

January 29, 1988

To: [REDACTED]

From: Guy Stevens

Subject: Notes on Recent Trends in Plant and Equipment Expenditures  
and BOP Flows for Direct Investors in the US and US Foreign  
Investment Abroad

1. Chart 1 and Table 1 show that the BOP inflows associated with direct investment in the United States are now at unprecedented levels. Looking at the plant and equipment flows and takeovers financed by the above financial flows, these too have increased in the US. It is very hard to say how much the depreciation of the dollar has caused this trend, given the other factors involved, but there does seem to be evidence that both the BOP and P&E flows have been increased by the depreciation of the dollar. I discuss this at more length below.

Outflows also have reached unprecedented levels. The 1986 BOP outflow of \$28 billion was the highest of the decade, and our forecast of \$35.6 is higher still. It is true that both levels should be adjusted downward by \$8.8 and \$8.3 billion, respectively, because of bookkeeping adjustments due to exchange-rate gains. However, the adjusted outflows are still relatively high and increasing. Of course the model is predicting a high fourth quarter outflow of \$11.2, which may not come about. Part of the persistently high dollar level of the direct investment outflow is probably related to the declining dollar: given a predetermined level of real plant and equipment expenditures, firms will be reluctant to borrow in foreign currencies to finance the capital accumulation; this can lead to more financing in the United States. Moreover, once again given the level of real planned investment abroad,

firms face a temporary situation similar to a J-curve; since the great bulk of real foreign investment is spent on foreign goods priced in foreign currencies, it takes more dollars to finance a given level of real spending abroad. The upshot of these considerations is that (1) as long as the dollar is expected to fall, a larger percentage of direct investment financing is likely to come from the United States; and (2) as long as real plant and equipment expenditures by US subsidiaries abroad continue at high levels, for whatever reason, direct investment outflows in dollars will tend to be high. As a final point, it might be observed that from Chart 1 it is clear that the level of plant and equipment spending projected abroad has begun to decline in **real** terms: the fairly constant dollar level observed for the past three years is considerably smaller in foreign currency terms, and lower still when foreign price increases are taken into account.

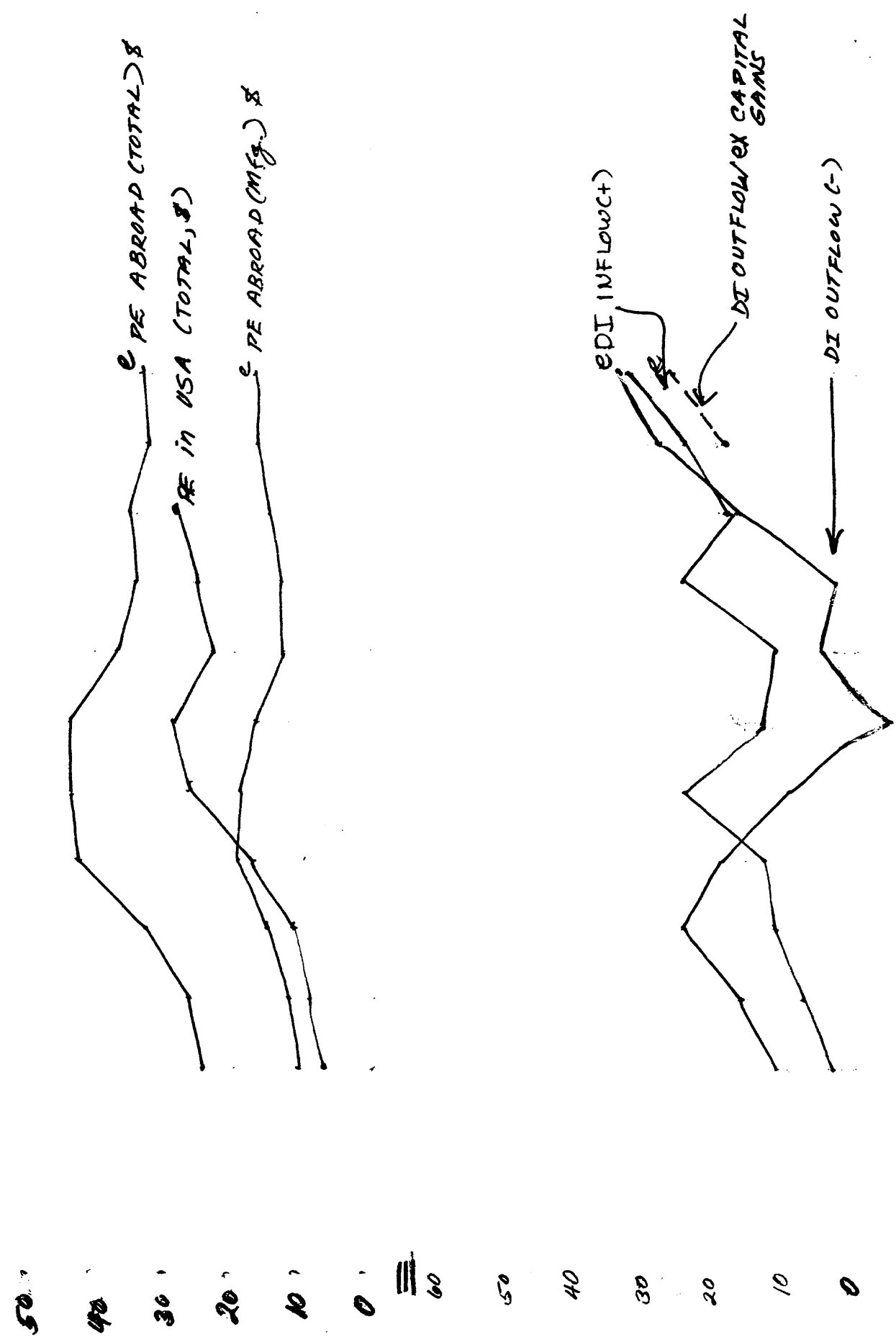
2. The lessons from looking at plant and equipment flows are less clear concerning the impact of the exchange rate. On the positive side, the rapid increase in acquisition data for affiliates in the US (our latest data are for 1986) suggests the declining dollar may have had some impact. (Note that we have only the acquisition data for 1986; P&E data for existing subsidiaries are only available through 1985.) Chart II and Table II show that European and Japanese investors have been extraordinarily active, particularly in 1986. Moreover, a look at the attached BEA Table 6B shows the remarkable and unique attention that the Japanese have been paying to real estate: of the total of \$4 billion acquired in 1986, the Japanese purchased \$2.7 billion. Anecdotal information suggests that the exchange rate played a big part in such activity.

On the negative side, plant and equipment expenditures (at least in dollar terms) do not seem to have been highly correlated with present and previous exchange-rate changes. It is to be expected that other factors such as economic growth would also have very powerful effects on P&E spending. Thus, for example, foreign spending in the US increased in every year except 1983 -- despite the huge appreciation of the dollar from 1980 to 85. As well, P&E by foreign affiliates of US companies increased in dollar terms from 1977 to 79 as the dollar depreciated, and has declined only slowly from its peak in 1982 as the dollar appreciated (and as European growth was modest). Chart I shows the overall picture and also shows that the P&E picture was not related to oil; the same pattern emerges for foreign affiliates in manufacturing.

cc: Current Account Forecasting Group

I. DIRECT INVESTMENT

(10) PLANT & EQUIPMENT EXPENDITURES\* (TOTAL) AND BOP FLOWS. (\$, BILLIONS)



\* The two PE series are not comparable, because US series includes only 'new' PE.

Table 1

Foreign Investment in U.S. (Total)  
(billions of dollars)

Direct Investment Flow (1)	New P&E (2)	Acquis. & Estab.* (3)	Acquis. Alone (4)	R=(4)/(3) (percent) (5)	(2)+R(3) = (2)+(4) (6)	Change in Total Assets (7)	Total Assets (8)	Gross Plant (9)	Investment Deflator (10)	(6)/(10) Real Investment (11)
1977	3.7	7.6					133.8	53.8	.726	
1978	7.9	9.3				35.6	169.4		.745	
1979	11.9	11.2	15.3	13.2	86	44.8	214.2		.803	32.7
1980	13.7	16.9	13.1	9.0	69	77.8	292.0	127.8	.869	29.8
1981	25.2	26.7	23.2	18.2	78	115.0	407.0	188.0	.045	47.5
1982	13.8	28.1	10.8	6.6	61	69.4	476.4	225.2	1.000	34.7
1983	11.9	23.2	8.1	4.8	59	55.3	531.7	244.0	1.004	27.9
1984	25.3	25.2	15.2	11.8	78	70.8	602.5	269.5	1.015	36.4
1985	19.0	28.4	23.1	20.1	87	133.7	736.2	293.6	1.032	47.0
1986	25.1	n.a.	31.5	25.5	81	n.a.	n.a.	n.a.	1.049	n.a.
1987	33.7 <sup>e</sup>									

\* Value of takeovers and new establishments. Some of P&E by new establishments is double-counted in column (2); columns (5) and (6) try to correct for this. 5/87 article says much of new acquisitions because of tax reform legislation.

U.S. Foreign Investment Abroad (Total)

Direct Investment Flow (12)	P&E Total (13)	PE-Mfg. (14)	Change in TA (15)	TA (16)
1977	11.9	24.1	10.5	443.4
1978	16.1	26.1	12.0	
1979	25.2	32.6	15.4	(No survey 1978-80)
1980	19.2	42.4	19.5	
1981	9.6	43.7	19.2	731.1
1982	-4.7	43.8	16.8	20.4
1983	4.9	36.4	13.6	-0.7
1984	2.8	34.1	13.6	92.0
1985	17.3	34.9	14.9	77.9
1986	28.0	32.6	16.4	837.9
1987	35.6	33.6 <sup>e</sup>	17.3	

II. FOREIGN INVESTMENT IN THE US by EUROPEAN & JAPANESE INVESTORS.  
 \$ Billions

- $\Delta$ TA: CHANGE IN TOTAL ASSETS; \$
- NEW PE EXPEND. \$
- NEW PE PLUS ESTIMATE OF VALUE OF TAKEOVERS.

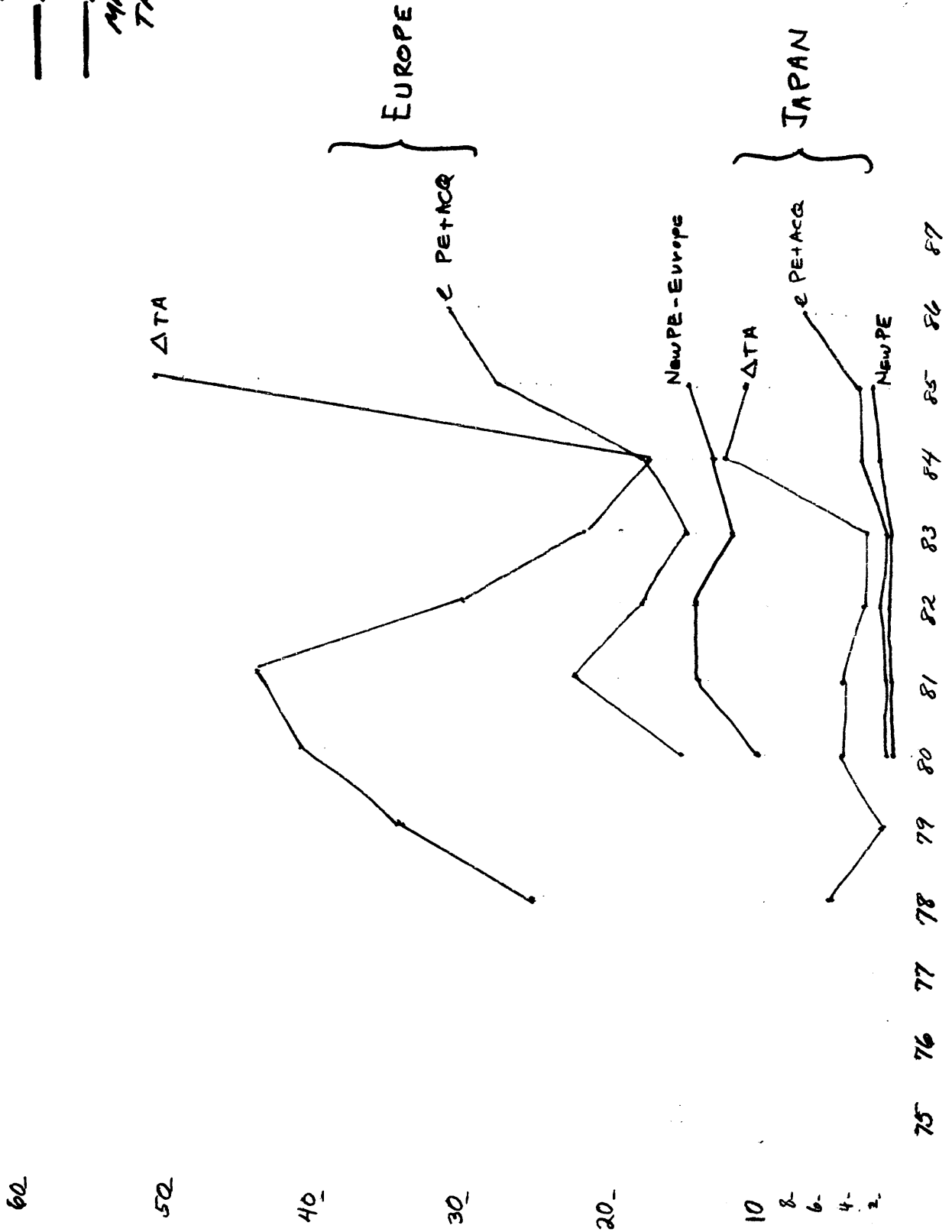


Table 2

Foreign Investment in U.S. by Country & Area  
(billions of dollars)

## JAPAN

	<u>Direct Investment Flow</u> (1)	<u>New P&amp;E</u> (2)	<u>Acquis. &amp; New Estab.</u> (3)	<u>(2)+R(3)*</u> (4)	<u>ATA</u> (5)	<u>Total Assets</u> (6)	<u>Gross Plant</u> (7)
1976							
1977	0.59	n.a.	n.a.	n.a.	n.a.	15.6	n.a.
1978	0.99	n.a.	n.a.	n.a.	5.1	20.7	n.a.
1979	0.74	n.a.	0.26	n.a.	2.0	22.7	n.a.
1980	0.73	1.2	0.60	1.61	4.9	27.6	5.3
1981	2.77	1.3	0.62	1.78	4.8	32.4	6.8
1982	1.98	1.8	0.59	2.16	3.3	35.7	8.7
1983	1.65	1.7	0.39	1.93	3.2	38.9	10.9
1984	4.37	2.3	1.81	3.71	13.0	51.9	15.5
1985	3.39	3.0	1.15	4.00	11.7	63.6	18.4
1986	4.1	n.a.	4.72	7.70 <sup>e</sup>	n.a.	n.a.	n.a.
1987	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.

## EUROPE

	(8)	(9)	(10)	(11)	(12)	(13)	(14)
1977	2.9	n.a.	n.a.	n.a.	n.a.	84.1	n.a.
1978	5.2	n.a.	n.a.	n.a.	25.8	109.9	n.a.
1979	8.2	n.a.	11.7	n.a.	34.6	144.5	n.a.
1980	8.3	10.5	7.7	15.8	41.6	186.1	90.3
1981	13.0	14.7	10.6	23.0	44.7	230.8	117.8
1982	10.4	14.7	6.4	18.6	30.6	261.4	137.6
1983	9.1	12.5	4.9	15.4	22.4	283.8	144.5
1984	14.6	13.6	6.5	18.7	18.5	302.3	156.9
1985	12.7	15.5	15.4	28.9	52.0	354.3	172.5
1986	20.5	n.a.	17.1	>32 <sup>e</sup>	n.a.	n.a.	n.a.
1987	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.

\*See note for Table 1.

Table 6B.—Investment Outlays, Country of Ultimate Beneficial Owner by Industry of U.S. Business Enterprise, 1986

[Millions of dollars]

	All industries	Mining	Petroleum	Manufacturing	Wholesale trades	Retail trade	Banking	Finance, except banking	Insurance	Real estate	Other
<b>All countries</b> .....	<b>31,472</b>	<b>323</b>	<b>829</b>	<b>13,712</b>	<b>761</b>	<b>5,070</b>	<b>207</b>	<b>1,533</b>	<b>1,523</b>	<b>3,993</b>	<b>3,523</b>
<b>Canada</b> .....	<b>5,175</b>	( <sup>D</sup> )	( <sup>D</sup> )	<b>770</b>	<b>3</b>	( <sup>D</sup> )	<b>0</b>	(*)	( <sup>D</sup> )	<b>159</b>	( <sup>D</sup> )
<b>Europe</b> .....	<b>17,086</b>	<b>97</b>	<b>129</b>	<b>11,107</b>	<b>662</b>	<b>1,228</b>	<b>30</b>	<b>233</b>	<b>1,398</b>	<b>942</b>	<b>1,260</b>
<b>European Communities (12)</b> .....	<b>15,541</b>	<b>97</b>	( <sup>D</sup> )	<b>9,782</b>	( <sup>D</sup> )	<b>1,228</b>	( <sup>D</sup> )	<b>232</b>	<b>1,398</b>	<b>870</b>	<b>1,198</b>
Belgium.....	355	0	( <sup>D</sup> )	155	( <sup>D</sup> )	0	0	0	0	( <sup>D</sup> )	2
Denmark.....	( <sup>D</sup> )	0	0	0	4	0	0	0	0	0	( <sup>D</sup> )
France.....	1,745	0	(*)	1,655	(*)	4	0	0	0	40	46
Germany.....	1,236	1	0	( <sup>D</sup> )	( <sup>D</sup> )	( <sup>D</sup> )	0	( <sup>D</sup> )	0	( <sup>D</sup> )	( <sup>D</sup> )
Greece.....	0	0	0	0	0	0	0	0	0	0	0
Ireland.....	1,298	0	0	1,298	0	0	0	0	0	0	0
Italy.....	( <sup>D</sup> )	0	0	( <sup>D</sup> )	0	0	0	0	0	0	0
Luxembourg.....	( <sup>D</sup> )	0	0	0	0	0	0	0	0	1	( <sup>D</sup> )
Netherlands.....	4,268	0	( <sup>D</sup> )	( <sup>D</sup> )	( <sup>D</sup> )	( <sup>D</sup> )	0	0	( <sup>D</sup> )	249	103
Portugal.....	4	0	0	0	0	0	4	0	0	0	0
Spain.....	16	0	0	0	( <sup>D</sup> )	0	0	0	0	5	( <sup>D</sup> )
United Kingdom.....	6,527	96	8	3,024	421	( <sup>D</sup> )	( <sup>D</sup> )	( <sup>D</sup> )	( <sup>D</sup> )	407	1,002
<b>Other Europe</b> .....	<b>1,545</b>	<b>0</b>	( <sup>D</sup> )	<b>1,325</b>	( <sup>D</sup> )	<b>0</b>	( <sup>D</sup> )	<b>1</b>	<b>0</b>	<b>71</b>	<b>62</b>
Austria.....	1	0	( <sup>D</sup> )	0	0	0	0	0	0	0	1
Finland.....	25	0	0	0	0	0	( <sup>D</sup> )	0	0	0	0
Liechtenstein.....	( <sup>D</sup> )	0	0	( <sup>D</sup> )	0	0	0	0	0	2	0
Norway.....	7	0	0	0	0	0	0	0	0	2	0
Sweden.....	1,131	0	0	1,059	( <sup>D</sup> )	0	0	1	0	( <sup>D</sup> )	( <sup>D</sup> )
Switzerland.....	321	0	0	236	0	0	0	0	0	( <sup>D</sup> )	( <sup>D</sup> )
Other.....	( <sup>D</sup> )	0	0	0	0	0	( <sup>D</sup> )	0	0	64	20
Other.....	( <sup>D</sup> )	0	0	0	0	0	0	0	0	0	0
<b>Japan</b> .....	<b>4,724</b>	( <sup>D</sup> )	<b>25</b>	<b>990</b>	<b>54</b>	( <sup>D</sup> )	( <sup>D</sup> )	( <sup>D</sup> )	<b>0</b>	<b>2,655</b>	<b>89</b>
<b>Australia, New Zealand, and South Africa</b> .....	<b>2,367</b>	<b>2</b>	<b>0</b>	<b>212</b>	( <sup>D</sup> )	( <sup>D</sup> )	<b>2</b>	( <sup>D</sup> )	<b>0</b>	( <sup>D</sup> )	( <sup>D</sup> )
<b>Latin America</b> .....	<b>570</b>	<b>0</b>	( <sup>D</sup> )	<b>81</b>	<b>5</b>	<b>0</b>	<b>0</b>	( <sup>D</sup> )	( <sup>D</sup> )	<b>64</b>	<b>53</b>
<b>South and Central America</b> .....	<b>379</b>	<b>0</b>	( <sup>D</sup> )	<b>81</b>	<b>5</b>	<b>0</b>	<b>0</b>	( <sup>D</sup> )	<b>0</b>	<b>37</b>	( <sup>D</sup> )
Argentina.....	1	0	0	0	0	0	0	0	0	1	0
Brazil.....	2	0	0	0	0	0	0	0	0	0	2
Mexico.....	68	0	0	( <sup>D</sup> )	(*)	0	0	0	0	32	( <sup>D</sup> )
Panama.....	6	0	0	0	0	0	0	0	0	4	2
Venezuela.....	( <sup>D</sup> )	0	( <sup>D</sup> )	0	0	0	0	0	0	0	0
Other.....	( <sup>D</sup> )	0	0	(*)	5	0	0	( <sup>D</sup> )	0	1	(*)
<b>Other Western Hemisphere</b> .....	<b>190</b>	<b>0</b>	<b>0</b>	( <sup>D</sup> )	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	( <sup>D</sup> )	<b>27</b>	( <sup>D</sup> )
Bahamas.....	4	0	0	0	0	0	0	0	0	4	0
Bermuda.....	105	0	0	3	0	0	0	0	( <sup>D</sup> )	( <sup>D</sup> )	( <sup>D</sup> )
Netherlands Antilles.....	( <sup>D</sup> )	0	0	0	0	0	0	0	0	( <sup>D</sup> )	0
United Kingdom Islands, Caribbean.....	( <sup>D</sup> )	0	0	( <sup>D</sup> )	0	0	0	0	0	0	0
Other.....	0	0	0	0	0	0	0	0	0	0	0
<b>Middle East</b> .....	<b>522</b>	<b>0</b>	<b>0</b>	<b>392</b>	( <sup>D</sup> )	<b>0</b>	<b>0</b>	( <sup>D</sup> )	<b>0</b>	<b>78</b>	<b>6</b>
Israel.....	0	0	0	0	0	0	0	0	0	0	0
Other.....	522	0	0	392	( <sup>D</sup> )	0	0	( <sup>D</sup> )	0	78	6
Kuwait.....	( <sup>D</sup> )	0	0	( <sup>D</sup> )	1	0	0	0	0	18	0
Lebanon.....	(*)	0	0	0	0	0	0	0	0	(*)	0
Saudi Arabia.....	100	0	0	0	( <sup>D</sup> )	0	0	( <sup>D</sup> )	0	53	1
United Arab Emirates.....	5	0	0	0	0	0	0	0	0	0	5
Other.....	( <sup>D</sup> )	0	0	( <sup>D</sup> )	0	0	0	0	0	6	0
<b>Other Africa, Asia, and Pacific</b> .....	<b>1,029</b>	<b>0</b>	<b>330</b>	<b>160</b>	<b>2</b>	<b>0</b>	( <sup>D</sup> )	( <sup>D</sup> )	<b>0</b>	( <sup>D</sup> )	<b>8</b>
Other Africa.....	346	0	330	0	0	0	0	0	0	11	4
Other Asia and Pacific.....	684	0	0	160	2	0	( <sup>D</sup> )	0	0	( <sup>D</sup> )	4
Hong Kong.....	533	0	0	32	2	0	( <sup>D</sup> )	0	0	0	1
Philippines.....	0	0	0	0	0	0	0	0	0	0	0
South Korea.....	130	0	0	127	0	0	0	0	0	(*)	3
Other.....	20	0	0	0	0	0	4	0	0	16	0
<b>United States</b> .....	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>
<b>Addendum—OPEC</b> <sup>1</sup> .....	<b>789</b>	<b>0</b>	( <sup>D</sup> )	( <sup>D</sup> )	<b>3</b>	<b>0</b>	<b>4</b>	( <sup>D</sup> )	<b>0</b>	<b>72</b>	<b>6</b>

<sup>D</sup> Suppressed to avoid disclosure of data of individual companies.

\* Less than \$500,000.

1. See footnote 1, table 5.

NOTE.—Data for 1986 are preliminary. Where more than one investor participated in a given investment, each investor and each investor's outlays are classified by the country of each individual ultimate beneficial owner.