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Frederick Cutler: 967-4415

U.S. DIRECT INVESTMENTS ABROAD

Direct-investment capital outflows do not produce rewards quickly, according to data from a comprehensive survey by the Commerce Department's Office of Business Economics.

The survey was designed to cover essentially all foreign direct investments by U.S. residents in 1966. Information on the directly measurable balance of payments transactions between direct-investment enterprises and their U.S. owners has just been published in U.S. Direct Investments Abroad, 1966, Part I: Balance of Payments Data.

Data from the survey point out that:

---Despite the very large increases in direct-investment outflows and in income paid to U.S. owners, the difference between the two flows has remained surprisingly stable, with income significantly above capital outflows.

---While a large part of the capital flow went to recently established affiliates, nearly 90 percent of earnings were produced by affiliates established before 1958. Although the reasons are complex, these findings suggest that in the short run direct-investment capital outflows do little to generate earnings or help the balance of payments by generating income payments. These calculations, however, do not take account of the impact of direct investment on trade nor of changes in other foreign claims and liabilities of corporations.

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Capital Flows

Net annual capital outflow for direct investment in 1966 was $4.3 billion, $3.65 billion higher than in 1950 -- the year OBE conducted the first complete postwar investment survey. Direct investors saw their combined revenues -- interest, dividends, branch profits, fees, royalties and rentals -- increase about $3.5 billion in the 16-year span. As a result, the surplus of income over direct-investment capital flow was reduced from $900 million in 1950 to $770 million in 1966.

The manufacturing sector registered the fastest increase in capital outflows--tenfold--from $192 million in 1950 to $1,966 million in 1966. Income returns to investors grew only fourfold, from $450 million to $1.6 billion.

Younger affiliates received over half of the net capital outflow in 1966 -- $2.4 billion. Firms acquired or established before 1958 received $1.4 billion. The older affiliates are less dependent on their U.S. parents as suppliers of capital since they generate a considerable portion of their capital requirements through reinvesting earnings, and providing for depreciation, depletion, and amortization reserves.

Earnings and Income Payments

Of the total net direct-investment earnings of $5.6 billion in 1966 nearly 90 percent was produced by affiliates established or acquired by their U.S. owners before 1958. Affiliates established or acquired from 1962 to 1966 accounted for less than 2 percent of all net earnings. For European Common Market countries, net earnings of affiliates acquired or established before 1958 were higher than total earnings because enterprises that were acquired or established after 1960 showed an aggregate net loss of $80 million.

About 90 percent of dividend and interest payments and branch profits came from affiliates predating 1958. Only about 2 percent of such payments came from affiliates organized or acquired in the 1962-66 period. In view of a similar pattern in earnings, this suggests a fairly steady payout ratio.

About the Survey

The survey data represent benchmark statistics covering 3,400 reporters and 23,000 foreign affiliates. They provide definitive measures of all direct-investment transactions for the year 1966 that are separately identified in the balance of payments accounts. The data are being used to assess the adequacy and efficiency of the sampling process used in estimating the balance of payments statistics on a current basis. The findings generally support the validity of earlier balance of payments estimates prepared for 1966 by OBE on the basis of the quarterly reports.

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The 1966 survey contains the most extensive breakdowns by industry, country, and type of transaction ever attempted.

Part I of the survey shows how much new capital was invested in 1966, and how much was transferred back to the United States in the form of dividends, interest, and branch profits or in the form of royalties, fees, and service charges. Also shown are U.S. owners' share in the earnings of these enterprises and the amount of such earnings reinvested in the foreign business. The total of new capital investment and reinvested earnings measures the net addition to the book value of U.S. owners' direct investment abroad.

Part II of the survey will be published later in separate segments based on the industry classifications of the U.S. owners. It will include data on the financial statements and operating statistics of the foreign affiliates.

Copies of U.S. Direct Investments Abroad, 1966-Part I: Balance of Payments Data may be purchased from the Superintendent of Documents, U.S. Government Printing Office, Washington, D.C. 20402 or from Field Offices of the U.S. Department of Commerce. 240pp. $1.75.

(Statistical tables attached.)

Table 1. -Capital Flows and Combined Income Receipts

(In millions of dollars; balance of payments outflows (-))

Area and country	Capital flows 1950	Capital flows 1966	Capital flows Change	Interest, dividends and branch earnings 1950	Interest, dividends and branch earnings 1966	Interest, dividends and branch earnings Change	Royalties and fees 1950	Royalties and fees 1966	Royalties and fees Change	Net flows 1950	Net flows 1966	Net flows Change
All countries total	-621	-4267	-3646	1294	3938	2644	231	1099	868	904	770	-134
Developed countries	-463	-3577	-3114	440	1520	1080	122	821	699	99	-1236	-1335
Canada	-287	-1336	-1049	294	725	431	35	222	187	42	-389	-431
Europe	-121	-1970	-1849	118	644	526	73	490	417	70	-836	-906
Rep. of So. Africa	-23	-28	-5	13	55	42	3	14	11	-7	41	48
Japan	-7	-54	-47	2	42	40	4	42	38	-1	30	31
Australia	-24	-175	-151	11	44	33	6	50	44	-7	-81	-74
New Zealand	-1	-14	-13	2	10	8	1	3	2	2	-1	-3
Less developed countries	-158	-690	-532	854	2418	1564	109	278	169	805	2006	1201
Latin American Republics	-45	-276	-231	513	911	397	65	155	90	533	790	256
Other Western Hemisphere	-6	-149	-144	10	165	155	1	12	11	5	28	22
Other Africa	-10	-80	-70	24	259	235	1	18	17	15	197	182
Middle East	-63	-68	-5	211	889	678	11	27	16	159	848	689
Other Far East	-9	-58	-49	84	125	41	31	46	15	106	113	7
International	-25	-60	-35	11	70	59	n.s.s.	22	22	-14	32	46

Note: Detail may not add to totals because of rounding.
n.s.s. - Not separately shown.

Table 2. Net Earnings and Net Capital Flows for 1966, by Year of Establishment or Acquisition of Foreign Affiliate

(In millions of dollars)

Area and Country	Total	Year of Establishment or Acquisition									
		1957 and prior years	1958	1959	1960	1961	1962	1963	1964	1965	1966
Net Earnings for 1966:											
All countries, total	5614	4891	160	192	180	91	55	32	16	-18	14
Developed Countries	2590	2254	83	89	111	48	10	27	-22	-8	-5
Canada	1224	1088	14	10	24	25	9	16	13	20	3
Europe	1045	890	66	73	60	16	-8	19	-36	-28	-8
Common Market	362	372	20	22	29	-7	-24	-4	-24	-15	-5
Other Europe	683	518	46	51	32	23	15	23	-12	-12	-3
Republic of South Africa	111	89	1	3	13	1	1	2	**	**	1
Japan	80	72	**	1	4	6	2	-5	1	-1	-1
Australia	115	102	2	2	9	**	5	-3	-1	**	**
New Zealand	15	13	**	**	1	**	1	-2	1	1	**
Less Developed Countries	3025	2637	77	102	69	43	45	5	37	-11	21
Latin American Republics	1193	1037	34	26	26	26	10	-10	34	5	3
Other Western Hemisphere	200	161	1	5	16	4	2	5	6	**	1
Other Africa	272	256	8	15	7	-2	2	-13	-2	1	1
Middle East	941	907	6	28	3	1	-5	19	-10	-15	6
Other Far East	186	123	10	2	5	12	24	-	3	3	4
International	233	153	18	26	12	2	12	4	6	-5	6

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Table 2. Net Earnings and Net Capital Flows for 1966, by Year of Establishment or Acquisition of Foreign Affiliate

(In millions of dollars)

Area and Country	Total	Year of Establishment or Acquisition									
		1957 and prior years	1958	1959	1960	1961	1962	1963	1964	1965	1966
Net Capital Flows for 1966 (outflows (-)):											
All countries, total	-4267	-1371	-95	-107	-118	-134	-175	-270	-336	-603	-1059
Developed Countries	-3577	-1382	-61	-66	-77	-120	-155	-199	-267	-469	-780
Canada	-1336	-804	-16	-8	-13	-11	-38	-54	-148	-148	-97
Europe	-1970	-537	-41	-55	-65	-75	-119	-104	-105	-261	-606
Common Market	-1229	-342	-32	-40	-23	-63	-84	-40	-63	-85	-456
Other Europe	-741	-195	-10	-15	-42	-12	-35	-63	-43	-175	-150
Republic of South Africa	-28	-15	-1	**	3	**	-2	-1	-3	**	-8
Japan	-54	-24	**	**	**	-5	**	-11	-3	**	-11
Australia	-175	9	-3	-3	-2	-29	5	-28	-8	-59	-58
New Zealand	-14	-11	**	**	**	**	-1	-1	**	-1	**
Less Developed Countries	-691	12	-35	-40	-40	-13	-22	-71	-69	-134	-279
Latin American Republics	-276	69	-24	-44	-2	-2	-33	-21	-39	-45	-134
Other Western Hemisphere	-149	-55	-17	**	-8	1	**	-6	-16	-4	-45
Other Africa	-80	36	-4	**	-22	-12	-2	-31	-2	-22	-23
Middle East	-68	-57	**	-6	-1	**	6	2	-6	-3	-2
Other Far East	-58	27	-3	-2	-	1	-5	-11	-7	-26	-31
International	-60	-8	13	12	-7	-1	12	-4	1	-34	-44

Note: Detail may not add to totals because of rounding.

** Less than $500,000.

Problems of presentation

This new presentation of the balance of payments reflects the results of a review begun last year by the Interagency Committee on Balance of Payments Statistics convened by the Office of Management and Budget. There had been growing dissatisfaction with the presentation and analysis focusing on the liquidity balance and the official reserve transactions balance.

The "official" balance is a rough proxy for exchange market pressures on the dollar resulting from transactions with the United States. But the exchange market and the balance are subject to large and erratic shifts as interest rates change, here and abroad, and as expectations about currency rates shift. Thus, although this balance might be the most important indicator of changes in our external position over the longer run, it is too volatile to serve in the short run as an indicator of underlying, more fundamental developments.

The liquidity balance, reflecting changes in U.S. reserves and in liquid liabilities to all foreigners, had served for a number of years as a rough indicator of underlying trends. However, two developments reduced its usefulness. For one thing, it was distorted by special financial transactions. The most important group of these transactions shifted funds--mostly of foreign official agencies--from liquid to nominally nonliquid categories, improving the recorded liquidity balance but having no real impact on the underlying liquidity position.

A second development reducing the usefulness of the liquidity balance occurred in 1969. Tight monetary policy in the United States, combined with certain U.S. banking regulations, resulted in heavy Eurodollar borrowing by U.S. banks through their foreign branches, which in turn attracted funds from the United States. As a result, there were large outflows (mostly unrecorded) of U.S. funds to the Eurodollar market accompanied by large inflows through the foreign branches of U.S. banks. The increase in liquid liabilities to foreigners enlarged the liquidity deficit. However, the increase in U.S. residents' liquid claims on foreigners which resulted from the flow of U.S. funds to the Eurodollar market is not treated as an offsetting item in the calculation of the liquidity deficit as defined. The problem of definition was compounded by the fact that the outflows were largely unrecorded.