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Overview

Foreign direct investment (FDI) has grown over the past three decades to become a central force in global economic activity. While world nominal GDP has increased fourfold and world bilateral trade flows have grown more than sixfold since 1980, the stock of FDI has swelled by roughly 20 times over from an already reasonably large base. Today the global sales of foreign affiliates of multinational corporations (MNCs) equal roughly two times the amount of total world exports, making foreign investors considerably more important than trade in delivering goods and services around the globe. Within the realm of trade, MNCs are the largest players in arm's-length transactions, and one-third of the movement of goods and services across borders takes place within their intrafirm networks. MNCs account for about half of the world's total research and development (R&D) expenditure and more than two-thirds of the world's business R&D. The bulk of technology flows between countries takes place within the confines of MNC production systems.

The Peterson Institute for International Economics (PIIE) has launched a twin effort to address the implications of this growing role of multinational corporate investment for the US economy. This study on outward FDI from the United States is a sister volume to the 2013 PIIE study on inward FDI into the United States by Theodore H. Moran and Lindsay Oldenski. These two volumes come to a common conclusion: The policy challenge in the years ahead is to create a more favorable setting for multinational investors to locate their best jobs, most beneficial operations, and most dynamic activities here in the United States. As US MNCs expand their global operations, they become more productive, expand output, hire more workers, and conduct more R&D at home and abroad. Thus it is in the interest of the United States to create a policy environment that encourages the growth of both US MNCs investing abroad and foreign MNCs investing in the United States.

While the increasing importance of multinational corporate investment in the international economy represents an opportunity, it also generates understandable apprehension. This study addresses one of the most widespread sources of apprehension—concerns about the consequences for the US home economy as American MNCs spread technology and reposition production around the globe.

The concern about outward investment by US multinationals is certainly not new. The origins go back to the Burke-Hartke legislation (sponsored by the AFL-CIO) in the 1970s and appeared to culminate—at least rhetorically—with Ross Perot's prediction in 1992 that the North American Free Trade Agreement would result in a "giant sucking sound" as jobs migrated south of the border. If today's rhetoric on the issue is slightly less colorful, it is often no less intense, with President Barack Obama earnestly pledging to end tax breaks for corporations that ship jobs overseas.[1]

But what does the evidence show to be the most beneficial US policy toward outward investment by US multinationals? The answer depends on whether outward FDI by these multinational firms—in expanded production and assembly and in the new phenomenon of more R&D conducted abroad—comes at the expense of home-country economic interests or whether, in contrast, this spread of US multinational activities around the globe complements and strengthens the home economy.

Apprehension about outward investment by US multinationals springs from three distinct fears: first, that such investment replaces production of goods and exports of products that might be undertaken at US MNC plants at home; second, that outward investment by US-based MNCs siphons away capital, replacing investment that might be made at home; and third, that the globalization of R&D weakens America's technological capabilities by placing those capabilities elsewhere. The common theme in each of these fears is that outward investment by US-based MNCs is a win-lose phenomenon that harms the American economy.

Each source of apprehension is subject to empirical analysis. For each of the three, it is possible to examine how the home operations of US MNCs have changed as these firms have expanded or contracted their foreign operations. Based on the observed behavior of some 1,500 US MNCs over two decades, we can address the question of whether the US economy would likely be better or worse off if US policies (in particular tax policy) were to be reconfigured to make it harder for US multinationals to carry out operations abroad.

This is the empirical investigation undertaken in this study. First, however, it is important to establish the importance of this issue for American policymakers by examining the role that US MNCs play in the domestic economy and by carefully tracing how their operations within the United States have evolved over time.

1. The statement by the president reads: "We don't need a President who plans to ship more jobs overseas, or wants to give more tax breaks to companies that are shipping jobs overseas." "Remarks by the President at a Campaign Event," White House press release, July 16, 2012, www.whitehouse.gov/the-press-office/2012/07/16/remarks-president-campaign-event (accessed on March 25, 2013).