Why are economists unconcerned about foreign investment in the United States?

The counterpart of the huge U.S. current account deficit is an equally large U.S. capital account surplus. In other words, the rest of the world is sending us goods and services today in exchange for claims on future income, such as stocks and bonds or real investment in assets like automobile factories.

Foreign investment creates jobs and raises wages for local workers, lowers interest rates for local business investment and permits consumers to borrow more cheaply when times are tough. Indeed, 19th century economists lowered interest rates for local business investment and permitted consumers to purchase stocks and bonds or real investment in assets like automobile factories.

Anxiety about international investment in the United States dates back at least to World War I, when Americans were concerned about German investment in strategic industries. During the 1980s, Americans worried about Japanese investment in landmarks like Rockefeller Center. More recently, heavy Chinese government purchases of Treasury securities has garnered criticism.

Although critics do not usually carefully define the problems with foreign investment, one might infer three concerns: 1) Foreigners could obtain interests in militarily sensitive industries; 2) Foreigners could suddenly dump their holdings of U.S. assets, harming the U.S. economy; or 3) High foreign investment could disguise problems with low domestic savings.

Economists are not usually very concerned about the first two reasons. While foreign investment could potentially compromise sensitive military technology, the president has the authority—under the Exon-Florio Amendment to the Omnibus Trade and Competitiveness Act of 1988—to block such acquisitions.

What if the foreign investors dump U.S. assets to pressure the U.S. for political reasons? A sudden decline in demand for U.S. assets would drive up U.S. interest rates and reduce the value of the dollar, but such a decline would also reduce the real value of the foreign investments in the United States. If a major holder of a particular asset tried to sell its holdings overnight, large losses would surely result.

Perhaps the most serious issue with foreign investment is that it effectively disguises a lack of domestic savings. But domestic savings are the result of Americans’ individual and governmental decisions and are only modestly influenced by foreign demand for U.S. assets. We have our economic destiny in our own hands.

Submit your question in a letter to the editor. (See Page 2.) One question will be answered by the appropriate economist in each issue.