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Exchange Rates and U.S. Direct Investment into Latin America

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Abstract:

This paper analyzes the impact of exchange rate levels and exchange rate uncertainty on U.S. foreign direct investment into Latin America. By decomposing exchange rate uncertainty into temporary (short-run) and permanent (long-run) components, we further explore whether the nature of uncertainty matters. Our empirical findings support the view that exchange rate uncertainty has a negative impact on U.S. investment flows into Latin America. Moreover, it is the persistency in uncertainty rather than transitory uncertainty that mostly deters foreign investment. In contrast, investors do not appear to be affected by discrete movements in exchange rate levels.