November 6, 1991

MAKING AMERICA MORE COMPETITIVE WITH FOREIGN INVESTMENT

INTRODUCTION

Foreign direct investment in the United States has contributed greatly to the country's economic growth over the past two centuries.[1] In the 1800s, foreign capital financed most of America's bridges, canals, railroads and other infrastructure. Today, foreign investment is responsible for the employment of 3.7 million Americans, $112 billion in wages to Americans, and $7 billion in research and development spending.[2]

Yet despite the contribution of foreign direct investment to America's economic well-being, Congress is on the verge of increasing the already tight restrictions on foreign investment in the U.S. In August, George Bush signed into law H.R. 991, introduced by Representative Thomas Carper, the Delaware Democrat. This bill extended the Exon-Florio provision of the 1988 Omnibus Trade and Competitiveness Act that had expired in October 1990. Sponsored originally by Nebraska Senator James Exon and then-New Jersey Congressman James Florio, both Democrats, the provision restricts foreign investments for alleged national security reasons.

Greater Role For Congress. Many members of Congress now criticize Exon-Florio for its failure to stop significantly the increase of foreign direct investment. As a result, many policy makers want a new provision even tougher than the original, requiring government review of all foreign investments and allowing Congress a greater say over when Americans can sell their enterprises to foreign-

1 Foreign direct investment refers to the cumulative net book value of foreign investors' equity in, and outstanding loans to, U.S. business enterprises of which foreign investors hold at least 10 percent.

2 From remarks by William E. Barreda, Deputy Assistant Secretary of the Treasury for Trade and Investment before the Subcommittee on Commerce, Consumer Protection, and Competitiveness of Committee on Energy and Commerce, U.S. House of Representatives, June 12, 1991.

ers. Political rather than national security considerations likely would guide Congress in such decisions. If the Exon-Florio provision is expanded, foreign investment would be discouraged and America's economy would weaken.

American businesses increasingly face competition from enterprises in Asia, the European Community, and a host of emerging market economies in Eastern Europe and Latin America. Foreign investment thus should be welcomed to America, not discouraged or driven out. Foreign investment capital finances new enterprises, expands existing businesses, and researches and develops new products and production methods. Yet despite the advantages of foreign investment, the federal government restricts or bans foreign ownership of airlines, banks, shipping lines, and utilities. The current financial problems of airlines and banks in particular make clear the need to eliminate such restrictions: foreign investments in such enterprises could save them from bankruptcy.

During the past two decades, American firms have turned increasingly to foreign capital to finance innovation and modernization, sometimes with success, but sometimes frustrated by the federal government.

Example: Materials Research Corporation of America, based in New York, was purchased by the American subsidiary of Japan's Sony Corporation, which provided the capital needed to keep the firm in business.

Example: America's Moore Special Tool Company, based in Connecticut, was scheduled to sell a 40 percent share to Fanuc Ltd. of Japan to acquire needed capital. Protests from Congress killed the deal.

Example: The Bush Justice Department attempted to stop Semi-Gas Systems, Inc., an American firm based in California, from being purchased by Japan's Nippon Sanso KK. Semi-Gas had the Justice Department restriction overturned in court.

Many members of Congress have become alarmed at foreign investment, fearing that foreigners are "buying too much" of America. The Exon-Florio provision ostensibly is meant to protect American businesses from acquisitions by foreigners when it could damage U.S. security. Yet the provision poorly defines exactly when national security interests might be compromised by an acquisition. The result has been an increase of U.S. government oversight of many non-defense related investments.

The U.S. needs a more open market to foreign direct investment, especially in today's recession. To encourage the foreign investment that fuels economic growth, the Bush Administration should take five steps:

STEP #1: Repeal the Exon-Florio provision.

STEP #2: Allow foreign investors the freedom to purchase a larger stake in U.S. airlines and to operate domestic U.S. flights.

STEP #3: Allow foreigners to own and operate banks in the U.S.

STEP #4: Inject greater competition into the commercial shipping industry by allowing foreign investors to own and operate ships within U.S. waters.

STEP #5: Allow foreigners to own and operate public utilities.

By increasing foreign access to these areas, American firms gain capital for innovation and modernization. The increased competition in areas like commercial airlines and shipping, moreover, will benefit the U.S. consumer.

FOREIGN INVESTMENT IN THE UNITED STATES

The U.S. traditionally has allowed foreigners to purchase and own businesses and other assets in its territory. It has long been understood that the infusion of foreign capital helps spur economic growth. In 1791, for example, Alexander Hamilton urged the new federal government to allow foreigners access to the American market, arguing that foreign capital would be necessary for economic growth.

Hamilton was right. During America's early history, much of its infrastructure, such as bridges, canals, and railroads, was financed by foreign investment. Federal and state governments paid for these public works projects by issuing bonds. By the middle of the 1800s, foreigners owned half of these state and local bonds, while holding about a quarter of all federal bonds.[3] In addition, many private enterprises such as manufacturing facilities were owned by foreigners. The U.S. remained what is now pejoratively referred to as a "debtor" nation—that is, foreigners had more capital invested in America than Americans had invested overseas—until the early 1900s. Yet this "debtor" status in fact was a source of great economic strength. Only when World War I forced many Europeans to sell their American holdings did this situation change.

Attractive Market. In the past two decades, with foreign businesses growing prosperous and looking for places to invest, and with the American economy growing robustly as a result of Ronald Reagan's tax cuts, America once again became a very attractive market for foreign direct investment. Foreigners poured money into the strong and secure U.S. economy. Foreign direct investment in the U.S. increased from $83 billion in 1980 to $185 billion in 1985. By 1989 it had reached a total of $401 billion.[4] This inflow of foreign investment was both a cause and a consequence of America's economic strength.[5]

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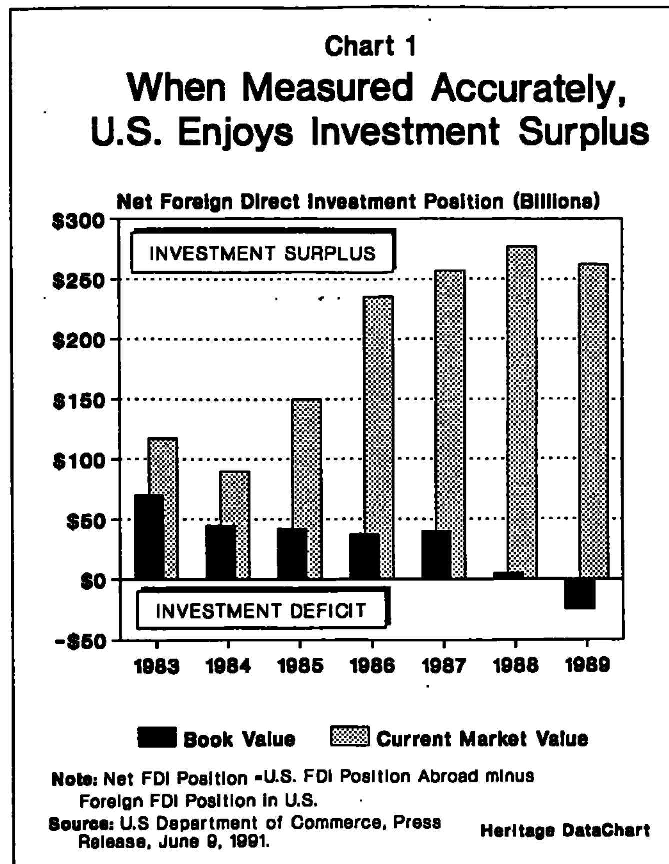
3 Michael V. Seitzinger, *Foreign Investment in the United States: Major Federal Restrictions* (Washington, D.C.:, Congressional Research Service, April 7, 1989), p. 4.

4 *Patterns and Trends in Foreign Direct Investment in the United States* (Washington, D.C.: U.S. Department of Commerce, International Trade Administration, April 1991, Staff Paper No. 91-2), p. 1.

5 Barreda, *op. cit.*

Despite its growth in the 1980s, foreign direct investment still accounts for only a tiny fraction of total U.S. assets. It amounts to less than 3 percent of U.S. domestic net worth, or total value of all land and fixed assets held in the U.S., and less than 1 percent of all U.S. land holding as of 1990.[6] Thus concerns that foreigners are in a position to control America's economic destiny are absurd. Ownership by American firms of a much higher percentage of assets in other countries, such as Canada, has not enabled the U.S. to force the governments of these countries to alter their policies.[7]



Moreover, even though debtor status due to an inflow of investment is a source of strength, not weakness, and even though America has enjoyed a surge of foreign investment in recent years, the U.S. still has more direct investments overseas than foreigners hold in the U.S. The reason that many Americans are misled into believing otherwise is because of deficiencies in the way assets are measured. Assets tend to be valued on the basis of their original cost, not according to their current value, which normally is higher and indicates today's market value. Thus, although the value of foreign investments in the U.S. has surpassed the value of U.S. investments abroad on the basis of original cost, America's investments tend to be older. If current market values are used as the basis for calculation, U.S. investments abroad have a higher total value than foreign-owned assets in the U.S. Further, the U.S. remains the biggest single foreign investor in the world.[8]

6 From the remarks of Susan W. Liebeler, former chairman of the U.S. International Trade Commission, before the Committee on Ways and Means, United States House of Representatives, January 25, 1990.

7 See Christopher Whalen, "Should Americans Be Worried About Foreign Investment in the U.S.?" Heritage Foundation *Backgrounder*, No. 720, July 20, 1989.

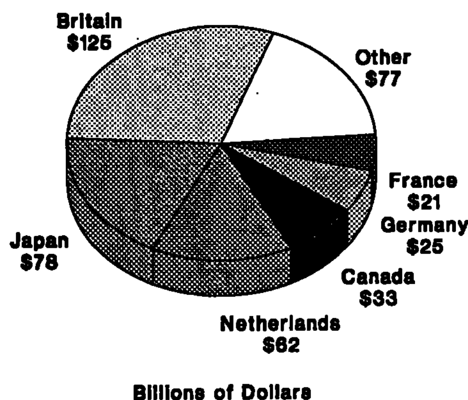
8 U.S. Department of Commerce, *op. cit.*

THE BENEFICIAL IMPACT OF FOREIGN INVESTMENT IN THE U.S.

Foreign direct investment in the U.S. builds factories, spurs modernization, and creates jobs. Studies by the Department of Commerce estimate that foreign investment in the U.S. is responsible for the jobs of 390,000 Americans in California, 330,000 in New York, 207,000 in Illinois, and 178,000 in Pennsylvania. In total, approximately 3.7 million Americans owe their jobs to foreign investment. And according to the Department of Commerce, foreign investment accounts for 9.1 percent of all the manufacturing jobs in America. Among the states gaining the most manufacturing jobs from foreign investment: Maryland — 13 percent, Tennessee — 12 percent, Georgia — 12 percent, and North Carolina — 11 percent.

Largest Investors. According to the Department of Commerce, Britain was the single largest direct investor in the U.S. As of 1990, Britain had a total of $125 billion in investments in the U.S., Japan had $78 billion, the Netherlands 62 billion and Canada $33 billion . Moreover, these investors brought not only contributed capital to American businesses and the economy, but also management techniques, production skills, and technology.

Chart 2
Total Foreign Direct Investment in the U.S.:1990



Note: FDI position estimated using 1990 capital inflows.
Source: Bureau of Economic Analysis
Heritage DataChart

In many cases this infusion of foreign capital and know-how has kept U.S. firms afloat that otherwise might have gone bankrupt. Japanese investment in the U.S. steel industry, for example, has injected large amounts of capital for modernization and innovation. This has helped turn around what was an inefficient and failing industry in the 1980s.

In short, foreign investment has contributed greatly to the economic success of America. Without it, millions of Americans would be without jobs, many businesses would be forced to shut down, and capital for expansion, modernization and innovation would be much more expensive for all firms. If America is to continue to be a strong economic power, foreign investment must be readily available to U.S. firms.

RESTRICTIONS ON FOREIGN CAPITAL

There is no specific constitutional provision granting the federal government the power to restrict foreign investment in the U.S. Yet many legislators point to the power to the federal government, granted in the U.S. Constitution, to regulate federal powers over immigration and naturalization,[9] the power to regulate interstate and foreign commerce,[10] and to provide for the national defense[11] as justifications for limiting foreign investment. Based on this reasoning, Congress has passed a variety of laws to limit or ban foreign investment in specific industries. The argument is that notwithstanding any general beneficial impact, heavy foreign investment in certain industries may harm U.S. interests. The industries affected include:

The Airline Industry. U.S. laws regulating the American aircraft industry prevent a foreign citizen from owning and operating a commercial aircraft within the United States or from purchasing more than 25 percent of an established American airline. These laws effectively prevent significant foreign investment in the U.S. airline industry. There are some exceptions. A foreign air carrier may operate within the United States, carrying passengers between two or more American cities, providing U.S. airlines receive reciprocal access to the foreign airline's market home. At the moment, no foreign carrier operates in this way in the U.S. market.[12]

Banking. Foreign ownership and investments in American banks have been regulated since 1791.[13] Yet it was not until the International Banking Act of 1978 that uniform guidelines were established for banks operating in the U.S.[14]

The Library of Congress's Congressional Research Service (CRS) has found that certain of these regulations hinder foreign investment in the banking sector. In an April 1989 report, for example, CRS analyst Michael Seitzinger notes that "these requirements appear to have discouraged foreign entry by means of subsidiaries because since 1791 Congress has required that all directors of national banks must be citizens of the United States."[15] This requirement was changed in 1978, but U.S. citizens still must make up at least two-thirds of the board.

The Maritime Industry. Title 46 of the United States Code comprises three major laws which regulate foreign direct investment in the maritime industry. The Shipping Act of 1916, the Merchant Marine Act of 1929, and the Merchant Marine Act of 1936 establish guidelines under which foreign direct investment is banned in such areas as commercial shipping and merchant marine services. These laws thus prevent any foreign ownership of U.S. merchant shipping ves-

9 Article I, Sec. 8, cl. 4.
10 Article I, Sec. 8, cl. 3.
11 Article I, Sec. 8, cl.12.
12 49 U.S.C. App. 1401 (b).
13 Chapter X, 1 Stat. 191 (1791).
14 P.L. 95-369, 92 Stat. 607.
15 Seitzinger, *op. cit*, p. 22.

sels.[16] In addition, the Merchant Marine Act of 1920, also known as the Jones Act, requires goods being transported between U.S. ports to be carried on U.S. ships.

Utilities. Title 16 of the U.S. Code establishes procedures for granting licenses for the construction, maintenance, and operation of facilities for developing, transmitting, and using electric and other sources of power. These licenses are issued only to U.S. citizens or to domestic corporations. Similar restrictions exist for other types of utility. These must be owned and operated by American companies or local governments. Although foreigners may invest in utilities, like telephone companies, they cannot own and operate such facilities. Included under the legal definition of a public utility is mineral extraction, including mining coal, copper, gold and uranium. Mining on private lands is permitted to foreigners, but mining on federal lands generally is restricted to U.S. citizens and domestic corporations.

During the past two decades, the federal government has added more layers of regulation, ostensibly to monitor foreign direct investment. These include:

- **The International Investment Survey Act of 1976.**[17] This Act requires the President to collect data on foreign investors. Jimmy Carter delegated this authority to the Departments of Commerce and Treasury. The Commerce Department collects data on the trends in foreign investment, while the Treasury monitors specific investments in an effort to protect national security and to avoid the transfer of sensitive technology. These departments publish reports on foreign direct investment.
- **The Domestic and Foreign Investment Improved Disclosure Act of 1977.**[18] This Act amended the Securities and Exchange Act of 1934 by requiring any person owning more than a 5 percent share in a company registered with the Securities and Exchange Commission to disclose his citizenship and residence to the Commission.
- **The Agricultural Foreign Investment Act of 1978.**[19] This statute requires any foreign citizen who acquires an interest in agricultural land to report that investment to the Department of Agriculture.

Support for such restrictions increased in 1987 when a U.S.-based company, the Fairchild Semiconductor Company, owned by the French, was scheduled to be sold to Japan's Fujitsu Limited. The Pentagon opposed that sale, claiming it would place a key high-tech U.S. military supplier under Japanese ownership.[20] This was peculiar reasoning, since Fairchild already was owned by French citizens. But Congress nevertheless passed the Exon-Florio provision the next year.

16 46 U.S.C. 12102 (a).
17 22 U.S.C. 3101.
18 P.L. 95-213.
19 7 U.S.C. 3501.
20 Stuart Auerbach, "Cabinet To Weigh Sale of Chip Firm," *Washington Post*, March 12, 1987, p. E1

- **The Exon-Florio Provision.** The Omnibus Trade and Competitiveness Act of 1988 granted the President the power to block the sale of an American-owned company to a foreigner when such a sale might affect national security. The Exon-Florio Provision, contained in that Act, stipulates that the President must first conclude that there are no other existing laws that can be used to stop the investment before invoking Exon-Florio.

HOW INVESTMENT RESTRICTIONS HURT U.S. ECONOMIC INTERESTS

It has become clear in recent years that these restrictions on foreign investment are very damaging to many U.S. industries. Rather than protecting them from perceived harm by foreign investors, the rules have denied those industries access to much-needed foreign capital. Faced with serious financial problems, for instance, struggling American airlines and banks would benefit from an injection of foreign capital or even a buyout by foreign investors. But U.S. law makes this difficult, if not impossible. Similarly, the Jones Act and restrictions on foreign ownership of U.S. merchant marine vessels has insulated the industry from competition and denied the industry less costly capital. This has raised the cost of shipping between U.S. ports. And thanks to the restrictions, the American consumer pays an estimated $9.7 billion in higher prices on products shipped on U.S. vessels.[21]

One of the most damaging of all the restrictions on foreign investment is the Exon-Florio Provision. The provision has given a previously non-existent power to the federal government. This power enables the U.S. government to prevent a foreign investment and even force an established foreign company to divest itself from an acquired U.S. company.

The rationale for the restriction is questionable to begin with. There is no empirical evidence suggesting that foreign companies are targeting American high-technology firms for purchase. If this were the case, then there would be a noticeable increase in foreign purchases of high-technology interests compared with all investments. Yet according to the Commerce Department, foreign acquisitions of high-technology industries actually decreased as a share of total foreign direct investment between 1980 and 1985, falling from 11.5 percent to 9 percent. From 1985 to 1988, foreign direct investment in high-technology industries climbed back up to 11 percent. There is, in other words, no trend towards increased foreign purchases of high-tech American firms.[22]

High-Tech Flow. Some policy makers support restrictions on foreign acquisitions of American firms not so much because of concerns about foreign control of key firms but out of a fear that sensitive technology will be transferred to a competitor in another country. This, it is said, would undermine American competi-

21 *The Economic Effects of Significant U.S. Import Restraints, Phase III: Services* (United States International Trade Commission Publication 2422, September 1991), table 1-2-7, p. 1-2-12.

22 Berreda, *op. cit.*

tiveness. Yet foreigners actually are acquiring less of America's latest technology than Americans are acquiring from foreign firms. Using payments of royalties and licensing fees to measure the value of technology flows, technology transfers from foreign firms to their U.S. affiliates were five times greater than technology transfers from U.S. affiliates to foreign owners between 1980 through 1989. Moreover, while the U.S. does experience a high rate of technology transfer abroad, most of it goes to affiliated American companies operating overseas. In fact, less than 25 percent of the transfers go to unaffiliated foreign companies.

A Committee on Investment. After signing the Omnibus Trade and Competitiveness Act of 1988, Ronald Reagan delegated the authority for reviewing sales to foreigners under the Exon-Florio to the Committee on Foreign Investment in the United States (CFIUS).[23] This committee was created in 1975 under the auspices of the Department of Treasury to monitor investments in the U.S. The Treasury committee was established in response to a perceived threat posed by increased investment by several Middle Eastern countries during the OPEC crisis of the 1970s.

By the end of 1990, CFIUS had received some 575 cases. Of these, it determined that only twelve warranted a full investigation.[24] And of these twelve, the President had blocked only one. Two other purchase proposals were withdrawn once the investigation began, and the others are still pending.[25]

Although the Exon-Florio provision might seem to have done little direct harm to the American economy, since few purchases have been scuttled because of it, in fact the provision has caused negotiating problems for the U.S. and adverse reactions abroad that threaten to escalate. For example, the U.S. is attempting to reach international agreements to eliminate barriers against foreign investment in the current Uruguay Round of the General Agreement on Tariffs and Trade (GATT) trade liberalization talks. But Exon-Florio restrictions on foreign investment in the U.S. are making it politically more difficult for the U.S. to mount a strong argument for its position in GATT.

In addition, Exon-Florio has added to mounting resentment overseas directed against formal or informal U.S. efforts to keep foreign firms out of America. One example of the U.S. attitude was the reaction to the purchase in 1990 by Japan's Matsushita Electronics Incorporated of MCA Corporation. In that sale, the Japanese firm also acquired an MCA subsidiary that operated concession stands at Yosemite National Park. Interior Secretary Manuel Lujan declared that the Japanese should not be allowed to own such a "national treasure" and the Japanese effectively were forced to sell the concession business.

23 Executive Order 12661, issued on December 27, 1988.

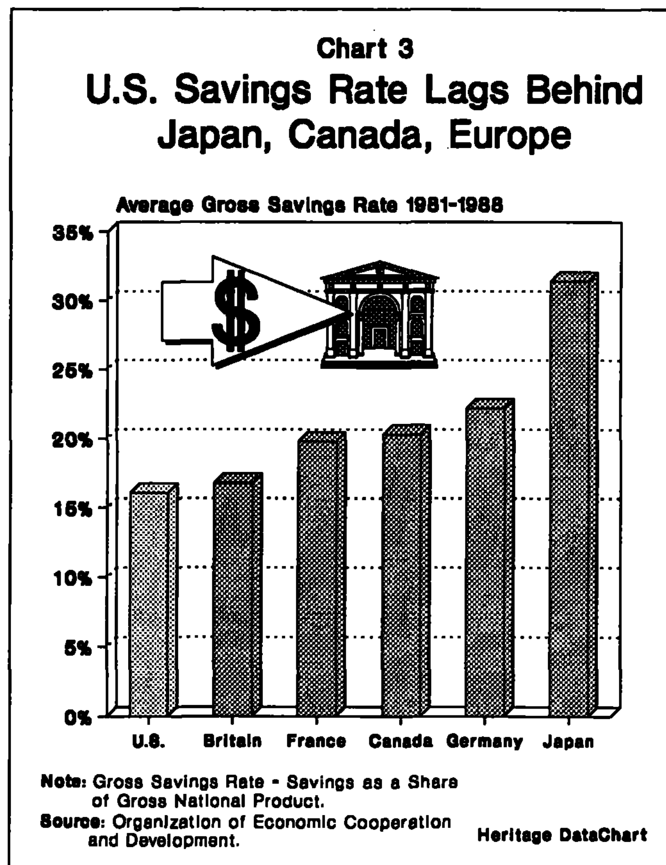
24 In a full investigation the committee investigates the case and issues a recommendation to the President.

25 "Foreign Investment, Analyzing National Security Concerns," Report to the Chairman, Subcommittee on Oversight and Investigations, Committee on Energy and Commerce, House of Representatives by the United States General Accounting Office (GAO/NSAID-90-94), Washington, D.C. March 1990, p. 9.

Interim Step. The Exon-Florio provision was made permanent this August. But Congress viewed that only as an interim step until lawmakers could broaden its scope. One proposal being considered by critics of Exon-Florio provision who believe it does not go far enough is to subject all foreign investments to a government committee investigation, whether national security questions are an issue or not. Other lawmakers favor a direct role for Congress in such decisions. For example, Representatives Richard Gephardt of Missouri and Mel Levine of California, both Democrats, plan to introduce a bill to increase congressional oversight of the foreign investment review process.[26] Such legislation is likely to be introduced in the 1992 session of Congress.

HOW INVESTMENT RESTRICTIONS FRUSTRATE U.S. FIRMS

Proposals for even tighter federal government controls on foreign investment would harm, not help, the U.S. economy. American businesses increasingly are turning to foreign sources of capital and technical support in order to remain competitive. When a country's savings rate is low, it decreases the amount of available capital banks can lend, and increases the cost of the existing capital. Traditionally, the U.S. national savings rate has been higher than the gross private domestic investment rate. Thus, there has been enough domestic capital to fuel domestic investment. In 1980, however, this situation changed. The U.S. savings began declining and foreign capital has been needed to fund domestic investment. Today, the U.S. savings rate remains substantially lower than most of its competitors. Thus foreign capital has flowed from countries in the European Community and Japan to the U.S. This foreign direct investment has greatly benefitted American firms. In some instances, it has even kept the firms from bankruptcy. In other cases, foreign investment has given U.S. companies access to technologies that are far more



26 Council on Competitiveness,"Foreign Investment Case Sparks U.S. Policy Debate," *Challenges*, April 1991, p. 4.

advanced than they had access to previously. Some examples:

♦♦ **Materials Research Corporation—Sony U.S.A.** Materials Research Corporation (MRC), based in Rockland County, New York, is an American firm producing semiconductor manufacturing equipment and silicon wafers used in computer chips. Sony U.S.A. is the American subsidiary of Japan's Sony Corporation, which manufactures mainly consumer electronics.

The Chairman and CEO of Materials Research Corporation, Sheldon Weinig, explains that "In 1989, [MRC], which I founded, was faced with a critical challenge: raise capital or probably fail. The capital we finally raised came from Japan. We are now a wholly owned subsidiary of Sony U.S.A....in 1988 we realized the company could not develop the next generation of equipment without fresh capital. Because of lower-than-expected activity in the worldwide semiconductor markets, we were capital-short."[27]

The company tried to raise the money through American banks, which would only reschedule MRC's existing debt. MRC sought help from its major suppliers, such as IBM, who in the past had helped other suppliers. But IBM refused MRC's request. Then MRC went to Wall Street financiers, who recommended breaking up the company and selling its assets. The company turned to a European-based competitor interested in an acquisition. But that firm did not have the capital.

Finally, Sony agreed to buy the company. This generated the capital necessary for MRC's modernization. The acquisition enabled MRC to stay in business, strengthen its competitive position, keep its team of scientists and engineers working together on new technologies, and secured the jobs of its employees.

♦♦ **The Moore Special Tool Co.—Fanuc Ltd.** Moore Special Tool Co., based in Bridgeport, Connecticut, makes customized manufacturing equipment used in the production of high-tech products such as atomic weaponry. The company is the only American supplier of certain products used by the departments of Defense and Energy.

The company was having difficulty in 1990 finding domestic investors to supply the capital it needed for the research and development of new products and modernization of its facilities. But Fanuc Ltd., the Japanese manufacturer of machine tools and robotics, in January this year offered Moore $10 million for a 40 percent minority share. The Committee on Foreign Investment in the United States and the Bush Administration agreed to the sale. However, after increased congressional complaints that the sale would jeopardize national security, Fanuc withdrew its offer.[28]

♦♦ **Semi-Gas Systems, Inc.—Nippon Sanso KK.** Based in San Jose, California, Semi-Gas is an American manufacturer of specialized equipment used in the production of semiconductor chips. Nippon is a Japanese manufacturer of semiconductors. Nippon wanted access to American production facilities to gain more

27 Sheldon Weinig, "The Guys in White Hats from Sony," *New York Times*, June 10, 1990, p. F13.

28 Council on Competitiveness, *op. cit.*, p. 4; "Japanese Drop a U.S. Investment," *New York Times*, February 20, 1991, p. D1; "U.S. Clears Japanese Stake in Atomic-Arms Toolmaker," *New York Times*, January 18, 1991, p. A5.

market share in the U.S. Typical of Japanese companies, Nippon found it difficult to sell semiconductors in America as a result of the 1986 U.S.-Japanese Semiconductor Agreement, which restricted the flow of Japanese semiconductors entering the U.S.[29] To secure access to the U.S. market, Nippon offered to buy Semi-Gas for $23 million.

Semi-Gas is a subsidiary of the American aerospace firm Hercules, Inc. Hercules wanted to sell Semi-Gas, including its technology, to raise funds for research and development projects. The technology that Nippon would acquire was considered by its owners to be "old" technology. Hercules had no intention of giving the Japanese access to its other technologies. The Justice Department, however, objected to the sale and tried to stop it on national security grounds under the Exon-Florio provision. Hercules responded by taking the case to court, and this March won a ruling allowing the sale.[30]

These examples show that foreign investment can be very helpful to American companies. Materials Research Corporation was on the verge of bankruptcy. It had tried all domestic avenues and found no willing American buyers. Without the investment from Sony, the company would have shut down.

In the Moore Special Tool Company case, the persistent roadblocks erected by Congress forced the frustrated Japanese investor to pull out. In this case, just the threat of increased restrictions on foreign investment was enough to sour the deal.

HOW TO REFORM INVESTMENT CONTROLS

Foreign investment has greatly helped to sharpen America's competitiveness. Most of America's infrastructure was built with foreign capital. And today, foreign capital employs millions of Americans and provides billions of dollars to U.S. companies for research, modernization, and the development of new products. The Bush Administration and Congress thus should remove restrictions on foreign investment, not add to them. Specifically, the U.S. economy would benefit if Congress were to take the following steps:

STEP #1: Repeal the Exon-Florio provision.

Almost all of the cases that have been brought before CFIUS have turned out not to involve any threat to national security. Only one proposed deal was blocked by the President. Yet the threat of government investigations and delays makes the U.S. less appealing to foreign investors. This denies many American firms access to foreign capital and thus limits their ability to compete.

29 See Bryan T. Johnson, "The U.S.-Japan Semiconductor Agreement: Keeping up the Managed Trade Agenda," Heritage Foundation *Backgrounder* No. 805, January 25, 1991.

30 "Court Lets Japanese Concern Buy U.S. Company," *New York Times*, March 27, 1991, p. D2; "Court Clears Way for Hercules Inc. Sale of Unit to Japan," *Wall Street Journal*, March 27, 1991, p. A16; "Does Foreign Investment In U.S. Pose a Threat," *Washington Post*, October 23, 1990, p. C1.

An expanded version of Exon-Florio, covering all foreign investments and giving Congress effective control over which companies can invest in America, would be disastrous. Such a provision rightly would be seen by foreigners as a tool for lawmakers to penalize particular foreign firms and as a backdoor device to close the U.S. market to foreign investment. Retaliation would surely result. Thus an expansion of Exon-Florio not only would harm American firms operating in the U.S., but also would threaten American firms operating overseas.

STEP #2: Allow foreign investors the freedom to purchase a larger stake in U.S. airlines and to operate domestic flights.

Foreigners are prevented by law from acquiring more than 25 percent of U.S. airlines and from operating domestic flights in the U.S. Allowing foreign purchases and investments in this sagging industry would provide needed capital for several financially-strapped U.S. airlines. Scandinavian Airline System's offer to invest a significant amount of money in Continental Airlines shows how foreign capital could save an American company. Texas Air, the holding company for Continental, already has lost one of its airlines — Eastern — to bankruptcy.

An infusion of foreign capital could help avoid further layoffs in the industry, allow restructuring, and enable some U.S. airlines to expand their operations. In addition, the increased competition resulting from permitting foreign airlines to enter the American market would give more choices to travellers and spur greater efficiency in the industry.

STEP #3: Allow foreigners to own and operate banks in the U.S.

Foreign banks are heavily regulated in the U.S. In particular, foreigners are not permitted to control the board of directors of a foreign bank operating in the U.S., such as Barclays North America. Moreover, foreigners are restricted from owning a U.S. domestic bank like Citibank. Allowing foreign access to own and operate this protected industry would boost efficiency by allowing foreign banks to open across the U.S. Foreign investors also might be interested in buying out certain failing U.S. banks, enabling them to escape bankruptcy and thus avoiding bailouts by U.S. taxpayers.

STEP #4: Inject greater competition into the commercial shipping industry by allowing foreign investors to own and operate ships within U.S. waters.

Federal law currently requires that all goods transported between U.S. ports must be carried in American ships, even when using foreign ships would reduce transportation costs and so lower costs to consumers. In addition, foreigners are prohibited from owning and operating American-flagged merchant vessels. These restrictions add billions of dollars a year to U.S. products carried by ship. The lack of competition has made the industry inefficient and wasteful. Opening the industry up to foreign capital and competitors thus would cut costs to consumers and provide much needed incentives for the U.S. shipping industry to modernize.

STEP #5: Allow foreigners to own and operate public utilities.

Title 16 of the U.S. Code restricts foreigners from owning and operating U.S. utilities, such as energy plants. But many state and local governments, as well as private firms, today are finding it difficult to raise capital domestically for mod-

ernizing public utilities. This forces utilities either to raise prices to acquire investment funds or to increase their indebtedness by selling bonds. Yet in the past, much of America's infrastructure was built with foreign capital. Today that nourishing inflow of capital is being stifled by red tape.

CONCLUSION

Foreign investment has made an important contribution to America's economic growth and has helped to improve the living standards of all Americans. Much of America's infrastructure was built by foreign investment. Today, many companies are turning to foreign investors and partners to increase their capital resources for research and development, and to increase their access to foreign technology. This allows American firms to survive and expand in the face of fierce international competition.

But existing and proposed laws threaten that access to foreign capital. The impetus for these restrictions is the fear among some lawmakers that foreign direct investment results in loss of technology. But this is unfounded. There is no evidence that foreign firms target high-tech industries for takeover. Nor is there evidence of any net loss of technology secrets abroad because of purchases by foreigners of interests in U.S. firms. Tightening current foreign investment restrictions in response to unfounded fears would seriously cripple America's ability to compete.

The world is growing ever more economically interdependent. Direct investment by foreigners in U.S. industries and American investment in foreign firms is a necessary part of that interdependence, and makes all the firms involved more efficient. It also raises the living standards of both Americans and foreigners.

Recipe for Strength. For the U.S. government to try to buck this trend would be economic suicide. That would allow firms in other countries to gain the benefits of using foreign capital while denying U.S. firms that same benefit. The result would be a reduction in U.S. competitiveness and a loss of jobs. Instead, the Bush Administration and Congress should work together to increase the access of U.S. firms to foreign investment and to foreign competition. Trying to insulate the U.S. economy from the rest of the world is a recipe for weakness, not strength.

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