Foreign Direct Investment and its Literature Review

Khaldoun Maddallah Al-Qaisi*

Vice Dean of Scientific Research and Graduate Studies, Amman Arab University, P.O. Box: 2234, Code 11953, Jordan

Abstract: The types of investment that are made abroad are known as foreign and have majorly affected countries that engage in these activities of business. The various factors which are to be considered such as –political factor, social factor and economical factor as these factors affect the allocation of international capital. This research paper will examine and analyze the literature review which is focusing on movement of capital under foreign direct investment. Existence of a positive effect on the economy of a country that is injected with these substitutes has led to a better performance of the overall GDP and increase in national output. The same is related to economic growth. It is argued that the study based upon verified documents involves all the countries irrespective of their geographical area whereas the fact is that many of them are concerned with largest recipients of foreign direct investment such as- Asian and Latin American countries.

Keywords: FDI, GDP, Literature Review.

INTRODUCTION

(FDI) is a global perspective of transacting businesses of a country made by a company /entity which exists in another country. In FDI, investment should be in the form of ownership/controlling ownership in the foreign company. Over the last few decades, foreign direct investment has been a matter of academic study (Globalization has inspired the companies to formulate various types of approaches to globalize their business, which results in activities like FDI. FDI can have both favorable and adverse impact on country’s economy. The international monetary fund, foreign direct investment requires relationship on long term basis–which shows the interest of resident company in one’s economy. “(Thomas, 2016) argued about Economic sustainability of host countries in regards to the national output and gross national product”. There are various case studies and articles which focus on FDI’s determinate factors and the end results that are obtained. There is a heavy penalty and contributes to the overall goal of maintain the flow of funds and factors of production into the economy. In nutshell, we can say that FDI has an impact on economic growth of the country.

The aim of this research paper is to present a literature review of verified paper (based on facts rather than theory) and result of each case study will be discussed. The given verified paper will be discussed according to the date of publication. Therefore, four different periods will be studied in brief in this paper. In this research paper sample which is taken is relatively greater. For this paper, verified paper case studies are selected rather than those which are theoretical one. This aspect facilitates investigation to be done on the statistical methods which are applied during these periods. In short words, a large period is considered which will be discussed according to the date of publication. “(Blemmion, 2010) said about a review of the empirical literature on FDI determinant in the Atlantic economic review”.

LITERATURE REVIEW

Foreign direct investment can be defined as ownership or control in foreign company which is 10% or more of company’s voting securities. The Foreign direct investment requires new technology, capita and management skills. Foreign direct investment allows a company that engages in supply of important and consumable goods into the market and the services to the people to have the stability and certainty in the going concern over the foreseeable future. They are only two types of FDI which included the horizontal and the vertical all of which heavily contribute to sustaining the economy of countries and bringing stability and also a suitable currency which is not subject to fluctuations. These investments of business are outside their own country that it operates at their own country (domestic country). In horizontal foreign direct investment company wants to take the advantage of international platform by selling their good and services all over the world with the help of globalization and foreign direct investment. It provide platform to companies to showcase their talent and take the advantage of same to increase the wealth of their domestic country. Horizontal foreign direct investment is a traditional model which is followed by Japanese to expand their business. According to them, this model
has certain advantages. It helps them to reduce the risk, share their resources which are already developed by them at home (domestic country). There are certain companies who enter into vertical foreign direct investment to reduce the cost of raw material used by them or supply of some important components.

Economic growth per capital is derived by bringing improvement in productivity, also known as efficiency of an economy. Improving the productivity refers to generating various goods and services by using the right amount of labor, capital and raw material. Basically it means reducing the wastage of resources.

Encourage agricultural activities that promote Productivity of land during the evolution that facilitated green movement was a detrimental initiatives that led to successful plantation and new method of farming that improve the cash crop production. The described era of green revolution introduces use of new grain hybrid to increase the output all over the world. High rate of expectancy has a direct relationship with standard of living. The economic is always calculated in real terms. In economics, economic growth and its theory means production at full employment. GDP growth indicates the domestic production is carried out effectively and efficiently.

These investments are known to impact positively in such a way that there is a result which are positive and increase in the flow of money in the economy. There is direct impact on economic growth of the country due to accumulation of capital, incorporating improved inputs & use of updated foreign technology in the activity of manufacturing of the another country. To analyze the benefits of FDI theoretically there are various models which are widely used such as- empirically, endogenous, neoclassical. But results varied from model to model because of selection of sample (developed country versus developing countries), use of various types of techniques, time duration for which they are selected and use of different methodology.

Tradeoff is defined as the relationship in business transactions conducted by the host countries by engaging in export promotion and import substitution in a global perspective. This aspect brings the balance of payment between the markets of the foreign commodities and enhance that the mutual benefit derived is sufficient to sustain the economy into running. The appropriate performance is considered where there is context of longer term performance thus emancipating from the issue that there is a gap generated by these activities that reduces the level of growth in these markets currently emerging. Catch up process are as result of the investments that are initiated with the growth of economy known to be impeded in the nature that it leads to benefits of the trading countries such as Taiwan, Indonesia, Mexico, and Greece shows a positive inward investments. An extensive research has been conducted which has enhanced using of data in a revised and detailed format that contributes to over dependence of the spills overs by the industries that gains access to these flows of the FDI.

Local markets are the determinants as to whether there will be a growth noted into the foreign partners where the growing economy has a positive ramifications that are have strength in the matter that

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Research on relationship between FDI & economic growth.
foreign affiliates and firms based on a locally based are able to engage in a fair competition. The inferior industries are protected from the power of monopoly all over the world and this promotes competition that is equitable and leads to mutual sustainability between the partners that promote the trade conducted in these regions. Introduction of goods and services into the market of the host country is the resulting effect of the foreign trade activities that involve the investments carried out by the nations for the main goal of the accelerated production and an increase in the domestic market inflows and overseas exportation.

Asian countries have been identified as one of the largest FDI recipient in the world hence being a major boost in the country’s economic growth. In the recent years Kenya has become a major attraction to global investors due to its high potential of growth especially after the introduction of the new constitution that has opened up various investment opportunities all over the country through the introduction of counties and through international forums like the Global Entrepreneurship Summit 2015.

In regards to the conference of the nations that have consented to have similarities in the global perspective of conducting trade (U.N.C.T.A.D) world investment report 2015, India’s foreign direct investment in 2014 hit 97.8billion a 95% increase from sh49.9billion in 2013. This is expected to double since this year has witnessed huge FDI inflow compared to the previous years. For example in the Global Entrepreneurship Summit of 2015, number of deals concerning foreign investment were agreed upon which include;

Sh. 450million given by the coca cola foundation to fund a new youth empowerment initiative to train the youth on business skills and provide employment, Sh. 20billion granted by the United States overseas private Investment Corporation to Equity bank for lending to SMES driven by youth and women over the next 5years.

Global entrepreneurship networks committed sh10billion to fund programs that support entrepreneurs and the development of their networks. IBM plans to invest sh6billion in Africa which includes a partnership with Kenya Education Network on technology courses.

General Electric to invest sh200 billion across Africa included a partnership with Kipeto Energy on a wind power firm in. If such investments will be fully implemented they will have positive impact on the economy. “(Harvey, 2016) said that the major economic data that was contained in the global convention of the 21st century that was discussing he perspective of the nationals’ wealth in the world”.

For years the joint service of the Foreign Investment Advisory Service, the International Finance Corporation and the world bank have been in pursuit of helping African governments to promote an enabling environment for foreign direct investment. The Latin American government has been receptive to this advice and it has made tremendous progress in improving the basic framework of FDI in Asian countries. This has created an upward trend in terms of foreign direct investments in the country over the past few years.

The lowest decline in FDI witnessed in African countries between the years 2008 and 2010 was as a result of post-election violence witnessed after the 2007 general elections. In 2012 a decline in FDI was as a result of uncertainty of the 2013 general elections whereby foreign investors were afraid of investing in the country due to the losses incurred after the 2007 elections. Since then the trend has been increasing over the past few years at a high rate. This serves as an indication that political stability is a major determining factor of FDI in a country.

FDI and its connection with human capital have gained lots of attention. Inward foreign direction has favorably affects the economic growth of the country through its interaction human resources and capital. “(Thomas, 2016) said that Economic sustainability of host countries in regards to the national output and gross national product. Contribution of FDI in economic growth of the country is more than the domestic investment. According to researchers, manpower is directly related to growth of the country’s economy. As per the sample of American countries, country must have economic stability, human capital resources and there should be liberalization in the market for significant positive impact of FDI on economic growth of the country. As per the sample data of 84 countries during the period 1970 to1999, it is found that FDI directly or indirectly affects the economic growth of the country through its interaction with manpower. “(Amin, 2014) said Foreign Direct Investment and Economic Growth Literature Review from 1994 to 2012 is evidence of the economic growth rate”.

There is an argument that FDI has positive effect on economy of the country only for short period of span. In
long run foreign direct investment has adverse impact on country's economy. The reason behind negative effects that are achieved to the resulting economy in long run is that the institutions that are developed with the support of foreign investment demands more foreign investment and causes negative impact like, unemployment among the people, disparities of income, over-urbanization, increasing inequality between rich and poor. Different measure is selected for foreign direct investment that is total percentage of FDI which is contribute by general economy of the country makes the sum to increase in the budget of the nations which are investing, but it is still illustrating adverse impact on country's economy in the long run.

From the summary of major countries and those that do not adhere to the OECD are termed as countries during the period ranging from the 1970-1990. Growth is on a spread and accountable basis in the home country is ascertained by various types of technologies also skills of the contributing country to another country (host country). Their impact is calculated by substitution of FDI from domestic investment. In sample of non-OECD, it is concluded that benefits of growth is limited to those countries whose income are more as compared to other countries. From the sample of 78 developing countries, they also founds that benefits of growth is limited to those countries whose income are more as compared to other countries. It is concluded from above that regime of trade is very important for transmitting the favorable growth impact on foreign direct investment. Sample the data of 46 countries which are developing in fixed model which is backed by foreign direct investment growth effect in positive manner for countries who are promoting export but negative impact on the countries for importing countries. In same manner error correction techniques are used to improve economic growth in various countries like Mexico, Taiwan, and Hong Kong.

**REVIEW OF PERIODS**

**Period 1950 – 1973**

Started empirical works during this period and applied various regression analysis in order to study the impact of resource funding in foreign direct investment inputs and impact of framework of industry on capital flows (private) and domestic economic activity. This study included foreign direct investment in United Kingdom (1952-1962) and in USA (1950-1963). Variables which were studied during the period include

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portfolio of the countries, FDI, capacity utilization (Index) and ratio of long term bond yields (British to American). Study clearly indicate that there is difference between how the countries private FDI reacts to changes in the capacity utilization index. “Belgrade said about knowledge-and-physical-capital model of international trade flows, foreign direct investment, and multinational enterprises”.

An economist also applied various other regression analyses in the same year to find out whether the capital allocation at the international level is affected by the establishment of EEC. The variables used are FDI obtained by U.S.A & Western European countries (1951-1964). Research results concluded that EEC establishment has no influence on the capital allocation. A cross-section analysis was also conducted by Griffin (1968) to find out the impact of foreign capital inflows in the Colombian economic growth during 1950 – 1963. This study concluded that capital inflows from foreign has reduced domestic savings. An accountant by the name Cristobel Argued that Literature review of 100 empirical studies of Foreign Direct Investment”.

also investigated the factors of the US FDI (1952 – 1966) by Applying the OLS3. The study concluded that as per FDI determinants only the market size of the host country is statistically important. FDI has applied multiple regression analysis to find out the impact of the creation of trade associations in the international allocation of resources. The study regarded the EEC and the EFTA (1951 – 1965), rate of US FDI and profit rates of the FDI. On the basis of above research, presented research of which applied OLS to study the impact of the trade tariffs in the US FDI to EEC and EFTA.

The research included study of rate of growth of US FDI in EEC and EFTA; during (1955-1969) multiple regression technique was applied by Elbe (1970) to discover the causes of the capitals movement (Private) in Germany. The variables which were included are net flow of capital (Private), trade balances and the rate of interests (German and European). It was concluded that the flow of capital doesn’t affect the balance of trade. Various variables such as net capital inflows, international interest rates, and trade balance and income velocity of money were used to study the movement of capitals among the 6 OCED countries during 1960 to 1969 by applying multiple regression analysis by “Anderson, 2013 argued that gravity with gravitas is a solution to the border puzzle”.

It was observed by the researchers that these variables help to attract foreign capitals. By examining various variables like growth rate of GDP (real), BOP, domestic savings and fixed capital formation tried to study the interdependence among savings, investment and growth in 43 countries.

By examining capital formation (gross domestic, private and Government) and increase in stock by using OLS he wanted to investigate foreign capitals inflow and their effect on the Korean economic Growth.

This study suggests that it is very important for the Korean economy to sustain high growth rates of the tax revenues and exports so as to achieve sustaining growth. To study the impact of foreign capital inflows in 8 countries (1950-1969) applied multiple regression analysis technique. Variables which were studied included growth rate of GDP, exports and trade liberalization. The conclusions of this research suggest that there is low correlation between exports and economic growth.

Period 1974 – 1989

This period that started after the collapse of Fordism development model, presents various important studies in FDI analysis, particularly, as they applied OLS to study the international capital flows and the balance of payments in 4 countries during the period 1960 – 1970. The following variables were used total inflow of capitals (Private), foreign incomes, exchange rates, domestic assets, domestic stock of wealth and the account balances. This study concluded that a change in income contributes to changes in capital flows, whereas capital flows adapts to the host countries’ monetary policies. By

The application of variables like the rate of economic growth, gross domestic investments, net FDI and the FDI stock Stone man (1975) wanted to study their effect during 1945 – 1970 using multiple regression analysis method.

The results of this study concluded that ODA and domestic savings contribute to economic growth. Foreign research also applied OLS to study the relation between monetary policy and FDI in Germany (1960 – 1970). The following variables were thoroughly studied, net capital inflows, domestic stock of wealth, interest rates (Domestic), exchange rates, foreign incomes, domestic assets and the current account balances. This study concludes that monetary policies of
Germany offset FDI. Some years later, to study the relation between (domestic) savings and international capital movement (1960 – 1979) applied OLS. The variables that were taken into account for the study were net FDI, GDP and domestic savings.

To identify the interaction between FDI and efficiency of spillovers in Mexico in 1970 used OLS. The following variables were taken into account total assets, the Herfindahl index, and gross production on an average basis in host economies, average effective work day, total number of employees employed in foreign companies, average of effective work days and the ratio of white to blue collar employees. The research concluded that labor productivity in Mexico is associated in a positive way with the presence of subsidiary companies.

In order to investigate the impact of FDI on mining and constructions in 62 countries (1967 – 1978), applied multiple regression analysis technique. The study contained following variables FDI stock in constructions, (real) gross fixed capital formation, total population, per capita GDP and FDI.

The result of the study concluded that the FDI stock in the construction sector is associated in a positive way with the borrowing only in the USA, whereas only the African countries were affected by the FDI. Also, FDI in the mining sector is not associated with the accumulation of public debt. Further, in order to investigate relation between FDI and the export and also import value in 30 countries, applied OLS. This included the following variables imports and exports value, total population, GDP, and FDI stock. As per the study it is argued that there is much stronger correlation among the exports, G.D.P. and FDI stocks for less populated countries than countries with more population.

To study the determinants of location of FDI in the 6 countries of Europe (1969 – 1982), has applied OLS and GLS. The study included the use of following variables FDI, growth rate of GDP on annual basis, tariff barriers, costs of labor and the nominal interest rate differential. This study reached to the final conclusion that the growth rate, size of the market and the tariff barriers were the most important location determinants in attracting FDI. It is thus observed that the size of the European market is not considered to be a main factor to attract the FDI deriving from the U.S.A. “(Metaxas, T. (2016), Literature review of 100 empirical studies of Foreign Direct Investment”.

Period 1990 – 2004

This period is recognized for the rapid development of developing countries around the world and for process of transition of various former eastern countries into European Union Environment in 2004. With the view to investigate the relationship between the creditworthiness and FDI in 47 LDC (1980 –1986), applied OLS and a two – stage limited – dependent variable method. The following variables were considered, commercial inflows, capital reschedule intention and various other variables affecting creditworthiness. This study has indicated that the amount of inflows of capital has a significant impact on the host countries’ creditworthiness and that inflows of foreign commercials were not directly associated with the increased creditworthiness.

For investigating the determinant factors of the Taiwanese F.D.I., used OLS; variables which were studied are FDI in Taiwan, Taiwanese economic reforms and the various periods during which FDI reached their peak. According to the findings incentives offered to foreign investors and the country’s economic performance are not determinant factors in attracting FDI. To investigate the impact of social and political changes that has taken place during 1950 – 1982 in FDI in 15 LDC, applied multiple regression analysis. The following variables were taken into account were FDI in the manufacturing, mining and petroleum industries, GDP and the total population. Applied OLST to facilitate the study the relation between the economic growth and justice in Chile during the period 1951 – 1989. The variables which were used to study the same are growth rate of real GDP, GDP growth rate, effectively utilized stock of capital and the ratio of employment. It was concluded that recession has led to increase in the rates of unemployment that has negatively affected both the economic growth and the low and middle – income groups. “(Harvey, 2016) Major economic data that was contained in the global convention of the 21st century that was discussing the perspective of the nationals wealth in the world”.

By considering FDI, GDP, average wages, literacy ratio, infrastructures, SEZ’s, cities which are coastal, Economic and Technological Zones, applied GLS to find out and study the FDI in China (1990 – 2000). This study concluded that the FDI from Hong Kong in china was majorly affected by the labor cost in China, whereas the local demands has affected FDI from Japan. Also, FDI from Japan were mostly attracted to the Economic and Technological Development Zones,
whereas FDI from Hong Kong were attracted to the coastal cities and the Special Economic Zones. To study the impact of FDI & EFPI on the economic growth in 83 countries for the period 1979 – 1998 applied OLS. The following variables were used economic growth, FDI and the foreign portfolio investment (equity), economic development, corruption and the property rights. It was finally concluded from the study that F.D.I. and equity foreign portfolio investment do not directly affect the economic growth but they do contribute for the improvement of the absorption capacity.

**Period 2015 – 2016**

S.LS- techniques were used by Li and Liu to know the effect of FDI on country’s economic growth. It has been concluded that positive correlation exists between FDI and economic growth.

Generalized method of moments (GMM) - techniques was used by Agosin and Machado to know the effect of FDI on domestic investment in 12 countries. It is concluded that FDI does not affect domestic investment of the particular country.

OLA and FE- techniques were used by Schneider to know the interaction among international trade and economic growth. He studied various variables such as research and development expenditure, innovation rate, physical stock. From the study, it has been concluded that FDI in totality has positive effect on health status of the country.

FE, RE and cross were the techniques used by Ramman and Zurbuegg to analyze the connection between FDI and domestic investment. It has been concluded that FDI crowds in domestic investment. Foreign direct investment is encouraged by private investment.

OLS, RE, FE were the techniques used by Pazienza to know the environmental impact of foreign direct investment. Variables used were- the gross domestic product, literacy ratio, capital formation. It has been concluded that Foreign direct investment have no adverse impact on environment.

**CONCLUSION**

It can be concluded from the case studies of FDI & economic growth that foreign direct investment has favorable effect on economy of the investee country. Only in fewer cases it has adverse effect or null effect. It was also found that human capital interaction with foreign direct investment also plays a vital role. There is a well-developed financial market, using of high grading technology helps the foreign direct investment to support the economic growth of the country. But the quality of political environment should also be considered for foreign direct investment.” Roth, 2012 said Research note south-south fdi flows: how big are they? In: united Nations conference on trade and development division on investment, technology and enterprise development”.

Various researches have been conducted on the foreign direct investment over the last few decades. From the verified papers which are explained in this paper we have managed to draw a conclusion on the type of statistical methods used, samples which are chosen and the main areas on which researchers mainly focus. The present study is based on verified papers (facts) rather than theoretical model. Present case study is based upon statistical model where foreign direct investment is involved .In addition, verified papers (empirical papers) published after 2015 could also be added. Additionally, the affect from the income level of investee country is contradictory & the quality of political and environmental effects should also be considered, “(Batticemor, 2007) said about free trade agreements actually increase members' international trade”
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