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USA: Law & Practice & Trends and Developments

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Trends and Developments

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Overview

In 2022 and the first half of 2023, the USA was the leading recipient of inbound foreign direct investment (FDI) as well as the largest investor in outbound FDI worldwide, according to the OECD. And the USA topped the list in Kearney's Foreign Direct Investment Confidence Index as the most attractive market for FDI – for the eleventh year in a row. Perhaps this is just concomitant with the USA being the largest economy in the world. Perhaps it reflects the flight of FDI flows to a more stable and predictable jurisdiction in times of uncertainty in recent years. Perhaps it can be attributed to the simple good fortune of having access to abundant energy sources, being geographically removed from geopolitical strife, and dynamic and durable consumer spending.

Amidst a complex and changing political, economic and social backdrop, the USA has faced a number of factors that have influenced its position as one of the top jurisdictions for FDI again in 2023, including as a result of legislative and executive action with direct implications for FDI.

CFIUS and National Security

While the Committee on Foreign Investment in the United States (CFIUS) has been around for many years, the passage of the Foreign Investment Risk Review Modernization Act in 2018 and its implementation since adoption expanded the scope of transactions subject to review, required certain mandatory filings for the first time and enhanced the focus on transactions involving critical technologies, critical infrastructure and sensitive personal data. Using this broadened grant of authority, CFIUS reviewed 440 total filings made by transaction parties in 2022. It identified for consideration an additional 84 transactions that had not been notified by the transaction parties.

In September 2022, President Biden signed an Executive Order titled Ensuring Robust Consideration of Evolving National Security Risk by the Committee on Foreign Investment in the United States, which for the first time provided specific presidential direction to CFIUS on the risks that it should consider in its reviews of inbound investment transactions by non-US persons. The Executive Order highlighted a number of areas, including US supply chain resilience, US technological leadership (including in sectors such as microelectronics, artificial intelligence, biotechnology and biomanufacturing, quantum computing, advanced clean energy and climate adaptation technologies), risks of aggregate industry investment trends, cybersecurity and cyber-enabled malicious activity, and US persons' sensitive personal data (including health, digital identity and biological data). While the areas of focus identified are not explicitly targeted at any individual foreign nation, they reflect a broader policy trend within the Biden administration of repositioning the USA for a period of strategic competition with China and using CFIUS in particular to ensure that advanced technologies developed in the USA are adequately protected from access that may enhance China's capabilities.

Overall, for deal practitioners, the CFIUS process is well established in the deal landscape for inbound M&A and other forms of investment. Although the CFIUS process has remained fairly consistent from the Trump administration to the Biden administration and the vast majority of transactions notified to CFIUS are still being approved, recent data suggests that CFIUS has realigned towards a more vigilant posture, with extended reviews and onerous inspection likely to continue for the foreseeable future.

Federal Government Stimulus

In recent years, the Biden administration has succeeded in passing a number of significant pieces of legislation that have had a profound impact on the FDI landscape in the USA, drawing interest from companies around the world to invest and grow their US operations.

In November 2021, the US Congress passed the Infrastructure Investment and Jobs Act providing for USD550 billion in new investment in transportation infrastructure, clean energy and water, and broadband internet access, including USD60 million for clean-energy-related projects. In August 2022, the US Congress passed the Inflation Reduction Act, which allocated USD369 billion to energy security and climate change. Also in August 2022, the US Congress passed the CHIPS and Science Act, intended to boost innovation and national security with respect to semiconductors and other advanced technologies by allocating USD200 billion to scientific research and development, USD53 billion to semiconductor manufacturing and USD24 billion to tax credits for domestic chip production.

The combined effect of these acts, as well as numerous other governmental policies, has been to supercharge investment in the USA in the areas that the Biden administration views as critical to national security and to winning a strategic competition with China over advanced technologies and supply chains. Since the passage of these acts, there has been a sharp increase in US construction spending for manufacturing facilities, with real manufacturing construction doubling since the end of 2021, and at least USD224 billion in cleantech and semiconductor manufacturing projects have been announced in the USA. According to the US Bureau of Economic Analysis, FDI in new US manufacturing production capacity increased 247% from 2021 to 2022, reaching USD5.3 billion and reversing a multi-year downward trend that began in 2019. Approximately USD2,230 billion or 42.4% of inbound FDI in the USA in 2022 was in the manufacturing sector, which shows the effect of financial and regulatory incentives in growing domestic manufacturing capabilities. In November 2023, the Biden administration announced the creation of the White House Council on Supply Chain Resilience, tasked with supporting the resilience of America's critical supply chains and in turn facilitating lower costs for American families.

Whether through investments in background research that enables technological breakthroughs or the training of a talented workforce or the allocation of tax credits to support domestic manufacturing operations or the upgrading of infrastructure that is critical to transporting products within the USA and to export markets, these acts have stimulated an increase in inbound FDI to the USA on top of existing economic and geopolitical tailwinds.

Focus on China

While one primary objective of the CHIPS and Science Act was to foster research and development and semiconductor manufacturing at home in the USA, another key factor in its adoption was the development of the Chinese semiconductor industry and its ability to develop its own advanced technologies. In fact, the White House announcement of the act overtly stated that the "CHIPS and Science Act Will Lower Costs, Create Jobs, Strengthen Supply Chains, and Counter China". One requirement under the act for receipt of the financial incentives and tax credits is that the recipient not invest in expanding semiconductor manufacturing in China during the following ten years – effectively facilitating the investment in the US semiconductor industry while simultaneously impeding the growth of China's semiconductor industry. This is consistent with National Security Advisor Jake Sullivan's statement in December 2022 that the USA "must maintain as large of a lead as possible" in certain key technologies.

The Biden administration went further in October 2022 when the US Department of Commerce's Bureau of Industry and Security (BIS) adopted a series of updates to its export control regulations targeting both advanced computing and semiconductor manufacturing in China. In October 2023, the BIS updated and expanded the export control regulations with two new rules to increase the effectiveness of export controls and "shut off pathways" to evade BIS restrictions. Citing concerns about China's military-civil fusion strategy and the development of frontier intelligence capabilities that could lead to advanced weapon systems, the new regulations expressly sought to keep technologies that are important to the development of artificial intelligence, automation and surveillance beyond the reach of Chinese companies or state actors.

The expanded regulations – which are exceedingly complex – apply not just to US-based firms but in some cases also to non-US companies that produce items using technology developed in the USA. The regulations also restrict the ability of US persons to support the development or production of semiconductors at certain Chinese facilities without a licence.

Chinese FDI into the USA had already been significantly hampered by aggressive CFIUS enforcement and the trade war policies enacted under the Trump administration. But the steps taken by the Biden administration in 2022 and 2023 have led to a new chapter for FDI between the USA and China, and the world as a whole. Looking across new FDI into the USA, new Chinese FDI accounts for less than 0.5% of the 2022 total, according to the Bureau of Economic Analysis. In fact, in mid-2023, Mexico surpassed China as the largest trading partner of the USA. If the USA and China continue down a path of "decoupling" in the coming years, then countries across the globe may be forced to choose sides between them and in essence participate in either a US-centric FDI ecosystem or a China-centric FDI ecosystem. While the politics of "near-shoring" and "friend-shoring" that arose from the supply chain disruptions during the worst of the COVID-19 pandemic began to nudge the world in this direction, further FDI and other restrictions from both the USA and China would only accelerate the separation of supply chains and investment and technological spheres.

Outbound FDI Regulation

On the other side of the ledger, the USA was the leading investor in outbound FDI to other countries in 2022 and the first half of 2023. Large US multinational companies across industries from the technology sector to the automotive industry to the hospitality space have continued to invest heavily abroad, even during the past few challenging years. Given the rapid rebound from the COVID-19 pandemic in the USA, US multinational companies were in a prime position to take advantage of investment opportunities in countries that had a slower path to recovery.

However, on the regulatory front, there has been growing momentum in Washington, DC to focus on the potential national security risks of outbound FDI in addition to the more traditional scrutiny of inbound FDI through CFIUS. A draft bill titled the National Critical Capabilities Defense Act has been proposed several times in Congress in recent years and would create a new framework for national security screening of certain outbound FDI from the USA. Proponents of the bill argue that US companies investing in technology development overseas can increase the capabilities of US competitors and adversaries, thereby creating national security risks equivalent to those that may result from non-US companies acquiring US-based businesses. The bill would also provide the US government with stronger tools to monitor and influence the supply chains of US companies, including any links to countries like Russia, China and others.

Critics of the bill argue that it would harm the competitiveness of US companies investing abroad or even result in a raft of new similar legislation in countries around the world in response that could hamstring inbound FDI to the USA and the global economy at large. Just as CFIUS served as an influential model for inbound FDI review regimes adopted around the world in recent years, a US-led push to screen outbound FDI may be the next wave of regulation to buffet FDI flows globally.

Although the National Critical Capabilities Defense Act has not been enacted, in August 2023, President Biden issued an executive order addressing many overlapping concerns. The executive order declared a national emergency relating to certain countries (namely, China) exploiting US outbound FDI to develop certain sensitive technologies and products critical for military, intelligence, surveillance and cyber-enabled capabilities, including semiconductors, quantum information technology and artificial intelligence. In accordance with the executive order, the US Treasury Department issued an Advance Notice of Proposed Rulemaking detailing a new outbound FDI programme prohibiting outbound FDI involving sensitive technologies and requiring notification of certain types of outbound FDI to "countries of concern", which, as proposed, includes only China (including Macau and Hong Kong). The regime previewed by the executive order and the US Treasury Department's Advance Notice of Proposed Rulemaking is not expected to become effective prior to 2024.

Although the Administration has proposed an outbound investment screening regime to be implemented via executive action, there is still bipartisan support in Congress for legislative action.

Conclusion

It is as challenging as ever to look into the crystal ball to predict whether the USA will retain its top spot for both inbound FDI flows and outbound FDI flows in 2024 and beyond. Yet many of the headwinds that have been impacting growth in recent years appear to be subsiding – from gradually decreasing inflation to interest rates at (or near) their expected peak to a rising (if still volatile) stock market.

Yet it is the constants in the USA market that are likely to provide the biggest boost to inbound FDI in the years to come – a skilled and innovative workforce, access to a large and affluent consumer market, stability and predictability of judicial outcomes, and favourable tax rates and regulatory regimes. Heading into a pivotal election year in 2024, it would be prudent to recognise that it is these constants that have made the USA the world's pre-eminent jurisdiction for FDI and any changes that jeopardise them need to be approached with due caution.

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