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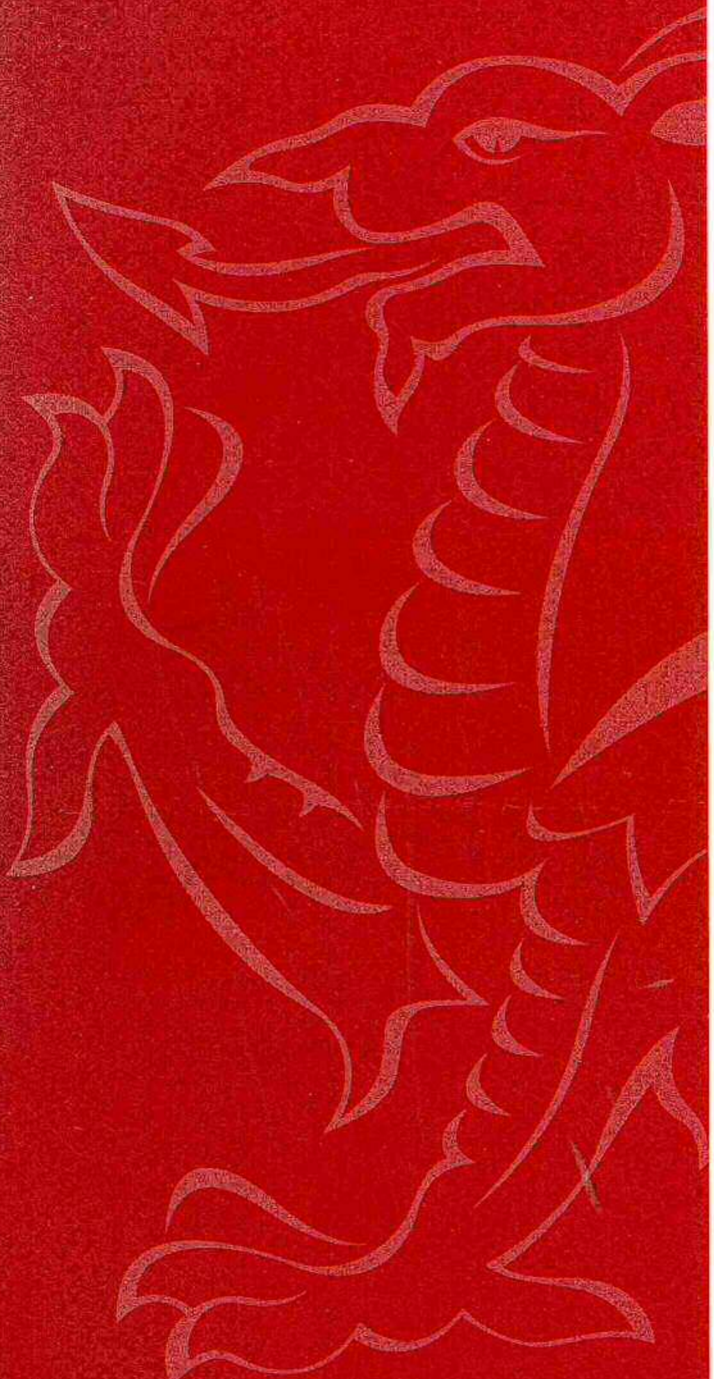

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The *Welsh Economic Review* is produced twice yearly, by the Welsh Economy Research Unit (WERU) at Cardiff Business School. The aim of the *Review* is to provide an authoritative and objective analysis of the Welsh economy in a manner that promotes understanding and informs decision-making. The 'core' section of the Review is written by members of WERU, with feature articles contributed by academics or practitioners within or outside Wales. The *Review* is circulated widely within Wales, to both private and public sector organisations, including the education sector and the National Assembly.

Notes for Contributors

Authors should send papers for potential publication in the *Welsh Economic Review* to the Editor at the address given below, preferably via e-mail in a Word for Windows format. Papers are welcome on any topic that would be of general interest to the readership, and should be written in a style suitable for non-specialist readers. Papers should be approximately 3,000-4,000 words and any graphs or figures should be accompanied by the underlying data to allow reproduction.

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Foreign Direct Investment: Prospects for Wales

As shown earlier in this edition of the *Welsh Economic Review* (WERU Conference reports), increasing attention is being given to issues of regional entrepreneurship and the role of indigenously controlled SMEs in the Welsh future. Whilst this is desirable, it is likely that attracting new inward investment from overseas will remain an important factor driving regional economic prospects for the foreseeable future. Serious reversals in the foreign-owned sector of Welsh manufacturing have been experienced in the recent past, particularly in the electronics sector. But what of the future? This section provides a summary of recent trends in global, European, and UK foreign direct investment (FDI). The conclusions examine 'inward investment' prospects for Wales. The majority of figures used in this section are derived from United Nations Council of Transnational and Development (UNCTAD) reports and the press releases detailed in the references.

Global Foreign Direct Investment Trends

FDI is an investment by a firm made outside its home country, but inside the investing company, and where control over the resource remains within the investing company. FDI is then an activity of a multinational enterprise (MNE), defined as a firm that owns and controls income generating assets in more than one country. This definition of FDI includes, for example, the creation of wholly owned subsidiaries on greenfield sites, and also take-overs of indigenous firms by foreign firms, and joint ventures between foreign and indigenous enterprises.

In 1990 global FDI inflows were estimated at $202bn, rising to an estimated $1,271bn by 2000. Over the period 1990-1999 the global inward FDI stock grew from $1,761bn to $4,772bn. In the same period the assets of the foreign affiliates of MNEs grew from $5,706bn to $17,680bn, whilst overseas employment in these affiliates increased from 23.6m to 40.5m. Figure 2 shows the upward trend in global FDI inflows during the 1990s. Developed countries as a whole accounted for an estimated 79% of global FDI inflows in 2000.

The predominance of the developed world in FDI inflows is explained by the significance of cross border mergers and acquisitions (M&As) in the figures. Cross border M&As to the EU, US and Japan were estimated at $1,057bn in 2000, up 55% on levels in 1999.The trend in global mega-mergers (i.e. with a value of more than $10bn) has a huge influence on the figures. Each of the last two years has been characterised by a very small number of very large mergers involving firms of US and Western European origins. Currently FDI which creates new businesses is only a small proportion of the global total.

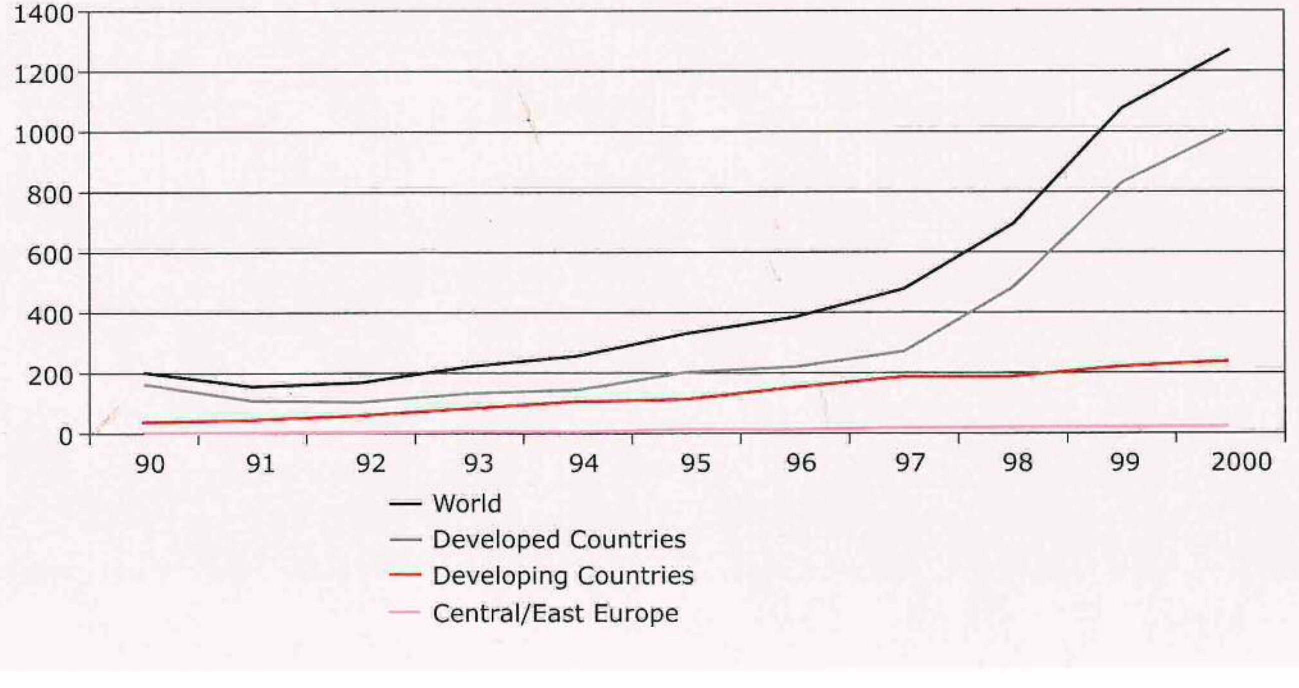
Figure 2 shows that FDI inflows into the developing world are expected to have grown by 8.1% in the 1999-2000 period. The main recipients of FDI inflows were China, Hong Kong and Brazil, which between them accounted for almost half of FDI inflows into the developing world in 1999. FDI into China is expected to increase in the near future, particularly as inward investors build a strategic presence in China ahead of its World Trade Organisation accession.

FDI inflows into Europe

FDI inflows into the EU-15 were an estimated $305.1bn during 1999. The increase in cross border M&A activity during 1999-2000 means that this total is expected to have increased for 2000 (cross border M&A sales from the EU-15 increased from an estimated $357.3bn in 1999, to $586.5bn in 2000).

The UK continues to be the main destination for FDI inflows into the EU-15. Table 6 shows that for the period 1996-1999 the UK accounted for around 26% of EU-15 FDI inflows, followed by France (14%), Holland (13%) and Sweden (12%). The UK and France also

Figure 2 FDI Inflows by Global Region in the 1990s ($bn)



accounted for around 60% of direct investment outflows from the EU-15 in 1999. The main EU destinations for FDI have higher FDI outward than inward stocks. This is particularly noticeable in the case of the UK, Sweden, France, Germany and the Netherlands. In the more peripheral states of the EU the opposite applies, as, through time, inward investment flows have been much greater than outward flows from multinationals from these states. (Ireland, Austria, Greece and Portugal).

UK – Recent Performance.

The Department of Trade and Industry reports that 2000-2001 was a good year for inward investment into the UK. The DTI's INVEST-UK arm revealed that 869 inward projects had been initiated during the year (of which 494 were new as opposed to expansions or mergers), and that these were connected with just over 71,000 jobs. The US is still the dominant investor in the UK, accounting for 48% of the projects reported and 55% of associated jobs in the period 2000-01. The strong dependence on the US could be a source of future problems with the likely downturn in the US economy. Several UK regional development agencies have already reported a drop in new enquiries from US firms.

The main inward investing sectors in the UK during 2000-01 were IT/Internet, and software. Services industry FDI has tended to fill some of the gap left by recent slower growth in new manufacturing projects. Top manufacturing sectors for new investment were electronics (83 projects) and automotive (52 projects). However, 2000-01 was a poor year among existing investors in automotive and electronics. Several large electronics and telecommunications equipment makers operating in the UK announced either closures of facilities or major redundancies during the year. Overall, the UK is expected to retain its position as the top EU inward investment location. However, its location competitiveness for manufacturing projects is falling, and it is expected to retain its position by virtue of new investments in services sectors.

Manufacturing Locations in the EU periphery

Wales, Scotland, Ireland, Portugal and Spain have been important EU destinations for manufacturing investments. However these areas are becoming vulnerable to the growing location competitiveness of Central and Eastern Europe (CEE). Some inward investors in Wales have already placed facilities in Central and Eastern Europe, and 'Welsh' jobs in electronics and automotive have already found their way to the Czech republic and Poland.

Table 7 shows FDI inflows into CEE over the period 1995-1999. Four CEE states accounted for 80% of FDI inflows. UNCTAD (2001a) estimates that FDI inflows into CEE increased to $25bn in 2000, up 9% on revised 1999 figures.

By far the most popular location in CEE has been Poland, which attracted 31% of the total FDI inflows to CEE over the period 1995-99. The Polish Agency for Foreign Investment (PAIZ) estimates that $10.6bn of inward investment was attracted in 2000. Much of the new investment (an estimated 43%) into Poland since 1990 has been in manufacturing sectors, with financial services accounting for 23%.

Other key destinations in CEE have been the Czech Republic and Hungary. In the former case increases in FDI inflows have largely resulted from an extensive privatisation programme. Leading investors in the Czech Republic are German and Austrian MNEs. Many Japanese producers of electronic consumer goods also have investments in the Czech Republic, and the location attractiveness of this area, in terms of factor costs, infrastructure, and labour productivity, poses a threat to existing Japanese consumer electronics investment in other parts of the EU. Sectors involved in the recent FDI growth in the Czech Republic include supermarkets, telecommunications, and the automotive sector (led by Skoda which is now part of VW).

Table 6 FDI Inflows into the EU-15 1996-1999 ($m)

	1996	1997	1998	1999	1996-99	% Share 1996-99
Austria	4426	2654	4567	2813	14460	1.8
Bel-Lux	14064	11998	22691	15862	64615	8.2
Denmark	742	2801	6716	7454	17713	2.2
Finland	1109	2114	12144	3023	18390	2.3
France	21960	23178	29495	39101	113734	14.4
Germany	6572	11097	21163	26822	65654	8.3
Greece	1058	984	700	900	3642	0.5
Ireland	2618	2743	8579	18322	32262	4.1
Italy	3546	3700	3065	4901	15212	1.9
Holland	15052	14463	41682	33785	104982	13.3
Portugal	1368	2278	2802	570	7018	0.9
Spain	6585	6375	11863	9355	34178	4.3
Sweden	5070	10963	19560	59968	95561	12.1
UK	**24435**	**33227**	**63649**	**82182**	**203493**	**25.7**
Total	108604	128574	248675	305058	790911	100.0

Source: UNCTAD (2000)