U.S. Inward FDI Policy: The Need for Rethinking, Revision, and Reform

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U.S. foreign direct investment (FDI) policy appears to be based on the principles of neutrality and equal treatment. However, in recent decades there have been departures from these principles either through legislative restrictions or through administrative barriers relating to policy implementation. Some restrictions are necessary, e.g. in the case of national security concerns, but others are not. Policy reform is necessary since heavier inflows of FDI capital will be needed in the future to supplement domestic savings deficiencies and to finance continued U.S. current account deficits on balance of payments.

INTRODUCTION

Few areas of economic analysis produce a universal consensus among economists. One such area involves the ongoing dependency of the U.S. economy on the heavy infusion of foreign capital. This dependency is clearly traceable to the savings deficiencies in the U.S. private and public sectors. Consumer and business savings are inadequate in funding private real investments and the government sector chronically dissaves in the form of budgetary deficits. These savings shortfalls translate into current account deficits in U.S. balance of payments that must be financed through the importation of foreign savings (McKinnon, 2004, Graham and Marchick, 2006, p. 76).

Historically, the U.S. has been successful in financing current account deficits primarily in the form of foreign portfolio investments, reflecting a willingness on the part of foreign investors to buy U.S. stocks and bonds. For example, in 2005, foreigners purchased $686 billion in U.S. securities, including Treasuries, which amounted to over 50% of the gross capital inflows for that year. By way of comparison, inward foreign direct investment (FDI) into the U.S. amounted to only $129 billion which amount to 9.9% of the total (See Table 1).

Although gross capital inflows continued to grow in 2006 (to $1,558.3 billion) and 2007 (to $1,697.3 billion) at a pace witnessed in 2005 and earlier (U.S. Bureau of Economic Analysis, 2009), the U.S./global financial meltdown and subsequent economic downturn in 2008 disrupted this trend and raised serious doubts about the ability of U.S. financial markets to borrow globally at a level necessary to close the ongoing savings gaps.

Table 1
Gross Capital Inflows into the United States
(By Type of Flow)
2005

Type of Inflow	Billions of $	% of Total Inflow
Foreign Purchase of U.S. Treasury Securities	$196.8	15.2
Foreign Purchase of Other U. S. Securities	$489.2	37.9
Inward Foreign Direct Investment	$128.6	9.9
Purchase of U.S. Assets by Foreign Governments	$220.7	17.1
Others (including Banking and Currency Liabilities)	$257.3	19.9
Total	**$1,292.6**	**100.0**

Source: U. S. Bureau of Economic Analysis, *U. S. International Transactions*, Graham & Marchick, 2006, p. 77.

Of particular concern in this regard were massive liquidations of U.S. Treasury securities in late 2008 (Thomson Reuters, 2009). Admittedly, this could prove to be a short term disruption, triggered by cyclical not secular concerns. Nevertheless, the implications of the U.S. losing its status as a net capital importer remain ominous.

It is the contention of this study that U. S. dependency on foreign capital will continue into the foreseeable future, but that FDI infusions will have to play a much larger role in financing ongoing current account deficits. Certainly, it would be desirable for the U.S. to finance its import needs and growth aspirations internally through a quantum jump in domestic savings, privately and publicly. This would require transitions not likely to occur over the short term, such as the cultural transformation of American income earners from less of a spending orientation to more of a saving orientation as well as a shift from chronic government budgetary deficits to budgetary surpluses. The latter is unlikely to occur soon given the massive expenditures of the early Obama administration on fiscal stimulation and financial sector bailouts. In addition, there will continue to be ongoing environmental, social, political, and military claims on governmental resources.

Given the likeliness of continued savings deficiencies or shortfalls in the U.S. over the foreseeable future, the successful attraction of heavy net infusion of foreign capital would remain a necessity. This dependency will predictably continue even after the U.S. economy recovers from the current economic and financial malaise. Without compensatory inflows, destabilizing pressure would be applied to U.S. financial markets raising interest rates and putting downward pressure on an already weak dollar (Business Week, 2007).

The question arises, of course, whether the U.S. can continue to count on massive amounts of foreign capital to fund its overseas obligations and growth aspirations. Given developments in global security markets, there is reason to be pessimistic in this regard. The problem will be in the area of foreign portfolio investments, historically the major source of foreign capital infusions (Fuerbringer, 2004, Wall Street Journal, 2007). In the past, U.S. security markets have had little or no global competition in reference to size, diversity, safety, and rates of return. Decades ago, foreign investors in stock and bonds had few viable alternatives outside of U.S. security markets.

Changes are occurring, however, altering the competitive intensity of global security markets. Asian and European security markets are growing and maturing, providing more competition to U.S. markets. Dollars, flowing out of the U.S. because of current account deficits, are no longer automatically returning in the form of foreign demand for U.S. private and government securities. Foreigners are diversifying their assets away from dollar dominated securities toward other investment opportunities. Investors in recent years have discovered that U.S. investments, while relatively low risk, are also relatively low return compared to investment opportunities in other markets. Risk/return factors that historically favored U.S. security investments no longer do so (Business Week, 2007).

Assuming that dramatic changes in the savings/spending culture of U.S. income earners and in the budgetary claims on U.S. government resources do not occur in the foreseeable future, the current dependency on foreign capital infusions will continue. If the attraction of foreign portfolio capital becomes more difficult because of competitive intensity, what are the alternatives? It is the position of this paper that heavier inflows of FDI capital could serve most effectively as a magnet for foreign savings providing unique positive spillover effects in the process. Although FDI gross inflows into the U. S. continue to be substantial, the U.S. has been a net exporter of FDI capital for most years since the mid 1970s (Table 2).

Table 2
Inward and Outward U.S. Foreign Direct Investment Flows
(in billions of $)

Year	Inward (FDIUS)	Outward (USFDI)
1975	2.56	13.98
1980	16.93	19.23
1985	20.01	14.06
1990	47.92	22.95
1991	22.02	31.36
1992	17.86	42.66
1993	41.13	72.60
1994	49.44	49.37
1995	57.80	98.78
1996	86.52	91.88
1997	105.59	104.83
1998	179.03	142.64
1999	289.44	224.93
2000	321.27	159.21
2001	167.02	142.35
2002	84.37	154.46
2003	63.96	149.90
2004	133.16	244.13
2005	109.75	199.07
2006	183.57	248.85
2007	232.86	313.79

Source: IMF *International Financial Statistics*, various issues

The paper is divided into five sections. Following this introduction, the second section presents the case for inward FDI. It is argued that the potential exists for a quantum jump in FDI capital infusions, more so than for foreign portfolio investments, and that inward FDI is capable of bestowing more secondary and tertiary benefits on the U.S. economy than in the case for the latter. The third section reviews U.S. government FDI policy, arguing that in reality it is more hostile than policy rhetoric implies. The paper concludes with a prescription for policy reform followed by a summary section.

FINANCING U.S. CURRENT ACCOUNT DEFICITS WITH INWARD FDI: THE ADVANTAGES

Unlike foreign portfolio investments, FDI inflows involve more than the importation of capital. It can be argued that inward FDI produces a more multidimensional growth stimulus for the host country through the importation of jobs, new technologies, and even new managerial techniques. Although some disagreement exists in the economics literature about the relative benefits of FDI, newer studies, using more sophisticated statistical techniques, tend to confirm the positive spillover effects that inward FDI produces (Lipsey and Sjöholm, 2005).

In reference to the labor market effects, there is growing evidence that FDI generates new jobs, particularly in high wage industries (Doms and Jensen, 1998). Wage rates aside, the pure employment effect of inward FDI have become significant in recent decades. By the mid 2000s, the employment of Americans by affiliates of foreign direct investors grew to exceed 5 million workers (U.S. Bureau of Economic Analysis, 2006 and Graham and Marchick, 2006, p. 78).

FDI spillovers extend beyond job creation and positive wage effects to include productivity gains and infusions of new technologies and new managerial techniques. FDI can generate productivity spillovers even for industrialized, target countries such as the U.S. (Blomstrom, Kokko and Zejan, 2000) and positive spillovers can either be horizontal, in which local U.S. competitors may gain knowledge or know-how operating at the same level of production as the affiliates of foreign firms, or vertical in which supply chain linkages between local U.S. firms and foreign affiliates operating on U.S. soil may provide the same benefits (Hanson, 2001 and United Nations, 2001).

Historically, of course, the fallacious notion emerged that U.S. firms have nothing to gain from either inward or outward FDI relationships because of the perception that U.S. technology and managerial know-how are universally superior. The success of inward FDI from Japan served to question that premise in the 1980s and early 1990s and the more recent infusions of FDI from Europe and elsewhere have further served to dispel it. Overall, U.S. technology and managerial skill rank among the most sophisticated in the world, but U.S. superiority does not extend to all areas nor do U.S. firms dominate R&D activities globally to the exclusion of other innovators (Graham and Marchick, 2006, pp. 84-89).

Given the dependency of the U.S. on foreign capital, which is likely to continue, there is a more compelling reason for financing ongoing current account deficits with more FDI rather than more foreign portfolio investments. Foreign firms, establishing “greenfield” investments in the U.S. or acquiring existing properties, are motivated by longer term strategic factors and, as a result, FDI inflows tend to be less volatile than foreign investments in U.S. stocks and bonds. The fact that foreign portfolio investments are more interest rate sensitive and exchange rate sensitive than FDI explains in large part the relative volatility of portfolio investments and the relative stability of direct investments.

The financial objectives of a foreign purchaser of a domestic bond may be single dimensional, but the objectives of the foreign purchaser of a domestic property asset tend to be multidimensional, not closely related to the current cost of money. It is true that FDI can be influenced by exchange rate fluctuations but, unless such movements are pronounced and prolonged, exchange rate effects tend to rank low in the list of factors that govern the FDI decision-making process (Sokoya and Tillery, 1992, p.73).

It is logical to conclude, therefore, that FDI is likely to provide funding support for U.S. current account deficits on a more stable basis and that a shift to some degree from inward portfolio investments to direct investments will translate into more U.S. interest rate and exchange rate stability than would otherwise be the case (Jackson, 2007).

The question arises, of course, whether U.S. FDI policy is supportive of this transition and whether this policy has evolved over time in response to the needs of the U.S. economy or in response to other pressures, political or otherwise. The following section addresses such questions in the form of a historical policy review.

THE EVOLUTION OF U.S. FDI POLICY

On the surface, U.S. FDI policy historically appears to be based on the principle of equal treatment, not enticement, and the policy specifics seem to be consistent with a philosophical commitment to neutrality.

What is the essence of an FDI policy of neutrality? Government must be consistent in adhering to two principles. The first relates to the freedom to enter and expand. A neutral policy would disallow any government-imposed obstacles designed either to block the initial entry of the foreign multinational or to limit its freedom to move and grow. Secondly, a neutral policy involves a "level playing field" for established foreign direct investments. Government must not impose any special burden on the foreign company in comparison to its treatment of domestic firms (Graham and Krugman, 1995, p.122). In short, government policy must involve a bias neither in favor nor in opposition to foreign ownership of domestic productive resources.

Despite the fact that the U.S. commitment to the principle of neutrality has been affirmed and reaffirmed historically, most notably in the 1977 and 1983 declarations by the Carter and Reagan administrations respectively (Graham and Krugman, 1995, p. 122), in reality U.S. policy modifications and implementations have frequently produced sharp departures from the same. These departures have taken the form historically of either legislative restrictions or administrative barriers relating to policy implementation.

Not all departures from the principle of FDI neutrality are without justification of course. In the early evolution of this policy, dating back to the late 19th and early 20th centuries, exceptions to neutral treatment of foreign firms occurred only in cases of industries subject to Federal regulation, particularly those that contribute to national security. Predictably, foreign investments continue to be restricted today in such security-sensitive industries as coastal shipping, air transport, and atomic energy. U.S. policy is not unique in this regard inasmuch as most industrialized countries employ similar policies of restrictions in the name of national security (OECD, 1995, p. 31).

Historically, the most severe FDI restrictions have occurred during wartime, most notably to German investments during the World War I and II periods. Concerns in 1917 led to the passage of the Trading with the Enemy Act (TWEA) which authorized the seizing of assets owned by foreign persons. Virtually all assets in the U.S. owned by German firms were seized in 1917 and 1918 (Graham and Marchick, 2006, p. xvi). The TWEA was again invoked in the early 1940s, again directed primarily towards German investments.

FDI restrictions were institutionalized in a more formal way in 1988, with the passage of a significant piece of legislation (with modifications in 1991 and 1992) as an amendment of the Defense Reduction Act of 1950. This so-called "Exon-Florio" provision gives the U.S. president the power to suspend or ban inward FDI (specifically mergers or takeovers) if it can be demonstrated that U.S. national security is threatened. Also, divestiture of established foreign investments can be ordered by executive decree under the same provision.

In implementing this piece of legislation, the reviewing mechanism is the Committee on Foreign Investment in the United States (CFIUS), composed of members from the Departments of Treasury, Commerce, Defense, Justice, and State as well as from the Council of Economic Advisors, the Office of Management and Budget, and the Office of the United States Trade Representative. The CFIUS is empowered by law to review the security implication of any foreign direct investment (Economic Policy Council, 1991, p. 33).

Unfortunately, in passing the Exon-Florio, Congress failed to properly define “national security”, permitting the CFIUS freedom to interpret this term as broadly as possible, which in recent decades has become a reality.

Various events dating back to the 1980s have induced CFIUS to scrutinize FDI applications more closely and to impose tougher requirements on potential foreign investors before approval. Agreements over time have become more intrusive and restrictive. The concept of “national security” has been broadened in the thinking of CFIUS to mean “national interest”, including economic interests, technological interests, and sovereign rights interests (Kang, 1997, p. 303).

Concern over the loss of political autonomy in the 1980s was rooted in the xenophobic response to the heavy infusion of Japanese FDI which during this period exceeded all others quantitatively and occurred in very visible sectors of the U.S. economy (Kim and Kim, 1993). Attitudes in the U.S. government, included in the CFIUS, were influenced by public opposition to inward FDI. For example in 1989, 70% of Americans polled by the Pew Research Center took the position that foreign ownership of U.S. companies per se was “bad for America” (Pew Research Center, 2006).

In the extreme, Japan bashing in the 1980s took the form of accusing the Japanese not only of buying controlling interests in key U.S. industries, but of buying Washington as well. In his 1990 book, appropriately entitled Agents of Influence, Pat Choate painstakingly describes the strategy employed by Japanese lobbyists in currying the favor of Washington politicians, in influencing administrative and legislative decisions, and in shaping U.S. government policy from the outside. What frightens Choate is not the effort but the apparent degree of success. He argues that "Japan's inside track allows its firms and organizations to short-circuit U.S. government decisions long before most people in the bureaucracy even know that something is afoot" (Choate, 1990, p. 62). If one is to believe Choate, U.S. FDI policy has not deviated from its historical emphasis on openness. U.S. markets remain open to heavy infusions of FDI and favorable treatment of foreign firms, once established, continues because of supportive U.S. government policy. However, in Choate's view, government policy is supportive not because of any philosophical commitment in Washington to free international capital flows or any conviction that FDI bestows benefits on the U.S. economy, but rather because permissive U.S. policy decisions have been unduly influenced by powerful foreign lobbyists, particularly the Japanese.

The quantum jump in Japanese FDIUS witnessed in the 1980s did not continue throughout the 1990s; however, xenophobia reactions to inward FDI were simply redirected. Some were directed at OPEC members because of the market power of this cartel and the effect on oil pricing (Kang, 1997, p. 302). The most visible signs of xenophobic feelings in the U.S. were triggered by the proposed acquisition in 2006 of six U.S. port terminal operations by a company owned by the government of the United Arab Emirates. The public outcry was at least in part responsible for the ultimate U.S. congressional ban of this acquisition (Jackson, 2006).

Of course, one can argue that closer scrutiny and more restrictive measures against inward FDIUS are justifiable following 9/11, particularly in the case of countries with linkages to terrorist groups. Inward FDIUS did decline sharply after 9/11 (See Table 2). However, negative attitudes about FDIUS extend well beyond national security issues. The tendency for CFIUS to “cast a jaundiced eye” at inward Chinese FDIUS is a case in point. The Byrd Amendment to Exon-Florio directs CFIUS to scrutinize foreign companies owned or controlled by foreign governments more aggressively. Most Chinese companies fall under this category (Graham and Marchick, 2006, p. xix). Clearly, the concern with Chinese FDIUS is not based on the threat of terrorism but rather the loss of U.S. technological secrets through industrial espionage and even legitimate means.

U.S. policy seems to miss the point in this regard. Technology transfer through FDI is not a zero sum game. Foreign companies that invest overseas both export and import technology. If the foreign company and investing country gain through FDI-induced technology transfer, this does not mean that local companies in the host country and the local economy lose. The free movement of technology across international boundaries can “lift all boats” as is the case with free trade and free capital flows.

Although, on the surface, U.S. FDI policy seems to support the concept of a level playing field for domestic and foreign firms, related acts of Congress seem to contradict this principle. In the 1990s, Congress passed several laws designed to promote more effective industry-government collaboration and to support private-sector technological development. Since this increased emphasis on business-government cooperative efforts was designed to enhance the competitiveness of U.S. firms, the participation of foreign firms in these domestically-designed programs became an issue.

Several laws were passed in the 1990s designed to promote technological development in U.S. industry through private sector/public sector cooperation. Three laws in particular, the American Technology Preeminence Act of 1991, the Energy Policy Act of 1992, and the Technology Reinvestment Project under the Defense Appropriations Act of 1993 all permitted foreign firm participation, but only under reciprocity arrangements. Applications from foreign firms are approved only if it can be demonstrated that American companies have equal access, not only to the domestic programs per se, but also to comparable programs in the home countries of foreign applicants. Also, the participation of foreign firms in the three programs requires the demonstration of adequate and effective protection of U.S. intellectual property rights (OECD, 1995, p. 41).

All firms, domestic or foreign, must show that participation in these Federal programs would be in the economic interest of the U.S. However, considering the added burden of proof involved in the application process of foreign firms, domestic firms would seem to have a comparative advantage in gaining entry. The additional "hoops" that the foreign firm must jump through may not amount to prohibitive entry barriers, but they at least serve as psychological deterrents.

In the 1990s, new Federal legislation, promoting private sector - public sector collaboration in technology development, typically involved at the very least reciprocity requirements. Also, the updating of old legislation, such as the 1993 update of the National Cooperative Research Act, added the same requirements. Exceptions exist to the practice of imposing conditions on foreign participation in U.S. government sponsored programs, such as the High Performance Computing and Communications Program launched in 1991. The legislation establishing this particular program imposed no eligibility criteria (OECD, 1995, p. 41), but this type of legislative neutrality, fairly commonplace in the 1980s and before, became quite atypical in the 1990s.

For decades, the United States played the role of leader in promoting an open-border, non--

discriminating approach in the treatment of FDI. Historically, the U.S. has been uniquely open to the inflow, as well as the outflow, of FDI capital. In fact, it has been argued that the single most important non-macroeconomic factor explaining the rapid growth of FDI in the 1980s was the rapid dismantling of investment barriers in the world, which had the effect of spurring the international movement of capital (Economic Policy Council, 1991, p. 16). As other countries, particularly in the industrialized world, began to emulate the openness of U.S. FDI policy, the results were predictable. U.S. leadership in the 1980s was at least partially responsible for the liberalization of international capital flows.

In the 1990s and 2000s, the leadership role of the U.S. government in promoting free international capital movements has been questioned, however. Although the official U.S. policy remains one of neutrality and openness, particularly in reference to FDI, the U.S. government in the 1990s clearly has demonstrated increased sensitivity to the issue of equal competitive opportunity for U.S. firms abroad, including equal entry requirements for and treatment of U.S. multinationals. To American interest groups, reciprocity requirements may appear to be a necessary means of securing a "level playing field." To foreign interest groups, however, this may appear to be a subtle or not-so-subtle retreat of U.S. policy from historical positions of openness and neutrality.

The danger is that U.S. leadership in promoting capital mobility across international boundaries may be compromised by the foreign suspicion that beneath the rhetoric of reciprocity is a hidden agenda, namely, the promotion of U.S. competitive advantage in the global economy. Like Caesar's wife, it may be argued that the U.S. government should avoid even the appearance of an indiscretion, such as the introduction of a beggar-thy-neighbor industrial policy though the back door by the imposition of FDI restrictions.

How can the U.S. regain its global leadership and, in the process, capture more benefits from inward FDI? Although the answer to this question is not simple, a necessary first step is policy reform and a reordering of priorities with policy implementation.

PROPOSALS FOR CHANGE

In order to attract the volume of inward FDI needed to support the capital and other needs of the U.S. economy, fundamental changes must occur in the structure and implementation of U.S. FDI policy. These should include the following:

Revisions in the Exon-Florio Statute Designed to Sharpen the Definition of “National Security”

The absence of a clear definition of national security in the current statue opens the door for broad, sweeping interpretation by the CFIUS of what is best for the U.S. economy. A list of critical U.S. strategic industries should be identified, subject to modifications over time. Inward FDI applications may be blocked, but discretionary authority in identifying such industries, currently in the hands of the CFIUS, should be reduced.

Revisions in the Exon-Florio Statute to Prevent the CFIUS from Blocking Inward FDI, Based Purely on Domestic Economic Interests

The CFIUS should not be empowered to protect the competitive positions of U.S. firms and U.S. industries. Finding the “proper mix” of U.S. owned and foreign owned U.S. property assets should not be the responsibility of the CFIUS. Protecting inefficient U.S. industries from foreign takeovers outside of areas of national security will only contribute to an inefficient allocation of global resources. Also, blocking inward FDI for protectionist reasons costs the U.S. economy the positive spillover effects that accompany foreign capital infusions.

Interestingly, on several occasions congressional members have attempted unsuccessfully to broaden the scope of Exon-Florio to specify that economic security, as well as national security, should be justification for blocking inward FDI (Graham and Marchick, 2006, p. 172). In fact, Congress should move in precisely the opposite of these initiatives.

Depoliticize the CFIUS Decision-Making Process

This, of course, is easier said than done. Members of the CFIUS from the Department of Treasury, State, Defense, Homeland Security, etc. are parts of the political establishment in Washington and are subject to intense political pressures. Certainly the Secretaries of Defense and Homeland Security should be represented on the CFIUS, but at times their concerns seem to outweigh those of the Treasury and Commerce Departments within which more balanced views of the relative merits of inward FDI tend to emerge. Perhaps, the proper place for personnel change in the CFIUS should take place at the staff level. Additional staff could be added from the Treasury and Commerce Departments particularly in the form of specialists, economists included, who could reinforce the CFIUS decision-making process with a broader database relating to the overall impact of inward FDI. These would be permanent economic staff members, not occasional consultants.

Mandate a More Formal Reporting Requirement for the CFIUS to Congress

Even if it is not possible to alter the composition of the CFIUS for political or other reasons, changes should be made in the recording and reporting requirements of the CFIUS to guard against the possibility of arbitrary and inconsistent decision-making processes. Currently, adequate records of formal and informal deliberations between the CFIUS and prospective foreign investors are not kept and the CFIUS chronically fails to consult or share information with Congress on inward FDI applications and deliberations. This enhances the possibility that deliberations and decisions will be colored by political pressures arising from xenophobic responses to occurrences such as 9/11 or the Dubai controversy.

If the CFIUS succumbs to such pressures, then Congress should know about it through open recording and reporting requirements. Of course, if such requirements are instituted, this may reduce the occasions when the CFIUS unduly does succumb to the same. The CFIUS should not be permitted to operate as a “star chamber” in secretly deliberating with prospective foreign investors and secretly discouraging them from pursuing their FDI applications for reasons far removed from national security concerns.

Promoting a More Proactive Inward FDI Policy

Given the importance of inward FDI to the growth and stability of the U.S. economy, it is time for U.S. policy to become more proactive in the area of investment promotion. Most countries in the world have investment promotion agencies (IPAs) that target and recruit those foreign companies that provide the best resource matches for the local economies. The concept of IPAs has been institutionalized globally through an online service such as the World Association of Investment Promotion Agencies (WAIPA) that assists member countries in their quest to attract inward FDI (WAIPA, 2008). The U.S. government currently does not actively participate in aggressive investment promotion. It does sponsor an “Investment in America” program which tends to be primarily informational.

It is true that the various U.S. states engage in investment promotion. Specific incentive packages include tax incentives, financial assistance, infrastructure support, worker training subsidies, natural resource support, and the establishment of foreign trade and enterprise zones (Casey, 1998, pp. 133-137). However, these state programs resemble “zero sum games” more than “positive sum games” in which aggressive states attract FDI capital at the expense of others with less effective investment promotion approaches. Accordingly, national interests are not adequately served if IPAs exist only at the state level.

The U.S. government should establish a more aggressive national IPA which would partner with the states in targeting the type of inward FDI which would best benefit the national economy as well as the state economies. The U.S. government would support state IPAs in providing both research data and financial benefits in order to identify and attract those foreign multinational companies that would provide the largest number of positive spillovers in the areas of jobs, wages, productivity, and technology/managerial skill. Inward FDI has become too important to the future of the U.S. economy for U.S. policy to continue to be based primarily on the principle of neutrality and on national security concerns.

CONCLUSIONS

It is not outside the realm of possibility that over time cultural and organizational changes in the U.S. private sector and political changes in the government sector will combine to dramatically reduce U.S. dependency on the net importation of foreign savings. However, this is not likely to occur in the foreseeable future. Unfortunately, the willingness on the part of foreign investors to supplement deficient U.S. savings through the purchase of U.S. stocks and bonds is diminishing. Foreign security markets are becoming more competitive and the U.S. dollar has become more unstable. As a result, the U.S. can no longer be guaranteed that foreign portfolio investment inflows will be adequate to “paper over” sizable U.S. current account deficits on balance of payments.

Accordingly, a quantum jump in FDI inflows may be necessary in the future to avoid further destabilizing pressure on U.S. financial markets, interest rates, and on the value of the dollar. Fortunately, if adequate FDI inflows do occur, the U.S. will capture benefits well beyond capital importations. Positive spillovers are likely to occur through wage, productivity, and employment benefits as well as through the infusions of new technologies and managerial techniques.

The attractiveness of the U.S. as a target area for foreign direct investment depends in part on U.S. government FDI policy. Although historically U.S. policy has been receptive to FDI inflows based on the principles of neutrality and equal treatment, in recent decades U.S. policymakers and policy implementers have retreated from these principles because of national security and other concerns. Policy reform and revisions are needed to guarantee that the U.S. will remain an attractive venue for inward FDI. Reforms should include a more specific definition of national security restrictions relating to FDI inflows, a reduction in the politicization of the CFIUS process, increased disclosure requirements on CFIUS deliberations and decision making, more complete CFIUS record keeping, changes in the composition of CFIUS and a more proactive role on the part of the U.S. government in investment promotions. National “security” concerns must be respected, but FDI inflows should not be blocked because of vaguely articulated concerns for the U.S. economy or for U.S. firms. Restricted investments can be as damaging to economic welfare as restricted trade.

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