Chapter 6

America's Role in International Capital Flows

Just as international supply chains are vital for goods trade to function, international capital flows are essential to a resilient global monetary system, allowing savings to flow across borders to facilitate investment.[1] The United States participates actively in both sending and receiving funds internationally, whether by domestic citizens buying foreign equities or foreign investors helping to finance new semiconductor plants on U.S. soil.

International capital flows are cross-border investments in financial assets recorded in the financial account of the balance of payments. These flows include investment in stocks and bonds known as portfolio investment, real assets such as factories and equipment known as foreign direct investment (FDI), and cross-border lending by global banks. Capital inflows thus provide an important source of funds that finance investment in the United States. Analogously, U.S. firms and investors provide significant amounts of capital to finance investments in stocks, bonds, and factories around the world.

The strength and resilience of the U.S. post-pandemic recovery helped to make the United States a magnet for foreign investment. Equally important, the Biden-Harris investment agenda in infrastructure, clean energy, and semiconductor technology has served as a productive target for inflows.[2]

[1] International capital flows provide the United States numerous benefits, including access to financing, increased capital allocation efficiency, and enhanced diversification and risk sharing across borders. More broadly, global financial flows allow capital to be allocated to the most productive global investment opportunities.

[2] A significant share of this new foreign direct investment into the United States originates from trading partner countries, such as Canada, Japan, South Korea, and the United Kingdom (CEA 2023a).

The United States has increased its dominance of global financial flows, receiving the highest share of international capital flows in 2022-2023. Approximately 41 percent of global gross inflows were destined for the United States, almost doubling the country's pre-pandemic share of 23 percent (Allen and Bems 2024). The United States' currency also plays a unique role on the international stage, functioning as a reserve currency, denominating an outsized share of global trade, and denominating a large share of cross-border financial transactions (Boz et al. 2020).

A balance of pull and push factors helps determine the pattern of international capital flows (Fratzscher 2012; Forbes and Warnock 2012; Obstfeld 2024). Pull factors are domestic macroeconomic fundamentals, such as strong economic growth relative to trading partners, that can draw in foreign capital flows, allowing countries to invest in amounts exceeding the domestic savings pool. The strength of property rights institutions, investor protections, and corporate governance standards can also serve as pull factors on foreign capital (Chari 2020). Emphasizing pull factors and demand-based explanations suggest that some countries invest more than they save domestically due to expenditures at home financed by foreign capital inflows. Here, domestic macroeconomic fundamentals and domestic absorption patterns in receiving countries are the underlying drivers of current account deficits.

Push factors are common global factors that can move global savings towards certain destinations. Events like flights to safety during times of heightened global economic uncertainty can push funds, as can precautionary motives for channeling savings into reserve or safe haven currencies (Chari, Dilts Stedman, and Lundblad 2022; Goldberg and Krogstrup 2023). Another push factor dynamic was described by former Federal Reserve chairman Ben Bernanke in 2005 in the context of the "global savings glut," where excess savings in the rest of the world drove down global real interest rates (Bernanke 2005). In certain cases, such global imbalances can have damaging effects on capital-receiving countries, lowering savings rates and contributing to bubble investments (Obstfeld and Rogoff 2009), or sapping aggregate demand when there is short supply in the context of global liquidity traps (Eggertsson and Egiev 2019).

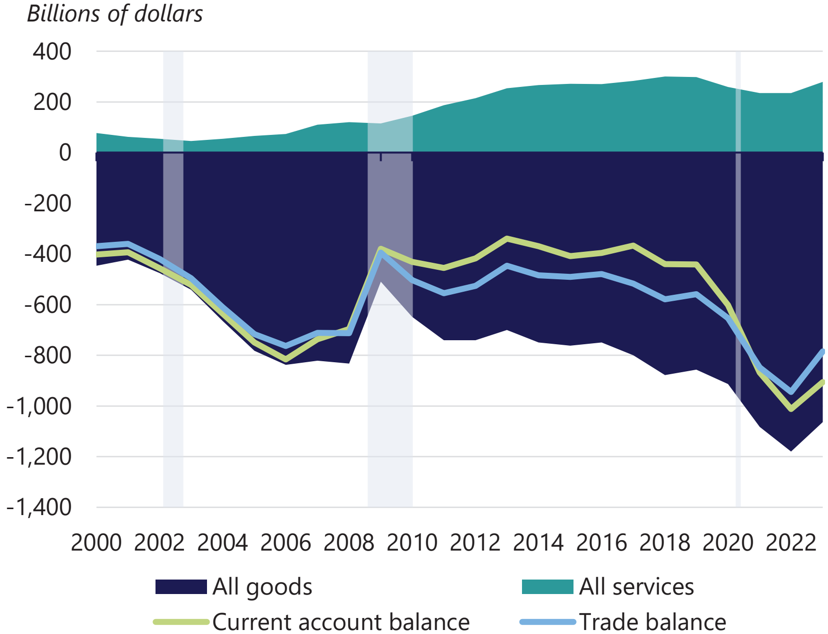
Both a strong economic recovery (pull factors) and investments into safe debt assets (push factors) have fueled the growing dominance of the United States in international capital flows. After a brief discussion of the U.S. current account, this chapter explores the financial account of the United States by tracking its different types of claims and liabilities. Given that flows of international capital into and out of the United States are the counterparts to the international trade transactions of imports and exports, we begin by providing a broad overview of the U.S. current account. Next, we explore the U.S. financial account and the international capital flows landscape. The chapter delves into the different classes of investment, beginning with portfolio investments in debt and equity and the returns that accrue to them, followed by changes in FDI and changes in other investments that primarily include cross-border bank lending. Attention is also paid to the international role of the dollar and the holdings of U.S. dollar reserves as safe assets by foreign investors.

The Current Account and Financial Account

Balance of payments accounts divide international transactions into three broad categories: the current account, the capital account, and the financial account. While the financial account captures the capital flows described above, the current account captures international trade transactions and net factor income from abroad.[3] For the balance of payments to balance, U.S. financial account surpluses that reflect tremendous global investor appetite for U.S. assets, financial and real, are mirrored by current account deficits.

[3] The current account includes statistics on the international trade of goods and services as well as receipts and payments of primary and secondary income. The capital account is usually a small part of the balance of payments records and includes capital transfer transactions like foreign aid and transactions of non-financial, non-produced assets like intangible capital. According to the Bureau of Economic Analysis, the financial account refers to "investment transactions—including direct investment, portfolio investment, other investment, reserve assets, and financial derivatives—between U.S. residents and nonresidents" (Bruner 2021).

Figure 6-1. U.S. Trade and Current Account Balances



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Sources: Census Bureau; Bureau of Economic Analysis; CEA calculations.

Note: Trade data are on a balance of payments basis. Gray bars indicate recessions.

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The current account has long been a subject of economic analysis, in part because the United States has nearly continuously run a current account deficit since the early 1980s. Because prior *Economic Reports of the President* have extensively covered the current account deficit, this chapter briefly touches on the subject before moving on to an in-depth analysis of the U.S. financial account (CEA 2022; CEA 2023b; CEA 2024a).

Figure 6-1 shows the U.S. current account from 2000 to 2023. The current account has averaged a deficit of $552 billion over the period, representing 3.3 percent of GDP. In 2023, the current account deficit was $905 billion, of which the balance on trade in goods and services was almost $785 billion. In 2023, income receipts were $1.57 trillion, and income payments were $1.69 trillion (BEA 2024a). Canada, China, and Mexico were the top U.S. trade partners in 2023, accounting for more than 30 percent of the country's exports and imports.

Breaking down the trade deficit into goods and services provides useful insight. The U.S. goods deficit ($1.1 trillion in 2023) overshadows the surplus in U.S. services trade ($278 billion in 2023), but notably the United States maintains a global comparative advantage in services exports.

Most of the services surplus has been driven by digitally-enabled services, which include all activities performed with information and communication technologies. Digital services are the fastest-growing trade category as the United States moves toward an increasingly services-based and digitally-enabled economy (CEA 2024b).

Economists have alternative views about the fundamental causes of America's persistently negative trade balance. Aligning with a focus on global push and pull factors, some economists note the role played by high savings rates in other countries, which can contribute to large capital inflows into the United States (Bernanke 2005; Pettis 2017). Such flows can boost productive investment. They can also depress savings rates and raise aggregate demand if they lower interest rates or contribute to the formation of bubbles.[4] The latter dynamic can contribute to more debt-fueled consumption than is healthy (Obstfeld 2017). Additionally, such flows tend to appreciate the country's exchange rate, and can contribute to an increase in the trade deficit if a country's exports become more expensive and uncompetitive on world markets while imports become cheaper. Recent trends in the exchange rate show that the U.S. dollar (hereafter referred to as the dollar) has risen by 7.4 percent in nominal terms relative to a representative basket of trading-partner currencies since 2020, according to the Federal Reserve's Broad Dollar Monthly Index as of October 2024, and the real trade-weighted value of the dollar is 15 percent above its 20-year historical average.

Foreign countries can have high savings rates for various reasons, ranging from demographic factors like an aging population to government policies suppressing consumption and thereby encouraging savings. Relevant government policies include limited public retirement systems or insufficient social safety nets leading households to save more than they otherwise would for precautionary purposes (Zhang et al. 2018). The implication of this dynamic is that trading-partner countries can play a role in shaping trade balances of other countries (Gourinchas et al. 2024).

It is important to recognize that a negative trade balance does not constitute a negative "score" for an economy. Indeed, the United States' post-pandemic recovery has been uniquely characterized by high levels of business investment, one third of which has gone toward factory construction (Van Nostrand 2024a). As a result, much of America's investment appears to be going to productive ends. Productivity is rising, business formation is increasing, and it is likely that these potentially lasting and transformative advances would not be possible without the supportive role played by international financing.

[4] A widely cited example of unproductive investment is the housing bubble of the early 2000s accompanied by a consumption boom that culminated in a global financial crisis with lasting negative effects on the U.S. economy.

Moreover, the global increase in international trade with U.S. trading partners has been essential in increasing the supply of goods, services, and capital. It has given rise to many new domestic business opportunities and jobs in export sectors. It has fostered competition and boosted productivity. This latter dynamic has been an especially favorable development over the past few years, motivated in large part by legislation that is crowding in private capital from abroad into critical new sectors of U.S. domestic production (CEA 2023a; CEA 2024c).

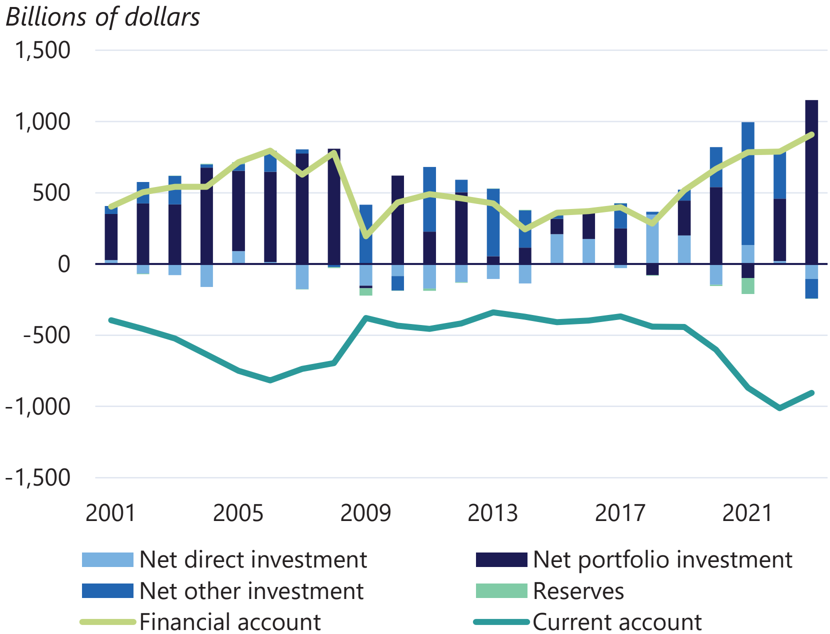
However, it is also important to recognize that certain aspects of trade flows can have downsides. Non-market practices and policies deviating from rules-based trading conventions have hurt communities over the past few decades (USTR 2024). In this vein, the Administration has taken consequential actions to protect American workers, producers, and taxpayers from violations of rules-based trade, particularly against China's long-applied strategy of capturing global market share, gained via subsidies and non-market policies and practices. The Administration has also addressed urgent national security challenges, for example, by blocking exports of advanced technologies to those who might use them against the United States, and regulating investments that can be exploited to pose risks to U.S. national security in certain technologies and products in countries of concern (White House 2024).

Turning back to the other side of the balance of payments ledger, figure 6-2 shows that the United States has run a steady financial account surplus throughout the 21st century. Between 2000 and 2023, the financial account balance averaged $530 billion.[5] The composition of gross capital inflows into the United States has varied over time. In 2023, the United States received approximately $1.9 trillion in foreign capital inflows, and U.S. investors and multinationals supplied nearly $979 billion in capital to foreign countries (BEA 2024b). These flows substantially exceeded their pre-pandemic levels. On a global scale, international capital flows retrenched from their pre-pandemic values, but the U.S. share of gross capital flows nearly doubled from 23 percent in 2019 to 41 percent in 2023 (Allen and Bems 2024).

Capital flows play critical economic roles. By internationalizing their portfolios, investors can increase returns while mitigating risk via diversification. The United States plays an important role in this process. U.S. Treasuries are considered safe assets worldwide due to low default risk, high liquidity, and a strong governance environment. Firms, investors, and

[5] The financial account includes asset transactions between the United States and foreign countries. If an investor living in the United Kingdom, for example, buys shares in an American company, the transaction appears as a liability in the U.S. financial account, since the investor has a claim on domestic profits. If an American investor buys shares in a British company, the transaction appears as a claim in the financial account.

Figure 6-2. U.S. Financial and Current Accounts



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Sources: Bureau of Economic Analysis; CEA calculations.
Note: Derivatives are excluded.
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governments hold U.S. Treasuries in their portfolios for precautionary and risk diversification purposes, especially in times of heightened uncertainty, such as the global financial crisis or COVID-19 pandemic, when investors seek to reduce the risk exposure of their portfolios (Chari, Dilts Stedman, and Lundblad 2020). Foreign investors also invest in U.S. equities and direct investment assets to realize higher returns than are available elsewhere.

Evidence suggests that incoming foreign financial flows lower the cost of capital in recipient economies, which can spur real investment and growth (Chari and Henry 2005; Chari and Henry 2008). Capital inflows have the potential to expand a country's productive capacity by increasing domestic investment, while closed economies have access only to the domestic savings pool. Therefore, when net capital inflows are positive (i.e., inflows exceed outflows), domestic investment can exceed domestic savings.

Investment flows other than portfolio equity and debt, such as cross-border lending and FDI, can play similar roles. In many instances, FDI can provide access to improved technologies leading to productivity improvements as well as knowledge transfers to the host country (Alfaro and Hammel 2007; Alfaro et al. 2010; Fons-Rosen et al. 2018; Branstetter 2006).

Additionally, access to international credit allows countries to smooth consumption over time, lending in good times and borrowing when faced with adverse shocks (Obstfeld and Rogoff 1996). International borrowing and lending can therefore insulate countries from the fate of lurching from feast to famine. Similarly, when there is a foreign appetite for purchasing a country's government bonds, international capital flows allow governments to finance their budget deficits at lower interest rates than would otherwise prevail.

The International Capital Flows Landscape

Shifts in the composition of international financial flows as a result of changes in foreign investor preferences or international shocks can impact U.S. financial asset prices, such as bond yields, stock prices, and the dollar exchange rate. Taking stock of changes in cross-border investment patterns is thus an important issue for policymakers and market participants.

Cross-border financial flows and portfolio holdings provide detailed information about the types of investors (foreign private or foreign official)[6] seeking U.S. assets, the geographies from which the investors come, and the types of instruments (stocks, bonds, or direct investment) that draw their attention across sectors and over time.

International capital flows have long played an important role in U.S. economic development. Capital inflows into the United States in the form of bonds and bank loans during much of the 19th century helped finance several key industries, most notably the railway sector (Wilkins 1991). Following World War I, the United States became a lender for the first time in U.S. history, but U.S. foreign investment leveled off during and after the Great Depression (Cardoso and Dornbusch 1989). After World War II, the post-war Bretton Woods system secured dollar dominance on the international stage (Siripurapu and Berman 2023). By the mid-1970s, however, U.S. net capital flows started to reverse as the economic situation in the United States resulted in trade deficits where once there had been trade surpluses (Reinbold and Wen 2020). Except in 1991, the United States has run a trade deficit since 1982.

Recent U.S. Capital Inflows and Outflows

Moving forward to the 21st century, capital inflows into the United States rapidly increased, peaking at more than $2 trillion on the eve of the global financial crisis in 2007. Figure 6-3 depicts the increase in foreign investment into the United States since 2020, reflecting the strength of the U.S.

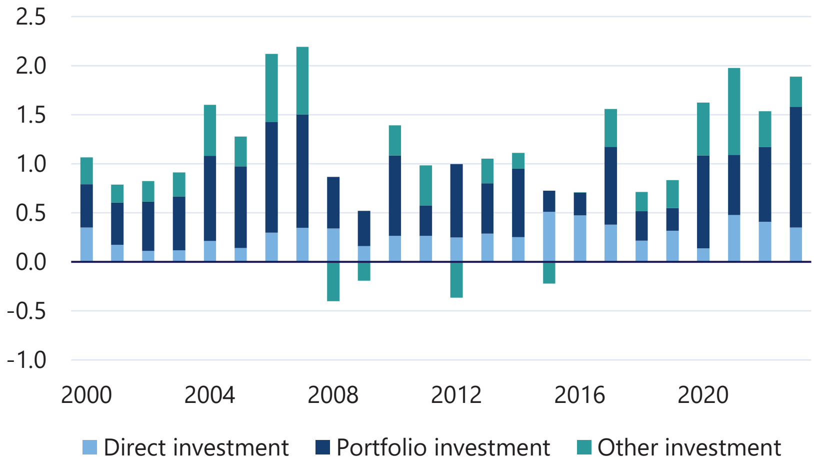
[6] Official flows, as classified by the U.S. Federal Government, represent purchases and sales of U.S. assets by foreign governments and central banks (Treasury 2024).

post-pandemic recovery. The growth was spurred in large part by a 30 percent increase in portfolio investment in lucrative U.S. equity and debt markets. Portfolio inflows increased to $1.23 trillion in 2023 during the Biden-Harris Administration, the highest annual amount on record.[7]

The pattern of inflows stands in contrast to figure 6-4, which shows more modest growth in U.S. outflows over the past few decades. Outflows

Figure 6-3. U.S. Capital Inflows

Trillions of dollars



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Sources: Bureau of Economic Analysis; CEA calculations.
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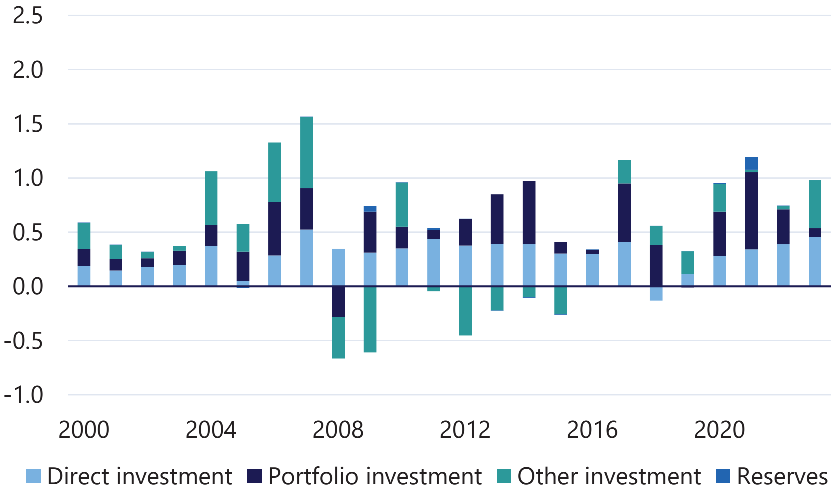
declined substantially in the wake of the global financial crisis but have recovered over the past decade and a half.

Figure 6-5 provides a snapshot of the composition of U.S. capital flows in 2023. The composition of the $979 billion in capital outflows was nearly evenly split between FDI outflows and other investment outflows, with a small fraction in portfolio outflows (figure 6-5a). On the other hand, nearly two thirds of the $1.9 trillion in inflows were in the form of portfolio debt and equity, with FDI and other investments that include cross-border lending by foreign global banks making up the rest of the balance (figure 6-5b).

[7] Negative inflows in the category of "other" investments refer to liquidations of cross-border lending in certain years, such as in 2008 during the global financial crisis.

Figure 6-4. U.S. Capital Outflows

Trillions of dollars



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Sources: Bureau of Economic Analysis; CEA calculations.
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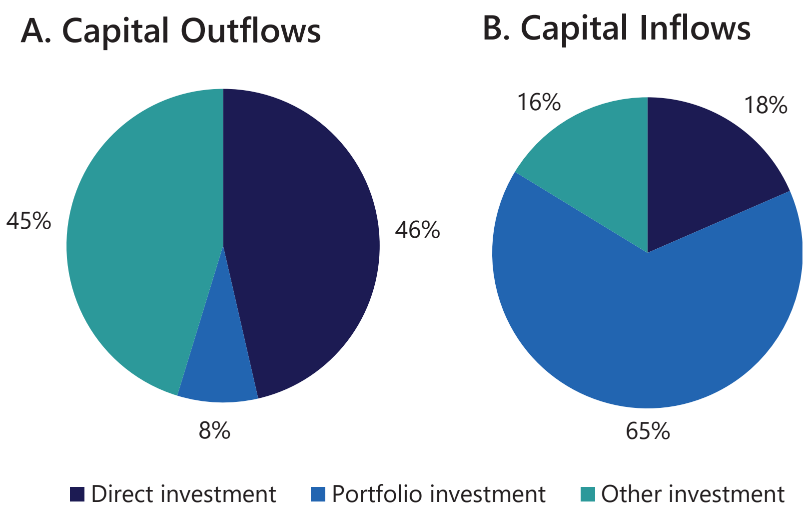
Figure 6-5. Capital Inflows and Outflows

2023 shares



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Sources: Bureau of Economic Analysis; CEA calculations.
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Table 6-1. Top Contributors and Recipients of U.S. Flows in 2023, by Country

Countries	*Net US Inflows (billions of dollars)*	*Countries*	*Net US Outflows (billions of dollars)*
United Kingdom	368.9	United Kingdom	263.0
Canada	157.0	Canada	133.3
France	100.4	France	62.3
Luxembourg	99.5	Singapore	45.2
Singapore	77.8	Hong Kong	37.8
Japan	76.3	Australia	32.1
Germany	73.0	Netherlands	31.5
Taiwan	67.7	Luxembourg	24.3
South Korea	46.0	India	12.4
Netherlands	42.3	Mexico	12.1
Total	1108.7	Total	654.0

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Source: Bureau of Economic Analysis.
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The Geography of Capital Flows

Unsurprisingly, most of the top contributors to U.S. capital flows are also top trading partners and geopolitical allies of the United States. In 2023, the United Kingdom was the top contributor to U.S. inflows, followed by Canada and France (see table 6-1). Offshore financial centers like Luxembourg and Singapore also feature in the set of top contributors and recipients of financial flows.

Mirroring U.S. inflows, the United Kingdom was also the top recipient of U.S. outflows for three out of the four years from 2020 to 2023. The United States is a diverse investor, often allocating large amounts to different sets of countries each year.[8]

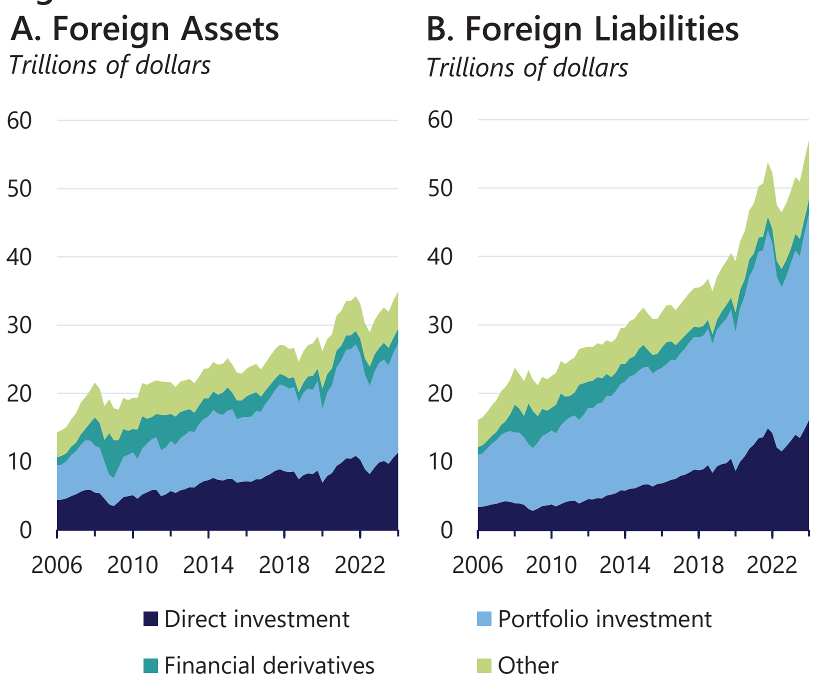
[8] Outward direct investment is a popular destination for U.S. outflows in 6 of the top 10 countries. For example, 84 percent of U.S. outflows to Singapore went to outward direct investment, the largest share of the top 10 countries. Reserve assets, conversely, received the smallest share of U.S. outflows for all countries in the top 10 in 2023. Most U.S. outflows to the United Kingdom and Hong Kong (77 percent and 81 percent, respectively) were in the form of loans and currency and deposits, whereas slightly more than half of U.S. outflows to France and Luxembourg were in the form of portfolio investments.

The International Investment Position

A final piece of the international capital flows picture is the international investment position (IIP), which records the stock of a country's international assets and liabilities accumulated over time (Lane and Milesi-Ferretti 2007). Current account surpluses or deficits (flows) accumulate into the stocks of foreign assets and liabilities. The difference between foreign assets and foreign liabilities is the U.S. net international investment position (BEA 2024b).

The U.S. net IIP stood at negative $21.3 trillion at the end of the first quarter of 2024, representing the difference between the stock of foreign assets ($36.0 trillion) and foreign liabilities ($57.1 trillion), as shown in figures 6-6a and 6-6b. By 2024, the U.S. stock of foreign assets more than

Figure 6-6. U.S. International Investment Position



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Sources: Bureau of Economic Analysis; CEA calculations.

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doubled from its value of $16.4 trillion in 2006, and the stock of foreign liabilities nearly tripled from $18.2 trillion over the same period.[9]

Valuation effects through changes in the prices of assets and liabilities and exchange rate fluctuations impact the outstanding stocks. For example, the rise in U.S. stock prices in 2023 exceeded the rise in foreign stock prices, increasing the market value of U.S. foreign liabilities relative to U.S. foreign assets (BEA 2024c). Valuation effects have played an important role in the change in the U.S. net international investment position over the past decade (Milesi-Ferretti 2021).

America as the World's Broker: Cross-Border Returns

Examining the purchases and flows of assets across borders provides insight into how investors view the international economic and financial landscape. The purchase of foreign equities or debt appears in a country's financial account under the category of portfolio investment. While foreign investors have long viewed American debt as safe investments, they increasingly see U.S. equity markets as attractive investment destinations due to their persistent dynamism and growth on a scale often surpassing that of other countries. Relative to those of the nation's trading partners, American companies continue to offer highly productive and, as a result, highly lucrative investment opportunities. Thus, the United States is increasingly the world's brokerage (Tabova and Warnock 2024).

The high and rising demand for taking part in the U.S. financial ecosystem is reflected in the rapid rise in U.S. foreign liabilities (i.e., domestic financial assets owned by foreign investors). Total U.S. international portfolio liabilities more than tripled between 2006 and 2024. The increase represents both changes in asset valuation and purchase volume.

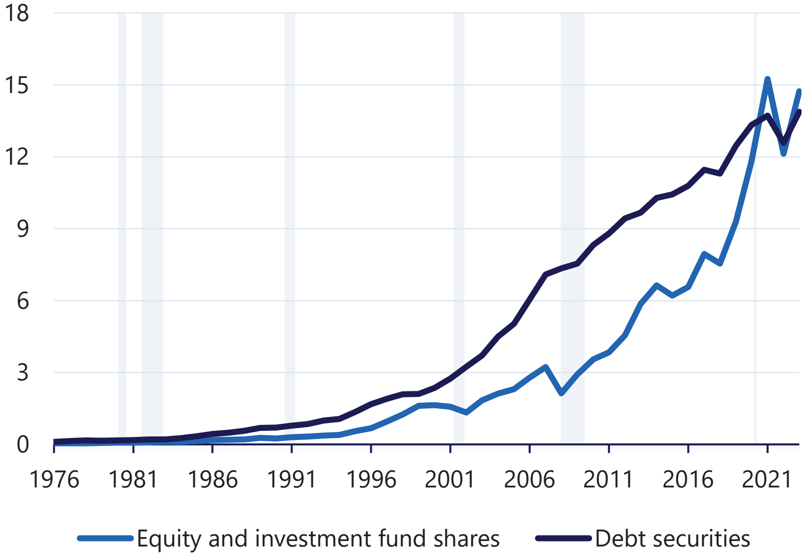
Although the increase in portfolio liabilities occurred in both debt and equity investments, the composition of U.S. liabilities has shifted from debt to equities (Tabova and Warnock 2024; Atkeson, Heathcote, and Perri 2023). Two decades ago, most foreign investors bought more U.S. debt than equities. In the last several years, U.S. equities have become more popular, with current total equity liabilities exceeding total debt liabilities (see figure 6-7), reflecting a steady increase in purchases from abroad as well as valuation effects.

This holdings composition explains why foreign investors now earn slightly more on their investments in the United States than domestic

[9] Foreign assets in the first quarter of 2024 included a stock of portfolio investments valued at $16.8 trillion, foreign direct investment of $11.3 trillion, and other investments, which include cross-border bank loans valued at $3.2 trillion and derivatives of $2.2 trillion. On the liabilities front, foreign investments in U.S. portfolio assets stood at $30.2 trillion, FDI was $16.1 trillion, other investments were $8.6 trillion, and derivatives were $1.6 trillion.

Figure 6-7. Foreign Investment in U.S. Equities and Debt

Trillions of dollars



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Sources: Bureau of Economic Analysis; Tabova and Warnock (2024); CEA calculations.
Note: Gray bars indicate recessions. Data through 2023.
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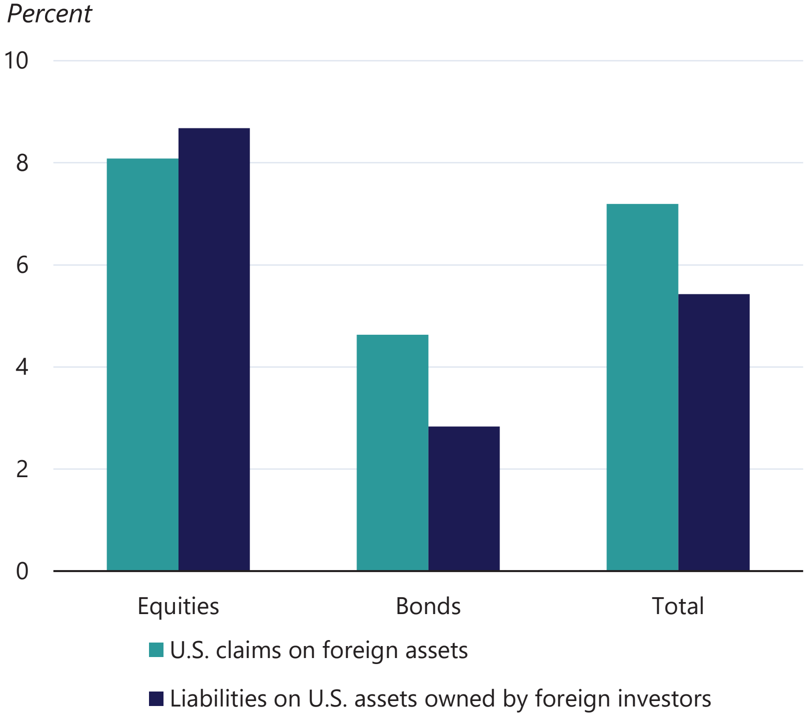
investors earned abroad from 2003 to 2023 (Curcuru, Thomas, and Warnock 2013; Tabova and Warnock 2024; Atkeson, Heathcote, and Perri 2023). Previously, foreign investors earned mostly low yields from American debt while U.S. investors received high returns from foreign equity and debt investments.[10]

The consistent demand for U.S. assets can be attributed to the relatively strong returns earned by foreign investors in U.S. markets. Figure 6-8 provides the average annual returns earned on investments by foreigners from 2003 to 2023 (denoted by liabilities on domestic assets) as well as the returns earned by Americans investing abroad (denoted by claims on

[10] Earlier evidence suggested that the U.S. returns differential abroad averaged 1.5 to 2 percent. Specifically, a 6.1 percentage point differential in FDI yields earned in foreign countries was responsible for the bulk of the 1.9 percentage point overall returns differential for the 1990–2011 period. Additionally, the returns effect (i.e., the yields component) accounted for almost the entire capital gains differential, with the U.S. earning higher yields abroad. The differential was, on average, almost entirely due to fluctuations in prices, rather than exchange rates (Curcuru, Thomas, and Warnock 2013).

Figure 6-8. Average Annual Investor Returns on U.S. and Foreign Portfolio Investments, 2003–2023



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Sources: Bureau of Economic Analysis; Tabova and Warnock (2024); CEA calculations.
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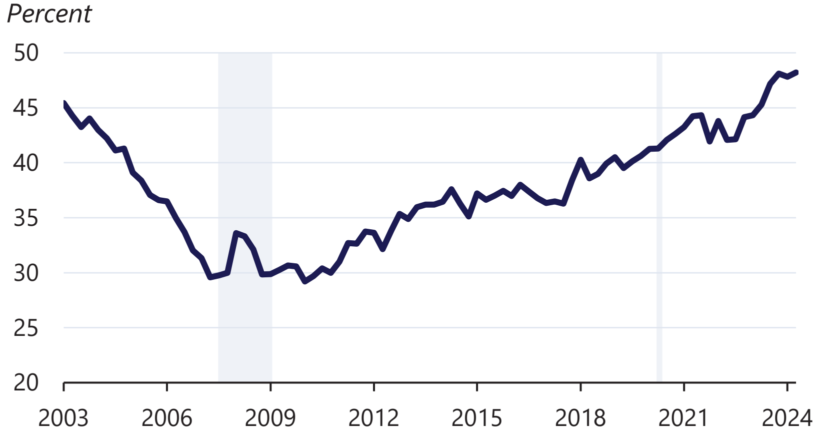
foreign assets).[11] During the period, foreign investors averaged 8.7 percent yearly returns on U.S. equities and 2.8 percent yearly returns on U.S. debt. Although portfolio values may fluctuate from year to year, the averages show investors have been rewarded for placing their money in U.S. financial assets. Across both asset classes, total returns for foreign investors were 5.4 percent over the decade. Foreign investor returns in dollar terms reflect the rise in the stock prices and the rising dollar since 2012.

The equity returns earned by foreign investors in U.S. equity markets were slightly higher, about 0.6 percentage points more on an annual basis, than the returns earned by U.S. investors in equity markets abroad, over the past two decades. The differential can be attributed to the faster growth U.S. equity markets have experienced over the last decade, which can be seen by

[11] Only arithmetic means are presented in figure 6-8. Geometric means tend to be lower for more volatile return streams. Tabova and Warnock (2024) show that the differential between American and foreign investment returns is lower using geometric averages.

Figure 6-9. U.S. Market Cap as a Share of World Market Cap



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Sources: Bloomberg; CEA calculations.
Note: Gray bars indicate recessions.
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comparing U.S. market capitalization to total world market capitalization (figure 6-9). The U.S. equity share achieved its highest value in two decades under the Biden-Harris Administration. As discussed more in the following section, FDI tells a similar story: Corporations with foreign ownership earn lucrative returns in the United States' large and dynamic domestic market.

The high returns earned by foreign investors on U.S. financial assets have been accompanied by American investors seeing large returns on their investments abroad. U.S. investors averaged 8.1 percent yearly returns on foreign equities and 4.6 percent yearly returns on foreign debt from 2003 to 2023. Indeed, when considering both debt and equities, American investors' returns abroad were higher on average than their foreign counterparts' returns on U.S. investments. The difference was historically due largely to higher yields on foreign debt compared to U.S. debt (Curcuru, Dvorak, and Warnock 2008). The low yields on domestic debt can be attributed to continued high demand for U.S. debt offerings, due to their safety and liquidity in the eyes of investors in the United States and around the world as well as steady Federal Reserve policy (Krishnamurthy and Vissing-Jorgensen 2012).[12]

Foreign Direct Investment

In addition to buying American stocks and bonds, foreign investors often acquire partial or full ownership in domestic companies. These purchases come under the "direct investment asset" category within a country's financial account of the balance of payments. Such FDI differs from portfolio investment, as investors gain a measure of influence over the target companies. FDI can occur through the following channels: multinational firms launching subsidiaries (known as "greenfield operations") in foreign countries, the expansion of existing foreign operations, the acquisition of new foreign assets through mergers and acquisitions, or investments in joint ventures (BEA 2024d).

The United States has historically been the largest recipient of FDI inflows (Commerce 2024a). The increase is consistent with both the strength of investment opportunities in the U.S. economic recovery and Biden-Harris Administration policies effectively crowding in foreign investment (CEA 2023a; Van Nostrand 2024b). The United States also invests in foreign companies around the world. The investments return earnings to American stakeholders while improving economic cooperation and knowledge transfers across partner countries. Indeed, primary income receipts—which include interest, dividends, and profits earned for American investors abroad—increased by nearly $200 billion in 2023 (BEA 2024a).

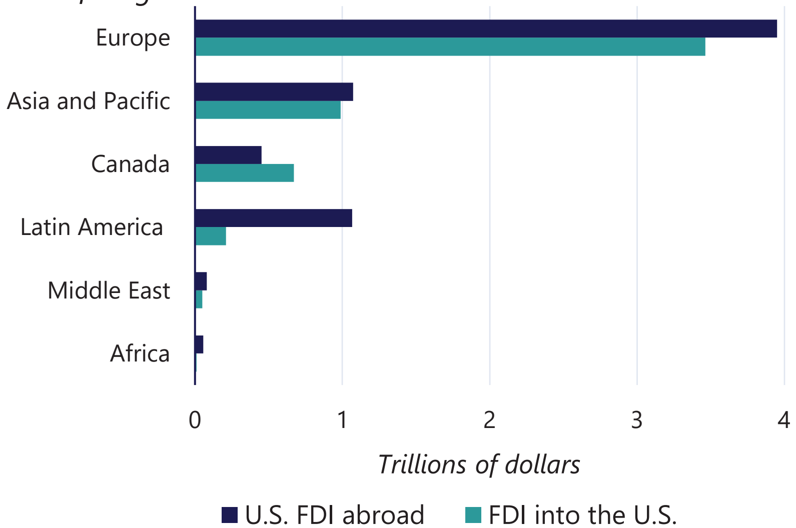
The Benefits of FDI and the Administration's Role in Stimulating Direct Investment

Firms engage in FDI for a variety of reasons, ranging from seeking resources to efficiency considerations, such as reducing costs or forming strategic alliances internationally. By providing capital, FDI fosters development in host countries. The resulting efficiency gains help stimulate economic growth and spur job creation. Another key FDI benefit is knowledge spillover gained by sharing expertise and know-how across borders, including the introduction of advanced technologies. Finally, FDI flows are crucial drivers of international economic integration and help establish supply chains with

[12] A final metric tells the same story of the high returns American markets offer. Internal rates of return (IRR) are defined as the interest rates required to set the net present value of an investment equal to zero. A high IRR indicates an elevated return, as the payoff from the investment must be discounted at a higher rate to reduce it to zero in net present value terms. Similar to the annual returns above, from 2003 to 2022 foreign investors had an IRR on their investments in the United States of 8.7 percent, slightly higher than the 7.9 percent that American investors had abroad (Tabova and Warnock 2024).

Figure 6-10. Foreign Direct Investment into and out of the United States

2023 foreign direct investment stock



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Sources: Bureau of Economic Analysis; CEA calculations.
Note: Data are on a historical-cost basis.
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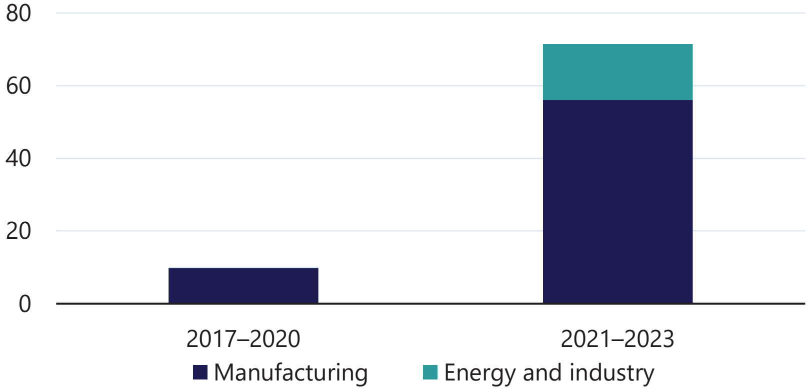
strategic partners across borders, also known as global value chains (Qiang et al. 2021; Lipsey 2004). See figure 6-10.

The Biden-Harris Administration has helped achieve record FDI levels by actively courting foreign investment in American industries, especially into manufacturing and clean energy. The strategy has been a critical part of the Administration's agenda to produce quality jobs. Indeed, a large share of the historic increase in manufacturing investment under the Biden-Harris Administration comes from foreign investors. The Administration has facilitated and encouraged the investments with targeted tax credits established by the Inflation Reduction Act and CHIPS and Science Act to promote renewable energy and semiconductor production. The incentives crowd in foreign investment to critical sectors and historically left-behind areas (CEA 2024c). In 2023, South Korea emerged as the biggest source of FDI into the United States, with announced commitments of $21.5 billion in new investments comprising 90 new projects across a range of industries (Chu 2024). FDI into clean energy and manufacturing of clean energy is more than seven times as large as it was under the prior administration (figure 6-11).

The Biden-Harris Administration policies, including the Made in America initiative, help ensure that the United States remains the world's

Figure 6-11. Announced Investment in Clean Energy Projects by Foreign Companies

Billions of dollars



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Sources: Clean Investment Monitor; CEA calculations.
Note: Energy and industry refers to new or expanded facilities to produce clean energy, capture carbon dioxide emissions, or decarbonize industrial activity. Manufacturing refers to the construction or expansion of factories that manufacture clean energy, clean vehicle, building electrification, or carbon management technology.
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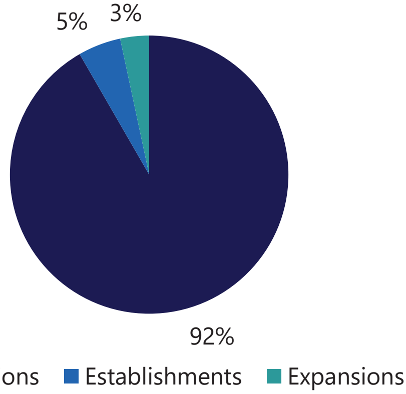
top destination for foreign investment. For example, Samsung Electronics received $6.4 billion in funding in 2024 to develop a computer chip manufacturing and research cluster (Commerce 2024b). This funding is in addition to the company's $61 billion in planned manufacturing projects expected to create more than 8,000 jobs (Tarasov 2023). Additionally, Taiwan Semiconductor Manufacturing Company (TSMC) financed a nearly $40 billion project to construct and operate a high-tech semiconductor fabrication plant in Arizona, whose yields have recently been announced to surpass factories in Taiwan (Reuters 2024; Hawkins 2024). Similarly, Panasonic Energy announced a $4 billion investment in a lithium-ion battery factory in Kansas, expected to create 4,000 jobs (Panasonic 2024).

Investment into the United States

Due to its highly productive companies and the Biden-Harris Administration's policies, the United States continues to be the top international investment destination for FDI flows. FDI is commonly decomposed into new investments and the accumulated stock of prior investments, the former representing the acquisition, establishment, or expansion of U.S. businesses (BEA 2024e).

Figure 6-12. New Foreign Direct Investment in the United States

2023 shares



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Sources: Bureau of Economic Analysis; CEA calculations.
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The breadth of foreign firms investing in the United States also reflects the attractiveness of the country's large consumer market, advanced infrastructure, and business-friendly environment. The total stock of FDI into the country has more than doubled in the last 16 years and reached $5.4 trillion in 2023, up from $2.1 trillion in 2009 (BEA 2024f). In 2023, new net FDI totaled $148.8 billion domestically (BEA 2024e). Acquisitions tend to dwarf establishments and expansions (see figure 6-12).

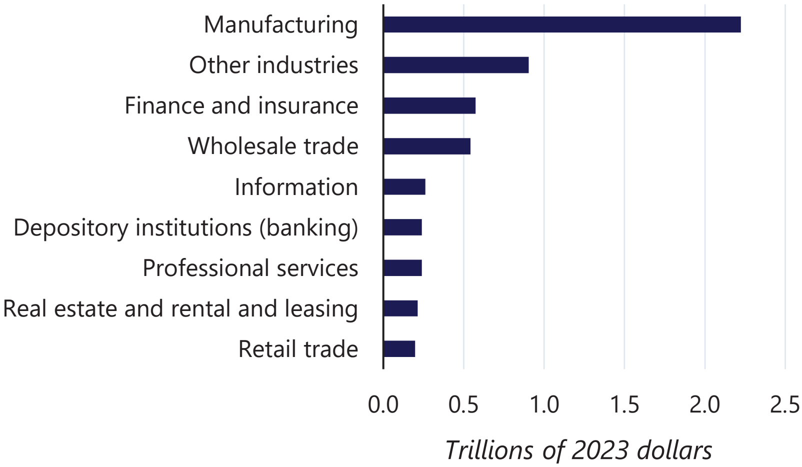
One critical aspect of these 2023 FDI flows is that they overwhelmingly originate from U.S. allies and strategic partners. Measured according to the location of the foreign parent company, the top three investors in terms of the total FDI stock in 2023 were the Netherlands ($717.5 billion), Japan ($688.1 billion), and Canada ($671.6 billion).[13] Cumulatively, Canada, Japan, the United Kingdom, and the Netherlands made up more than half of FDI flows into the United States in 2023, reflecting the Biden-Harris Administration's goal of forming strong financial linkages with partner countries (BEA 2024f).

Companies in a range of sectors, including retail trade ($199 billion), real estate ($213 billion), and professional and scientific services ($239 billion), benefitted from FDI funds in 2023 (BEA 2024f). The industry with the highest FDI position through 2023 was manufacturing, at $2.2 trillion (see figure 6-13). The FDI stock in manufacturing has risen 16 percent since

[13] All FDI statistics are on a historical-cost basis, meaning the price of the investment at the time of investment.

Figure 6-13. Foreign Direct Investment in the United States, by Industry

2023 stocks



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Sources: Bureau of Economic Analysis; CEA calculations.
Note: Finance category excludes depository institutions. Professional services includes scientific and technical services.
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2020, reflecting the Biden-Harris Administration's goal of revitalizing the American manufacturing industrial base (White House 2022).

As with stocks and bonds, foreign investors receive substantial returns on their direct investments in the United States,[14] averaging 7.4 percent annually from 2003 to 2023 on an arithmetic mean basis.[15]

Investment into Other Countries

Because U.S. companies develop and use cutting-edge technology, foreign countries and businesses often welcome American FDI. Along with funding, the investments bring technical know-how and knowledge spillover (Lipsey 2004). In 2023, the stock of FDI by U.S. firms worldwide totaled $6.7 trillion. During 2023, new FDI abroad totaled $364 billion (BEA 2024f).

The United States benefits from outward FDI into other countries by acquiring market share abroad, strengthening supply chains, accessing

[14] Although FDI statistics are imprecise due to ambiguity regarding where corporations locate profits, the returns broadly suggest the magnitude and direction of profits.

[15] The literature attributes the difference between yields on U.S. direct investment abroad and FDI into the United States to differences in (i) taxes, (ii) risk-adjusted returns, (iii) affiliate/subsidiary age, and (iv) other factors, such as transfer pricing, industry mix, and intangibles. See Curcuru, Thomas, and Warnock (2013) for a literature summary.

know-how abroad, and bringing earnings back home (Cohen 2007; Chari, Ouimet and Tesar 2010; U.S. Chamber of Commerce 2021). U.S.-based multinational companies earned $577 billion in income from investments abroad in 2023, much of which makes its way back to American stakeholders (BEA 2024f). Other countries benefit from the investments, and American technical expertise and capital spreads abroad (Loungani and Razin 2001; Mohseni-Cheraghlou 2021).

The majority of countries engaged in global trade receive U.S. FDI in some form. Indeed, more than 50 countries received at least $1 billion in new investment from the United States in FDI in 2023. The United Kingdom ($1.1 trillion), the Netherlands ($980 billion), and Luxembourg ($532 billion) were the top three recipients, measured by total stock of U.S. FDI (BEA 2024f). In terms of outward direct investment, America engages overwhelmingly with strategic partners.

At the same time, inbound investments from China and outbound investments have ticked downward. The Chinese footprint in the United States measured via the stock of accumulated direct investments declined by 23 percent from 2017 to 2023 (BEA 2024f).

While the Biden-Harris Administration has deepened America's financial integration with its allies and partners, it also protects against potential risks from direct investment. The Committee on Foreign Investment in the United States (CFIUS) considers transactions on a case-by-case basis, evaluating any potential risk arising from FDI irrespective of its country of origin (CFIUS 2023). CFIUS upholds the United States' longstanding commitment to an open investment economy, while recognizing that a critical component of FDI is identifying and mitigating national security risks. CFIUS ensures that any risks to national security arising from FDI are sufficiently addressed through the narrow tools at the Committee's disposal.

The Biden-Harris Administration has also been particularly focused on securing the intangible benefits that often accompany U.S. outbound investments in certain national security technologies and products—notably in the semiconductors and microelectronics, quantum information technologies, and artificial intelligence sectors—which could be used to undermine U.S. national security (White House 2023). Similarly, the Biosecure Act has increased oversight of the pharmaceuticals sector.

Cross-Border Lending and Global Banks

The cross-border lending market is another important aspect of global financial integration. Grouped in the category of "other flows" in the financial account of the balance of payments, capital flows intermediated through foreign and global banks are an important part of cross-border credit flows.[16]

Making up an increasingly large share of total lending, cross-border lending plays a critical and growing role for the United States. Specifically, lending by foreign banks to firms in the United States serves a critical diversification function for banks around the world, and this lending also helps to stabilize the domestic banking system by accessing foreign bank balance sheets via internal capital markets (Gupta 2021). American bank branches abroad and U.S. government liquidity facilities perform a similar function for foreign banking systems.

Financial Intermediation within the United States

American cross-border financial ties are extensive and growing. The stock of U.S. cross-border lending assets increased from $3.2 trillion in the fourth quarter of 2019 to $3.8 trillion in the second quarter of 2024. The stock of U.S. cross-border lending liabilities increased from $3.5 trillion to $4.8 trillion over the same time period, according to the Bank for International Settlements' locational banking statistics (BIS 2024a).

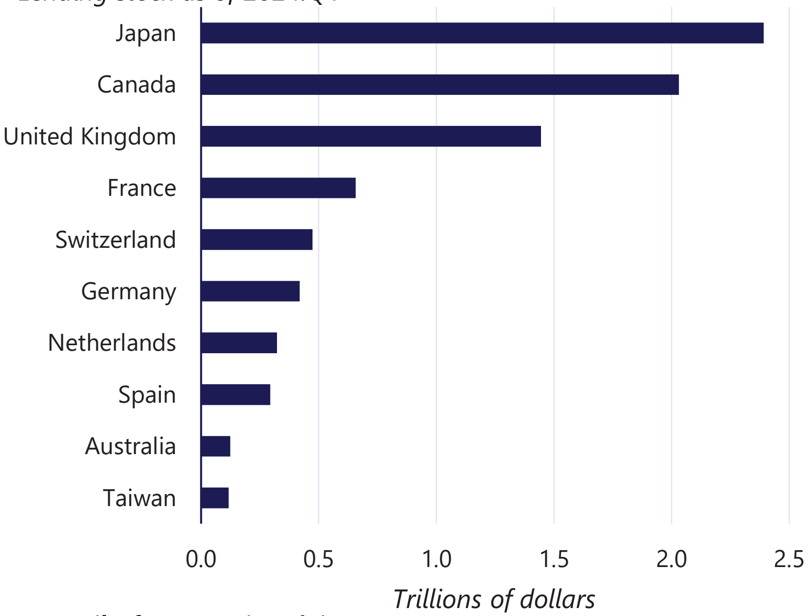
Foreign lending represents a large share of credit provision in the United States (Cetorelli, Goldberg, and Ravazzolo 2020). As of September 2024, foreign banks accounted for $1.1 trillion in U.S. loan provision and held $3.1 trillion in aggregate assets, approximately 13 percent of the U.S. banking system's total assets. The total assets of branches and agencies as well as foreign subsidiaries currently total more than $4 trillion (Federal Reserve Board 2024). Like other forms of investment moving to U.S. shores, the loans signal a continued faith in the profitability and creditworthiness of American businesses.

The presence of global banks in domestic financial intermediation can act as a stabilizing force during times of financial market strain. Foreign banks can access liquidity from their parent firms though internal capital markets, thereby overcoming the liquidity shocks and frictions faced by domestic local banks (Cetorelli and Goldberg 2011). When adverse shocks hit the U.S. economy, the continuation of credit provision through foreign-hosted branch lending can provide an important buffer for domestic financial intermediation, thus providing diversification by playing a stabilizing role in the U.S. banking system (Cetorelli and Goldberg 2012). At the same time, foreign banks can also channel funds to their U.S. operations, ensuring the robust continuation of credit provision during a crisis or funding liquidity strain (Choi et al. 2022; Obstfeld, Shambaugh, and Taylor 2009).

[16] Cross-border credit refers to any financing that spans international jurisdictions and includes loans and trade credit made by U.S. banks to borrowers abroad or foreign banks to U.S. borrowers. Cross-border credit also includes international debt issuance.

Figure 6-14. Lending Claims on the United States, by Country

Lending stock as of 2024:Q1



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Source: Bank for International Settlements.
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As with FDI, cross-border lending funds primarily originate from U.S.-allied countries, strengthening financial ties with strategic partners (see figure 6-14). According to the Bank for International Settlements' consolidated banking statistics, the top three countries for cross-country lending are Japan ($2.4 trillion), Canada ($2.0 trillion), and the United Kingdom ($1.4 trillion) (BIS 2024b).[17]

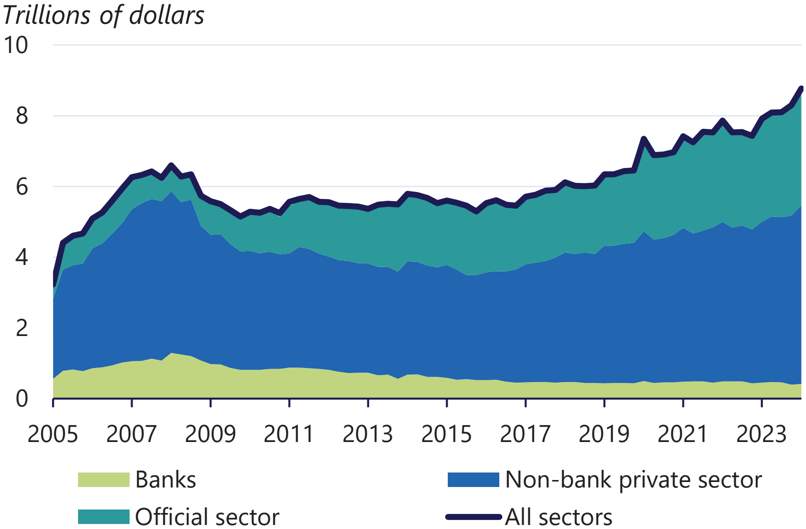
Changes in Cross-Border Lending

Cross-border lending has evolved dynamically over the decades. In the 1980s, banks primarily engaged in sovereign lending, which shifted into interbank lending activity across borders. More recently, global banks have engaged in direct lending to non-bank financial intermediaries and non-financial corporations (Buch and Goldberg 2024).

Figure 6-15 depicts the recent shifts, decomposing cross-country claims into the banking sector, non-bank private sector, and the official sector. While total cross-border claims almost tripled between 2005 and 2024,

[17] The tally of total claims, based on BIS data, is likely an underestimate due to missing data and country underreporting.

Figure 6-15. Lending to the United States, by Sector



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Sources: Bank for International Settlements; CEA calculations.
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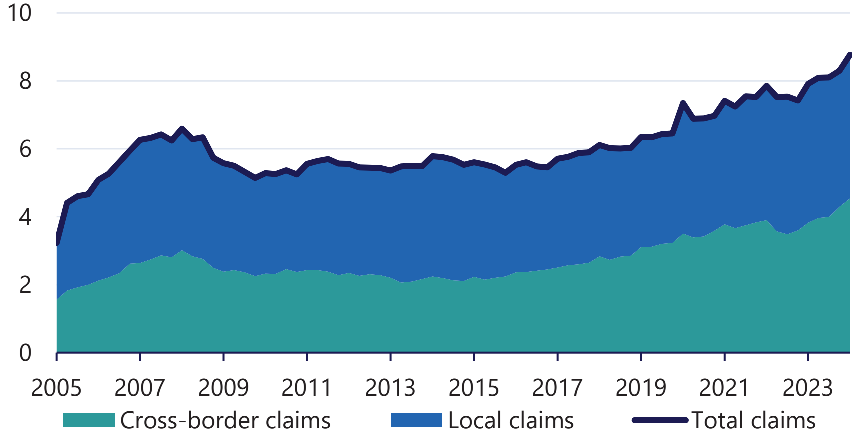
their composition also changed. Cross-border lending by banks fell significantly from a pre-crisis peak of approximately 20 percent of total claims in 2008 to 4.8 percent in 2024. In contrast, cross-border non-bank private sector (e.g., mutual funds and hedge funds) and official sector claims have increased significantly since the mid-2010s. The liquidity and financial stability risks associated with non-bank financial intermediation and the rise of the shadow banking sector outside the purview of the regulatory perimeter are the subject of considerable current policy discussion (Claessens 2024; Chari 2023).

Global banks also establish branches and subsidiaries in foreign countries that engage in domestic lending (McCauley et al. 2017; Buch and Goldberg 2024; Goldberg 2024)—for example, German banks establishing branches in the United States and lending directly to U.S. firms or U.S. banks establishing branches in Mexico to lend directly to Mexican firms.[18] Both local and cross-border lending have increased since the pandemic, representing a further financial integration of the world economy and greater diversification of risk (see figure 6-16).

[18] Statistics on cross-border credit provision understate the role of foreign ownership as a subset of foreign banks that are chartered in the United States and subject to the country's regulatory and supervisory framework as U.S. banks.

Figure 6-16. Local and Cross-border Lending Claims

Lending to the United States (trillions of dollars)



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Sources: Bureau for International Settlements; CEA calculations.
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Finally, differences in funding costs and exchange rate movements can impact the provision of credit in a particular currency (Hattori and Shin 2009). Monetary policy tightening and broad-based dollar appreciation reduced the provision of cross-border dollar credit (loans plus debt securities holdings) in 2022, while yen depreciation and below-zero interest rates in Japan led to a rapid increase in yen credit. In 2023, banks in Japan reported increased claims on the U.S. non-financial sector as credit to non-banks in the United States grew (BIS 2024c). The pattern is consistent with vast amounts of carry trade activity, with the yen being the funding currency invested in dollar lending.[19]

Flight to Safety: U.S. Treasuries and the Dollar

In addition to serving as a destination for profitable investment and bank lending, the United States plays a critical role in offering safe assets to the

[19] A carry trade is a speculative financial strategy where investors borrow in currencies with low interest rates (funding currencies) and invest in high interest rate currencies (target currencies). The aim is to make speculative profits from the interest rate differential between two countries in expectation that the differential will not be offset by unfavorable exchange rate movements. Carry trade profits therefore depend on the high-yielding currency either remaining stable or appreciating. Carry trades in foreign exchange markets are often executed by institutional investors and speculators looking to exploit differences in global interest rates.

world in the form of government debt.[20] A safe asset is a debt instrument that is expected to preserve its value across various states of the world, including adverse systemic events (Eisenbach and Infante 2017). Flights to the safety of U.S. Treasuries often happen during periods of stress or heightened uncertainty in international financial markets (Gourinchas, Rey, and Govillot 2017; Krishnamurthy and Vissing-Jorgensen 2012). The United States' currency also functions as a reserve currency on the international stage, underpinning trade and financial transactions (Boz et al. 2020). As noted above, U.S. debt offerings fall under the portfolio investment category in a country's financial account.

Today, U.S. currency and debt offerings still command a dominant position in the international financial system. However, debt brinkmanship of the type that occurs during debates over raising the U.S. debt ceiling—a Congressionally mandated ceiling on the amount the Federal Government can borrow—has the potential to damage this valuable status (CEA 2023c). Losing U.S. Treasuries' status as safe assets would be economically harmful, reducing U.S. fiscal capacity. In addition, the dollar's role as a reserve currency has economic and security benefits. The dollar's broader role in financial flows and payments ensures that capital flows through a system with strong governance, rule of law, and high-quality anti-money laundering rules that help to counter the financing of terrorism (Shambaugh 2024).

U.S. Debt as a Global Safe Asset

A wide range of investors hold U.S. Treasuries, displaying an international consensus in the safety of U.S. debt. The share of foreign holdings in publicly held outstanding Treasuries was approximately 14 percent in 1990 and peaked at 34 percent in 2014. In 2023, foreign official and foreign private investors accounted for nearly a quarter of U.S. Treasury holdings (figure 6-17).

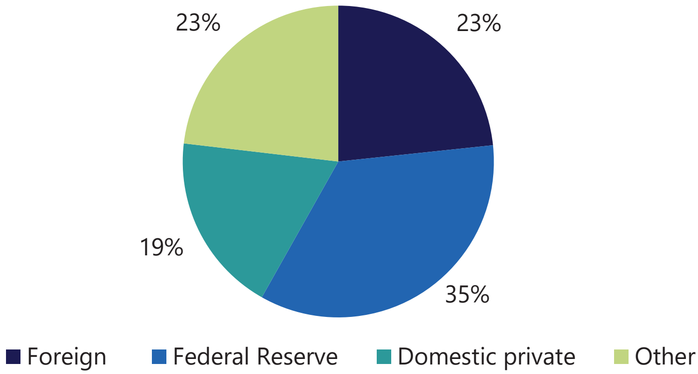
The demand for U.S. Treasuries spans the globe (see figure 6-18). Of foreign-held Treasuries, European investors accounted for more than a two-fifths share (44 percent) and investors from Asia and the Americas held approximately 25 percent each in 2023. The top three investor countries, as of August 2024, were Japan ($1.1 trillion), China ($774.6 billion), and the United Kingdom ($743.8 billion). Saudi Arabia, the United Arab Emirates, Kuwait, and several other oil producers also held significant Treasuries.[21]

[20] In a world where there is a scarcity of safe assets, U.S. Treasuries meet the global demand for safe, liquid, and collateralizable assets (Gorton and Ordonez 2022; Holmstrom and Tirole 1998; Greenwood, Hanson, and Stein 2015).

[21] The other oil producing countries with reported U.S. Treasury holdings include Algeria, Gabon, Iraq, Nigeria, and Oman. Iran and Qatar, two additional oil-exporters, did not report U.S. Treasury holdings in 2022.

Figure 6-17. U.S. Treasury Holders, by Type

Share of total Treasury holdings, 2023



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Sources: U.S. Department of the Treasury; CEA calculations.
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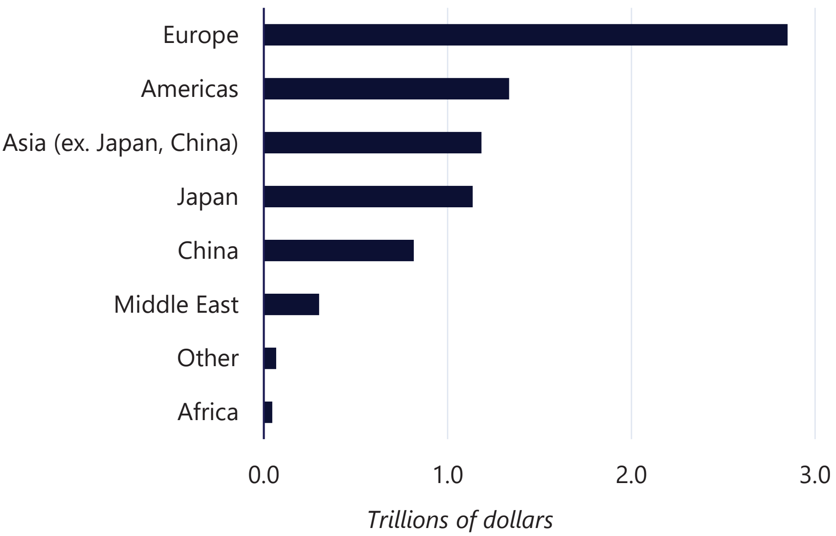
Figure 6-18. Holdings of U.S. Treasuries, by Geographic Region



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Sources: U.S. Department of the Treasury; CEA calculations.
Note: Data are for 2023. End-of-period values are used. Americas includes Canada, Latin America, and the Caribbean.
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While foreign official holdings of U.S. Treasuries held steady at about $3.5 trillion over the 2013–2023 period, foreign private holdings more than doubled from approximately $1.3 trillion in 2013 to $3.0 trillion at the end of 2023. Foreign holdings suggest that reserve managers at most foreign central banks continue to view U.S. Treasuries as safe investments, which also constitute a stable source of demand.[22] Foreign countries also hold dollar reserves in the event that they need to stabilize their exchange rates through interventions in currency markets. The evidence refutes arguments that the dollar is losing its dominance in the international financial system or that U.S. Treasuries are no longer desirable as safe haven investments.

The rising worldwide demand for U.S. Treasuries plays a key role in reducing the cost of financing American debt (Weiss 2022). Researchers have estimated the magnitude of foreign official purchases of U.S. government securities on Treasury yields (Bertaut and Judson 2014; Warnock and Warnock 2009; Beltran et al. 2013).

Both America and the world benefit from U.S. safe assets, a principle exemplified by the flight to safety that occurred during the global financial crisis. Although the United States was at the epicenter of the crisis, foreign and domestic investors sought the safety of U.S. government debt instruments. The share of Treasuries held by private and official investors abroad, which had been unchanged over the early 2000s, saw dramatic increases following the crisis, suggesting that the assets were viewed as particularly safe during a time of economic stress (Neoth and Sengupta 2010). Indeed, evidence suggests that the United States has a greater risk-bearing capacity than the rest of the world (Gourinchas, Rey, and Govillot 2017; Maggiori 2017; Sauzet 2023; Kekre and Lenel 2024).

The increase in demand for U.S. Treasuries was large enough during the crisis that Treasury prices rose despite a massive simultaneous supply increase (Neoth and Sengupta 2010). Bond purchases by the Federal Reserve during the period of quantitative and monetary policy easing also served to lower yields (Krishnamurthy and Vissing-Jorgensen 2011). In other words, the surge in demand for Treasuries exceeded the supply increase, resulting in elevated bond prices and lowered yields (He, Krishnamurthy, and Milbradt 2016).[23] In addition to providing a safe asset source, heightened Treasury purchases during the global financial crisis lowered financing costs for the

[22] Foreign official demand for U.S. Treasuries is particularly notable in an environment of quantitative tightening, when the U.S. Federal Reserve is reducing the size of its balance sheet.

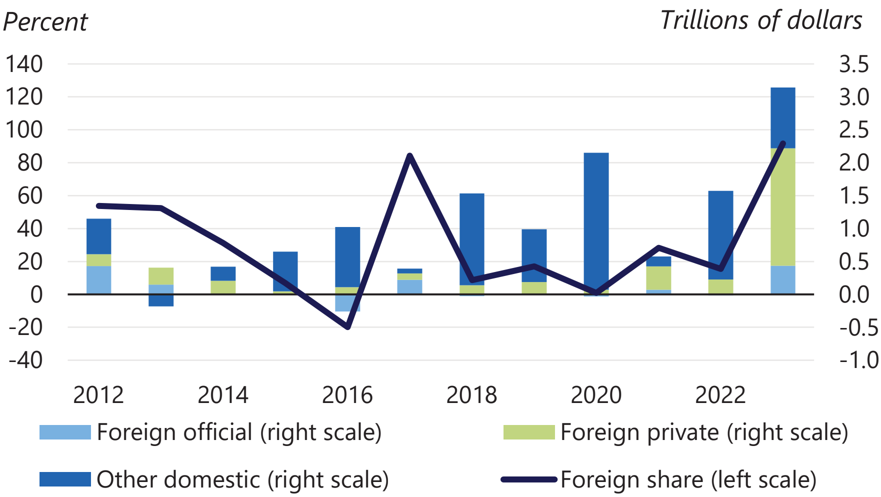
[23] The price increase was unexpected given that the Treasuries supply rose substantially to fund the Emergency Economic Stabilization Act of 2008, a $700 billion program designed to take bad assets off the books of the U.S. financial sector. The increase was unexpected because any increase in supply would have resulted in decreased prices or increased yields had the demand for Treasuries remained unchanged (Neoth and Sengupta 2010).

United States. The rising prices indicated that the yield to maturity (i.e., the government's cost of raising additional funds) fell.[24]

Foreign investors also turned to U.S. debt during the period of uncertainty surrounding the COVID-19 pandemic. At the onset of the pandemic, private and official foreign investors sold U.S. Treasuries to cover precautionary liquidity needs (referred to as the "dash for cash"), but the demand for Treasuries quickly rebounded (Barone et al. 2022; He and Krishnamurthy 2020).[25] In fact, foreign absorption of Treasury net issuances increased in 2021 (Weiss 2022).

U.S. Treasury demand remained high into the post-pandemic period. Foreign private investor net purchases of Treasuries in 2023 were more than ten times their pre-pandemic (2017–2019) average (see figure 6-19).

Figure 6-19. Absorption of Treasury Net Issuance, by Sector



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Sources: Bertaut and Judson (2022); U.S. Department of the Treasury; Federal Reserve Bank of New York; CEA calculations.

Note: Shares can sum to less than 0% and to more than 100% due to valuation changes in Treasury holdings not tracked by official data as well as due to purchases of Treasuries issued in a prior year.

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[24] The yield to maturity is defined as the interest rate that makes the present value of a bond's payments equal to its price.

[25] Outside the global financial crisis, net sales by foreign official investors, especially from emerging market countries, are a common occurrence during stress episodes (Weiss 2022). Therefore, the pandemic-induced sales in March 2020 were not unusual given the extreme uncertainty that accompanied the pandemic shock.

On average, foreign investors absorbed roughly 19 percent of Treasury net issuance in the five years preceding the pandemic (Weiss 2022). Over the 2021–2023 period, foreign investors absorbed an average of 45 percent annually.

The Dollar as Global Reserve Currency

Foreign exchange reserves allow countries to finance the purchase of imports denominated in reserve currencies and make payments on their foreign currency-denominated debts.[26] When faced with adverse shocks or turmoil, accumulated foreign exchange reserves provide countries with buffers that can be drawn upon to pay for imports and service foreign debt.

The role of the dollar as the world's dominant reserve currency was cemented after World War II (Nelson and Weiss 2022; Siripurapu and Berman 2023). The share of the dollar in global foreign exchange reserves grew from about 13 percent in 1947 to 85 percent by 1972, when the dollar became the currency of denomination for trade in commodities like oil and world trade invoicing. Today, the foreign borrowings of many countries are predominantly in dollars, and the dollar occupies a central position in the international monetary system, playing an outsized role in facilitating international trade (Eichengreen 2012; Ilzetzki, Reinhart, and Rogoff 2019).

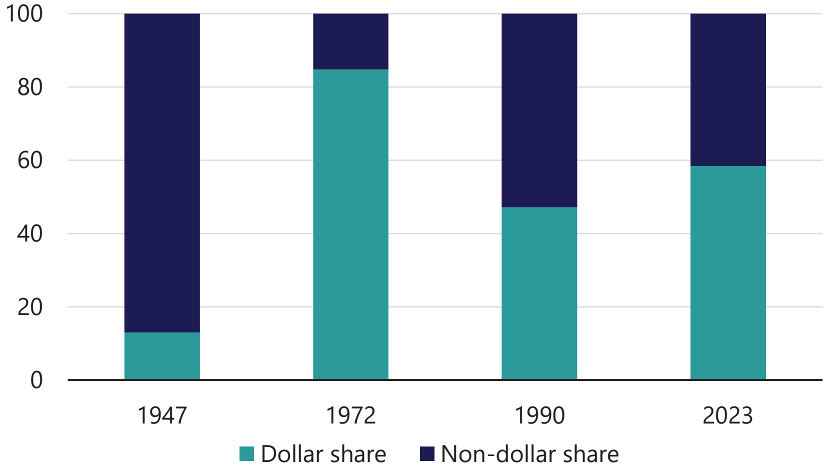
In 2023, the dollar accounted for about 60 percent of global foreign exchange reserves (Atlantic Council 2024; IMF 2024).[27] About 54 percent of international trade is invoiced in dollars as of 2022, and about 64 percent of all international loans and international debt securities are denominated in dollars as of 2024 (Boocker and Wessel 2024). The dollar dominates the foreign exchange market, which has a $7.5 trillion daily turnover, and nearly 90 percent of all trades in 2022 involved the dollar on at least one side (BIS 2022; Nelson and Weiss 2022).

Reserve currency status confers several benefits on the United States. While the dollar plays a pivotal role as an international medium of exchange, it also functions as an important store of value. Countries use their dollar reserves to purchase dollar-backed safe assets, namely U.S. Treasuries. The dominant reserve currency status and global demand for safe assets allow the United States to issue debt at relatively low yields compared to other sovereign nations (Chen et al. 2022; Maggiori, Neiman, and Schreger 2019). The ability to borrow and pay for imports in dollars shields the United States from adverse exchange rate movements and the potential for balance of payments crises.

[26] Reserve currencies are foreign currencies held on central bank balance sheets to fulfill debt obligations and finance imports.
[27] Other major reserve currencies include the Australian dollar, the British pound, the Canadian dollar, the Chinese renminbi, the euro, the Japanese yen, and the Swiss franc (IMF 2024).

Figure 6-20. Composition of Foreign Exchange Reserve Holdings

Percent of total reserves



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Sources: IMF Currency Composition of Official Exchange Reserves; Gluschenko (2024); CEA calculations.

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The dollar's global reserve currency status was boosted by the fact that the Bretton Woods fixed exchange rate system was based on the dollar as well as denomination of oil in dollars, or petrodollars, in the 1970s (Tran 2024). At the time, oil-exporting countries reinvested their dollar revenues in U.S. government debt. While there may be a gradual decline in the dollar share in foreign exchange reserves (figure 6-20), this is not matched by the rise in other major currencies like the euro, the British pound or the Japanese yen (Crow 2024). Rather, there has been a recent emergence of non-traditional reserve currencies and digital currencies as well as increased allocations into gold (Arslanalp, Eichengreen, and Simpson-Bell 2022; Tran and Matthews 2023; Gopinath 2024).

Recent evidence suggests, however, that the decline in the dollar share of reserves is primarily driven by a small group of countries, both due to monetary policy reasons and due to a small group of large foreign exchange reserve balance countries (Goldberg and Hannaoui 2024). The extent of international payment system fragmentation also remains modest (Gopinath et al. 2024). SWIFT data show that 80 percent of trade finance transactions continue to be settled in dollars. Commodity trade also continues to be invoiced and settled predominantly in dollars and the dollar's strength bears testimony to foreign investors moving into dollar assets (Gopinath 2024).

Reserve currency status allows the United States to use the dollar as a tool for international diplomacy and advancing its foreign policy objectives. While the recent use of financial sanctions has led to de-dollarization fears, the depth and liquidity of U.S. Treasury markets and robust global demand for Treasuries as a safe asset suggest that the dollar's utility remains intact (Siripurapu and Berman 2023; Lu 2023).

A Full Accounting of International Accounts

This chapter explores the recent evolution of major international investment policies under the Biden-Harris Administration, with a focus on the financial account of the U.S. balance of payments.

A detailed analysis of capital flows into and out of the United States is critical for understanding America's role in the international financial system. A variety of motivations, ranging from seeking the high returns that accompany economic growth to investing in U.S. assets for precautionary or safety reasons, drive international capital flows into the country. The United States is considered a safe haven by investors around the world, as evidenced by the demand for U.S. Treasury assets, which is significant and has remained stable or even risen over several decades. The role of the dollar as the world's dominant reserve currency also remains steady, and the demand for portfolio investments has increased substantially over the last two decades, as evidenced by the country's thriving equity and debt markets.

The Biden-Harris Administration's industrial policy agenda to encourage investments to facilitate the green transition and shore up supply chain resilience in critical sectors has facilitated a welcome surge of FDI from the nation's allies and partners. The importance of the United States in global capital markets continues to go from strength to strength reflecting our robust economy.