LATIN AMERICA: Commodity prices will weigh on FDI

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Abstract

The outlook for inward FDI.

A drop in foreign direct investment (FDI) in Latin America and the Caribbean in 2014 marked a change of trend, according to a report released on May 27 by the UN Economic Commission for Latin America and the Caribbean (ECLAC). The decline, attributed principally to lower commodity prices, was the first since 2009 and is likely to persist this year.

Full text

SUBJECT:The outlook for inward FDI.

SIGNIFICANCE:A drop in foreign direct investment (FDI) in Latin America and the Caribbean in 2014 marked a change of trend, according to a report released on May 27 by the UN Economic Commission for Latin America and the Caribbean (ECLAC). The decline, attributed principally to lower commodity prices, was the first since 2009 and is likely to persist this year.

ANALYSIS: Impacts.

At 2.6% of GDP, inbound FDI in 2014 was its lowest since 2009 and will remain slightly below its long-term average this year.

Lower commodity prices reduced average returns on FDI to around 5% in 2014, down from over 9% in 2006-08; no rapid upturn is likely.

Most investment abroad by LAC companies is within the region and, in 2015, will continue to be constrained by its sluggish growth.

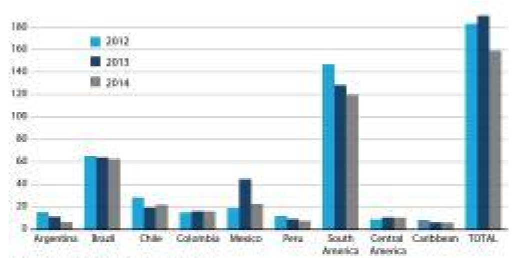
In its new report, Foreign Direct Investment in Latin America and the Caribbean 2015, ECLAC estimates that FDI in the region -- excluding Caribbean financial centres -- reached 158.8 billion dollars last year, down by 16.4% from a record 190.0 billion dollars in 2013 (see LATIN AMERICA: Brazil will weigh on regional FDI - June 10, 2014).

This marks a break in a decade-long increase. Drops in 2006 and 2009 were followed by a rapid recovery. Investment in natural resources and services and manufacturing for the domestic market led FDI.

Share of global FDI.

Based on UNCTAD data, ECLAC estimates that global FDI dropped by 7% in 2014 to some 1.3 trillion dollars, but that flows into developing economies rose by 5%.

This was the result of a 15% increase in FDI in Asia, with China and Hong Kong as the world's two largest recipients, while the drop in Latin America and the Caribbean (LAC) reduced its share of global FDI to 13%, down from 14% in 2012 and 2013, albeit still well above an average of 7% in 2005-09.



Inbound FDI, 2012-14 (billion dollars)
Source: ECLAC

Mexico.

At 49%, the drop in Mexico was one of largest in the region after Venezuela (88%) and Bolivia (63%). This was due largely to two one-off factors:

It reflected comparison with an unusually high figure in 2013, boosted by the 13.2 billion dollars paid by Belgium's AB InBev for the 50% of the Modelo brewery it did not yet control.

In 2014, US-based AT&T had to sell its stake in the America Movil telecommunications company for regulatory reasons. This divestment alone reduced net FDI by 5.6 billion dollars.

ECLAC noted that, as a two-year average, FDI in Mexico in 2013-14 was a record. Given the large number of manufacturing projects announced, particularly in the car industry, it anticipates a possible increase this year (see MEXICO: Auto industry enjoys strong momentum - April 17, 2015).

Further, regulatory changes will facilitate investment in some service industries

South America.

In 2014, FDI in South America dropped 7% to 119.5 billion dollars, down from 128.3 billion dollars in 2013 and a peak of 146.9 billion dollars in 2012. There were wide variations in the performance of different countries:

Brazil .

FDI in Brazil declined for the third consecutive year, according to the report -- which did not use a new methodology introduced recently by the Brazilian government which gives a substantially higher figure.

The 2% drop to 62.5 billion dollars reflected a 58% reduction in investment in natural resources to 7.0 billion dollars, attributed principally to the impact of lower oil prices on investment in the hydrocarbons sector.

On the other hand, investment in the car industry reached a record 4.2 billion dollars while investment in services, principally retail, telecommunications and financial services, increased 27% to 33.1 billion dollars.

Chile.

With an increase of 14% to 22.0 billion dollars, Chile was the only major LAC country where FDI rose. This occurred despite lower copper prices and was apparently at odds with an overall 6.1% contraction of investment, measured as gross fixed capital formation (see CHILE: External factors condition economic outlook - February 23, 2015).

Around half of the inflow corresponded to mergers and acquisitions through which local groups divested of important assets in what was interpreted in Chile as a sign of their lack of confidence in the economy's prospects.

Colombia .

At 16.1 billion dollars, FDI in Colombia showed little change on 2013. In recent years, investment there has diversified significantly away from natural resources into services and manufacturing. This has helped to cushion it against the drop in commodity prices that was a key factor in lower FDI in, for example, Peru.

Central America.

FDI figures for Central America, where there was a drop of 2% last year, are explained largely by Panama which accounted for 45% of the sub-region's inflow of 10.5 billion dollars. Panama has Latin America's highest FDI/GDP ratio (followed by Chile), a trend that is expected to persist due to expansion of the Panama Canal.

El Salvador saw a 53% increase in FDI, albeit from only 179 million dollars in 2013, due largely to investment by a US-based LED manufacturer. Other Central American countries, except for Costa Rica, also saw small increases.

Caribbean .

In 2014, FDI in the Caribbean was down for the second consecutive year, dropping by 5% to 6.0 billion dollars. This reflected principally a 30% reduction in FDI in Trinidad and Tobago to 1.4 billion dollars, attributed mainly to lower oil prices.

On the other hand, FDI in the Dominican Republic, the sub-region's other large recipient, increased 11% to 2.2 billion dollars, reflecting a more balanced inflow that includes manufacturing, tourism and other services as well as natural resources.

Outbound FDI .

In 2014, FDI by Latin American companies investing abroad -- the so-called trans-Latins or "multilatinas' -- dropped to 29.2 billion dollars, down from 33.3 billion dollars in 2013 and a peak of 49.4 billion dollars in 2012 (see LATIN AMERICA: Record FDI is balance-of-payments risk - May 16, 2013).

The largest outflow was from Chile where it reached 12.1 billion dollars, up from 10.3 billion dollars in 2013, followed by Mexico, with 7.6 billion dollars, albeit down from 13.1 billion dollars in 2013, and Peru, with 4.5 billion dollars, up from 1.2 billion dollars.

CONCLUSION: ECLAC anticipates that FDI in the region could drop by up to 10% this year. This reflects not only lower mineral and oil prices but also the impact of the region's weak growth -- which it is currently forecasting at 1%, similar to its level in 2014 -- on manufacturing and services projects targeting domestic markets. This would represent a significant setback for the region's future growth capacity and, particularly because of manufacturing and services, the labour market.

Details

Subject	Economic conditions; Automobile industry; Foreign investment; Gas industry; Economic growth; Manufacturing; Metal industry; Mining industry; Natural resources; Petroleum industry; Prices; Service industries; Commodity markets
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