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**Further Evidence  
on the Consequences of  
Foreign Direct Investment  
for the New Zealand Economy**

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The considerable debate within New Zealand concerning the impact of foreign direct investment (FDI) has been conducted with little regard to evidence on the matter (Enderwick, 1995, p.2)

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# 1. Introduction

After 1984 the New Zealand economy underwent a radical transformation, moving from, arguably, the most regulated economy in the western world to the world's freest market economy (Passow, 1992). One aspect of this economic deregulation involved major changes in the area of foreign investment - restrictions in areas such as exchange control, overseas borrowing and access to capital markets were gradually removed. These new, liberal policies and an extensive privatisation program opened up a number of opportunities to overseas investors (OECD, 1993). Subsequently, in the early 1990s, the government declared a further relaxation of policies and introduced an investment promotion program.

The political and economic impact of foreign investment in New Zealand has been the subject of intense public debate. Recently Dr Don Brash, Governor of the Reserve Bank of New Zealand, has made arguments in favour of foreign investment, concluding that 'Almost all foreign investment will be of benefit to New Zealand and New Zealanders' (Brash, 1995, p.254). Dr Brash asserts that foreign investment provides capital, technology, market knowledge, and market contacts. On the other hand, concerns are raised that foreign investment threatens New Zealand's sovereignty and results in the exploitation of our markets and resources. Also, concerns have been expressed over the economic motivations of some overseas investors, especially in areas such as rural land and leisure facilities (Enderwick and Akoorie, 1994).

Our study builds on the Enderwick's (1995) report, *The Contribution of Foreign Direct Investment to the New Zealand Economy*, which was prepared for the American Chamber of Commerce. Our objective is to examine the consequences of foreign investment for the New Zealand economy. To this end we investigate the following areas:

- Transfer of capital
- Management practices
- Repatriation of earnings
- Training effects
- Technology transfer and innovation
- Competition and consumer choice
- Managerial decision making
- Access to export markets
- Community support
- Commitment to the New Zealand market
- Employment effects
- Linkages with indigenous firms.

## 2. Literature Review

Research on foreign investment and its impact on the economy is generally equivocal (Denison, Dutton, Kahn, and Hart, 1996). Kahley (1990, p.153), however, noted that most economists agree that international capital flows help companies use world resources. Foreign investment is thought to increase competition via entry of new firms that cut costs, increase productivity, or enhance product quality. Consumers should benefit from lower prices, better choice and improved quality of available products and services. In theory, foreign investment should benefit workers and company owners (Kahley, 1990): Workers may benefit through increased wages and rises in employment rates. Owners may benefit because the availability of foreign capital may decrease the cost of some plant investment projects and thus increase the value of the firm.

Although an increased supply of capital through foreign investment may lower interest rates and therefore decrease interest income of domestic savers, foreign investment is generally seen as beneficial because, theoretically, it should increase economic growth. On the other hand Duncan (1994) reports that although foreign direct investment (FDI)<sup>1</sup> can increase domestic investment in some circumstances, current account deficits may widen unless domestic savings also increase. In any event, any causal links between FDI and the rate of economic growth cannot be taken as self-evident.

From a social perspective a number of benefits have been proposed to derive from inward FDI. Duncan (1994) notes that FDI brings new management and technical expertise, and improves access to export markets through connections with foreign distribution systems. Enderwick (1995) points out possible employment and training creation effects of inward investment and that local research and development capabilities may be strengthened. He also states - rather obviously - that foreign-owned companies contribute millions of dollars in tax to the New Zealand economy.

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<sup>1</sup> Foreign direct investment is defined by Statistics New Zealand as: Investment that is made to acquire a lasting interest in an enterprise; the investors purpose being to have a significant influence in the management of the enterprise. Such an influence is inferred to exist when an investor holds more than 25% of voting share capital.

Transfer of management expertise was also examined by Enderwick (1995) whose research in New Zealand indicates that new management methods may be beneficial to the companies pursuing reform. Nevertheless these findings are inconsistent with those of early survey research by Campbell, Bollard, and Savage (1989) that show no significant relationship between foreign ownership and increased competitiveness.

The effect of FDI on employment has proven especially difficult to measure. Enderwick (1995) studied some of the foreign-owned companies that had entered the New Zealand market through acquisition, and found that most of these companies added to net employment or maintained before-acquisition employment levels. Although his findings are based on case studies of only eleven companies, Enderwick asserts that for acquisitions the absence of foreign investment is likely to result in substantial job losses. On the other hand, Graham and Krugman (1989) suggest that the number of jobs created by foreign investment is about the same as that created by domestic investment.

The impact of foreign investment on research and development activities appears largely unexplored. Although Enderwick (1995) asserted that inward foreign investment strengthens local research and development capabilities, there is no substantial evidence to support this view. On the other hand, the transfer of technology has been supported by somewhat more convincing data.

The threats that are mostly associated with foreign investment are possible loss of economic activity, loss of sovereignty, change of ownership levels, and capital flight (Enderwick and Akoorie, 1994). Brash (1995) argues that there is very little danger to New Zealand sovereignty, because all foreign companies must comply with New Zealand laws and regulations, and these laws are designed not only to attract FDI but also to ensure that the ultimate authority resides with the New Zealand Government (see Fox and Walker, 1996). As to capital flight, some writers assert that economic developments that will encourage foreign companies to invest elsewhere will have similar effects on domestic savers (Enderwick and Akoorie, 1994).

Although the issues regarding threats and benefits of foreign investment have been widely discussed, in practice it is very difficult to accurately estimate the net economic impact of FDI on any economy. It is not our intention to undertake such an onerous task, rather we seek to

add to our knowledge of the consequences foreign investment as manifested in the controlling shareholdings of some large New Zealand based companies.

### **3. Method**

The sample for this research was drawn from the *Management* magazine's Top 200 New Zealand companies, determined by annual turnover in 1995. Seventy-eight companies among the Top 200 were more than 50% foreign-owned. Contact details for these firms were obtained from *New Zealand Business Who's Who*. A questionnaire - based largely on Enderwick's (1995) study - was mailed to the chief executive officer (CEO) of each firm in September 1996. Nineteen questionnaires were returned, giving a response rate of 24 per cent.

### **4. Results**

#### **4.1 Transfer of Capital and Repatriation of Earnings**

One criticism of foreign direct investment is that the capital raised locally by foreign investors leads to increased interest rates in host countries (Enderwick, 1995). There is, however, little empirical data in support of this view. Our results show that the nineteen companies responding to our survey committed almost a billion dollars to additional investments in New Zealand over the past three years, an average of \$52 million per company. Of our sample companies, sixteen gave information about whether they obtained additional investment finance within New Zealand, or from overseas. For these companies, 36% of the finance for additional investments was obtained from overseas. These figures are in contrast with Enderwick's (1995) findings, which found that all finance was obtained from overseas sources.

Nine of our respondents saw some advantages in borrowing overseas as opposed to within New Zealand; eight respondents saw no benefits in borrowing overseas; two respondents did not answer this question. The main advantages of borrowing overseas mentioned by the respondents was lower interest rates. For debt finance minimising exchange risks was also



mentioned. Greater availability of capital was also mentioned as an advantage of gaining equity finance overseas.

Respondents were also asked if they saw any disadvantages in obtaining investment funds overseas: nine said *yes*; eight said *no*; two did not respond. A number of disadvantages of borrowing overseas were mentioned, including - for debt finance - foreign exchange exposure, withholding tax, appreciated NZ dollar, administration costs, political turmoil and better terms in New Zealand and - for equity finance - foreign-exchange exposure and inability to use tax credits.

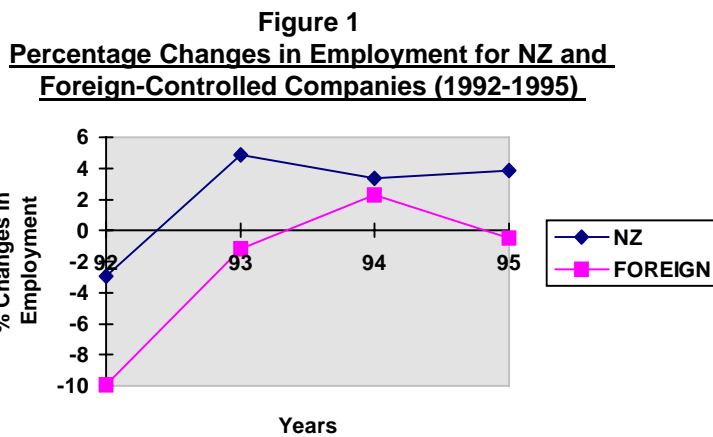
Another criticism of foreign investment is that foreign-owned companies repatriate most of their earnings (Enderwick, 1995). The respondents in our study stated that they re-invested, on average, 80% cent of their earnings in New Zealand. Furthermore, nine of the sixteen companies (56%) that responded to that question re-invested 100% of their earnings. The main reasons given by respondents for re-investing funds in New Zealand were to finance company growth, develop, improve and expand as well as to reduce debt.

## **4.2 Employment and Training Effects**

A positive impact of foreign investment on employment rates has been mentioned by various researchers (Enderwick, 1995; Kahley, 1990). Enderwick (1995) analysed the employment changes within eleven companies, and found that these companies increased or, at least sustained, the employment levels from the time of business acquisition. He concluded that the 'absence of foreign investment could have been associated with substantial job loss' (Enderwick, 1995, p.12). Ebashi (1993), reported that, for the 1989-91 period, there was significant growth in employment in firms with more than 50% overseas ownership.

Still, the exact impact of foreign investment on employment is very difficult to quantify. This study examined the employment effects of foreign investment using both primary data obtained from the survey and secondary data that have been published in the December issues of *Management* magazine for the years 1992-95. Using this data percentage changes of employment rates within twenty-two companies that were at least 50% foreign-owned were

compared with similar changes of employment within thirty-six New Zealand owned<sup>2</sup> companies for the 1992-95 period. A one-way ANOVA showed that, for the year 1992, the percentage change of employment from 1991 in New Zealand owned companies differed from that of foreign owned companies at the 0.05 significance level. For the years 1993, 1994 and 1995, the percentage change of employment was not significantly different between New Zealand and foreign owned firms. Longitudinally the test shows that, for New Zealand owned companies, no two years were significantly different at the 0.05 level, whereas, for foreign-owned companies, change of employment in the year 1992 was significantly different from the other three years. These changes are illustrated in Figure 1.



From these findings we conclude that rates of change on employment for New Zealand owned companies were relatively stable for 1992-95. However, it is important to stress that the analysis of these data suffer from the limitation of dealing with a small sample of companies.

One of the concerns raised about foreign investment is that foreign-owned companies have a tendency to bring managers from overseas (Enderwick, 1995). Our study examined the percentage of managers employed within each company that were from overseas. Only 30 overseas managers were employed among a total of 2,409 managers (i.e., 1.2%). Ten of the nineteen companies in our survey did not employ any overseas managers. These findings indicate that foreign companies rely heavily on New Zealand managers. In our survey, CEOs were also asked, ‘What benefits do you believe that being foreign-controlled gives your company in terms of employee training?’ Ten of the nineteen respondents stated that foreign

<sup>2</sup> These are companies with 50% or more New Zealand ownership.

companies can offer overseas training within the parent company and their subsidiaries. These and other benefits listed by the respondents are shown in Table 1.<sup>3</sup>

**Table 1**  
**Perceived Benefits in Terms of Employee Training**  
**(19 companies)**

<b>Benefit</b>	<b>No. of Respondents</b>
Overseas training within parent company or their subsidiaries	10
Access to good trainers and expertise	6
Access to proved technology or management systems	5
Global experience	3
Economies of scale	2
Overseas promotion	2
None	2

Respondents were also asked about disadvantages of being foreign-controlled for employee training. The majority of respondents (fourteen out of the eighteen respondents - 78%) who answered this question believed that there were no such disadvantages.

### **4.3 Competition and Consumer Choice**

It is often argued that foreign investment increases competition in local markets (Kahley, 1990). Seventeen of our nineteen respondents believed that their company's presence added to competition in the industry in which they operated; one company said the question was not relevant as they exported 98% of their products; another company just said the question was not relevant. Respondents were also asked to give reasons why they believed their company added to competition within the industry. Of the fifteen respondents answering this question: seven said that their presence in the industry as a major player increased competition; four

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<sup>3</sup> Note that respondents may have given more than one answer.

respondents said that competition was increased through their use of best practice, technology, or products. Our data are consistent with Enderwick's (1995) findings which indicate that foreign investment adds to competition in local markets.

#### **4.4 Management Practices**

Fox and Roy (1994) reported that foreign investors may introduce management skills into the companies operating in New Zealand, and that this can lead to improved performance. However, evidence of the transfer of new management practices is mixed (Callister, 1991). Some researchers have found that foreign ownership did not yield improvements in company competitiveness (Campbell et al., 1989).

Our study examined how the management skills used in foreign owned companies differed from those of New Zealand owned companies. Of our nineteen respondents: nine thought that their company's management practices differed in some important respect; four believed there was no difference; two didn't know if there was any difference; three said the question was not relevant (had no New Zealand competitors) and one did not respond. One reason for these differences may be that foreign owned companies are often part of large corporations and therefore may be more structured than smaller New Zealand companies.

Findings also showed that 84% of the companies have full authority over operational decisions, but only 32% have full authority over strategic decisions.

#### **4.5 Exports and Access to Export Markets**

One of the most frequently emphasised benefits of foreign investment is improved access to production, marketing and distribution networks that have been developed by overseas firms. Enderwick (1995) found that access to these corporate networks can improve market access offshore and effectively promote exports. Although most companies examined in Enderwick's research agreed that access to corporate networks was the most important factor in defining their success, export data were not provided. In contrast, some American studies of foreign investment's impact on exports show that, in 1977 and 1986, foreign manufacturing affiliates were less likely to export than their U.S. owned counterparts (Kahley, 1990).

The companies that were examined in our study exported, on average, 31% of the total value of their annual turnover. The percentage of the total value of turnover exported by these companies ranged from zero to 98%. Only three of the eighteen responding companies did not export at all.

Sixty-four per cent of the companies that did export typically used existing marketing chains developed within their parent organisation to do so. Most of the companies also had access to production, marketing and distribution networks of their parent company (this includes companies that do not export). These findings are shown in Table 2.

**Table 2**  
**Access to Networks of Parent Company**  
**(17 Companies)**

<b>Network</b>	<b>No. of Companies that have Access</b>
Production	15
Marketing	16
Distribution	14

The benefits that are gained from these networks are listed in Table 3. Other benefits that were mentioned by some of the respondents were: access to plant and new product lines and name recognition.

**Table 3**  
**Perceived Benefits Gained from Networks**  
**(16 companies)**

<b>Benefits Gained</b>	<b>No. of Respondents</b>
Access to market intelligence, knowledge or experts	7
Established Channels	6
Technology	3

#### **4.6 Linkages with Indigenous Firms**

Data from our survey shows that total supplies that were purchased from the local suppliers ranged from 2 to 100%, with an average of 56%. The companies in our sample distributed, on average, 19% of (the dollar value of) total output through local distributors, 8% through overseas distributors, and 73% through their own distribution networks.

Foreign investment can benefit the local economy through linkages with indigenous firms. These connections may include associations with suppliers, distributors and buyers (Enderwick, 1995). Although Enderwick acknowledged the positive effects of these linkages on the local economy the exact impact has proven difficult to establish. This study generated data suggesting that the foreign owned companies that participated in the survey had strong linkages with the local businesses. However 73% of the total output was distributed through their own distribution networks. This may be because most of the companies surveyed here are large and, therefore, may place a strong emphasis on vertical integration.

#### **4.7 Community Support**

In our study, CEOs were asked to list the benefits to the wider community that they believed resulted from their companies presence in New Zealand. Although such benefits may be associated with community project, sponsorships and donations, the majority of CEOs listed other factors that they believed were beneficial to the society. Such factors included an

increase in direct employment, technology transfer and a better choice of products - see Table 4.

**Table 4**  
**Perceived Benefits of Foreign Investment for the Wider Community**  
**(19 Companies)**

<b>Benefit to the Wider Community</b>	<b>No. of Respondents</b>
Creation of direct employment	9
Technology transfer	5
Better consumer choice	4
Donations and sponsorships	4
Transfer of knowledge, best skill or practice	3
Introduction of excellent products and services	3
Contribution in taxes	3

#### **4.8 Technology Transfer and Innovation**

Enderwick's (1995) research found that in some areas such as knowledge-intensive industries, access to global information systems was the source of major advantages for foreign-owned companies. Enderwick's assertions are consistent with findings of other researchers, such as Graham and Krugman (1989), Kogut (1991) and Reich (1990), all of whom agree that increased foreign investment helps to 'diffuse foreign technology and managerial skill into the host country' (Denison et al, 1996, p.459).

Of our nineteen respondents, fourteen said that they received some technology inputs from their parent company or sister affiliates; four said they did not; one respondent didn't answer this question. CEOs were also asked how these technology inputs benefit their companies. Only twelve CEOs answered this question. The main benefits cited were: increased business efficiency (4 respondents); increased competitive advantage (4 companies); product advances (3 companies).

## **4.9 Commitment to the New Zealand Market**

The companies in our sample appear very committed to the New Zealand market. All nineteen companies intend to continue their operations in New Zealand in the future: eighteen of nineteen companies (95%) companies said that it was *very likely* that they would still be operating in New Zealand in five years time; the remaining company said this was *likely*. The commitment of these companies to their New Zealand operations is also reflect by the length of time they have been operating here - 37 years on average (the range was 5 to 100 years).

## **5. Conclusion**

Although the literature on threats and benefits of foreign investment is quite extensive, empirical information on the impact of foreign companies on the New Zealand economy and the wider community is difficult to find. While the public debate on foreign investment continues in New Zealand, the foreign investment policies introduced in the past decade reflect the view that foreign investment is beneficial to the economy (Callister, 1991). The results generated in this study lend some support to this view.

Despite various limitations, including a small sample and the possibility of response bias, this paper adds to the limited data on the practices of foreign-owned companies and their impact on the New Zealand economy. The data gathered in this study indicate that foreign-owned companies show a strong commitment to the New Zealand market by re-investing, in some cases, all of their earnings (more than half of the companies surveyed did so). All of the companies surveyed have been operating in New Zealand for at least five years and believe that they will still be operating here in the future. The majority of the companies exported their products, utilising the already existing channels of their parent companies. In today's competitive global market place this is a major advantage for a host country, as these export markets may have never been captured by New Zealand companies. Foreign-owned companies generate local business by using local suppliers.



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