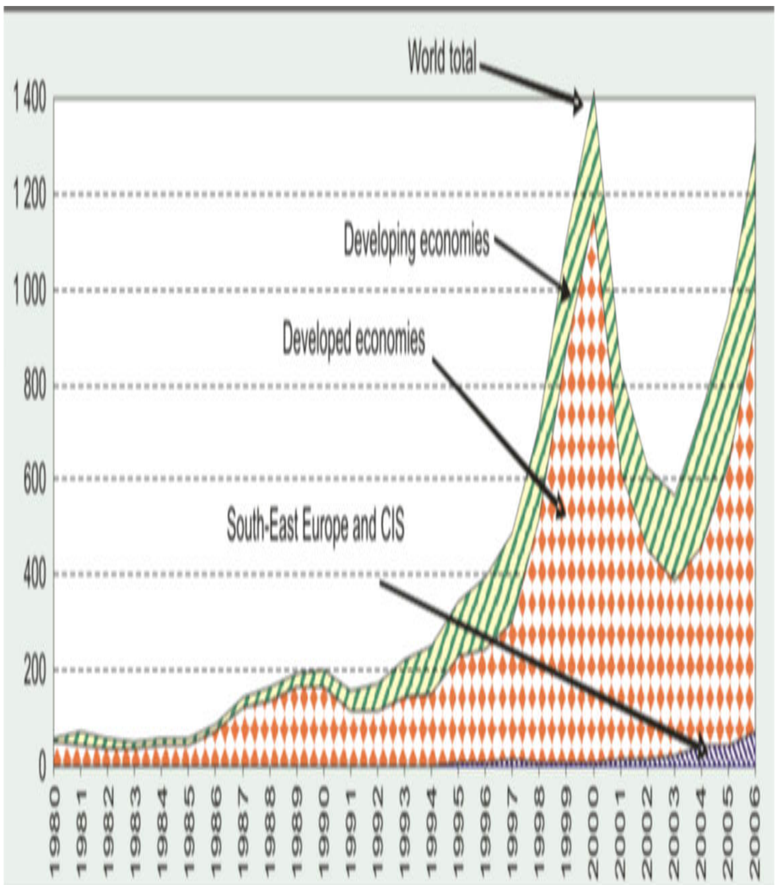
EMBARGO 16 October 2007
17:00 hrs GMT

UNCTAD

Part I
Widespread growth in FDI

Global FDI flows approach their 2000 peak level

FDI inflows, global and by group of economies, 1980-2006
($ billion)



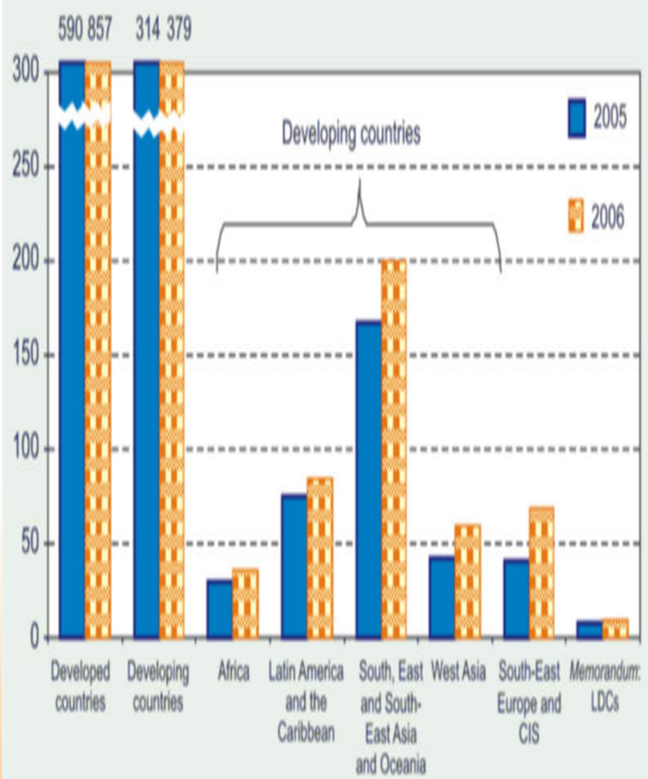
- **Global FDI flows grew for the third consecutive year to $1,306 billion.**
- **Inflows to developed country rose by 45% ($857 billion).**
- **Developing countries recorded a 21% growth rate ($379 billion).**
- **Inflows to South-East Europe and CIS countries jumped by 68%.**

Widespread growth of FDI inflows in 2006 due to:

(strong economic growth; increased corporate profits; increasing commodity prices; rise of cross-border M&As; and the weakening of dollar)

FDI flows by region, 2005 and 2006

FDI inflows ($ billion)



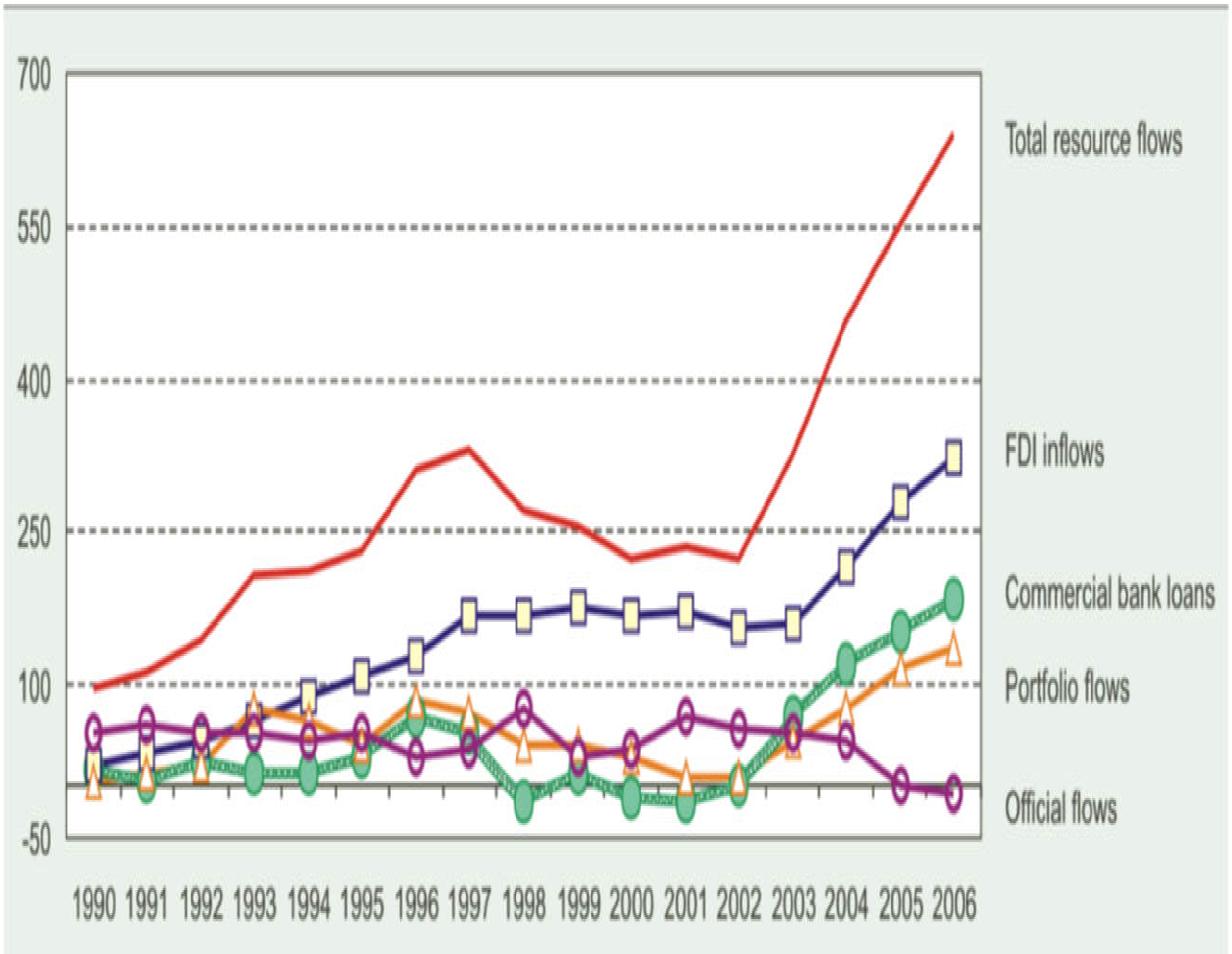
In developing regions:

- FDI inflows in Africa: a new record level (due to buoyant global demand for commodities).
- Inward FDI to Latin America and the Caribbean: unchanged if offshore financial centers are excluded.
- The FDI inflows to South, East and South-East Asia: maintained upward trend.
- Turkey and oil-rich states accounted for most of the FDI increase to West Asia.
- Flows to Asia accounted for most of the FDI increase in developing countries.

In developing countries FDI continues to be the most important source of external financing

Total net resource flows to developing countries, by type of flow, 1990-2006

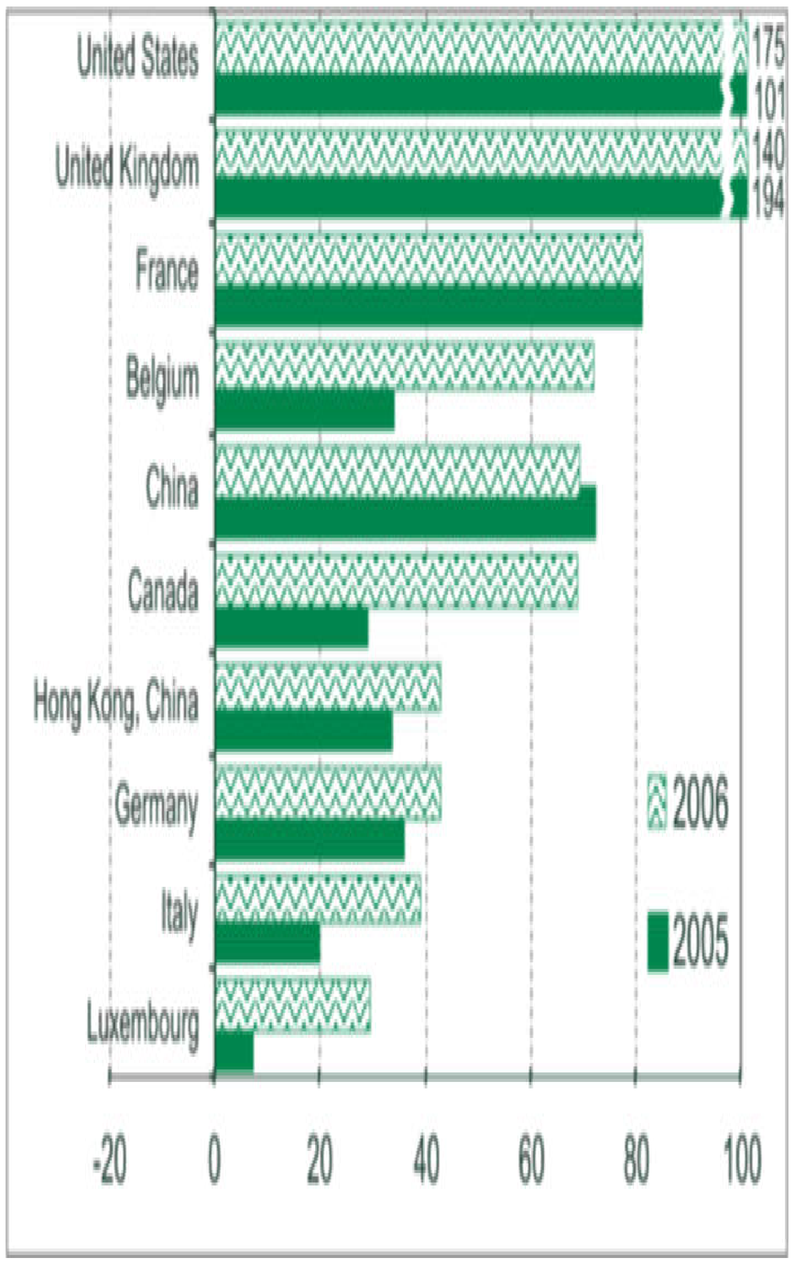
($ billion)



Top 10 recipients of FDI inflows

($ billion)

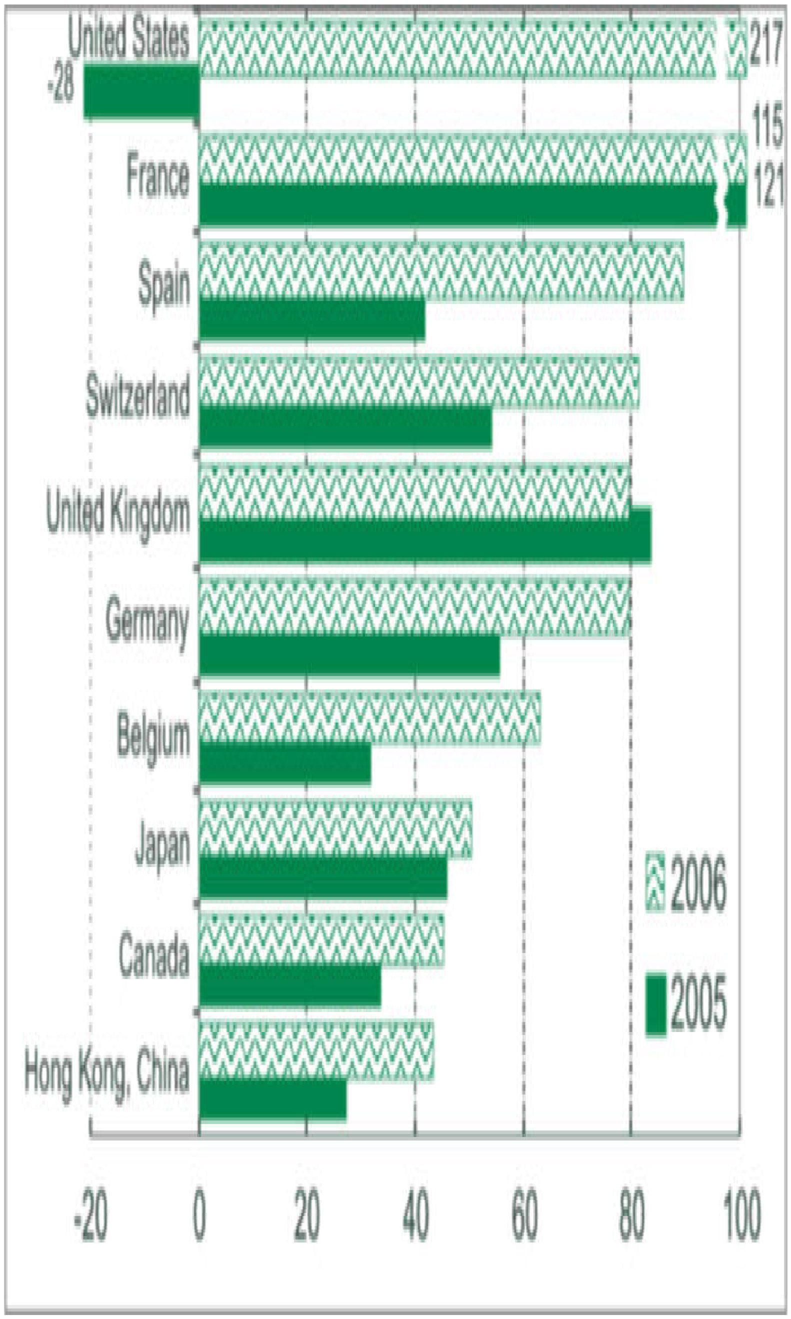
- United States regained first rank (M&As).
- Belgium, for the first time, the fourth world largest FDI recipient.
- China lowered its ranking compared to 2005.
- FDI inflows to Canada more than doubles (mainly in extractive industries).



Largest 10 sources of FDI outflows

- United States became the largest investor.
- Spain: record levels for the first time.
- Honk Kong (China) ranked within top ten investors.
- Brazil ranked 12th ($28 bil), Russian Federation 17th ($18 bil), China 18th ($16 bil) in the world.

($ billion)



Indices of inward FDI performance and potential

Inward FDI Performance Index ranking		
Economy	2005	2006
Luxembourg	5	1
Hong Kong China	4	2
Suriname	3	3
Singapore	7	4
Malta	11	5
Iceland	13	6
Bulgaria	8	7
Jordan	20	8
Estonia	6	9
Belgium	12	10

Inward FDI Potential Index ranking		
Economy	2005	2006
United States	1	..
Singapore	2	..
United Kingdom	3	..
Canada	4	..
Luxembourg	5	..
Germany	6	..
Norway	7	..
Sweden	8	..
Qatar	9	..
Iceland	10	..

- Bahrain and Tajikistan entered the top 20 rankings for inward FDI performance
- As to the potential index, there are no notable changes compare to last year indices
- Some country improved their FDI position in performance, potential or both (e.g. Botswana, Croatia, Lithuania)

Indices of outward FDI performance

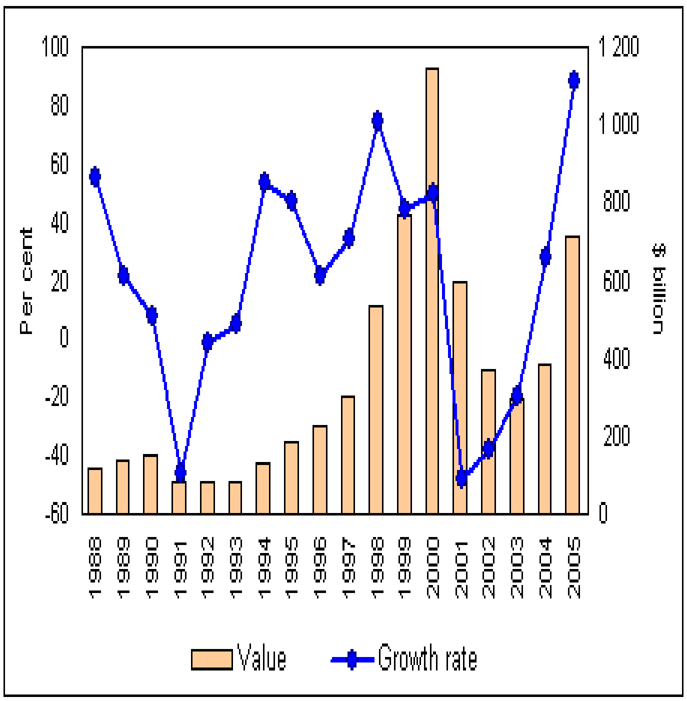
Outward FDI Performance Index ranking

Economy	2005	2006
Iceland	1	1
Hong Kong, China	3	2
Luxembourg	2	3
Switzerland	8	4
Belgium	7	5
Netherlands	6	6
Panama	4	7
Ireland	10	8
Azerbaijan	5	9
Bahrain	9	10

- Hong Kong (China) remained one of the top outward FDI perfomers.
- Israel and Estonia entered the top 20 for outward FDI performance

Main reasons for continued rise in cross-border M&As

Global cross-border M&As, 1988-2006



- **rising corporate profits**
- **higher stock market valuations (in developed countries and in emerging markets)**
- **favorable financing conditions**
- **increased participation of private equity funds/firms**

Main features of cross-border M&As

- Cash and debt financing rather than exchange of shares
- Doubled in value in North America due to deals in mining
- In Europe
  - the United Kingdom - the main target
  - Spanish companies - active acquirers
- Increasingly acquisitions by developing countries and economies in transition TNCs
- Emerging economies, awash with petrodollar (e.g. United Arab Emirates) and with foreign exchange (e.g. China) are active in cash-based acquisitions
- Growing importance of private equity funds

Growing importance of private equity funds in cross-border M&As

Cross border M&As by private equity funds

	Number of deals		Value	
Year	Number	Share in total (%)	$ billion	Share in total (%)
1996	390	8.5	32.4	14.3
1997	415	8.3	37.0	12.1
1998	393	7.0	46.9	8.8
1999	567	8.1	52.7	6.9
2000	636	8.1	58.1	5.1
2001	545	9.0	71.4	12.0
2002	478	10.6	43.8	11.8
2003	649	14.2	52.5	17.7
2004	773	15.1	83.7	22.0
2005	889	14.5	134.6	18.8
2006	889	12.4	158.1	18.0

- **Benefiting from ample liquidity**
- **Some equity funds are listed in the stock markets**
- **Doubts of their sustainability in FDI activity**
  - **competition is becoming stronger (lower returns)**
  - **financial instability (too much borrowing from banks; rising interest rates)**
  - **tax treatments being examined**

Current FDI surge resulted in further growth in international production

- Nearly 20% rise in FDI stock and assets of foreign affiliates
- Foreign affiliates accounted for 10% of world GDP (2006)
- Employment of foreign affiliates account for 3% of global employment

Selected indicators of FDI and international production, 2005-2006

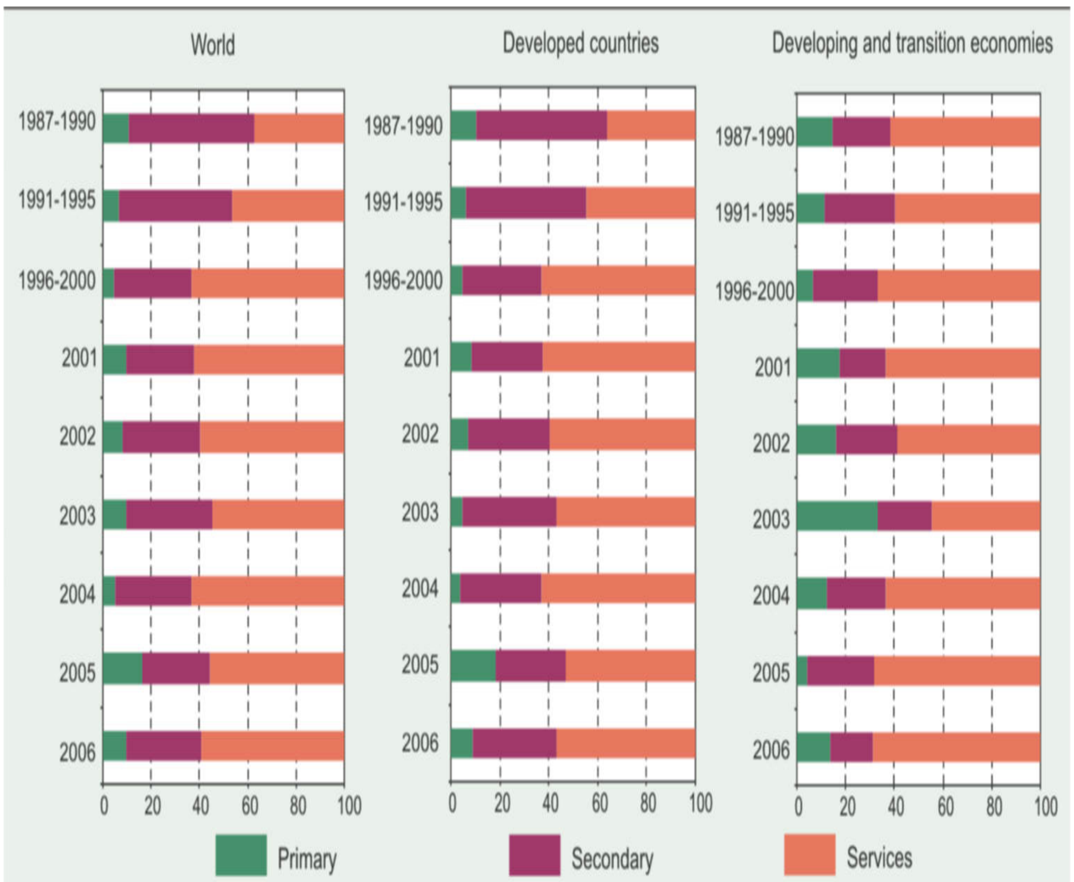
Item	Value at current prices (Billions of dollars)		Annual growth rate (Per cent)	
	2005	2006	2005	2006
Inward FDI stock	10 048	11 999	5.0	19.4
Outward FDI stock	10 579	12 474	4.2	17.9
Sales of foreign affiliates	21 394	25 177	3.0	17.7
Gross product of foreign affiliates	4 184	4 862	6.3	16.2
Total assets of foreign affiliates	42 637	51 187	9.3	20.1
Exports of foreign affiliates	4 197	4 707	10.7	12.2
Employment of foreign affiliates (in thousands)	63 770	72 627	16.3	13.9

The five largest South-South cross-border M&As deals

Value ($ billion)	Target company	Target economy	Acquiring company	Acquiring economy
4.4	Hutchison Port Holdings Ltd	Hong Kong, China	PSA Corp Ltd	Singapore
3.5	OAO Udmurtneft	Russian Federation	Sinopec Corp Qingdao Br,China	China
2.7	NNPC-OML 130	Nigeria	CNOOC Ltd	China
2.6	Pakistan Telecom Co Ltd	Pakistan	ETISALAT	United Arab Emirates
2.3	Tunisie-Telecoms	Tunisia	Investor Group	United Arab Emirates

Changing pattern of FDI by sector

Sectoral distribution of cross-border M&As, by industry of seller, 1987-2006 (%)



- **Shift towards services over the past quarter century**
- **Rebound of FDI in extractive industries**
- **Share of manufacturing has declined**

Changing pattern of FDI by country

- Geographical proximity has become important (e.g. in the top 50 pairs of countries with the strongest links in terms of bilateral inward FDI stock, in 2005 22 were from Europe compared to 17 in 1995)

- Geographical pattern of FDI towards greater South-South FDI (e.g. the second largest bilateral FDI stock was held in China by Hong Kong investors in 2005)

Top 20 bilateral FDI relationships, 1985, 2005

(FDI stock, $ billion)

Rank	Home economy	Host economy	1985	1995	2005
1	United Kingdom	United States	44	116	282
2	Hong Kong, China	China	..	120	242
3	United States	United Kingdom	48	85	234
4	Japan	United States	19	105	190
5	Germany	United States	15	46	184
6	United States	Canada	49	83	177
7	Netherlands	United States	37	65	171
8	China	Hong Kong, China	0.3	28	164
9	British Virgin Islands	Hong Kong, China	..	70	164
10	Canada	United States	17	46	144
11	France	United States	7	36	143
12	Switzerland	United States	11	27	122
13	Luxembourg	United States	0.3	6	117
14	Netherlands	Germany	5	34	111
15	Netherlands	France	10	31	102
16	United Kingdom	France	9	26	96
17	Netherlands	United Kingdom	17	27	93
18	Germany	United Kingdom	3	14	86
19	United States	Netherlands	8	25	84
20	France	United Kingdom	5	13	80

FDI relationship between host and home countries: how to measure?: an FDI intensity to compare the actual value and the expected value

FDI intensity ratio (R) = $FDI_{ij} / ExpFDI_{ij}$

FDI_{ij} = Actual amount of FDI stock from country i to j.

$ExpFDI_{ij}$ = Expected value of FDI stock from country i to country j

$$= \frac{FDI_{wj}}{FDI_{ww}} * \frac{FDI_{iw}}{FDI_{ww}} * FDI_{ww}$$

where,

FDI_{wj}=Total inward stock in the j country;

FDI_{iw}=Total outward FDI stock of i country in the world; and

FDI_{ww}=Worldwide inward or outward FDI stock.

If the intensity ratio is greater than 1, the FDI relationship is stronger than would be expected based on the relative importance of the two economies as home and host; if it is less than 1 it is weaker than expected.

FDI intensity index (results)

- The FDI intensity of United States as home:
  - with its traditional partners such as Japan, Canada, and the United Kingdom is higher than one;
  - while there is a growing importance of Asian host economy partners, the intensity with Latin American countries has fallen more than expected.

- Japan’s FDI intensity with respect to Asian developing countries is more stronger than other developing countries and has increased over the past decade.

- Bilateral FDI relationships between European countries have increased from 1995 to 2005.

- Home developing countries have established stronger than expected FDI intensity with other developing countries (e.g. China - Hong Kong (China); Malaysia - Cambodia; the Republic of Korea - China)

The world largest non-financial TNCs

- Top 100 account for 10%, 17% and 13% of estimated foreign assets, sales and employment of all TNCs
- Foreign sales and employment increase faster than domestic ones

($ billion and number of employees)

Ranking by:			Assets		Sales		Employment	
Foreign assets	Corporation	Home economy	Foreign	Total	Foreign	Total	Foreign	Total
1	General Electric	United States	412 692	673 342	59 815	149 702	155 000	316 000
2	Vodafone Group PLC	United Kingdom	196 396	220 499	39 497	52 428	51 052	61 672
3	General Motors	United States	175 254	476 078	65 288	192 604	194 000	335 000
4	British Petroleum Company PLC	United Kingdom	161 174	206 914	200 293	253 621	78 100	96 200
5	Royal Dutch/Shell Group	United Kingdom, Netherlands	151 324	219 516	184 047	306 731	92 000	109 000
6	ExxonMobil	United States	143 860	208 335	248 402	358 955	52 920	84 000
7	Toyota Motor Corporation	Japan	131 676	244 391	117 721	186 177	107 763	285 977
8	Ford Motor	United States	119 131	269 476	80 325	177 089	160 000	300 000
9	Total	France	108 098	125 717	132 960	178 300	64 126	112 877
10	Eléctricité de France	France	91 478	202 431	26 060	63 578	17 801	161 560

The largest non-financial TNCs from developing economies

- **Five largest TNCs account for one third of all foreign assets of the top 100 TNCs of developing countries**
- **Hong Kong (China) and Taiwan Province of China dominate as home of top 100 TNCs of developing countries**
- **The most important industry is electrical/electronic equipment, followed by petroleum**

($ billion and number of employees)

Ranking by:			Assets		Sales		Employment	
Foreign assets	Corporation	Home economy	Foreign	Total	Foreign	Total	Foreign	Total
1	Hutchison Whampoa Limited	Hong Kong, China	61 607	77 018	24 721	31 101	165 590	200 000
2	Petronas - Petroliam Nasional Bhd	Malaysia	26 350	73 203	12 995	44 353	4 016	33 944
3	Cemex S.A.	Mexico	21 793	26 439	12 088	14 961	39 630	52 674
4	Singtel Ltd.	Singapore	18 000	20 748	5 556	7 906	8 832	19 500
5	Samsung Electronics Co., Ltd.	Republic of Korea	17 481	74 834	62 100	79 017	27 664	80 549
6	LG Corp.	Republic of Korea	16 609	50 611	38 419	60 805	40 689	79 000
7	Jardine Matheson Holdings Ltd	Hong Kong, China	15 770	18 440	8 420	11 929	57 895	110 000
8	CITIC Group	China	14 891	99 059	2 109	8 042	15 915	93 323
9	Hyundai Motor Company	Republic of Korea	13 015	64 688	18 676	58 156	5 038	54 115
10	Formosa Plastic Group	Taiwan Province of China	12 807	57 910	9 708	37 664	61 626	82 380

Most policy changes in 2006 continue to favour FDI

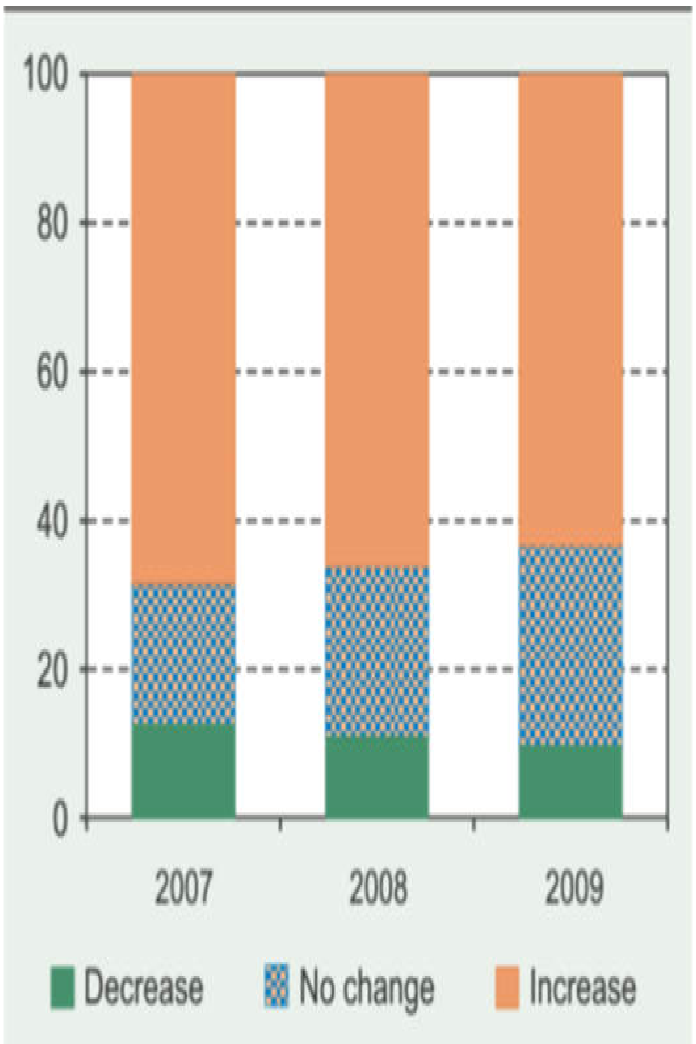
Item	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
Number of countries that introduced changes	43	56	49	63	66	76	60	65	70	71	72	82	103	93	93
Number of regulatory changes	77	100	110	112	114	150	145	139	150	207	246	242	270	205	184
More favorable to FDI	77	99	108	106	98	134	136	130	147	193	234	218	234	164	147
Less favorable to FDI	0	1	2	6	16	16	9	9	3	14	12	24	36	41	37

- 184 policy changes were introduced in 93 countries, 80% of which were favorable to FDI
- 59% of regulatory changes were adopted in developing countries
- Introduction of new promotional incentives (e.g. India, Brazil)
- Opening up of industries to FDI (e.g. services sectors in Italy; telecommunication in Botswana, Cape Verde and Kenya; banking industry in Belarus and Mali)
- Some restrictions emerging:
    - in extractive industries (e.g. Bolivia, Peru and Venezuela)
    - nationalization (e.g. Venezuela) or restrictions (e.g. Russian Federation) in “strategic sectors”

Prospects for FDI flows remain positive

Prospects for global FDI flows in 2007-2009:

UNCTAD survey responses (%)



- **However several risk could hinder FDI flows**
  - global current account imbalances
  - high and volatile oil prices
  - real estate market in the United States

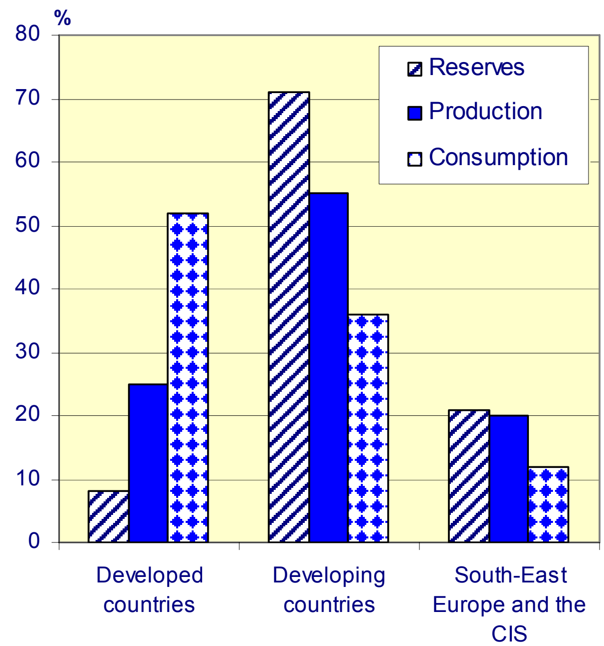
Part 2

Transnational Corporations, Extractive Industries and Development

Why Extractive Industries Matter

- Minerals are essential to all economies
- Mineral resources are unevenly distributed
- Many low-income countries depend on mineral resources
- Current boom: a window of opportunity
- TNCs key players for both host and home countries

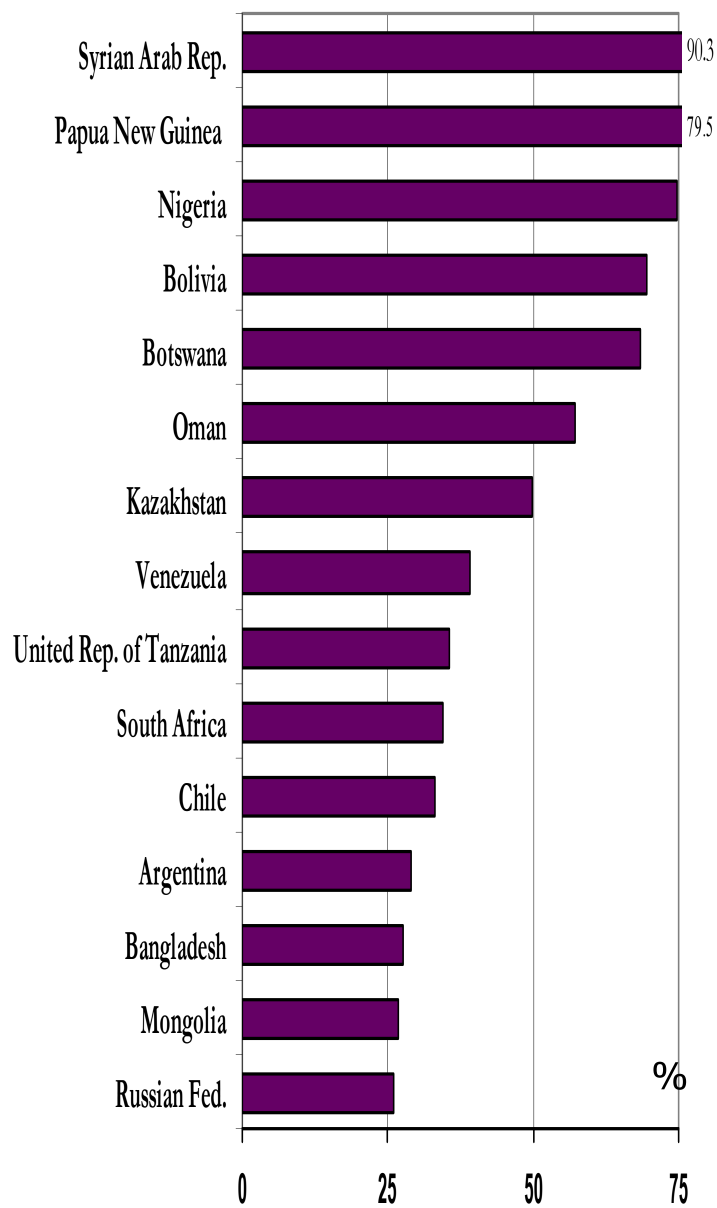
Oil and gas reserves, consumption and production, 2005



Some Countries Receive Much FDI into the Extractive Industries

- **Globally: share of EIs only 9% of inward FDI…**
- **…but share is high in some countries**

Share of extractive industries in inward FDI stock, 2005 or latest year, %

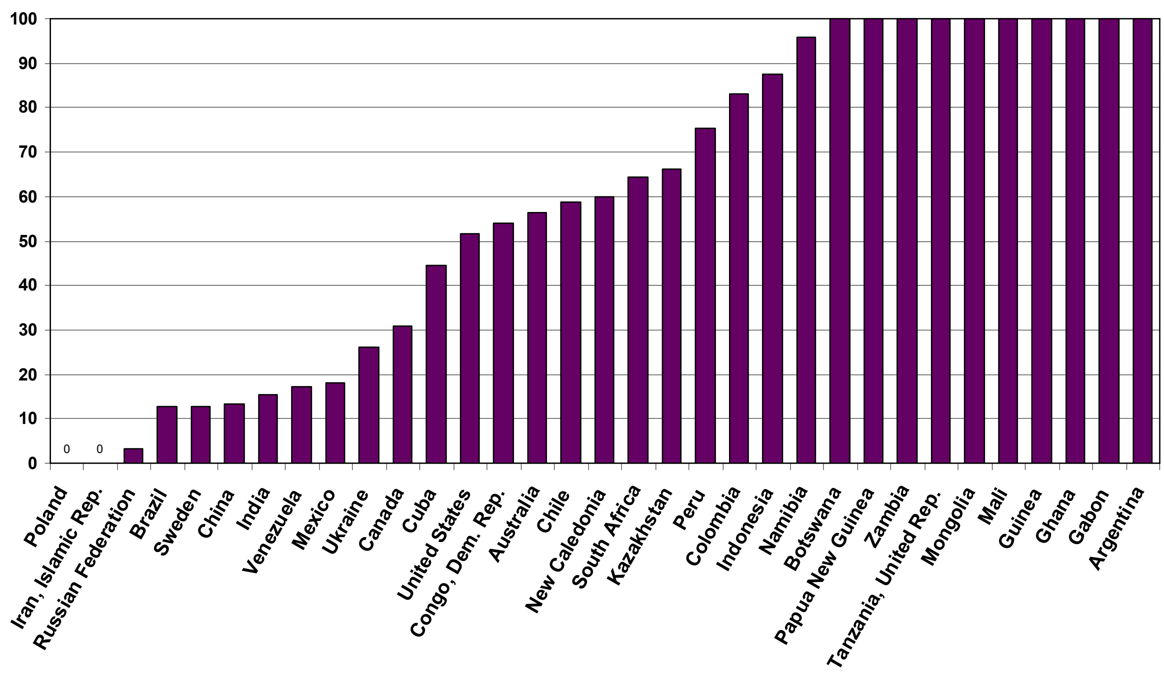


TNCs Involvement Different in Mining and Oil/Gas

Metal mining	**Oil and gas**
• Developed-country TNCs dominate world production • Top 3 (2005): BHP Billiton, Rio Tinto, CVRD • Concession – main form of TNC involvement	• SOEs from developing and transition economies dominate world production • Top 3 (2005): Saudi Aramco, Gazprom, NIOC • Production-sharing agreements – most common form of TNC involvement

Foreign Affiliates Key Players in Mining

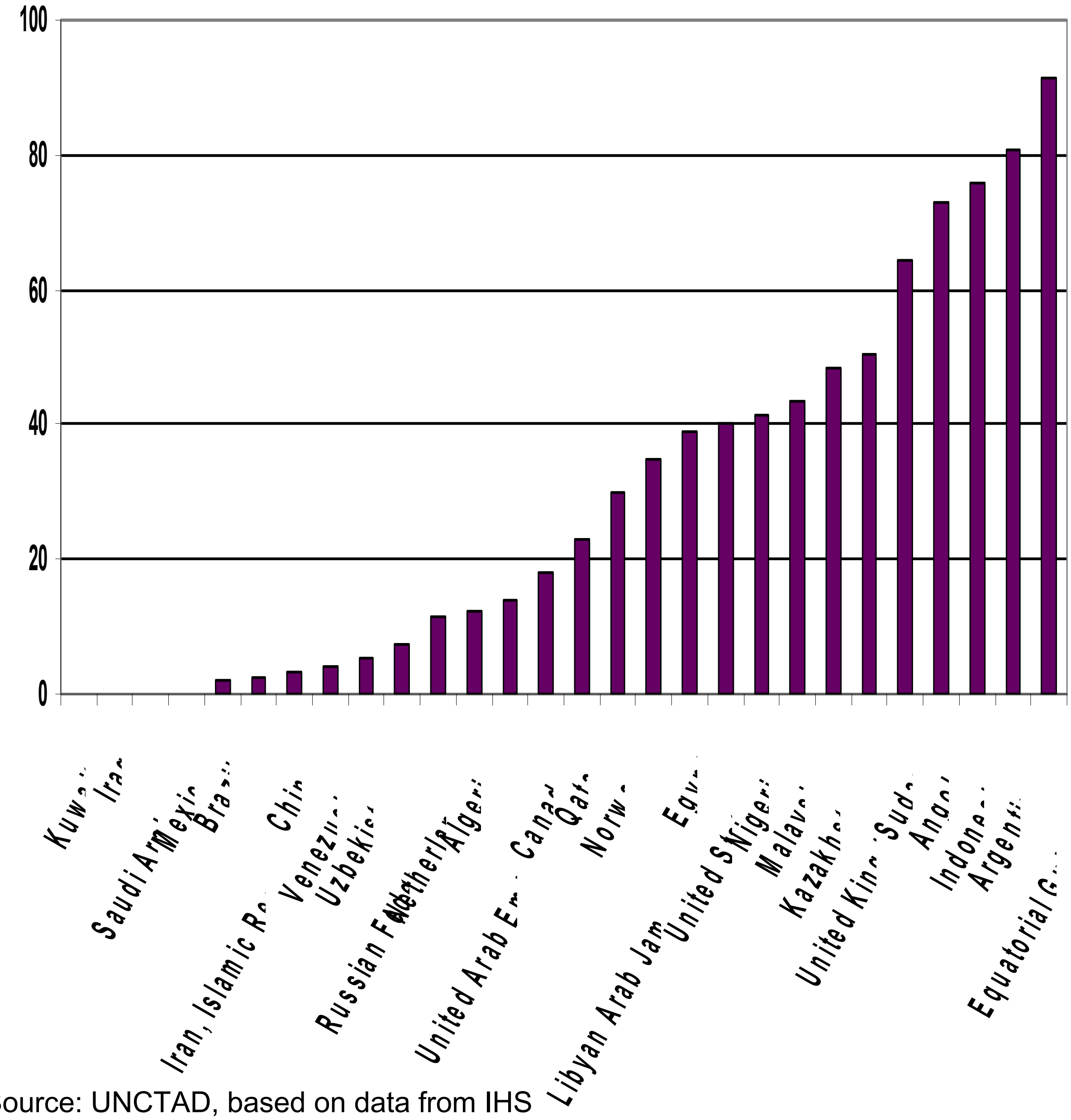
Foreign affiliates' share of non-fuel mining production, 2006, %



Source: UNCTAD, based on data from Raw Materials Group

Foreign Companies Less Prominent in Oil & Gas Production

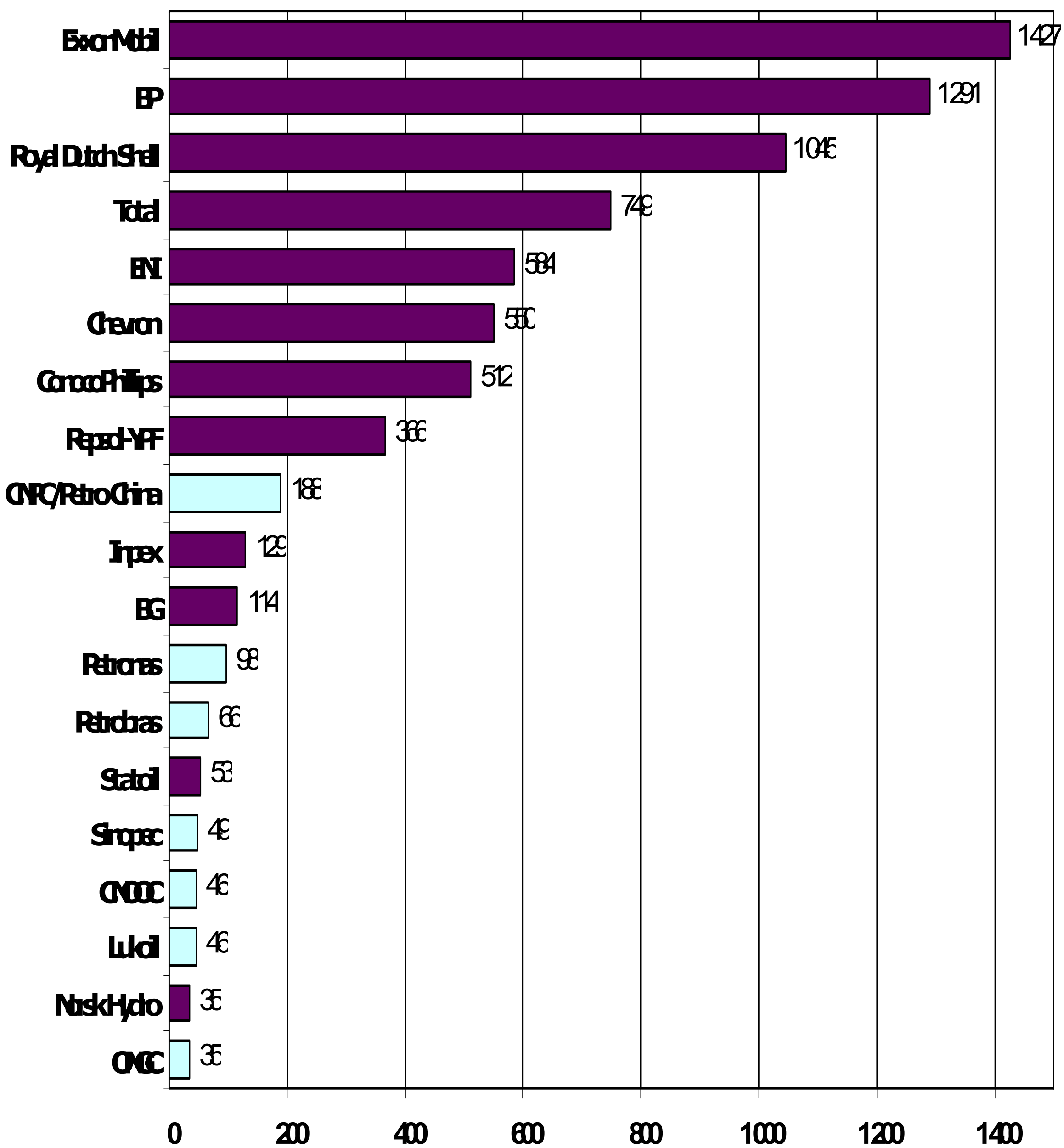
Share of foreign companies in oil and gas production, selected countries, 2006, %



Source: UNCTAD, based on data from IHS

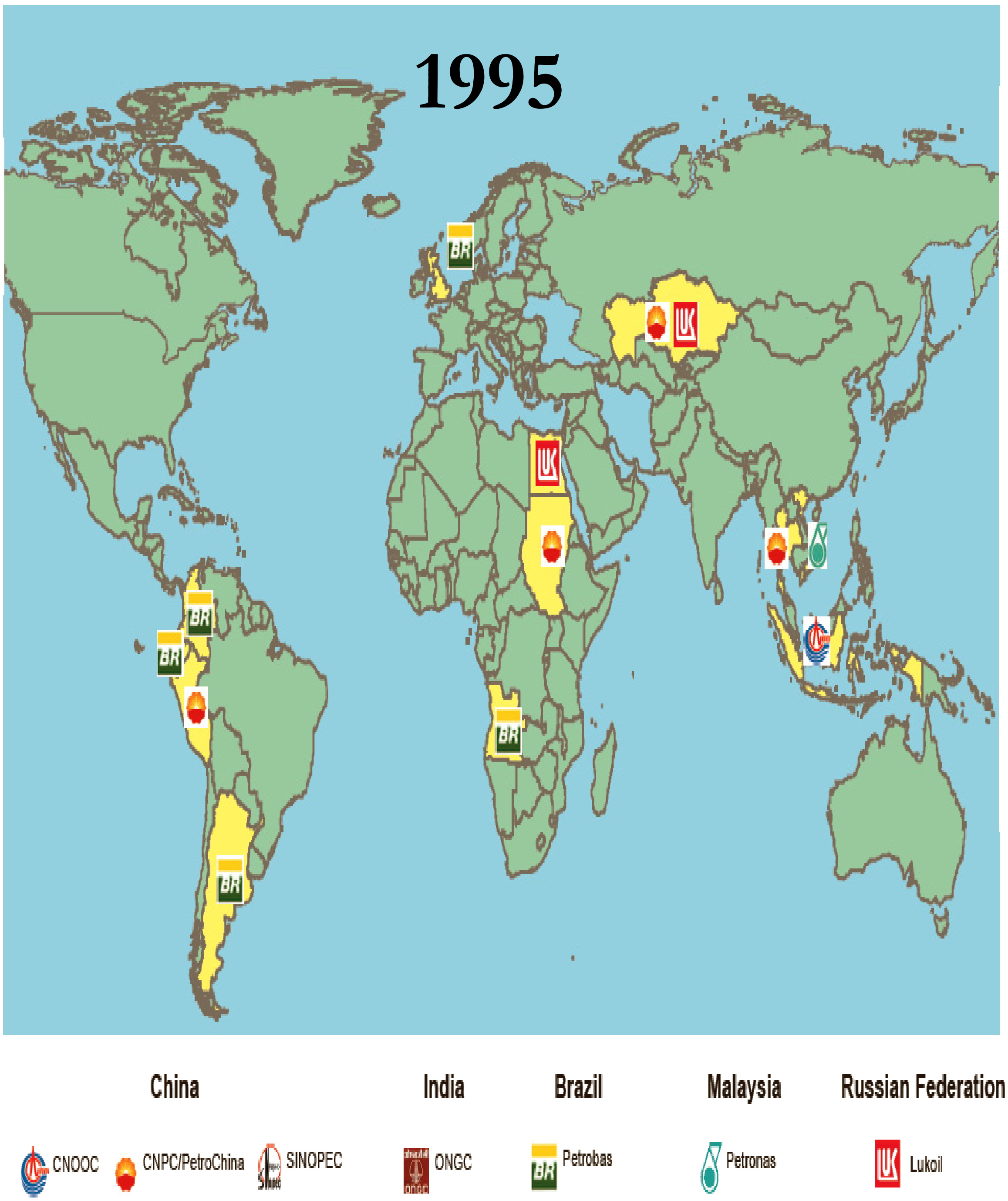
SOE TNCs in Oil & Gas are Expanding Abroad But From Low Level

Oil and gas production of selected TNCs outside their home country, 2005, million barrels of oil equivalent



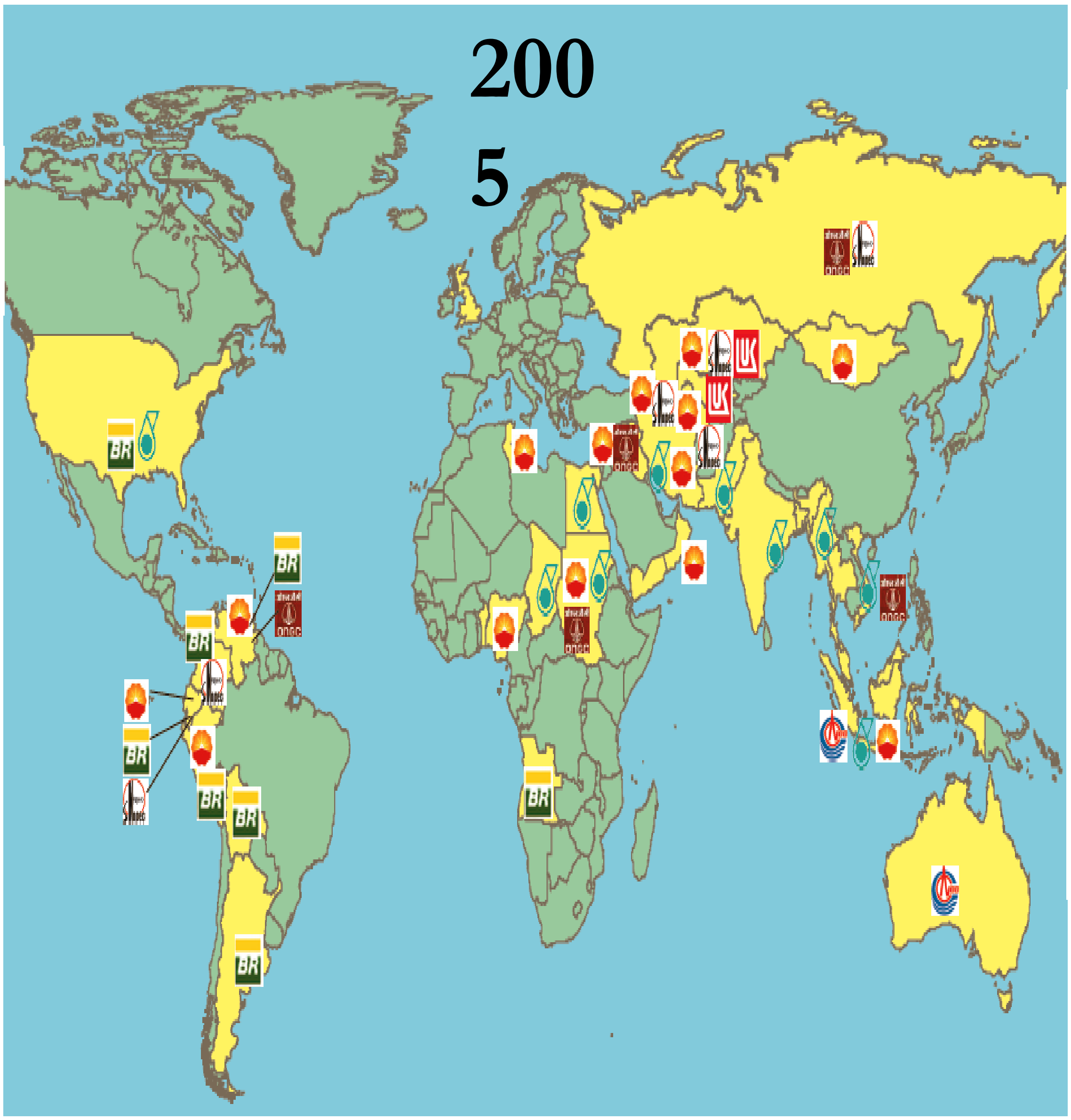
Source: UNCTAD, based on data from IHS

Foreign Production Locations of Oil & Gas TNCs from Emerging Economies



Source: UNCTAD, based on data from IHS

…and in



China: CNOOC, CNPC/PetroChina, SINOPEC

India: ONGC

Brazil: Petrobas

Malaysia: Petronas

Russian Federation: Lukoil

Source: UNCTAD, based on data from IHS

Key Development Challenges

- **The economic challenge**
  - To create value from the mineral deposits
  - To capture that value locally
  - To manage and use revenues efficiently and equitably.

- **The environmental challenge**

- **The social challenge**
  - How to protect human rights, compensate for resettlement and loss of traditional livelihoods;
  - How to address health concerns and workers' safety.

- **The political challenge**
  - How to avoid corruption and the apparition of "rentier States", unaccountable to their citizens and authoritarian.

Implications of Involving TNCs

- **Potential <u>economic</u> impacts:**
  - 👍 Capital, technology, management skills, income, government revenue
  - 👎 Share of rent, repatriation of profits, few linkages, few jobs

- **<u>Environmental</u>, <u>social</u> and <u>political</u> impacts implies need for appropriate policies as well as corporate social responsibility**

- **Net outcome depends on: global market conditions; host country's policies and institutions; TNC behaviour**

- **Challenge:**
  - Take advantage of TNCs as a catalysts for economic development while minimizing the costs
  - Balance social and environmental concerns against economic considerations.

Addressing Development Challenges Requires Concerted Effort From All Stakeholders

Host-country gov't

- Governance, institutions
- Sectoral policies and institutions
- TNC-specific policies (entry and operations, contracts, taxation,IIAs)

Home-country gov't

- Promote responsible TNC behaviour
- Assist host countries

TNCs

- Abide by local laws
- Uphold high standards when local governance is weak

Extractive activities

Int. Community

- Guidelines
- Pressure, sanctions
- Assist host countries

Civil society

- Monitor TNCs and governments
- Provide expertise

Making minerals work for sustainable development

Many International Initiatives Exist

- Extractive Industry Transparency Initiative
- Kimberley Process
- UN Global Compact
- Voluntary Principles on Security and Human Rights
- Global Reporting Initiative

But for greater impact, more firms - and more countries- need to be involved

Some Policy Recommendations

- Strengthen host-country governance and capacity to design and implement appropriate policies

- Strengthen capability to negotiate with TNCs

- Involve all stakeholders in decision-making process

- Use progressive taxation to cope with price fluctuations and avoid need for renegotiation

- More countries and companies should commit to enhanced revenue transparency

- Promote the use of high corporate behavioural standards

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