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THE CHANGING PATTERN OF INTERNATIONAL INVESTMENT IN SELECTED STERLING COUNTRIES

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This is the twenty-seventh number in the series ESSAYS IN INTERNATIONAL FINANCE *published from time to time by the International Finance Section of the Department of Economics and Sociology in Princeton University.*

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Two interlocking factors govern the subject matter of this essay. In the first place there is the problem of capital supply. Although at one time the United Kingdom was normally in a position to provide the resources needed for development purposes in Commonwealth countries overseas, since the war it has not been able to spare unlimited finance for this purpose. Secondly, the plans for post-war development in these countries have in several cases enlarged the demand for capital from abroad and to meet this demand new sources of capital supply have been explored. After ten years under these conditions it now seems time to note the results: to measure the actual flow of capital, examine its character, and determine its origin.

Although statistical difficulties preclude a comprehensive survey of the subject, data for a preliminary study can be derived from the detailed balance of payments estimates and cognate studies published in recent years.* These at any rate enable international capital movements to be charted more accurately and in greater detail than formerly. Moreover, the national income estimates now computed for most countries make it possible to assess in quantitative terms the extent of their dependence on external capital.

This paper gives a very summary survey. Its scope has been limited to investment capital as usually understood, thus excluding balance of payments items such as short-term capital and unilateral donations, although in certain cases the latter have been a substitute for investment capital in the normal sense. It excludes also, of course, drawings on a country's own external assets, which represent an inflow of capital only for the formal purposes of a balance of payments account. Furthermore, the survey is confined to those British Commonwealth countries which in the aggregate make up the greater part of the overseas sterling area and in the past have absorbed a large volume of external capital; this limitation excludes certain non-Commonwealth members of the sterling area where the capital inflow has been small as well as those where it is almost wholly concerned with oil production.

* Publications giving balance of payments estimates in considerable detail with explanatory notes and comment are now issued for Australia (Commonwealth Bureau of Census and Statistics) and New Zealand (Department of Census and Statistics).

I. THE VOLUME OF CAPITAL IMPORTS

To simplify the presentation, the countries concerned may be marshalled in a few groups. In the first may be placed Australia and New Zealand, whose rather similar economic structure is characteristically of the primary producing country type; moreover, as debtor countries they have always accounted for a large part of the United Kingdom's overseas investments. South Africa and Rhodesia also are akin by reason of a fundamental likeness in economic structure, which has made them to an exceptional degree dependent on external capital. India, Pakistan and Ceylon naturally fall together in a group which has special problems since all three rank as under-developed countries. Finally, it will be necessary to consider together the United Kingdom's colonial territories, also for the most part in the early stages of development but constituting in the aggregate a very extensive investment field which in recent years has become of increasing importance.

The data available on post-war capital imports into each of these groups will be examined in the following sections.

Australia and New Zealand

The inflow of capital into Australia after the war, as in other periods of rapid expansion, was on a very large scale. The balance of payments figures suggest that in the first 10 post-war years Australia imported from abroad capital of one kind or another which in the aggregate may have amounted to approximately £A1000 million. This total, in millions of Australian pounds, is made up as follows:

Government borrowing overseas	125
Recorded private investment	525
Other capital imports and exports (net)	400

The first two items rest on a firm foundation. The amount of public borrowing overseas is of course accurately known while recorded

For Rhodesia also fairly full coverage is available in the statements published in the *Monthly Digest of Statistics* (Central African Statistical Office). The estimates for South Africa given in the *Quarterly Bulletin of Statistics* of the South African Reserve Bank are unfortunately not nearly so full on the capital account and much the same is true of the estimates for India, Pakistan and Ceylon issued by the central banks of those countries. Little detail is available for the Colonial Territories. Special studies of capital imports have been issued by Australia (Bureau of Census and Statistics, *Survey of Companies with Oversea Affiliations, 1947/48 - 1954/55*, Canberra 1956), New Zealand (Census and Statistics Department, *Report on the Official Estimates of Balance of Payments for the years 1950/51 to 1954/55*, Wellington 1955), and India (Reserve Bank of India, *Report on the Survey of India's Foreign Liabilities and Assets as on 31st December 1953*, Bombay 1955).

investment (which includes reinvestment from profits) has since 1947 been computed from the results of special surveys which are believed to cover the most significant elements of private overseas investment in Australia.* The remaining item, however, is the residual in the balance of payments statement and is therefore more doubtful; it includes not only errors and omissions in the estimates (thought to be relatively unimportant) but also short-term capital, which for a time bulked large because of the prospects for an appreciation of the Australian pound. The inflow of genuine investment capital (public and private) may thus be put at a minimum of £A700 while if some of the residual item should properly be classed as investment capital, the total must be raised accordingly. On a fairly conservative basis it would probably be reasonable for present purposes to adopt a round figure of £A750 million as representing new investment from abroad. This may well be an under-estimate.

In any case, the data indicate a very high rate of capital absorption. The pre-war total of external capital invested in Australia, for the most part received over a period of perhaps 70 years (1870-1940), was probably appreciably less than £A1000 million, this figure including the public overseas debt of £600 million and known private investment of more than £200 million.† Thus, even when allowance is made for changes in the value of money, the estimates imply that since the war Australia has been importing capital at a rate very considerably greater than formerly.

The economy of New Zealand in many respects resembles that of Australia but is of course on a much smaller scale, while the lack of mineral resources tends to restrict development. In absolute terms, therefore, New Zealand's capital needs are very much less than those of Australia. Before the war the total external capital invested in the country was approximately £200 million, over three-quarters of this sum being represented by the external public debt.

Nevertheless, New Zealand, like Australia, has traditionally been dependent on capital imports for development: as lately as 1933 public debt held overseas represented more than 50 per cent of the total public debt. In post-war years, however, it has proved possible to maintain a high rate of development by utilising domestic resources, Government capital expenditure being financed partly through budget surpluses and

* Full figures for 1955-1956 are not yet available; the total shown should probably be increased by another £A50 million.

† The estimate of known private investment is from *The Australian Balance of Payments, 1928-29 to 1948-49*, p. 32 (Commonwealth Bureau of Census and Statistics, 1950).

partly through a very large expansion in the domestic debt. Public overseas borrowing up to 1955 was confined to two London loans, each of £10 million, and a loan of 16 million dollars from the Export-Import Bank. In addition there has been a certain inflow of private capital for investment; although details are not available for the earlier post-war years, the special surveys show that between 1949 and 1955 over £40 million was received in this way. With some allowance for the period 1946-1949, the aggregate inflow of capital from abroad since the war may thus be put at approximately £75 million.

South Africa and Rhodesia

South Africa has in recent years ranked with Australia as a field for the investment of capital from abroad, but unfortunately there is as yet no detailed survey of the amount involved; a census of foreign investment is to be taken in 1957. On the evidence of the balance of payments estimates the total inflow of new capital during the 10 years 1946-1955 was nearly £700 million. This figure, which up to 1951 is based on the residual element in the estimates, includes certain short-term funds and much flight capital transferred to the Union in the early post-war years; on the other hand it takes no account of reinvestment from profits. For present purposes possible over-estimation by the inclusion of flight capital may perhaps be taken to offset the exclusion of reinvestment. The more detailed figures published after 1951 show only a very small short-term or residual element.

In the past South Africa's development was effected mainly by means of large-scale capital imports: even in the 1920's these accounted for some 40 per cent of the Union's net investment and by 1936 the cumulative total of external capital received was estimated by Frankel at more than £500 million. Unlike Australia, however, public capital was not predominant. Although geographical factors necessitated heavy expenditure of public money on railways and harbour development, less than half (£224 million) of the estimated capital inflow represented borrowing on public account. The remainder (some £300 million) was invested in productive enterprise, concentrated very largely in the mining industry, which accounted for about two-thirds of all recorded private investment.

The heavy investment in mining and the extent to which this had occasioned an inflow of capital from abroad may be attributed to the part played by gold in the South African economy. The gold mines provided the chief attraction for capital and the main stimulus to development. In post-war years the same stimulus has operated since large-scale capital outlays were needed to open up the new Orange

Free gold mines; by 1955 about £200 million had been spent for this purpose. But in recent years development has comprised not only heavy investment in mining and massive Government expenditure on basic services but also a very great expansion in manufacturing industry. This in turn involved an additional demand for capital, which proved to be even greater than that from the mining industry.

A characteristic feature of the post-war inflow of capital was the extent to which private capital was predominant. Although the Union Government borrowed abroad on a not inconsiderable scale (approximately £100 million), much the greater part of the total (nearly £600 million) is represented by the inflow of private capital.

The Federation of Rhodesia and Nyasaland has an economy in many ways similar to that of the Union of South Africa, not least in respect of capital needs. In both cases the European population is small as compared with the African population (which tends to limit domestic savings) and much of the national income is derived from a highly-capitalised form of mining. In both, too, there has been a very great post-war expansion. The exploitation of the Orange Free State gold-fields in the Union has been paralleled in the Federation by further development of the copper mines in Northern Rhodesia while in Southern Rhodesia, as in the Union, industrialisation has made rapid progress.

The territories which now constitute the Federation have accordingly needed, and have been able to secure, very substantial imports of capital. To finance development the Government of Southern Rhodesia undertook soon after the war an extensive programme of overseas borrowing and the progress of development in the Colony soon attracted private capital; in Northern Rhodesia the mining companies invested heavily in the mines and in the provision of ancillary services. As a result of these diverse factors the inflow of different types of capital was in the aggregate very large. Between 1946 and 1955 Government borrowing abroad exceeded £100 million (about as much as in Australia or South Africa) while the balance of payments estimates indicate that private capital receipts may have amounted to approximately £200 million; of this sum the copper mining companies of Northern Rhodesia probably accounted for about £50 million.

The significance of these figures is brought out by comparison with the data for pre-war years. In the three territories now included in the Federation the cumulative total of external capital received up to 1936 has been estimated at £110 million, the main channels of investment, again according to Frankel, being the railways (£31 million) and the copper mines (£25 million). The figures for the past 10 years are a measure of the rapidity of post-war expansion, a total of some £300 million being received in this period as against not much more than £100 million in 50 years.

India, Pakistan and Ceylon

Although India is generally regarded as an under-developed country, it has in fact for many years experienced a continuing process of development. As part of this process a considerable volume of external capital was absorbed. Before World War I the amount of British capital invested in the country was estimated to be as much as £400 million, made up in approximately equal parts of public overseas debt and private investment. By 1930 the public overseas debt had risen to £400 million while private investment may have been about £350 million.*

During the war India's external indebtedness was transformed in two ways. In the first place, practically all of the Government sterling debt was repaid. Secondly, Indians acquired a good deal (perhaps as much as one-quarter) of the pre-war holdings of non-nationals in business investments. When the new India came into being in 1948 there was thus virtually no external debt on Government account but much foreign capital was still invested in private undertakings. In that year the book value of these investments was nearly £250 million; the market value was considerably higher, being estimated by the Reserve Bank of India at almost £400 million.

The Government of India has not borrowed in London since the war but within a very few years incurred quite a large dollar debt: by 1955 this was approximately 300 million dollars, one-quarter of the pre-war sterling debt, which of course had accumulated over a long period (and was in part allocable to the areas which became Pakistan). Dollar borrowing has comprised several different elements. International Bank loans account for just over 80 million dollars (excluding those to Indian companies under the guarantee of the Government of India). Debt owed to the United States Government is mainly the Wheat Loan of 1951 (190 million dollars) which, though originating in consumption needs, can be deemed a contribution to development since the sales proceeds of the loan wheat were credited to a special Development Fund. In addition, a proportion of United States Aid to India has recently been on a loan basis.

* The figure for public debt includes the sterling debt of the Government of India (£366 million in 1930) and a further amount of over £20 million attributable to other public borrowing. The estimate of private investment is based on the results of the 1948 census with allowance for war-time sales and investment in Pakistan.

In the private sector, post-war investment of external capital in business undertakings in India appears to have been very considerable: an estimate by the Reserve Bank of India, in its 1955 *Survey of India's Foreign Liabilities and Assets*, puts the total for the years 1948-53 at approximately £135 million. This seems high since it implies an increase of about one-half of the book value of the total in 1948 and the balance of payments figures give no indication of any inflow of such magnitude. The Bank's estimate, however, is based on the view that very little of the new capital was received as cash for investment, much the greater part being attributable either to reinvested profits or receipts in the form of goods and machinery. It is believed that since 1953 the inflow of private capital has continued at much the same rate.

Pakistan presents a different picture. In contrast with (post-partition) India, the territories which now constitute Pakistan seem in the past to have attracted relatively little investment capital, although of course they shared in public capital expenditure financed in part by overseas borrowing. Since the inauguration of the new state there is little evidence of any considerable inflow of capital from abroad. The Government development programme has in the main been financed from domestic resources, supplemented by United States aid and assistance under the Colombo Plan. Public borrowing overseas has been confined to loans from the International Bank totalling 30 million dollars, a £10 million loan from the United Kingdom Government, and the loan part of United States aid (20 million dollars). The International Bank has also lent 50 million dollars to Pakistan undertakings but private capital investment from abroad seems to have been very small; according to the exchange control records a total of less than £10 million was received up to 1955 and there is no evidence that there was any considerable inflow of capital in the form of goods and machinery not involving transactions in foreign exchange.

The economy of Ceylon, while in many ways similar to that of India and Pakistan, differs from each in certain respects. In the present context there is a contrast with Pakistan in that before the war Ceylon had attracted a great deal of external capital for investment in productive activity; on the other hand there is a contrast with India since there was very little overseas public debt, the capital inflow being mainly concerned with the plantation industries of tea and rubber. External capital invested in companies in Ceylon before the war has been estimated at some £65 million, including paid-up capital, reserves and debentures. The overseas public debt in 1939 was no more than £12 million. With some allowance for other investment the total external indebtedness may be reckoned as of the order of £100 million.

Post-war development has not involved any considerable inflow of capital on either public or private account. The Government has borrowed abroad on only two occasions; a £5 million loan was floated on the London market in 1954 and a loan of 19 million dollars was obtained from the International Bank in the same year. The balance of payments estimates afford no indication of any appreciable volume of private investment from abroad and in fact there has been a certain outflow of capital as Ceylon nationals have purchased existing enterprises established earlier by overseas interests.

The Colonial Territories

The overseas dependencies of the United Kingdom, though comprising territories which differ greatly in their economic structure, may for the most part be termed under-developed in the sense that before the war capital investment in individual colonies had usually been relatively small. In certain cases, however, (notably Malaya) a great deal of external capital had been invested and the total was in absolute terms quite considerable. Excluding Ceylon and Rhodesia, the figure for the whole colonial empire may have been as much as £400 million.*

The post-war years have brought a marked acceleration in the pace of development. This is evident in the development plans of colonial Governments, which assume the availability of finance on a scale much bigger than that formerly accepted as normal. Thus, in 1954 the estimated cost of the approved 10-year development plans (which of course refer to public expenditure only) amounted to no less than £450 million. The plans provide for about one-third of the required sum to be found by public borrowing.

Unlike some other sectors of the overseas sterling area, the Colonies were not before the war heavily indebted on Government account, the total of their loans being no more than £80 million. Since the war, from the re-opening of the London market in 1948, colonial Governments have borrowed fairly freely: up to 1955 loans floated in London (excluding conversion issues) amounted to more than £120 million. The flow of capital from the market was supplemented by a considerable volume of investment through public corporations created and financed by the United Kingdom Government. The Overseas Food Corporation spent some £40 million in Tanganyika (nearly all on the abortive groundnut scheme) while the Colonial Development Corporation by 1955 had invested capital to the extent of over £40 million.

* Estimate based on data drawn from the following sources. Frankel: *Capital Investment in Africa.* Callis: *Capital in S.E.Asia.* Royal Institute of International Affairs: Memoranda for International Studies Conference, Paris (1937).

From these three sources alone, therefore, a total of £200 million was received. In addition the Colonies were enabled to apply for loans from the International Bank but so far (apart from Rhodesia) there has been only one colonial borrower, the East Africa High Commission receiving a loan of 24 million dollars in 1955.

The amount of private capital invested in the colonies since the war cannot be computed with any claim to accuracy but an official estimate* puts the total at approximately £300 million and much the greater part of this sum can be attributed to individual colonies or large investment projects. The total would include as major items the cost of the new refinery at Aden (nearly £50 million); investment in Nigeria (probably at least £25 million); and a substantial though unknown figure (perhaps as much as £100 million) for East Africa. In the West Indies, oil investment in Trinidad may have exceeded £25 million while the bauxite industry in Jamaica accounted for more than £20 million. British Guiana is known to have absorbed at least £15 million. In the Far East a great deal of capital from China was transferred to Hong Kong but it is noteworthy that, apart from re-investment, there has been very little capital inflow into Malaya.

II. POST-WAR TRENDS AND SOME EXPLANATIONS

A study of this kind yields significant results only if organised on a comparative basis. It is accordingly necessary to set out the estimates given in the preceding section so as to facilitate comparisons between the different countries under review, with reference back to earlier data. Juxtaposition of the figures in this way shows the relative magnitudes involved, gives a synoptic view of post-war trends and helps to bring out the factors underlying such changes as have occurred.

Post-war Inflow and Pre-war Totals

The summary table below shows how the flow of capital was distributed among the various recipients. In Australia, South Africa and the Colonies capital imports, on a rather conservative estimate, appear in each case to have amounted to some £500-700 million; for the Federation of Rhodesia the comparable figure was about £300 million. On the other hand, in the immense territory of India, Pakistan and Ceylon taken as a whole the capital inflow was relatively small. In India it is estimated to have been over £250 million (though much of this was of a special character) but in Pakistan and Ceylon only very minor sums were recorded. The figure for New Zealand

* Hansard, 14th May 1956, col. 1802.