THE DYNAMICS OF THE FDI INFLOWS DURING THE LAST THREE DECADES. A COMPARATIVE ANALYSIS BETWEEN DEVELOPING AND DEVELOPED COUNTRIES

DIACONU MAXIM Laura [1]

"Alexandru Ioan Cuza" University of Iasi

Abstract

The global foreign direct investments started to increase especially since the last decade of the XXth century, when various stages of trade and investments' liberalization process took place. The aim of the present paper is to analyse the evolution of the FDI attracted by the developing and developed countries, during the last decades, and to identify the factors that influenced their trend. Our results show that, even if for a long period of time the FDI inflows into the developed economies had a considerable higher value than those attracted by the developing states, the 2007 crisis has changed this situation.

Keywords*: FDI inflows, developing countries, developed economies, economic and financial crisis*

JEL classification: *F21, P33*

1. Introduction

It is well known the fact that, during the last decades, the foreign direct investments (FDI) made by the multinational companies have increased at a faster rate than most other international transactions, especially after 1995. Some decisive moments for this evolution were represented by the completion of the Uruguay round and by the regional integration processes from Europe, Asia-Pacific region and America. The advantages brought by the trade and investments' liberalization, consisting in multinational corporations' access to new and large markets, have generated a global boom of the FDI.

[1] *Assistant Professor, Ph.D., Faculty of Economics and Business Administration, Department of Economics and International Affairs, "Alexandru Ioan Cuza" University of Iasi, Romania, dlaura_es@yahoo.com*

During time, there were made various theories which tried to explain the FDI. The earliest ones, dating from 1950s, were based on the cross-country differences in capital returns (Macdougall, 1960). The theory developed by Hymer in his PhD thesis in 1960 and subsequently published in 1976 argues that the decision of a firm to invest abroad is related to the existence of some firm specific advantages, such as access to raw materials, economies of scale, trade names, patents etc. (Hymer, 1976).

Developing the life cycle theory, Vernon (1966) explains that the FDI are part of a process that starts when a product is launched in the origin country. When the product is mature and standardized in the home market, the firm decides to establish the production facilities abroad, in order to benefit of lower production costs. Therefore, in the decline phase, the FDI will be directed to the less developed economies, where there are the best cost advantages.

Since the 1970s, various analysts have made different attempts to refine and test the Hymer and Vernon's theories. Therefore, in the middle of the 1970s several economists have contributed to the development of the internalization theory, aimed to explain why the cross-border transactions of intermediate products are hierarchical organised. In this context, Buckley and Casson (1976) underlined that, in order to overcome the market imperfections, firms can internalize their own markets, through a vertical-integration. According to this theory, firms will make foreign direct investments when the net benefits of their common ownership of domestic and foreign activities may exceed the advantages offered by external trading relationships.

The internalization theory represented a starting point for the Dunning's eclectic approach. His theory is considered to be one of the most comprehensive explanations for the FDI, since it combines elements of various theories, such as that of the international trade and the theory of the firm. According to Dunning (1980), the international production is the outcome of a process in which ownership, internalization and localization advantages work together.

Apart from these theories, other recent studies have also identified some factors that could influence the multinationals' decisions to relocate their production facilities abroad, through FDI. In a study conducted on Central and eastern European states, Bevan and Estrin (2004) consider that the labor costs, gravity factors, market size and proximity could be the major determinants of the FDI attracted by these economies. Conducting a research on 68 developing countries, Mottaleb and Kalirajan (2010) underline that the most successful states in attracting the FDI inflows were those with larger GDP and high GDP growth rate, higher proportion of international trade and with more business friendly environment. To these factors, the inflation rate and the interest rate could also be added (Çeviş, Çamurdan, 2007). It was demonstrated that the socio-political instability has a negative impact on investment flows, while a more predictable macroeconomic environment has a positive influence (Singh, Jun, 1999).

Depending on the reason for which the production's internationalisation occurs, Athukorala (2009) grouped the FDI into three main categories: market seeking, resource seeking and efficiency seeking FDI. Apart from these traditional factors, Nunnenkamp (2002) considers that availability of the local skills has gained importance in attracting the FDI. The same idea can be found at Checchi, De Simone and Faini (2007) who concluded that the existing endowment of human capital in the host country is a significant determinant of inward flows of foreign capital.

As it can be noticed, during time the analysts have identified a large number of factors that influence the FDI inflows into a country. However, there is a general agreement among the economists that the financial and economic downturns have a significant impact on the attracted investments (UNCTAD, 2009; Ucal et al., 2010). Trying to compare the magnitude of the crises' influence on the FDI inflows during time, Poulsen and Hufbauer (2011) found that the economic and financial downturn that started in 2007 had the biggest impact.

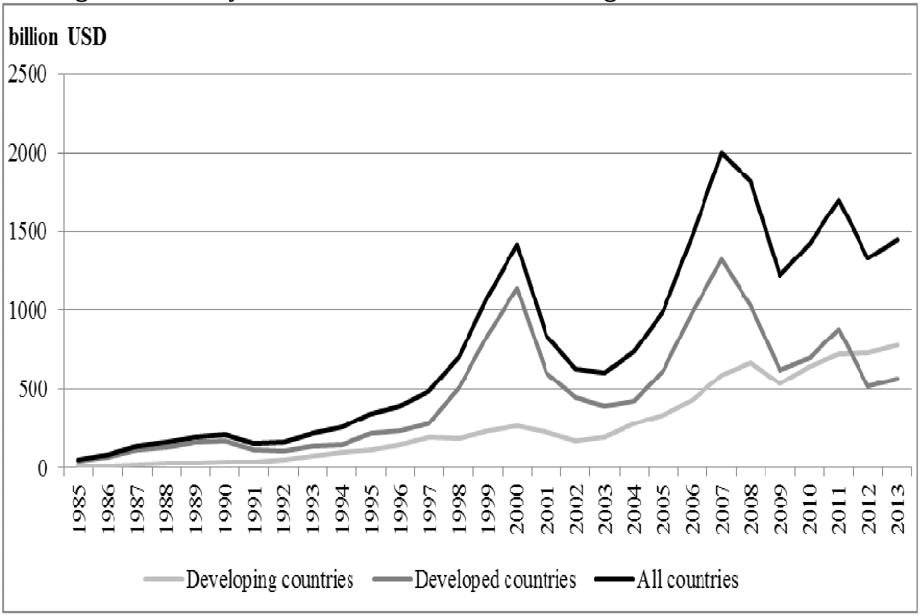
Considering all these aspects, the present paper intends to analyse the evolution of the FDI attracted by the developing and developed countries, during the last decades, and to identify the factors that have influenced their trend. In order to reach the established purposes, the paper, structured in two main parts and conclusions, includes several analyses which required collecting, tabulating and processing the statistical information from several international reports and databases.

2. Trends of the FDI inflows into developed and developing states during the last three decades

While between 1985 and 1990 the global FDI had reduced values, they registered a notable increase in the last decade of the XXth century, especially after 1995, due to global liberalization of trade and investments.

However, it can be noticed that this positive evolution was mainly generated by the increase in the FDI inflows into the developed economies, the developing states still amounting low values in the 1990s (see Figure 1).

Figure 1: The dynamics of the FDI inflows during the last three decades



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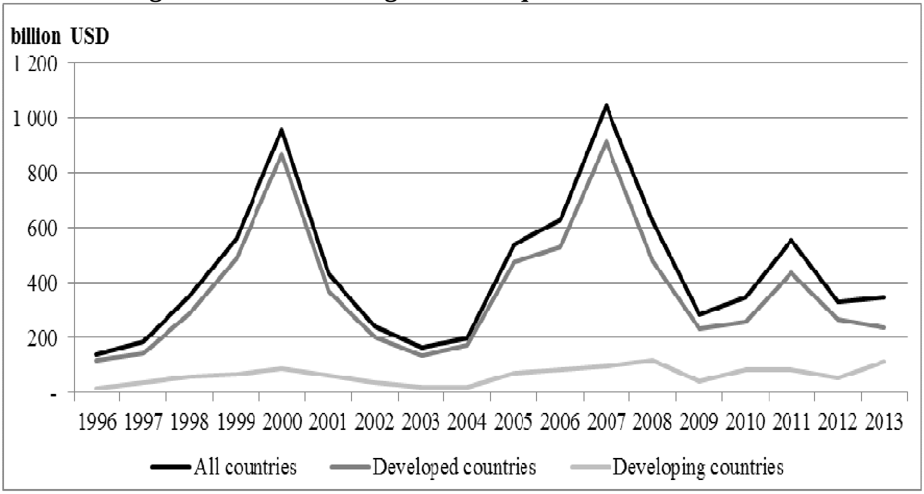
After reaching record levels in 2000, the positive global FDI inflows’ trend was temporarily interrupted. In 2001, they decreased by over 40%, the descendent evolution also continuing in 2002 when these investments dropped with another 21% (UNCTAD, 2003), to 629 billion USD. During time, the analysts offered various explanations for this situation. While some of them suggested that it might have been a result of the 1997 Asian crisis, others, among which Youssef (2002), have pointed out the fact that the world’s three largest economies entered into recession. A more comprising explanation was given by UNCTAD (2003) that considered this FDI downturn a result of macroeconomic, microeconomic and institutional factors, such as: decrease in the economic activities especially in the developed economies, low corporate profits, financial restructuring, decline of some large corporations etc. Other analysts, such as Matei (2004), argued that 2001 was the year when the FDI regained their normal values after the intense activity of mergers and acquisitions (M&A) that took place in the end of the 1990s and in 2000 (see Figure 2).

Figure 2: Value of mergers and acquisitions between 1996 and 2013



Source: Author's compilation and adaptation from UNCTAD, 2014b, *World Investment Report 2014: Annex Tables, Annex 09 - Value of cross-border M&As by region/economy of the seller,* http://unctad.org/en/pages/DIAE/World%20Investment%20Report/Annex-Tables.aspx

As it results from Figure 1, while the FDI inflows attracted by the developed states decreased very much between 2000 and 2003, these investments into developing economies remained relatively stable during the first three years of the XXIst century. The FDI's dynamics into the developing countries could be explained through the increased global competitive pressure, in the context of the slowdown of the developed economies, which determined the investors to continue looking for lower costs.

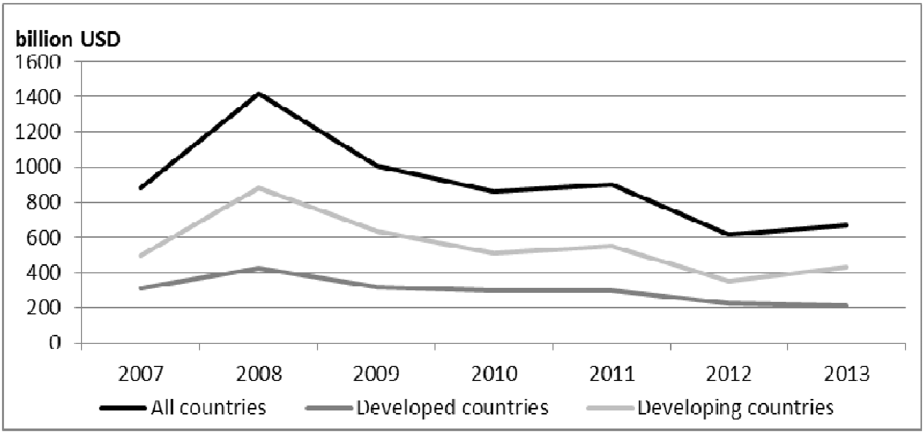
The period 2003-2007 was marked by a sustained increase of the FDI, both into the developed and developing states. It was the period when almost all the countries have experienced economic growth and the corporations registered high profits. According to the statistics, the reinvested profits accounted for approximately 30% of the total FDI inflows, especially in the developing countries (UNCTAD, 2008). During this peak period of the FDI, United States and China were counting for thousands of FDI projects every year. Next to China, another important Asian destination for the multinationals' investments was India. Meanwhile, the annual number of the cross-border investments in the European states has exceeded 10000 (Kokko, 2006). According to UNCTAD (2006), during the first years of the XXIst century, the African countries were among the economies with the fastest increases in the attracted FDI.

In 2007, the global FDI inflows have reached the highest value ever since, overpassing 2 trillion USD. However, the economic and financial recession has generated a collapse not only in the stock markets, global production and trade, but also in the investments' flows. As it can be noticed in Figure 1, in 2008 the global FDI inflows started to fell. In 2009, when the global output contracted for the first time in 60 years, it was felt the worst collapse of the FDI: they represented only 61% of the value achieved in 2007. It can be observed a partial recovery in 2010 and 2011, followed by a new drop in the investments' flows in the following two years. In 2013 FDI inflows had a slight increase, but they have still registered a value with 27% lower than in 2007.

When looking at the FDI trend after 2007 in the two types of countries that were analysed, we can observe a major difference: while the developed states faced a significant collapse of the inflows, with small recoveries in 2010 and 2011, the developing countries, despite the slight decrease from 2008-2009, have registered record levels since 2010. In 2013, the FDI attracted by the developing states have even surpassed those from the developed countries, accounting for 54% of the global FDI of that year. The resilience of the FDI in the developing states during the recession period can be explained through the fact that the economic situation determined the multinational companies look for lower costs – higher profits investments' opportunities. Related to this, another possible explanation could be the fact that the mergers and acquisitions, found especially in the developed economies (see Figure 2), faced a higher decrease compared to the "greenfield" investments, usually made in the developing states (see Figure 3). This was due to the fact that the situation from the financial markets has hidden the prices' signals, very important for M&A. Therefore, the difference between the FDI inflows into the developed and developing economies considerably diminished between 2009 and 2011.

Indeed, looking at the Figure 2 and Figure 3 we can notice that while M&A had substantially higher values in the developed states compared to the developing economies, the greenfield investments have constantly registered superior values in the developing countries than in the developed ones. Actually, we can say that the greenfield investments were the main way of the FDI access in the developing countries. Moreover, in the developing states we can notice that, even if the greenfield projects have slightly declined after 2008, in 2013 they were on an ascending trend, registering almost the same value as in 2007.

Figure 3: Value of the FDI greenfield investments between 2007 and 2013



Source: Author's compilation and adaptation from UNCTAD, 2014c, *World Investment Report 2014: Annex Tables, Annex 19 - Value of greenfield FDI projects, by destinations,* http://unctad.org/en/pages/DIAE/World%20Investment%20Report/Annex-Tables.aspx

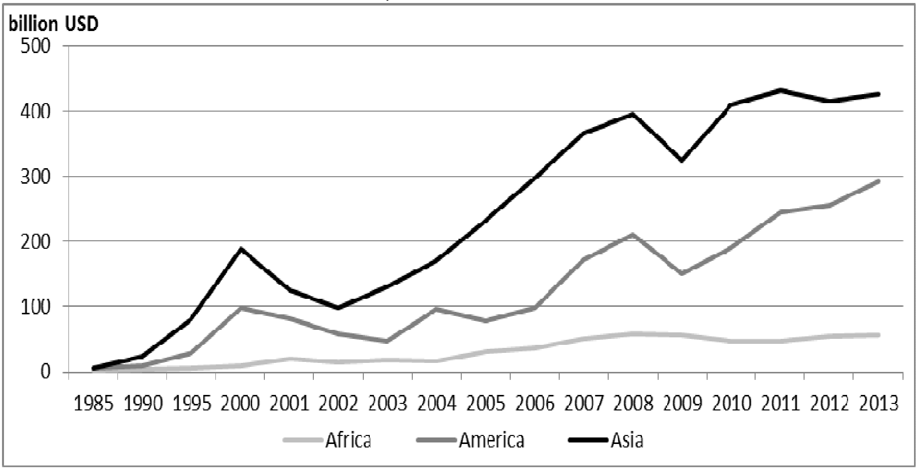
It is important to analyse the FDI on the two main types – the mergers and acquisitions and the greenfield ones – in order to determine the role played by these investments in the developed countries, knowing the fact that M&A do not bring the same benefits as the greenfield investments. Moreover, on short term, M&A may even generate negative effects, such as the unemployment due to restructuring. However, on long term, the two types of investments have similar consequences (UNCTAD, 2012).

Analysing the differences between the two major moments when the investments have slowed down – 2001 and 2008 – we can notice that between 2004 and 2006 the FDI grew faster than between 2011 and 2013 (in 2006 the value of the FDI has even overpassed the peak in 2000). A possible explanation could be the fact that at the beginning of the XXIst century the global economy grew faster than in the last four years: the global GDP increased 3.5 to more than 4.0% in each year between 2004 and 2006, while from 2011 to 2013 it has grown less than 3% per year (IMF, 2014).

3. Regional and sectorial evolutions of the FDI inflows during the last decades

Regarding the regional evolutions of the FDI inflows, we can notice some interesting aspects both for the developed and developing states. In the case of the developing economies, it results from Figure 4 that, until 1990, the investments inflows in developing states had negligible values in all the three analysed regions – Asia, America and Africa. After this year, they registered a positive trend, with significant values in the developing countries only from America and Asia. In the developing states from Africa there is a slight increase in the inflows between 1990 and 2013, but they rested at very low levels compared with the developing countries from the two other regions. A remarkable evolution can be seen in the case of the FDI attracted by Asia, which augmented more than 70 times between 1985 and 2013. Actually, Asia is the leading region, considering the developing states, in terms of FDI inflows during the period 1990-2013, despite the small decreases registered between 2001 and 2002 and in 2009. In 2011 and 2013 the FDI inflows in these states had the highest values from the entire analysed period: 1985-2013.

Figure 4: The dynamics of FDI inflows in the developing states from Africa, America and Asia

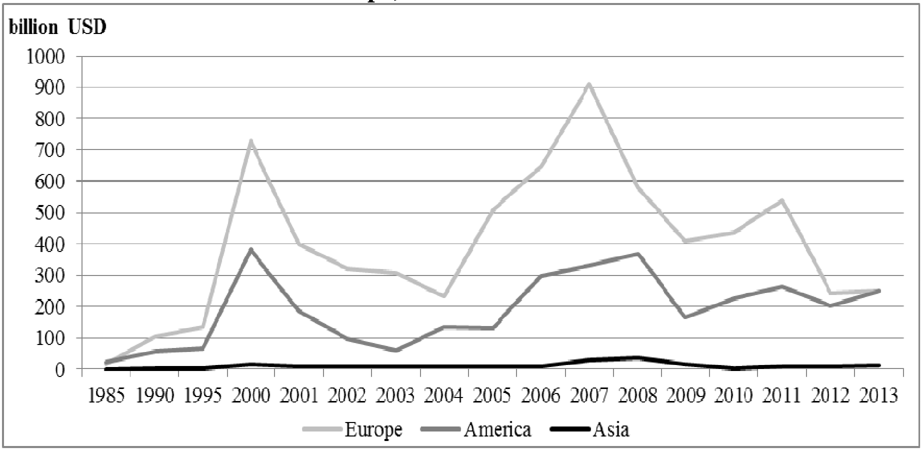


Source: Author's compilation and adaptation from UNCTAD, 2014a, *Foreign direct investment flows, http://unctadstat.unctad.org/wds/TableViewer/tableView.aspx?ReportId=88*

From the point of view of the FDI attracted by the developed states, we can notice from Figure 5 that Europe has been the leading region through the entire period 1985-2013, while Asia registered negligible values. However, we can see that the inflows into the developed states from Europe were more affected by the 2007 crisis than those from America since the value of the FDI attracted in 2013 by the first ones was almost 4 time lower than their value in 2007, while the American developed economies registered a decline of only one third during the same period. Under these circumstances, in 2013, the FDI inflows into the developed states from America have almost reached the value of those attracted by the developed economies from Europe, the difference between them being of only 1 billion USD.

Figure 5 reflects the fact that, during the entire period 1985-2013, the FDI attracted by the developed states from Europe and America had almost the same peaks and declining moments. However, analysing the values, we can argue that while the FDI inflows into developed economies from Europe were more affected by the 2007 crisis than by the 2001 downturn, in the case of those from America it was the reversed situation.

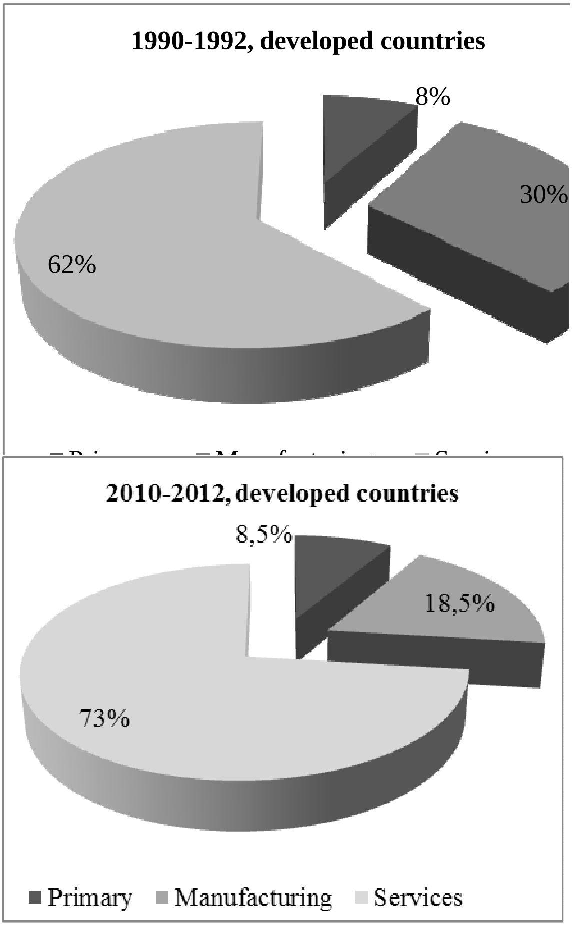
Figure 5: The dynamics of FDI inflows in the developed states from Europe, America and Asia

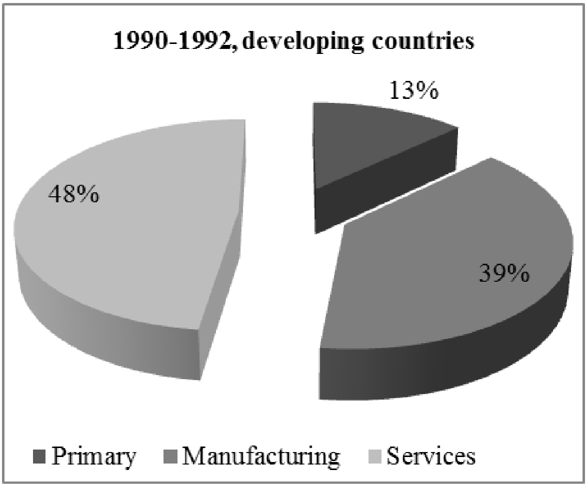


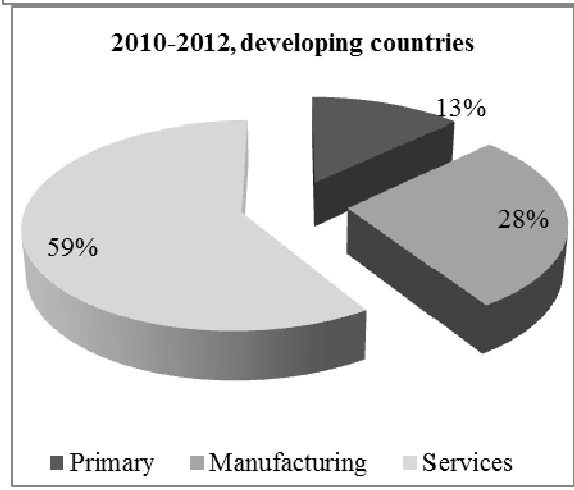
Source: Author's compilation and adaptation from UNCTAD, 2014a, *Foreign direct investment flows, http://unctadstat.unctad.org/wds/TableViewer/tableView.aspx?ReportId=88*

Regarding the distribution of the FDI on the three main activity sectors (primary, manufacturing and services), the differences between the developed and developing states and their evolution during the last two decades can be noticed in Figure 6. In the case of both developed and developing states, the FDI have considerably increased in the tertiary sector (services) during the last two decades, in the detriment of the secondary sector (manufacturing), where these investments have significantly diminished. In the primary sector, the FDI remained almost the same over the period 2010-2012 as in 1990-1992, in both types of countries.

Figure 6: Sectorial distribution of the FDI inflows in the developed and developing states between 1990-1992 and 2010-2012







Source: Author's compilation and adaptation from UNCTAD, 2014d, *World Investment Report 2014: Annex Tables, Annex 26 - Estimated world inward FDI flows, by sector and industry, 1990-1992 and 2010-2012,* http://unctad.org/en/pages/DIAE/World%20Investment%20Report/Annex-Tables.aspx

The growing share of FDI in the tertiary sector in developing countries has several explanations. First of all, the highest increases are registered in the newly industrialized economies, including ASEAN and South

Korea, countries that have created the proper infrastructure for the development of the financial, commercial and telecommunications' services (UNCTAD, 2004). Secondly, this trend can also be noticed in poorer countries due to considerable investments made in infrastructure and utilities. For example, in India and the Philippines there is a FDI increase in the IT sector. In addition to the financial, transport and telecommunications sectors, the FDI in tourism have gained a significant importance especially in the South-East Asian countries (UNCTAD, 2004).

4. Conclusions

Starting with the last decade of the XXth century, the global FDI inflows have registered a notable increase, mainly because of the investments attracted by the developed states. However, after the 2000 peak, a combination of micro, macroeconomic and institutional factors have temporarily interrupted this positive trend. The most affected were the developed states, which faced a substantial decrease in the investments attracted between 2000 and 2003, compared to the developing economies that had a relatively stable level of the FDI inflows during this period. This situation was generated by the fact that the investors continued looking for lower costs during an unfavourable economic and financial period. The next years were marked by a sustained increase of the FDI, both into the developed and developing states, up to 2007, when the global investments' inflows have reached the highest value ever since. In 2008, in the context of the economic and financial crisis, the FDI inflows started to fell, facing the worst collapse in 2009. In the following two years, a partial recovery was achieved, but only temporarily because it was succeeded by a new drop. In 2013, the FDI inflows had a slight increase, but they have still registered a value with 27% lower than in 2007.

As in the case of the 2001 downturn, in the context of the nowadays recession the developed countries were the worst affected. While these states have faced a significant collapse of the investments' inflows since 2008, the developing countries have registered record levels especially after 2009. In 2012 and 2013, the FDI attracted by them have even surpassed those from the developed countries. Two main possible explanations can be found for this situation. The first one is the same as in the case of the 2001 downturn: the economic situation determined the multinational companies look for lower costs – higher profits investments' opportunities. In close relationship with this explanation is the second one, according to which the mergers and acquisitions, particular for the developed economies, faced a higher decrease compared to the “greenfield” investments, usually made in the developing states.

The analysis of the regional evolution of the FDI inflows showed that, from the point of view of the developing states, Asia is the leading region over the period 1990-2013, despite the small decreases of the investments between 2001 and 2002 and in 2009. When considering the developed states, we notice that Europe was the region that attracted the highest value of the FDI through the entire period 1985-2013. However, while the FDI inflows into the developed countries from Europe were more affected by the 2007 crisis than by the 2001 downturn, in the case of the American developed economies it was the reversed situation.

A sectorial analysis of the global FDI reflects the fact that, for both developed and developing states, the FDI have considerably increased in the tertiary sector during the last two decades, in the detriment of the secondary sector, where these investments have significantly diminished.

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