

Multinationals, Foreign Direct Investment and the New Regionalism in the Americas

Lorraine Eden

Professor of Management, Mays Business School, Texas A&M University, United States.

Summary

Regional integration agreements involving countries in the Americas have grown exponentially since the late 1980s. As a result, multinational enterprises now face a complex network of overlapping agreements with different rates, rules and dispute settlement procedures. How have firms responded to the spread of regionalism throughout the Americas? In this paper, we provide a broad overview of public policy changes and their impacts on multinationals and foreign direct investment in the Americas.

Earlier versions of this paper were presented at the Third IDB/CEPII Conference, "The New Regionalism" Progress, Setbacks and Challenges", Inter-American Development Bank, Washington, DC, February 9-10, 2006, and as a keynote address at Texas A&M International University's 11th Annual Conference "Global Trade & Investment Challenges for Western Hemispheric Development", Laredo, Texas, April 4-8, 2006. I want to thank Dan Li for her research assistance on an earlier version of this paper, and also thank Christian Daude, Alan Rugman and the conference participants for their helpful comments.

I. INTRODUCTION

Thirteen years have passed since the North American Free Trade Agreement (NAFTA) came into force on January 1, 1994. It has been 16 years the Southern Cone Common Market (MERCOSUR - *Mercado Común del Sur*) liberalized trade among Argentina, Brazil, Paraguay and Uruguay in 1991. Across the Americas, governments have cut trade barriers, privatized state-owned enterprises and opened previously closed sectors to foreign direct investment (FDI). Multinational enterprises (MNEs) now move more freely throughout the Western Hemisphere than in any time since perhaps the late 1800s. Tariff barriers are at historic lows in most products and countries. Governments

compete for FDI in "beauty pageants", using locational subsidies to attract inward, particularly knowledge-intensive, investments. The 1990s may have been a "golden era" for the MNE in terms of its ability to access host-country markets and resources.

Is the golden era over? There are some signs the pendulum is beginning to swing, and that MNE-state relations may be less cooperative over the next 10 years than they have been over the past 15 years. Raymond Vernon [1998] argued that economic, political and sociological forces would make MNE-state relations in the early years of the 21st century more confrontational than in the 1990s. He saw the late 1990s as the "eye of the hurricane"; he may have been prescient. Political roadblocks to FDI flows are starting to appear. The tightening of United States (US) border controls in response to terrorist attacks, illegal migration, and drugs trafficking is one sign. The election of socialist, anti-FDI governments in some South American countries, together with the slowdown in privatization of state-owned enterprises, is another. The paralysis of the Free Trade Area of the Americas (FTAA) and the failure of the World Trade Organization (WTO) Doha Round negotiations may be a third sign. On the other hand, the notification of regional trade agreements (RTAs) to the WTO continues unabated. Over 180 agreements are now in force, with many others under negotiation (Crawford and Florentino [2005]).

Because RTAs have multiplied over the past 15 years, MNEs now face a complex network of overlapping agreements with different rates, rules and dispute settlement procedures. How have MNEs responded to the spread of regionalism throughout the Americas? In this paper, we examine foreign direct investment patterns and the strategies of multinational enterprises as the Americas have become more closely linked through a "spaghetti bowl" of regional trade agreements.

II. CAUSE: THE CHANGING POLICY ENVIRONMENT

The policy environment for foreign direct investment has liberalized significantly over the past 16 years, at all levels -national, bilateral and regional-.

In 1994, I compared the formation of NAFTA to the removal of blocks scattered across a chessboard (Eden [1994] p. 193):

"Imagine a chessboard where, in addition to the chess pieces, there are immovable blocks scattered across the board. The impediments are more numerous in the middle of the board. Two players can maneuver the chess pieces around the blocks but clearly the game is less efficient than one without such barriers. Individuals who play regularly become skilled at taking the barriers into account in their game strategies. Some will hide behind them, others develop methods of avoiding the blocks, others use them to obstruct their opponents. Now suppose the rules of the game are changed and most of the blocks are removed. Several things happen. In the short run, some old strategies no longer work and individuals may lose games that they usually won. Costs are incurred in learning new strategies. It is possible that people who played the old game regularly may adapt more quickly to the new board, or perhaps new players without the handicap of history adapt more quickly. It is probable that flexibility and scanning ability will be key factors affecting success. In the long run, the game should be faster and the players more efficient. The question is: are we better off after removing the blocks?"

The analogy holds now, many years later, throughout the Americas due to the spread of regional integration schemes, the reduction in trade barriers, and the liberalization

of FDI regulations. MNEs move more freely throughout the Americas than in any time in memory. These changes have taken place at the regional, bilateral and national levels.

THE PROLIFERATION OF RTAs

One of the features of the new policy environment is the proliferation of regional accords on a worldwide basis. Currently, over 170 RTAs are in force worldwide, with an additional 70 RTAs "estimated to be operational although not yet notified", according to the WTO website (http://www.wto.org/english/tratop_e/region_e/region_e.htm). The website estimates that the total number of RTAs could reach 300 agreements this year.

This *ad hoc* proliferation of RTAs has been likened to a "spaghetti bowl" mixture of bilateral, trilateral and multilateral RTAs (IDB [2002]). The rapid proliferation of RTAs considerably complicates the analysis of their economic effects. A key problem is the creation of hub-and-spoke arrangements (Eden and Li [2004]). In the simplest hub-and-spoke pattern, one country (the hub) has bilateral RTAs with two other countries (the spokes). Trade barriers are eliminated within each RTA but not between RTAs. If the welfare impacts of the two hub-and-spoke RTAs are compared to the trilateral RTA, the benefits are clearly higher with the trilateral RTA. Two bilaterals leave trade barriers in place between the spokes, benefiting the hub; whereas one trilateral removes these intraregional barriers (Eden and Li [2004]; Wonnacott [1996]).

Moreover, due to the greater complexity, potential for rent-seeking behavior and inconsistencies of a hub-and-spoke system, administrative and transport costs will be higher. Instead of one tariff rate for one product, rates will vary depending on the RTA. Different rules of origin can apply to the same product. These inconsistencies encourage "treaty shopping"; firms will exploit arbitrage opportunities, searching for the lowest rates and raising the cost of administering the RTAs. Not only trade flows but also FDI can be affected (Eden and Li [2004]). Hub-and-spoke arrangements create "who is whose" problems that increase protectionism and reduce the overall welfare gains from RTAs (Bhagwati, Greenaway and Panagariya [1998]; IDB [2002]; Wonnacott [1996]). The welfare gains will also be distributed more unevenly. The hub country gains at the expense of the spokes because it has preferential access to all member countries. As a result, hub-country firms have duty-free access to buy and sell in spoke markets. Spoke-country firms, on the other hand, are relatively disadvantaged. They do not have duty-free access to other spoke markets; they face more competition in the hub market from the other spoke-market firms; and they are less competitive relative to hub firms because their input costs are higher (Harris [2005]).

THE NEW REGIONALISM IN THE AMERICAS

The new RTAs are so different from the old agreements that policy makers now distinguish between "old regionalism" and "new regionalism" (Devlin and Estevadeordal [2001]; Eden and Li [2004]; IDB [2002]; Iglesias [2002]). In North America, the old regionalism began with the 1965 Auto Pact, which removed cross-border trade barriers in autos and auto parts. In 1989, the Canada-US Free Trade Agreement (CUSFTA) extended the integration process to goods, business services and investments in almost all sectors of both economies. In 1990, President Salinas de Gortari of Mexico approached US President George H. W. Bush about a bilateral free trade accord, which subsequently became the 1994 NAFTA. This launched the first north-south RTA in the Western hemisphere. By

January 2003, with some exceptions for agricultural products, merchandise trade flows among the three countries have been basically tariff free.

In Latin America, the old regionalism was a complement to import substitution industrialization (ISI) strategies, enabling Latin American countries to lessen trade and FDI barriers among themselves while keeping (or raising) them against outsiders. Thus, the old regionalism was a substitute for taking part in the multilateral trading system (Ethier [2001]). Because of the protectionist, inward-looking motivations behind the old regionalism, early RTAs in Latin America, such as the Central American Common Market (CACM), the Latin American Free Trade Area (LAFTA), the Andean Group and the Caribbean Community (CARICOM) generated little crossborder trade or investment.

The new regionalism in Latin America began with the signing of MERCOSUR in 1991. In Latin America, MERCOSUR dominates the field of RTAs. It is quite different from NAFTA. NAFTA is a free trade agreement (FTA) that uses rules of origin to control duty-free access to national markets. MERCOSUR, on the other hand, is a customs union with a common external tariff. NAFTA has wide-ranging commitments to free trade in goods, business services, intellectual property and capital; whereas MERCOSUR is much weaker and remains primarily about trade in goods.

When the US Congress failed to extend fast track authority to President Clinton in 1995, leaving Chile out in the cold, the US withdrawal left the regional integration field wide open to other countries. Chile and other small Latin American countries responded by signing multiple RTAs. Mexico, for example, has signed bilateral RTAs with Chile, Bolivia, Costa Rica, the European Union (EU), Nicaragua, Israel, among others. Chile has bilateral RTAs with Canada, Mexico, the US, Colombia, Ecuador, and associate member status within MERCOSUR. While most of these agreements have been within the region, others have not (e.g., with the EU).

Finally, after many years of sitting on the sidelines watching other countries negotiate RTAs, the US government switched its course and begun negotiating with multiple countries after the enactment of the Trade Promotion Authority (TPA) in August 2003 (Cooper [2005]). The most important set of negotiations have been the 34-country FTAA agreement, which was supposed to conclude by 2005 and is now in limbo. In terms of smaller agreements, in January 2004, US free trade agreements with Chile and Singapore entered into force. Agreements with Australia and Morocco were signed and approved by Congress in 2004; the Australian agreement went into force in January 2005, while the Bahrain agreement has not yet been implemented. Trade agreements with the Central American countries and the Dominican Republic were combined into one agreement: US-Dominican Republic-Central America Free Trade Agreement (DR-CAFTA) that was approved by Congress in August 2005. The US is currently negotiating RTAs with Thailand, Panama, the Andean countries, and members of the South African Customs Union (SACU).

A list of the RTAs in the Americas that have been notified to the General Agreement on Tariffs and Trade (GATT)/WTO and are currently in force is provided in Table 1.¹ The agreements are in chronological order, by category. Category 1 agreements involve trade in goods and are differentiated by type (e.g., customs union or free trade agreement); category 2 agreements involve services. Some RTAs involve both goods and services and enter into force simultaneously (e.g., Canada-Chile); others involve both types but start at different dates (e.g., NAFTA); and still others involve only goods (e.g., US-Israel) or services (e.g., US-Singapore). The rapid expansion of RTAs is clear from the

table: the list includes one agreement in the 1960s, two in the 1970s, three in the 1980s, 10 in the 1990s, and 30 so far since 2000.

BILATERAL LIBERALIZATION

The proliferation of regional trade agreements is not the only widespread policy change in the Americas. Since the late-1980s, there has been enormous growth in bilateral arrangements linking countries: bilateral investment treaties (BITs), double tax treaties (DTTs) and transnational arbitration treaties (TATs). These two-way FDI accords signal an "open door" policy for FDI in the Americas. An international investment regime, at the regional level, is being created, based on the General Agreement on Tariffs and Trade (GATT) norm of national treatment. Activities of foreigners within a country's borders now receive the same treatment as activities of nationals (Eden [1996a and 1996b]). This new regime applies not only to goods, but also to services, investments and intellectual property. The regime is also helping to backstop domestic reforms in Latin America. The key impact of these BITs, DTTs and TATs is an explosion of multiple overlapping agreements of differing degrees of breadth and depth throughout the Americas. Table 2 provides data on the numbers of BITs and DTTs for several countries in the Western Hemisphere as of 2002. Most countries on the list have signed significantly more BITs than DTTs, with a few exceptions (notably, Brazil, Canada, Mexico, the US). This probably reflects the greater difficulties involved in negotiating tax treaties between countries than bilateral investment treaties.

NATIONAL LIBERALIZATION

At the national level, regulatory changes affecting FDI have also been proliferating in the Americas. United Nations Conference on Trade and Development's (UNCTAD) Division of Investment, Technology and Enterprise Development (DITE) has been tracking regulatory changes affecting foreign direct investment since 1992. Eight types of regulations are tracked: Foreign ownership, Sectoral restrictions, Approval procedures, Operational conditions, Foreign exchange, Promotion (including Incentives), Guarantees and Corporate regulations. In each case, DITE determines whether the regulatory change is more or less favorable to FDI. Table 3 provides statistics on regulatory changes in the Americas between 1992 and 2002. Not surprisingly, given that most national governments have been engaged in substantial liberalization since the late 1980s, the same pattern is evident in the Americas. I separate the data into three regions (the Caribbean, Latin America and North America) and their totals.²

By far the bulk of regulatory changes, by number, were Latin American. DITE recorded 234 policy changes over the 1992-2002 period and 178 of these (76%) occurred in Latin America, followed by the Caribbean (14%) and North America (10%). In the Caribbean, all but two of the 32 FDI regulatory changes were pro-FDI; the two less favorable were by Bahamas in terms of approval procedures. In Latin America, 14 of the 178 regulatory changes (8%) were anti-FDI. These were primarily actions by Brazil, Argentina and Ecuador in the areas of foreign exchange, and FDI promotion. All 24 regulatory changes in North America were pro-FDI. Of the 234 FDI policy changes in the Americas identified by DITE for 1992-2002, fully 93 percent were pro-FDI.

Statistics on regulatory changes at the individual country level are presented in Table 4. The table provides a count measure of the number of regulatory changes affecting

FDI in the Americas in 1992-2002. For all three regions, more than 90% of the changes were categorized by UNCTAD as favorable to FDI. The countries with the highest percent of less favorable changes were Bahamas (40%), Chile (25%), Venezuela (22%) and Brazil (19%). Percentages can be misleading, however, where the numbers of regulatory changes are small. Some countries made large numbers of changes, including Ecuador with 19 regulatory changes (#1), Canada and Venezuela (tied as #2), and Brazil, Colombia and Peru (tied for #3).

THE SPECIAL CASE OF TAX HAVENS

Discussing FDI regulatory changes in the Americas would not be complete without at least a brief mention of the unique changes currently affecting tax havens in Latin America (Eden and Kudrle [2005]). Even before the radically transformed international environment after September 11, 2001, focused international attention on secret financial transactions and the role played by tax havens, the Organization for Economic Co-operation and Development (OECD) released a 1998 report, which argued that harmful tax practices had diverted FDI and taxable income away from its member countries. In 2000, the OECD issued a second report that put 35 countries on a blacklist as "non-cooperating tax havens". Tax haven governments were encouraged to sign a Collective Memorandum of Understanding with various commitments, including transparency and information exchange. By June 2004, all the Caribbean and Latin American tax havens on the OECD blacklist had signed OECD Memorandum letters, committing their governments to eliminating harmful tax practices. While this does not mean they must raise corporate income tax rates, the benefits to offshore banking and other financial activities will be curtailed. MNEs and wealthy elite families, the primary users of and beneficiaries from tax havens, should, as a result, find it more difficult to engage in income shifting. A short-term critical issue for the tax havens, particularly for the smaller island economies, is the administrative costs of implementing the OECD letters. Here, the OECD has promised financial and technical aid. A critical long-term issue for these governments is the development of other sources of long-term competitive advantage. For many of the smaller islands, tourism and some agricultural exports (e.g., bananas) are the only other competitive sectors in addition to the offshore sector. These countries face difficult choices ahead in terms of attracting FDI. Table 5 below provides information on which countries in the Americas have been affected by the harmful tax practices initiative.

III. EFFECT: CHANGING FOREIGN DIRECT INVESTMENT PATTERNS

FDI PATTERNS: PERFORMANCE VERSUS POTENTIAL

The effects of liberalization of trade and FDI regulations throughout the Americas is clearly tied to the explosion of FDI that occurred over the same time period. Table 6 provides data on the growth in FDI stocks in the Americas. Since FDI inflows are notoriously variable, and for small countries one investment can make a huge difference in its numbers, FDI stock data from UNCTAD are reported, for selected years. The last two columns in the table show the percentage share for individual countries of the total non-US FDI stock in the Americas in 1988 and 2004.

A few key points emerge from this table. First, is the astonishing growth in FDI inflows over the period. Second, is the relative stability of country shares in total inward FDI stock. The four largest countries in terms of inward FDI stock are the US, Canada, Brazil and

Mexico, in that order. While the order has not changed over the period, Canada's share has fallen significantly from 19% in 1988 to 11% in 2004 of the Americas FDI stock. Looking at country shares of the total non-US FDI stock in the Americas even more clearly accentuates the Canadian loss: its share falls from 50.32% in 1988 to 29.6% in 2004. The third NAFTA partner, Mexico, on the other hand, has seen its share of the non-US total rise from 8.7% to 17.8%. Another country that has seen its share of the non-US total fall by more than two percentage points between 1988 and 2004 is Brazil (16.9% to 14.7%). While its share of all FDI in the Americas is up slightly, its share of the non-US FDI has fallen, suggesting that Brazil is not keeping pace with the rest of the non-US Americas. On the other hand, six countries have significantly raised their share of non-US FDI in the Americas: Argentina (3.6% to 5.2%), Chile (2.1% to 5.3%) and Venezuela (1.3% to 4.2%) and three tax havens (Aruba, British Virgin Islands, and the Cayman Islands).

Simple statistics on FDI stocks and flows may mask underlying patterns. For example, small countries may have small stocks of FDI but the stocks may be large relative to the size of the economy. For this reason, DITE has been calculating FDI potential and performance indices for countries since 1988. We examine the DITE indexes for the Americas over this period.

Table 7 reports on FDI potential indexes for the Americas, as measured by UNCTAD. These indexes proxy country attractiveness for inward FDI. UNCTAD calculates an average of 12 measures,³ which have been shown to be related to FDI, including Gross Domestic Product (GDP) *per capita*, the rate of GDP growth, exports/GDP, telephones *per capita*, energy use *per capita*, RandD/GDP, tertiary education, country risk, and share of world inward FDI stock I report data for 1988-1990 (15 years ago) and the two most recent available periods (1999-2001 and 2001-2003). Raw scores, ranking out of 140 countries and rankings within the Americas are reported. The US and Canada rank #1 and #2, respectively, followed by the Bahamas and Chile. At the bottom of the list in terms of FDI potential is Haiti, followed by Nicaragua.

DITE calculates inward FDI performance indexes on a rolling three-year average. The index ranks countries by the FDI they receive relative to their economic size, as the ratio of a country's share in global FDI inflows to its share in global GDP.⁴ A ratio greater (less) than one indicates that a country receives more (less) FDI than its relative economic size. A negative score means that foreign investors have disinvested in that period.

Table 8 shows the raw score, the country ranking out of all 140 countries, and the country ranking within the Americas for three periods: 1988-1990 (for a 15-year comparison) and the two most recent periods available 1999-2001 and 2002-2004. The big performers in terms of consistently attracting high levels of inward FDI relative to their economic size (indexes over 2) since 1999 have been Bolivia, Chile, Guyana, Jamaica, and Nicaragua. The countries least attractive to FDI relative to their size, since 1999, have been Suriname (#26 out of 26 in all three periods), Haiti (#25 out of 25 in all three periods), Guatemala and Paraguay.

EMPIRICAL WORK ON FDI RESPONSES TO REGIONAL INTEGRATION

Theoretical Framework

International trade economists have long studied the welfare impacts of RTAs, generally focusing on the customs union case, where the member countries reduce internal tariffs to zero and erect a common external tariff (Baldwin and Wyplosz [2003]; Bhagwati, Greenaway and Panagariya [1998]; Bhagwati and Panagariya [1996]; Brown, Kiyota and

Stern [2005]; Lipsey [1960]). The literature on the effects of regional integration on FDI patterns is considerably smaller than that on the trade effects; see, for example, Globerman [2002], Krueger [2000], Markusen [2004], and Yeyati *et al.* [2002].

Figure 1 outlines the theoretical framework used by most researchers (Buckley *et al.*, 2004; Eden [1994 and 2002]; Vernon [1994]; Levy Yeyati *et al.* [2002]). Two or more countries are assumed to form a preferential trading agreement, whereby they eliminate tariffs between themselves, but leave tariffs against non-member countries. The key issue is how trade and FDI patterns are affected inside and outside the RTA as "insiders" (countries and firms within the RTA) and "outsiders" (countries and firms outside the RTA) adjust to the new regional grouping.

The effects of regional integration on FDI can be analyzed from two angles - investment creation and investment diversion (Eden and Li [2004]). *Investment creation* occurs when the fall in trade barriers within the RTA causes a shift from lower-profitability investments to higher-profitability investments within the region. (This is the investment equivalent of trade creation; similarly, investment diversion is the equivalent of trade diversion). In addition, firms from outside the region, which had been exporting to countries inside the region before the RTA, may switch from exports to FDI in response to the larger regional market. This is also investment creation.

Investment diversion occurs when the RTA causes a shift away from higher-profitability external investments to lower profitability internal investments because the investments outside the region have become uncompetitive in the internal market (Eden and Li [2004]). In other words, if the RTA causes a diversion of investments into the region that were previously made in a nonmember country, this is investment diversion. An example is the movement of "cut-and-sew" garment firms from the Caribbean to Mexico in the mid-1990s when NAFTA gave Mexico preferential access to the US market.

Taking micro-level considerations into account, the effects of an RTA on FDI become more complicated and uncertain. Transport costs and plant-level economies of scale are two major concerns. Where transport costs are low and economies of scale large, insider firms are likely to concentrate production and supply the entire North American market from one location, reducing intra-RTA FDI. On the other hand, segmenting production stages and setting up vertically integrated plants to take advantage of factor price differences across member countries can lead to the increase in intra-RTA FDI. Thus, the production-location decisions of MNEs involve a tradeoff between the advantages of being close to the customer (which encourages market-seeking FDI) and the advantage of concentrating production to take advantage of scale economies (which encourages exports).

To the extent that investments by firms in one member country were originally made in another member country for tariff-jumping reasons, their reason for existence disappears once a RTA is introduced. As a result, disinvestments can occur. Big tariff cuts and large plant-level economies of scale cause firms to centralize production, lowering FDI and raising trade flows within the region (Eaton *et al.* [1994]). However, declining tariff rates do not automatically lead to FDI outflows because other locational attractions (e.g., a high-income market) may be more important than tariff cuts. For instance, Feinberg and her colleagues (1998) found that as Canadian tariff rates fell, US MNEs increased their capital and employment in Canada, contradicting the view that tariff liberalization would lead to an exit of US firms from Canada.

Moreover, MNE responses to regional integration in the Americas must be differentiated into two groups, as regional integration is less advanced in Latin America

than in North America. First, North American multinationals have engaged in locational reshufflings, designed to bring Mexico into a rationalized regional production pattern for the continental market post-NAFTA. That process is now mainly complete, especially for manufacturing firms (Baldwin, Caves and Gu [2005]). Future reshufflings will depend on subsequent deepening of NAFTA provisions (e.g., the removal of grandfathered sectors, disciplines over state/provincial subsidies, and harmonized tax treatment). Second, in South America and the Caribbean, the regional integration process is much less advanced. As a result, MNEs are still engaged in market-seeking investments, with some rationalization underway in the larger RTAs such as MERCOSUR (Chudnovsky and Lopez [2004], Frischtak [2004]). The largest Latin American MNEs are now reaching out beyond Latin America and establishing foreign affiliates in North America. As a result, a new group of regional MNEs are being created (Rugman [2005]).

The type of FDI in the Americas is also changing. Historically, business service sectors such as finance, insurance and banking, and public utilities such as telecommunications, hydro and electricity were closed to foreign investors. With the wave of privatizations in Latin America over the 1990s, and the inclusion of service sector provisions in RTAs and the Uruguay Round, these sectors have seen massive inflows of FDI over the past 15 years. At the same time, the information technology revolution (e.g., the Internet) has increased the mobility of services. Services are now being outsourced and off-shored in ways that were not possible 15 years ago. As a result, FDI in services now exceeds FDI in manufacturing (UNCTAD [2005]). We now see locational shufflings designed to rationalize the provision of business services within the MNE network, repeating the earlier pattern of rationalization of manufacturing plants. Economies of scale and scope, together with agglomeration economies, support the creation of regional headquarters, to direct and monitor the MNE's regional production network.

The Gravity Model

The impact of an RTA depends on characteristics of the host countries that make them more or less attractive than their RTA partners as a potential location of foreign investment (IDB [2002]). Researchers usually model the economic impacts of an RTA using a modified form of the gravity model originally developed to explain bilateral trade patterns, as below:⁵

$$\text{TRADE}_{ij} = \text{GDP}_i + \text{GDP}_j + \text{DISTANCE}_{ij} + \text{TRADE}_{ij} + \text{RTA} + Z \quad (1)$$

The gravity model assumes that trade between countries *I* and *J* is positively related to their GDPs (and/or their *per capita* GDPs) and negatively to the DISTANCE between them. FDI is assumed to be either a substitute or complement to trade flows (TRADE). A dummy variable (RTA) is added to the equation to test for the impact of the agreement. A vector *Z* of control variables that could also potentially explain FDI patterns is included to test for confounding hypotheses.

The gravity model has been used in several FDI studies, for example, Frankel and Rose [2002]; Harrigan [2001]; Hejazi and Pauly [2005]; Hejazi and Safarian [2005]; Krueger [2000]; Levy Yeyati *et al.* [2003], Di Mauro [2000], and Stein and Daude [2001]. The models show that FDI is strongly attracted to countries with large domestic economies and high levels of real per-capita income (Globerman and Shapiro [2002]; Graham [1999]). MacDermott [2002] applies both the traditional gravity model and the knowledge-capital model to analyze bilateral OECD FDI data from 1980-1997, and finds that implementing NAFTA led to an increase in FDI into member countries, particularly

for Mexico. Since NAFTA was mainly about adding Mexico to the preexisting Canada-US FTA, this result was not surprising. Levy Yeyati *et al.* [2002] show that the economic gains are smaller for countries that are less developed, closed to international trade, and unattractive to FDI.

RTAs appear to benefit member countries (insiders) and have little or negative effects on non-member countries (outsiders). Bertrand and Madariaga [2002], using panel data on US FDI in NAFTA and MERCOSUR between 1989 and 1998, find that regional integration affects US firms' location patterns. That fact that the US is an insider in NAFTA and an outsider in MERCOSUR matters for location decision. Their regression results indicate significant positive relationship between US (insider) FDI and the NAFTA dummy variable, but no relationship between US (outsider) FDI and the MERCOSUR dummy. Monge-Naranjo [2002] compares the effect of NAFTA on flows of FDI received by Mexico (an insider) and the countries in the region that were not included in NAFTA (regional outsiders). He finds that, with the exception of Costa Rica, the Central American outsiders lagged behind Mexico after NAFTA was formed. The most severe bias occurred in textile and apparel sectors, which represented most of the FDI flows in Honduras, El Salvador and Guatemala. Costa Rica appears to be the exception because its production of electronic components and medical equipment continued to attract US FDI.

FDI impacts may also vary depending on whether the motive for investment is horizontal FDI (replication of plants to satisfy the local market) or vertical FDI (linked production along the value chain). A major advantage of regional integration is the creation of economies of scale gains from replacing several small national markets with one large regional market. To the extent that an RTA merges several small markets into one, one might expect horizontal FDI (locational shufflings for efficiency reasons) to be the primary response by MNEs to the formation of the regional agreement (Markusen [2004]; Di Mauro [2000]). However, Levy Yeyati *et al.* [2003], in examining bilateral FDI patterns between 20 OECD countries and 60 host countries 1982-1998, find that RTAs tend to promote vertical over horizontal FDI. Waldkirch [2001] also finds that vertical integration explains the large increase in FDI in Mexico after NAFTA. Similar results are reported by Aizenman and Marion [2004] and Hanson, Mataloni and Slaughter [2001]. Moreover, location choices of multinationals are also affected by their national origins. Makhija and Williamson [2000] argue that, since US industries are mostly multidomestic, US MNEs are more likely to duplicate production activities across countries (horizontal FDI) and be less vertically integrated than MNEs from other OECD countries.

Few econometric studies focus on individual sectors and regional integration, probably because of FDI data limitations. The most important sector in terms of trade flows within NAFTA is autos and auto parts, representing between one-third and one-half of NAFTA trade (Eden and Molot [1992 and 1993]; Hunter *et al.* [1995]; Markusen *et al.* [1995]). The Canadian and US auto industries were not expected to see major location shifts after CUSFTA and NAFTA because of producers have had bilateral free trade since the 1965 Auto Pact. The key impacts were felt in Mexico as NAFTA opened and integrated the Mexican auto industry into the already integrated North American auto sector (Carrillo [2004], Eden and Molot [2002], Weintraub and Sands [1998]).⁶

Caveats and Conundrums

One difficulty in assessing the role of RTAs on FDI -particularly for a specific country's FDI- is there are many channels through which RTAs could potentially have

impacts on FDI flows (Levy Yeyati *et al.* [2002]). Confounding factors also make it difficult to separate out the impacts of regional integration from other macroeconomic and policy changes. The researcher must take these other explanations into account by including them as control variables in order to isolate the impact of the RTA on FDI patterns.

For example, *domestic economic reforms* can confound the analysis. For example, the 1994 peso shock and Mexico's 1993 law liberalizing inward FDI occurred concurrently with NAFTA. Graham and Wada [2000] find that Mexico attracted larger FDI inflows, starting in the late 1980s. Determining what exactly caused the FDI flows, however, was difficult since other confounding events occurred around the same time. In the late 1980s, Mexico not only joined the GATT, but also implemented many domestic policy reforms. The passage of NAFTA in 1994 was soon followed by the peso shock. In sorting out these various explanations, the strongest conclusion the authors could reach was that NAFTA probably kept FDI flows into Mexico from falling after domestic reforms had been fully implemented.

Globerman and Shapiro [2001] provide another example of how domestic economic reforms can confound the analysis. They identify two domestic explanations for Canada's declining share of inward FDI in North America: (1) higher taxes in Canada discouraged investment by domestic and foreign investors; and (2) Canada's declining capacity to innovate and support "new economy" activities discouraged FDI inflows. Moreover, confounding factors can have multiplier effects. Blomstrom and Kokko [1997] find the most positive impacts on FDI flows occur when regional integration occurs at the same time as domestic economic liberalization and macroeconomic stabilization. Harris [2005] also argues that FDI responses to regional integration can be offset by domestic policies. He uses simulation techniques to show how even a small amount of US protectionism can raise the cost of locating in Canada sufficiently high to cause the firm's preferred investment location to switch from Canada to the US.

FDI patterns are also affected by *factor costs and availability*. For example, US FDI flows into Mexico are clearly responsive to differences in US and Mexican unit labor costs in both the short and long runs. Similar influences affect US FDI in Canada, but are much weaker because labor costs are much closer (Eden [1994]; Love and Lage-Hidalgo [1999]). Market size and availability of resources are also critical factors influencing investment location (Bertrand and Madariaga [2002]; Eaton *et al.* [1994]; Eden [1994]; Harris [2005]). The different industrial composition of US FDI in Mexico and Canada suggests concerns about the extent to which Canada competes with Mexico in the US market may be overstated.

Exchange rate changes can also influence FDI patterns. Devaluations first in Brazil in 1999 and then later in Argentina in 2002 lowered export prices and raised import prices, causing large trade adjustments between the two countries. Devaluations can also provoke more direct forms of protectionism, for example, Argentina responded to its peso crisis by raising tariffs against Brazil. Since exchange rate swings can often be several magnitudes larger than tariff reductions, the impacts on trade and investment flows are likely to be much larger. Buckley *et al.* [2004] find the acceleration of changes in the exchange rate fostered US FDI into Canada. The degree of exchange rate volatility may be important. Di Mauro [2000] found that exchange rates only affected world-wide FDI patterns in the turbulent 1980s when FDI represented a way to reduce exchange rate risk. .

Lastly, when analyzing the economic effects of RTAs, it is important to distinguish between *de jure* and *de facto* liberalization. Start and end dates for trade agreements are often both fuzzy. Because RTA negotiations typically take several years,

some firms react during the negotiation period rather than wait for the outcome, hoping for first-mover advantages from pre-empting the competition. On the other end after the agreement is signed, reductions in trade barriers tend to be phased in over a transition period to give local firms time to adjust. In addition, many non-tariff barriers are grandfathered and some sectors (usually the most controversial, like agriculture) may simply be excluded from the agreement. So, it is hard to determine the true window for measuring the first-round investment effects.

IV. CONCLUSIONS

In this paper, we have provided an overview of changes in public policies towards multinationals and foreign direct investment in the Americas since 1990s. We explored the policy changes at the national and bilateral levels in the context of the spaghetti bowl of RTAs that now imperfectly links North and South America. We also investigated the changes in FDI patterns in the region, focusing on foreign investment performance and potential. Lastly, we reviewed recent empirical work using the gravity model to explain how changing regulatory patterns have influenced the FDI patterns of insider and outsider countries and firms.

One of the clear implications of our paper is that the spatial unit for the MNE is changing from the nation state to the macro-region (Eden and Monteils [2000]). We have argued that MNE responses to regional integration in the Americas must be differentiated into two groups because regional integration is less advanced in Latin America than in North America. North American multinationals have engaged in locational reshufflings, designed to bring Mexico into a rationalized regional production pattern for the continental market post-NAFTA. That process is now mainly complete, especially for manufacturing firms. On the other hand, in Latin America, the regional integration process is much less advanced. MNEs are still engaged in market-seeking investments, with some rationalization underway in the larger RTAs such as MERCOSUR.

From an economic perspective, the process of silent integration in the Americas appears inexorable (Eden and Molot [1992]). Perhaps Raymond Vernon [1998] was wrong and the Americas do remain in the eye of the hurricane. Yet, there are political storm clouds on the horizon with the election of populist leaders and rising anti-MNE sentiment in Latin America and the anti-off-shoring/anti-globalization movement in North America. This suggests that MNE-state relations will continue to be a vital topic for researchers, policy makers and MNE managers in the 21st century.

Notes

¹ This, of course, is only a small percentage of regional agreements. Many are in effect that have not been notified to the GATT/WTO.

² In the DITE dataset FDI regulatory changes are tracked for Latin America (Argentina, Belize, Bolivia, Brazil, Chile, Colombia, Costa Rica, Dominican Republic, Ecuador, El Salvador, Guatemala, Guyana, Honduras, Mexico, Nicaragua, Panama, Paraguay, Peru, Suriname, Uruguay and Venezuela), the Caribbean (Antigua and Barbuda, Bahamas, Barbados, Cayman Islands, Cuba, Jamaica, Puerto Rico, Saint Kitts and Nevis, Saint Lucia, Saint Vincent and the Grenadines, and Trinidad & Tobago) and North America (Canada and the United States).

³ See <http://www.unctad.org/Templates/WebFlyer.asp?intItemID=2470andlang=1> for details.

⁴ The index formula is $PERFORMANCE_i = FDI_i / FDI_w / GDP_i / GDP_w$ where $PERFORMANCE_i$ = the Inward FDI Performance Index of the i^{th} country, FDI_i = FDI inflows in the i^{th} country, FDI_w = World FDI inflows, GDP_i = GDP in the i^{th} country and GDP_w = World GDP.

⁵ See Deardorff [1998] for a history and analysis of gravity models in international trade.

⁶ Regional integration in autos had an interesting policy spillover. As a result of Japan taking Canada to the WTO, Canada was forced in 2002 to end the 1965 Canada-US Auto Pact and replace it with a uniform Canadian tariff on motor vehicle imports from non-NAFTA countries, ending the differentiation between the Big Three and Asian assemblers (Eden and Molot [2002]).

Table 1

RTAs IN THE AMERICAS NOTIFIED TO THE GATT/WTO AND IN FORCE AS OF 2006

Agreement	Category 1 (Goods Agreement) Date of entry into force	Type of Goods Agreement	Category 2 (Services Agreement) Date of entry into force
CACM (Central American Common Market)	12-Oct-1961	Customs union	
CARICOM (Caribbean Community and Common Market)	1-Aug-1973	Customs union	1-July-1997
LAIA (Latin American Integration Association)	18-Mar-1981	Preferential arrangement	
United States - Israel	19-Aug-1985	FTA	
CAN (Andean Community)	25-May-1988	Preferential arrangement	
MERCOSUR (Southern Common Market)	29-Nov-1991	Customs union	
NAFTA	1-Jan-1994	FTA	1-Apr-1994
Canada - Israel	1-Jan-1997	FTA	
Canada - Chile	5-Jul-1997	FTA	5-Jul-1997
Mexico - Nicaragua	1-Jul-1998	FTA	1-Jul-1998
Chile - Mexico	1-Aug-1999	FTA	1-Aug-1999
Mexico - EC	1-Jul-2000	FTA	1-Mar-2001
Mexico- Israel	1-Jul-2000	FTA	
Mexico- El Salvador	15-Mar-2001	FTA	15-Mar-2001
Mexico - EFTA	1-Jul-2001	FTA	1-Jul-2001
Chile - Costa Rica	15-Feb-2002	FTA	15-Feb-2002
Chile - El Salvador	1-Jun-2002	FTA	1-Jun-2002
Canada - Costa Rica	1-Nov-2002	FTA	
Chile - EC	1-Feb-2003	FTA	1-Mar-2005
Panama - El Salvador	11-Apr-2003	FTA	11-Apr-2003
United States - Chile	1-Jan-2004	FTA	1-Jan-2004
Chile - Republic of Korea	1-Apr-2004	FTA	1-Apr-2004
Chile - EFTA	1-Dec-2004	FTA	1-Dec-2004
Mexico - Japan	1-Apr-2005	FTA	1-Apr-2005
CAFTA-DR (Dominican Republic-United States-Central America)	1-Mar-2006	FTA	1-Mar-2006
United States - Jordan			17-Dec-2001
United States - Singapore			1-Jan-2004
United States - Australia			1-Jan-2005
United States - Morocco			1-Jan-2006

Note: FTA: Free Trade Agreement.

Source: Western Hemispheric RTAs extracted by author from WTO data on all RTAs by type as of 2006 (http://www.wto.org/english/tratop_e/region_e/type_e.xls).

Table 2

BITS AND DTTs IN THE AMERICAS, SELECTED COUNTRIES, 2002

Country	Double Tax Treaties (DTTs)	Bilateral Investment Treaties (BITs)
Argentina	24	54
Barbados	15	8
Bolivia	7	22
Brazil	33	14
Canada	99	24
Chile	7	47
Costa Rica	3	14
Cuba	6	57
Ecuador	8	27
El Salvador	1	23
Jamaica	12	15
Mexico	34	15
Nicaragua	0	14
Paraguay	2	24
Peru	4	27
Trinidad & Tobago	16	6
United States	169	45
Uruguay	5	28
Venezuela	21	22

Source: Author's calculations based on unpublished data from UNCTAD.

Table 3

FDI REGULATORY CHANGES IN THE AMERICAS, 1992-2002

Year	Region	Pro-FDI	Anti-FDI	Total	<i>Pro/Total</i>
All Yrs	Caribbean	30.00	2.00	32.00	0.94
All Yrs	CAR/Americas	0.14	0.13	0.14	
All Yrs	Latin America	164.00	14.00	178.00	0.92
All Yrs	LA/Americas	0.75	0.88	0.76	
All Yrs	North America	24.00	0.00	24.00	1.00
All Yrs	NA/Americas	0.11	0.00	0.10	
All Yrs	Americas	218.00	16.00	234.00	0.93

Source: Author's calculations based on confidential UNCTAD data.

Table 4

FDI REGULATORY CHANGES IN THE AMERICAS
January 1992-January 2002

Countries	More Favorable	Less Favorable	Total measures	Favorable/ Total	Ranked by % Less Favorable Changes	Ranked by Total No Reg Changes
Antigua and Barbuda	3	0	3	1.00	8	13
Argentina	12	1	13	0.92	7	5
Bahamas	3	2	5	0.60	1	11
Barbados	7	0	7	1.00	8	9
Belize	7	0	7	1.00	8	9
Bolivia	2	0	2	1.00	8	14
Brazil	13	3	16	0.81	4	3
Canada	18	0	18	1.00	8	2
Cayman Islands	2	0	2	1.00	8	14
Chile	6	2	8	0.75	2	8
Colombia	16	0	16	1.00	8	3
Costa Rica	6	0	6	1.00	8	10
Cuba	2	0	2	1.00	8	14
Dominican Republic	3	0	3	1.00	8	13
Ecuador	16	3	19	0.84	5	1
El Salvador	3	0	3	1.00	8	13
Guatemala	3	0	3	1.00	8	13
Guyana	1	0	1	1.00	8	15
Honduras	4	0	4	1.00	8	12
Jamaica	2	0	2	1.00	8	14
Mexico	15	0	15	1.00	8	4
Nicaragua	7	0	7	1.00	8	9
Panama	8	1	9	0.89	6	7
Paraguay	1	0	1	1.00	8	15
Peru	16	0	16	1.00	8	3
Puerto Rico	1	0	1	1.00	8	15
St Kitts & Nevis	6	0	6	1.00	8	10
St Lucia	2	0	2	1.00	8	14
St Vincent & Grenadines	1	0	1	1.00	8	15
Suriname	1	0	1	1.00	8	15
Trinidad & Tobago	1	0	1	1.00	8	15
United States	6	0	6	1.00	8	10
Uruguay	10	0	10	1.00	8	6
Venezuela	14	4	18	0.78	3	2
Caribbean	30	2	32	0.94		
Latin America	164	14	178	0.92		
North America	24	0	24	1.00		
<i>Total Americas</i>	<i>218</i>	<i>16</i>	<i>234</i>	<i>0.93</i>		

Source: Author's calculations using unpublished UNCTAD statistics.

Table 5

TAX HAVENS IN THE AMERICAS BY REGION, COUNTRY TYPE AND OECD (2000) STATUS

	Country	Region	Country Type/Linkages	On OECD (2000) List?
1	Anguilla	Caribbean	UK overseas territory	Yes
2	Antigua & Barbuda	Caribbean	Independent, Commonwealth member	Yes
3	Aruba	Caribbean	Kingdom of the Netherlands	Yes
4	Bahamas	Caribbean	Independent, Commonwealth member	Yes
5	Barbados	Caribbean	Independent, Commonwealth member	Yes
6	Belize	Caribbean	Independent, Commonwealth member	Yes
7	Bermuda	Caribbean	UK overseas territory	Coop*
8	British Virgin Islands	Caribbean	UK overseas territory	Yes
9	Cayman Islands	Caribbean	UK overseas territory	Coop*
10	Dominica	Caribbean	Independent, Commonwealth member	Yes
11	Grenada	Caribbean	Independent, Commonwealth member	Yes
12	Montserrat	Caribbean	UK overseas territory	Yes
13	Netherland Antilles	Caribbean	Kingdom of the Netherlands	Yes
14	Puerto Rico	Caribbean	US possession	No
15	St. Kitts & Nevis	Caribbean	Independent, Commonwealth member	Yes
16	St. Lucia	Caribbean	Independent, Commonwealth member	Yes
17	St. Vincent & Grenadines	Caribbean	Independent, Commonwealth member	Yes
18	Turks & Caicos Islands	Caribbean	UK overseas territory	Yes
19	US Virgin Islands	Caribbean	US overseas territory	Yes
20	Costa Rica	Central America	Independent	No
21	Panama	Central America	Independent	Yes
22	Uruguay	South America	Independent	No

Note: * "Coop" means that this jurisdiction agreed to eliminate its harmful tax practices and therefore was not included in the OECD (2000) list of abusive tax havens.

Table 6

INWARD FDI STOCK IN THE AMERICAS
Selected Years 1988-2004

Country	1988	1992	1996	2000	2002	2004	% Non-US 1988	% Non-US 2004
Anguilla	---	33	103	230	303	441	0.00	0.04
Antigua and Barbuda	188	365	461	644	835	1,121	0.10	0.11
Argentina	6,839	16,303	33,557	67,601	43,146	53,697	3.60	5.23
Aruba	13	293	302	934	976	1,294	0.01	0.13
Bahamas	578	585	830	1,587	1,842	2,195	0.30	0.21
Barbados	152	193	241	308	344	451	0.08	0.04
Belize	50	122	192	296	465	693	0.03	0.07
Bermuda	14,037	19,569	27,968	56,393	71,894	77,602	7.38	7.55
Bolivia	604	1,188	1,991	5	6	10	0.32	0.00
Brazil	32,055	39,975	50,195	103,015	100,847	150,965	16.85	14.69
British Virgin Islands	37	-1	1,886	11,363	11,763	11,876	0.02	1.16
Canada	95,728	108,503	132,978	212,716	224,185	303,818	50.32	29.57
Cayman Islands	1,621	1,768	3,977	24,973	29,087	36,172	0.85	3.52
Chile	3,928	11,289	24,595	45,753	42,311	54,464	2.07	5.30
Colombia	3,011	3,891	11,773	10,992	17,830	22,278	1.58	2.17
Costa Rica	1,045	1,713	836	2,709	3,739	4,815	0.55	0.47
Cuba	1	19	59	74	81	74	0.00	0.01
Dominica	41	102	211	275	302	341	0.02	0.03
Dominican Republic	561	896	1,803	5,214	7,210	8,468	0.29	0.82
Ecuador	1,207	1,976	4,118	7,081	9,686	12,482	0.63	1.21
El Salvador	198	253	421	2,001	2,431	3,686	0.10	0.36
Grenada	47	111	196	364	486	613	0.02	0.06
Guatemala	1,599	1,919	2,278	3,420	4,155	4,441	0.84	0.43
Guyana	36	201	545	759	859	933	0.02	0.09
Haiti	131	161	157	215	226	240	0.07	0.02
Honduras	289	483	736	1,482	1,850	2,390	0.15	0.23
Jamaica	558	1,152	1,752	3,317	4,412	5,783	0.29	0.56
Mexico	16,615	35,680	46,912	97,170	155,151	182,536	8.73	17.76
Montserrat	25	53	60	77	80	85	0.01	0.01
Netherlands Antilles	382	481	304	78	81	-30	0.20	0.00

Table 6 (continuación)

INWARD FDI STOCK IN THE AMERICAS Selected Years 1988-2004								
Country	1988	1992	1996	2000	2002	2004	% Non-US 1988	% Non-US 2004
Nicaragua	122	210	462	1,395	1,749	2,201	0.06	0.21
Panama	2,011	2,451	3,660	6,775	7,413	9,217	1.06	0.90
Paraguay	316	597	829	1,325	778	1,024	0.17	0.10
Peru	1,217	1,501	6,720	11,062	12,549	13,310	0.64	1.30
Saint Kitts and Nevis	71	196	287	505	676	805	0.04	0.08
Saint Lucia	243	417	543	825	943	1,157	0.13	0.11
St Vincent & Grenadines	30	72	224	500	558	669	0.02	0.07
Suriname	-309	-568	-626	-719	-819	-955	-0.16	-0.09
Trinidad & Tobago	1,834	2,408	3,953	7,008	8,633	10,443	0.96	1.02
Turks and Caicos Is	2	5	3	4	4	5	0.00	0.00
United States	314,754	423,131	598,021	1,256,867	1,340,011	1,473,860	165.47	143.43
Uruguay	592	715	1,265	2,088	1,403	2,110	0.31	0.21
Venezuela	2,516	6,033	10,432	35,480	39,007	43,575	1.32	4.24

Country	1988	1992	1996	2000	2002	2004	Share 1988	Share 2004
Caribbean & Other	20,551	28,875	45,320	114,888	140,738	159,806	0.041	0.064
South/Central America	73,941	125,933	200,906	399,746	444,630	563,947	0.146	0.225
North America	410,482	531,634	730,999	1,469,583	1,564,196	1,777,678	0.813	0.711
Total Americas	504,975	686,442	977,225	1,984,217	2,149,565	2,501,430	1.000	1.000
US as % Americas	62.33	63.10	61.64	61.20	61.20	59.54		
Canada as % Americas	18.96	18.03	15.81	14.03	13.61	10.96		
Mexico as % Americas	3.29	3.58	5.20	4.23	4.80	4.87		
Brazil as % Americas	6.35	5.95	5.82	7.20	5.14	6.79		

Source: Author's calculations using data from the 2005 *World Investment Report*.

Table 7

**FDI POTENTIAL INDEXES FOR THE AMERICAS
1988-2003**

	Score			Rank (140 Countries)			Rank (Americas)		
	1988-1990	1999-2001	2001-2003	1988-1990	1999-2001	2001-2003	1988-1990	1999-2001	2001-2003
Argentina	0.139	0.218	0.187	59	52	66	14	7	9
Bahamas	0.260	0.269	0.235	28	38	48	3	3	3
Bolivia	0.106	0.163	0.158	81	83	83	21	18	13
Brazil	0.165	0.181	0.178	48	73	70	8	14	11
Canada	0.533	0.465	0.457	2	5	4	2	2	2
Chile	0.180	0.242	0.231	41	47	50	5	4	4
Colombia	0.141	0.146	0.132	58	101	103	13	22	21
Costa Rica	0.159	0.188	0.179	50	70	69	9	13	10
Dominican Republic	0.131	0.203	0.189	66	62	63	16	9	8
Ecuador	0.127	0.139	0.125	69	104	109	17	23	23
El Salvador	0.106	0.166	0.142	80	80	96	20	17	19
Guatemala	0.077	0.150	0.134	102	97	101	25	20	20
Guyana	0.079	0.201	0.144	101	63	94	24	10	18
Haiti	0.044	0.028	0.066	115	135	137	26	26	26
Honduras	0.106	0.148	0.114	83	98	118	22	21	25
Jamaica	0.135	0.342	0.158	61	75	84	15	15	14
Mexico	0.176	0.229	0.227	44	49	51	7	5	5
Nicaragua	0.094	0.128	0.116	95	109	113	23	25	24
Panama	0.151	0.219	0.211	54	51	56	10	6	7
Paraguay	0.127	0.136	0.129	70	107	105	18	24	22
Peru	0.109	0.169	0.153	78	78	89	19	16	16
Suriname	0.177	0.157	0.153	43	86	88	6	19	15
Trinidad & Tobago	0.145	0.200	0.215	57	64	54	12	11	6
United States	0.727	0.669	0.659	1	1	1	1	1	1
Uruguay	0.145	0.191	0.145	56	67	93	11	12	17
Venezuela	0.205	0.208	0.175	37	58	74	4	8	12

Source: author's calculations using UNCTAD data from <http://www.unctad.org/Templates/WebFlyer.asp?i ntItemID=2471&lang=1>.

Table 8

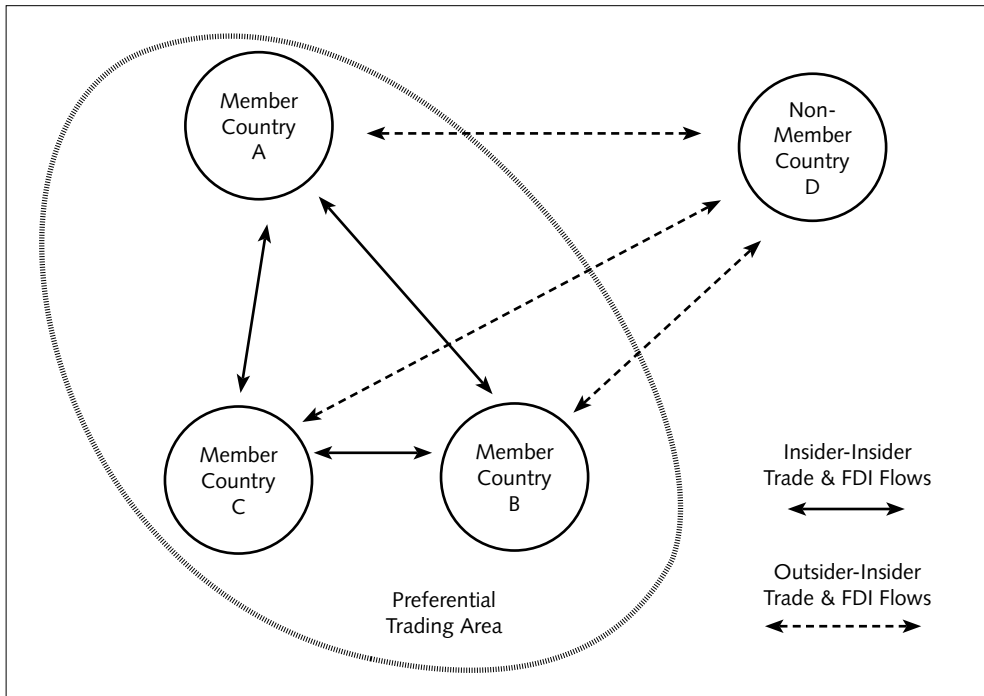
**INWARD FDI PERFORMANCE INDEXES FOR THE AMERICAS
1988-2004**

	Score			Rank (140 Countries)			Rank (Americas)		
	1988-1990	1999-2001	2002-2004	1988-1990	1999-2001	2002-2004	1988-1990	1999-2001	2002-2004
Argentina	1.199	1.311	1.195	39	42	82	12	12	19
Bahamas	0.518	0.987	1.932	66	66	52	18	14	10
Bolivia	1.695	2.735	2.188	29	14	43	7	2	8
Brazil	0.408	1.443	1.610	77	37	62	20	11	13
Canada	1.256	1.642	0.734	38	30	94	11	7	21
Chile	3.107	2.273	3.472	10	19	21	1	4	3
Colombia	1.106	0.700	1.450	42	80	69	15	20	15
Costa Rica	2.550	0.871	1.937	18	73	51	2	17	9
Dominican Republic	1.877	1.633	1.769	26	31	58	6	8	12
Ecuador	1.485	1.523	2.750	32	35	34	8	10	7
El Salvador	0.256	0.459	1.360	89	95	73	22	21	17
Guatemala	2.003	0.405	0.003	22	99	120	4	22	24
Guyana	0.687	2.316	2.852	59	17	31	17	3	6
Haiti	0.366	0.119	0.122	82	123	133	21	25	25
Honduras	1.389	1.130	1.917	33	55	53	9	13	11
Jamaica	1.906	2.001	4.225	25	23	17	5	5	2
Mexico	1.337	0.900	1.236	35	72	79	10	16	18
Nicaragua	0.075	2.810	2.891	96	13	30	24	1	5
Panama	-2.786	1.581	3.034	116	32	29	25	9	4
Paraguay	0.699	0.372	0.484	58	104	107	16	24	22
Peru	0.136	0.726	1.576	91	78	64	23	18	14
Suriname	-18.691	-1.613	-3.996	117	140	140	26	26	26
Trinidad & Tobago	2.381	1.811	4.527	20	27	15	3	6	1
United States	1.115	0.719	0.376	41	79	114	14	19	23
Uruguay	0.496	0.394	1.434	71	100	70	19	23	16
Venezuela	1.177	0.902	0.980	40	71	86	13	15	20

Source: author's calculations using UNCTAD data from <http://www.unctad.org/Templates/WebFlyer.aspx?i=ntItemID=2471&lang=1>.

Figure 1

IMPACT OF AN RTA ON FDI PATTERNS



Source: Eden and Li ([2004] p. 30).

Bibliography

- AIZENMAN, JOSHUA AND NANCY MARION. "The Merits of Horizontal Versus Vertical FDI in the Presence of Uncertainty", in *Journal of International Economics*, Vol. 62(1), pp. 125-148. 2004.
- BALDWIN, JOHN R.; RICHARD E. CAVES AND WULONG GU. "Responses to Trade Liberalization: Changes in Product Diversification in Foreign -and Domestic- Controlled Plants", in Lorraine Eden and Wendy Dobson (Eds.) *Governance, Multinationals and Growth*. Cheltenham, UK: Edward Elgar Publishing. 2005.
- BALDWIN, ROBERT AND CHARLES WYPLOSZ. "The Economics of European Integration". Book manuscript. Available at: <http://heiwwww.unige.ch/~baldwin/papers/BW/bw.htm>. 2003.
- BHAGWATI, JAGDISH; DAVID GREENWAY AND ARVIND PANAGARIYA. "Trading Preferentially: Theory and Policy", in *The Economic Journal*, 108: pp. 1128-1148. July, 1998.
- BHAGWATI, JAGDISH AND ARVIND PANAGARIYA. *The Economics of Preferential Trade Agreements*. Washington, DC: AEI Press. 1996.
- BERTRAND, OLIVIER AND NICOLE MADARIAGA. *U.S. Greenfield Investments and M&A Location: Impact of American Continental Integration and Insider vs. Outsider Position*. Working Paper at TEAM, Université Paris I Sorbonne et CNRS. 2002.
- BLOMSTROM, MAGNUS AND ARI KOKKO. *Regional Integration and Foreign Direct Investment: A Conceptual Framework and Three Cases*. World Bank Policy Research Working Paper N° 1750. April, 1997.
- BROWN, DRUSILLA K.; KOZO KIYOTA AND ROBERT M. STERN. "Computational Analysis of the Free Trade Area of the Americas (FTAA)", in *North American Journal of Economics and Finance*, 16: pp. 153-185. 2005.
- BUCKLEY, PETER J.; JEREMY CLEGG, NICHOLAS FORSANS AND KEVIN T. REILLY. "Evolution of FDI in the United States in the Context of Trade Liberalization and Regionalization", in *Journal of Business Research*, 56(10): pp. 853-857. 2004.
- CARRILLO, JORGE. "Transnational Strategies and Regional Development: The Case of GM and Delphi in Mexico", in *Industry and Innovation*, 11.1/2: pp. 127-153. 2004.
- CHUDNOVSKY, DANIEL AND ANDRÉS LÓPEZ. "Transnational Corporations' Strategies and Foreign Trade Patterns in MERCOSUR Countries in the 1990s", in *Cambridge Journal of Economics*, 28.5: pp. 635-652. 2004.

- COOPER, WILLIAM H. *Free Trade Agreements: Impact on US Trade and Implications for US Trade Policy*. CRS Report for Congress. Order Code RL31356. December 6, 2005.
- CRAWFORD, JO-ANN AND ROBERTO V. FIORENTINO. *The Changing Landscape of Regional Trade Agreements*. WTO Discussion Paper N° 8. WTO: Geneva. 2005.
- DEVLIN, ROBERT AND ANTONI ESTEVADEORDAL. *What's New in the New Regionalism in the Americas?* Working Paper N° 6. INTAL-ITD-STA Series. Buenos Aires: IDB-INTAL. 2001.
- DI MAURO, FRANCESCA. *The Impact of Economic Integration on FDI and Exports: A Gravity Approach*. CEPS Working Document N° 156. November, 2000.
- EATON, B. CURTIS; RICHARD G. LIPSEY AND A. EDWARD SAFARIAN. "The Theory of Multinational Plant Location in a Regional Trading Area", in L. Eden (Ed.), *Multinationals in North America*, Industry Canada Research Series, Volume 3, pp. 53-77. Calgary: University of Calgary Press. 1994.
- EDEN, LORRAINE. "Regional Integration and Foreign Direct Investment: Theory and Lessons from NAFTA", in M. Kotabe, P. Aulakh, and A. Phatak (Eds.), *The Challenge of International Business Research*. Cheltenham, UK: Edward Elgar Publishing. 2002.
- _____. "The Emerging North American Investment Regime", in *Transnational Corporations*, 5(3): 61-98. 1996a.
- _____. "Deep Integration: Tax Harmonization and Investment Policies in North America", in *Investment Rules for the Global Economy: Enhancing Access to Markets*, Pierre Sauvé and Daniel Schwanen (Eds.). Policy Study N° 28, pp. 293-323. Toronto: C.D. Howe Institute. 1996b.
- _____. "Who Does What After NAFTA? Location Strategies of US Multinationals", in L. Eden (ed). *Multinationals in North America*. Industry Canada Research Series, pp. 193-252. Calgary: University of Calgary Press. 1994.
- _____ AND ROBERT KUDRLE. "Tax Havens: Renegade States in the International Tax Regime", in *Law and Policy*. 27.1: pp. 100-127. January, 2005.
- _____ AND DAN LI. "The New Regionalism and Foreign Direct Investment in the Americas", in Sidney Weintraub (Ed.), *Strengthening the North American Community: NAFTA at Ten*. Washington, DC: Center for Strategic and International Studies. 2004.
- _____ AND ANTOINE MONTEILS. "Regional Integration: NAFTA and the Reconfiguration of North American Industry", in J. H. Dunning (Ed.) *Regions, Globalization and the Knowledge-Based Economy*. Oxford: Oxford University Press. 2000.

- EDEN, LORRAINE AND MAUREEN APPEL MOLOT. "Insiders, Outsiders and Host Country Bargains", in *Journal of International Management*, 8(4): pp. 359-433. 2002.
- _____. "Insiders and Outsiders: Defining "Who Is Us?" in the North American Auto Industry", in *Transnational Corporations*, 2(3): pp. 31-64. 1993.
- _____. "The View from the Spokes: Canada and Mexico Face the US", in S. Randall, H. Konrad and S. Silverman (Eds.), *North America Without Borders? Integrating Canada, the United States, and Mexico*. Calgary: University of Calgary Press. 1992.
- ETHIER, W. "The New Regionalism in the Americas: A Theoretical Framework", in *North American Journal of Economics and Finance*, 12: pp. 159-172. 2001.
- FEINBERG, SUSAN; M. P. KEANE AND M. BOGNANNO. "Trade Liberalization and 'Delocalization': New Evidence from Firm-level Panel Data", in *Canadian Journal of Economics*, 31(4): pp. 749-777. 1998.
- FRANKEL, JEFFREY A. AND ANDREW K. ROSE. "An Estimate of the Effect of Common Currencies on Trade and Income", in *Quarterly Journal of Economics* 117(2): pp. 437-466. 2002.
- FRISCHTAK, CLAUDIO. "Multinational Firms' Responses to Integration of Latin American Markets", in *Business and Politics* 6.1: pp. xx-xxx. 2004.
- GLOBERMAN, STEVEN. "Trade, FDI, and Regional Economic Integration: Cases of North America and Europe". Paper presented at the Conference *Enhancing Investment Cooperation in Northeast Asia*. Hawaii. August 7-9, 2002.
- GLOBERMAN, STEVEN AND DANIEL M. SHAPIRO. "Global Foreign Direct Investment Flows: The Role of Governance Infrastructure", in *World Development*, 30(11): pp. 1899-1919. 2002.
- _____. *Assessing Recent Patterns of Foreign Direct Investment in Canada and the United States*. Working Paper. Western Washington University. 2001.
- GRAHAM, E. M. "Foreign Direct Investment Outflows and Manufacturing Trade", in D. J. Encarnation (Ed.), *Japanese Multinationals in Asia*. Oxford: Oxford University Press, pp. 87-99. 1999.
- _____. AND E. WADA. "Domestic Reform, Trade and Investment Liberalisation, Financial Crisis, and Foreign Direct Investment into Mexico", in Keith Maskus (Ed.), *The World Economy*. Washington, D.C.: Institute of International Economics, pp. 777-797. 2000.

HANSON, GORDON H.; RAYMOND J. MATALONI AND MATTHEW J. SLAUGHTER. *Expansion Strategies of U.S. Multinational Firms*. NBER Working Paper N° W8433. National Bureau of Economic Research, Inc. 2001.

HARRIGAN, JAMES. *Specialization and the Volume of Trade: Do the Data Obey the Laws?* NBER Working Papers 8675. National Bureau of Economic Research, Inc. 2001.

HARRIS, RICHARD. "FDI in an FTA with Uncertain Market Access", in Lorraine Eden and Wendy Dobson (Eds.), *Governance, Multinationals and Growth*. Cheltenham, UK: Edward Elgar Publishing. 2005.

HEJAZI, WALID AND PETER PAULY. "How do Regional Trade Agreements Affect Intra-regional and Inter-regional FDI?", in Lorraine Eden and Wendy Dobson (Eds.), *Governance, Multinationals and Growth*. Cheltenham, UK: Edward Elgar Publishing. 2005.

HEJAZI, WALID AND A. E. SAFARIAN. "NAFTA Effects and the Level of Development", in *Journal of Business Research* 58: pp. 1741-1749. 2005.

HUNTER, LINDA; JAMES R. MARKUSEN AND THOMAS F. RUTHERFORD, 1995. "North American Free Trade and the Production of Finished Automobiles", in *Modeling North American Economic Integration*, Timothy and Patrick Kehoe (editors), Kluwer, pp.117-130. 1995.

IGLESIAS, E. "Global Positioning of the European Union and MERCOSUR: Towards a New Model of Inter-regional Cooperation". Paper presented at the Annual Lecture at the Chaire Mercosur of the Institut d'Etudes Politiques de Paris, Paris. April 4, 2002.

INTER-AMERICAN DEVELOPMENT BANK - IDB. *Beyond Borders: The New Regionalism in Latin America*. Washington, DC: Inter-American Development Bank. 2002.

KRUEGER, ANNE. O. "NAFTA's Effects: A Preliminary Assessment", in *The World Economy*, 23): pp. 761-775. June, 2000.

LEVY YEYATI, EDUARDO; ERNESTO STEIN AND CHRISTIAN DAUDE. "The FTAA and the Location of FDI". Paper presented at the IDB-Harvard Conference on the FTAA in Punta del Este, Uruguay. December 7, 2002.

_____. *Regional Integration and the Location of FDI*. Inter-American Development Bank Working Paper #492. Washington, DC: Inter-American Development Bank. 2003.

LIPSEY, RICHARD G. "The Theory of Customs Unions: A General Survey", in *The Economic Journal*, 70.279: pp. 496-513. 1960.

- LOVE, JAMES H. AND FRANCISCO LAGE-HIDALGO. "Is There Competition for US Direct Investment? A Perspective on NAFTA", in *The World Economy*, 22: pp. 207-221. 1999.
- MACDERMOTT, R. "NAFTA and Foreign Direct Investment". Manuscript. Rutgers University Working Paper. Rutgers University. 2002.
- MAKHJIA, MONA AND SANDRA D. WILLIAMSON. "The Globalization of U.S. Industries", in *Globalizing America: The USA in World Integration*, Gavin Boyd and Thomas Brewer (Ed.). Edward Elgar Publishing. 2000.
- MARKUSEN, JAMES R.; THOMAS F. RUTHERFORD AND LINDA HUNTER. "Trade Liberalization in a Multinational-Dominated Industry", in *Journal of International Economics*, 38: pp. 95-118. 1995.
- MARKUSEN, JIM. "Regional Integration and Third-Country Inward Investment", in *Business and Politics*, 6.1: pp. xx-xxx. 2004.
- MONGE-NARANJO, ALEXANDER. "The Impact of NAFTA on Foreign Direct Investment Flows in Mexico and the Excluded Countries". Mimeo. Northwestern University. 2002.
- RUGMAN, ALAN. *The Regional Multinationals: Multinationals and "Global" Strategic Management*. Oxford, UK: Oxford University Press. 2005.
- STEIN, ERNESTO AND CHRISTIAN DAUDE. "Institutions, Integration, and the Location of Foreign Direct Investment". Mimeo. Inter-American Development Bank, Research Department. 2001.
- UNITED NATIONS CONFERENCE ON TRADE AND DEVELOPMENT - UNCTAD. *World Investment Report 2004: The Shift Towards Services*. Geneva: United Nations. 2005.
- VERNON, RAYMOND. *In the Hurricane's Eye: The Troubled Prospects of Multinational Enterprises*. Cambridge, MA: Harvard University Press. 1998.
- _____. "Multinationals and Governments: Key Actors in NAFTA", in L. Eden (Ed.), *Multinationals in North America*. Calgary: University of Calgary Press. 1994.
- WEINTRAUB, SIDNEY AND CHRISTOPHER SANDS. *The North American Auto Industry under NAFTA*. Washington, DC: Center for Strategic and International Studies. 1998.
- WONNACOTT, RONALD. "Trade and Investment in a Hub-and-Spoke versus a Free Trade Area", in *The World Economy*, 19: pp. 237-25. 1996.

