ZESZYT NAUKOWY
Wyższa Szkoła Zarządzania i Bankowości w Krakowie

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FOREIGN DIRECT INVESTMENTS IN SELECTED GROUPS OF COUNTRIES IN 2007 - 2014

Introduction

International capital flows have been considered for years as the development lever of the global economy. The financial crisis of 2008-2012 resulted in an evident decrease in foreign direct investment (FDI). The aim of the article is to analyze the influence of the crisis phenomena on FDI that was directed to selected groups of countries.

The trends in capital flow are presented in terms of the advantages and disadvantages of FDI flows.

Such an approach is related to the positive and negative consequences resulting from FDI flows both for the capital exporters and the host countries.

In order to assess the flows and, particularly, to determine the level of their sensitivity to economic situation, it seems rational to focus on the determinants that shape the investment climate in the FDI target countries. This is of primary importance in the first years of the financial crisis and that significance has been strongly emphasized in the article.

The dynamics of change in relation to particular groups of countries provides a substantial amount of information on the trends in FDI flows. The article presents separately the dynamics in the highly developed economies, where EU countries were distinguished, and in the economies of Asia, Africa and Latin America that are qualified as the developing ones.

Benefits and threats resulting from the FDI expansion

The transfer of capital in the form of FDI is one of the strongest symptoms of international business expansion. Apart from greenfield investments, there are the following forms of FDI:

- setting up branches,

- setting up divisions,
- mergers and acquisitions,
- hostile and friendly takeovers.

Apart from the expansion forms listed above, there are international non-investment flows, mainly[1]:

- licence flows,
- offshoring agreements,
- franchising agreements,
- subcontracting,
- consortia with activity profiles typical for particular regions.

Non-investment flows are not the object of the analysis below. FDI is the effect of the choice between the exports of particular goods and services and a transfer of capital with the aim to start manufacturing operations in a host country. The analysis of the advantages and disadvantages of both alternatives is decisive.

FDI –related benefits include the following aspects[2]:

- lower labor costs, particularly regarding staff remuneration;
- better competitive conditions on the foreign market than on the home market,
- bigger purchasing power of the foreign market;
- insignificant level of currency risk;
- better availability of natural resources and lower costs of raw materials acquisition;
- more efficient logistics and transport infrastructure;
- more favorable tax system;
- less bureaucracy as regards investment procedures;
- more transparent and simpler legal system in the host country in comparison to that in the home country (this factor concerns mainly the liberalization of environmental regulations).

[1] The forms concern mainly the European and North American markets, which is pointed out in: Z. Dworzecki,W. Mierzejewska (Ed.), *Zachowania polskich grup kapitałowych w czasach kryzysu,* Oficyna Wyd. SGH, Warszawa 2015, pp.124-129.

[2] This may also concern less rigorous law, lower penalties for the breach of regulations, especially regarding environmental protection.

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FDI-related threats concern particularly the following issues[3]:

- limitations to profit transfer;
- political risk resulting from an instable situation in this field, which may lead to the nationalization of vital sectors (for example of the mining or transport sector, which happens quite frequently in the global economy);
- undermining the image of incoming companies by potential competitors;
- the necessity to improve the qualifications of the host country staff, which may significantly raise the costs of entering the market.

Determinants and volume of FDI flows in the financial crisis

In the course of the latest great financial crisis of 2008-2012, a sudden and substantial global decrease of FDI could be noted in 2008-2012, while after this period, at the end of 2012 an increasing trend appeared which was continued and gained in momentum in 2013-2015. The estimations show that only as late as in 2015 the total global volume of FDI approached the figures of the best period, i.e. of 2007. The evolution of the volume of FDI is given in table 1. It can be concluded from the figures that after the crisis, the FDI flows rose as late as in 2015. However, one may wonder on the reasons of the drop in 2011-2014. They are reasonably simple to diagnose. Undoubtedly, the political unrest resulted in the decrease of interest in foreign investment. The investors remained cautious as they feared of a further escalation of terrorism and changes in legal systems. However, in time they got used to the situation, which resulted in a sudden rise of capital flow in 2015

Table 1. FDI flows in 2007-2015 (billions of USD)

	Year	Volume (billions of dollars)	Dynamics (previous year = 100)	Dynamics (2007 = 100)
1.	2007	1 872	100.0	100.0
2.	2008	1 490	-20.4	-20.4
3.	2009	1 187	-20.3	-36.6
4.	2010	1 328	11.9	-29.0

[3] See more in J. Rymarczyk (ed.), *Międzynarodowe stosunki gospodarcze,* PWE, Warszawa 2006, p.113 et seq. and J. Rymarczyk (Ed.), *Handel zagraniczny. Organizacja i technika*, PWE, Warszawa 2005, pp. 30-32.

5.	2011	1 565	17.7	-16.4
6.	2012	1 403	-10.4	-25.1
7.	2013	1 467	4.5	-21.6
8.	2014	1 228	16.3	-34.4
9.	2015	1 990	62.0	6.3

For 2015 : projections of UNCTAD and *World Business Report*, Washington – New York 2014, p. 17.

Source: Author's calculations and research based on : *World Investment Report,* United Nations Conference on Trade and Development (UNCTAD), New York 2012, 2014, Tables number 1.1.. – 1.3. *World, Economy, Years.*

On the basis of the presented above benefits and threats several reconsiderations can be made as regards the factors that determine capital flows. Thus, FDI can be analyzed from a different point of view and be divided by other criteria. Traditional determinants of capital flow in the form of FDI are related both to the motives of investors and the investment climate in host countries[4].

The first group includes such market and cost factors as[5]:

market absorption perceived as the size of population multiplied by personal incomes, which gives the volume of the market purchasing power;

- opportunities for a long-term market development (for the increase of its purchasing power);
- the implementation of barriers to capital outflow;
- the access to natural resources;
- the level of production costs;
- the level of labor costs;
- legal system, and particularly financial and tax systems;
- staff qualifications;
- the access to new technologies generated by R&D centers;

[4] Cz. Pilarska, *Bezpośrednie inwestycje zagraniczne w teorii ekonomii,* Zeszyty Naukowe Akademii Ekonomicznej w Krakowie, seria: Monografie, Kraków 2006, p. 11 et seq.

[5] K. Przybylska, *Determinanty bezpośrednich inwestycji zagranicznych w teorii ekonomicznej,* Zeszyty Naukowe Akademii Ekonomicznej w Krakowie, seria: Monografie, No. 144, Kraków 2001, p. 18 et seq.;

See also: D. Wawrzyniak, Determinanty lokalizacji bezpośrednich inwestycji zagranicznych, Gospodarka Narodowa No. 4/2010

- the opportunity to co-operate with local business;
- the level of investment risk and the projected financial position of the company that is involved in the FDI capital flow (based on ROE, ROA and ROI scores) [6].

The investment climate of host countries is created by[7]:

- political and economic stability;
- level of bureaucracy regarding the acceptance of foreign companies, i.e. the conduct standards of the authorities towards foreign investors;
- FDI legal regulations;
- host country's membership in international integration and economic organizations;
- the implementation of tariff and non-tariff barriers for the imports and exports of products and services;
- a system of investment incentives;
- the development of investment infrastructure (transport, telecommunication, IT);
- the development of the bank sector involved in international settlements;
- the operations of local marketing companies and their promotion instruments.

As it can be concluded from the determinants presented above, political factors have been marginalized to a large extent so far and they did not influence significantly the volume of FDI. However, the existence or even the escalation of extremely hostile, often religiously-based behavior suggests a substantial persistence of political trends that have an impact also on the economic issues. Thus, the conclusion is that purely political factors are the basic – or in some extreme cases - the only determinant of the FDI place of location.

Evolution of the volume of FDI inflow to selected groups of countries

Both the global flow volume and the flow volume for particular countries, particularly the groups of countries with a similar level of economic development, are the instruments that

[6] More on the scoring analysis and ROA, ROE, ROI indexes in: Pomykalska, P. Pomykalski, *Analiza finansowa przedsiębiorstwa,* Wydawnictwo Naukowe PWN, Warszawa 2007 and J. Czekaj, Z. Dresler, *Zarządzanie finansami przedsiębiorstw,* PWE, Warszawa 2009, and *Podstawy zarządzania finansami przedsiębiorstw – podstawy teorii*, pdf, Kraków 2013.
[7] J.H. Dunning , *Determinants of Foreign Direct Investment: Globalization-Induced Changes and the Role of Policies*, [in:] B.Tungodden,N. Stern, I. Kolstad (ed.), *Toward Pro-Poor Policies. Aid, Institutions and Globalization*,World Bank, Washington – New York 2004, pp. 23-27.

measure the FDI expansion. The figures concerning the flows help assess the level of investment attractiveness of host countries, while economic activities out of home countries testify to the competitive advantage and the investment power of the countries of origin of capital[8].

Thus, it seems rational to analyze the levels of FDI inflows with reference to selected groups of countries: the developed countries, the developing ones and EU countries[9]. The evolution of FDI inflows in the selected groups is given in table 2.

Table 2. Volume of FDI inflow to particular groups of countries in 2007-2014 (billions of USD)

	2007	**2008**	**2009**	**2010**	**2011**	**2012**	**2013**	**2014**
Developed countries	1 310	1 020	606	618	748	678	697	499
EU countries	854	542	356	318	421	401	325	288
Developing countries	574	650	519	617	684	639	671	681
Asian countries	350	380	315	384	423	401	428	465
African countries	51	58	53	43	44	56	54	54
Latin American countries	172	209	150	187	217	178	186	159
Transition countries	91	121	72	74	92	85	99	48

Source: *World Investment Report*, UNCTAD, New York 2012, 2015, Table 1.1., *Countries.*

The figures in table 2 show that the volume of FDI inflows to the developed countries has been decreasing since the time directly preceding the beginning of the crisis (i.e. since 2007). The flows dropped over 3.5 times in 2014, while in 2011 the volume was only twice as little. Evidently, there is a steady decrease in FDI inflows to that group of countries. The same trend applied to the EU countries. However, there was an opposite trend in the developing countries – the FDI inflows increased in the period under investigation. This trend is particularly visible in the Asian countries, while in Latin America – after a spectacular investment boom (over 217 billion US dollars) - a downward trend appeared as it happened in the whole global economy.

The recent drop is certainly connected with the global political situation – the escalation of terrorism, military conflicts and social unrests. Consequently, questions arise whether the crisis is over or its escalation may occur. The estimates for 2015 in table 1 indicate clearly to an increase of capital flows to approx. 2 billion USD, which testifies against the argument

[8] R. Oczkowska, Międzynarodowa ekspansja przedsiębiorstw w warunkach globalizacji. Motywy – Strategie – Tendencje, Difin, Warszawa 2013, pp.214.
[9] Ibidem, pp.242-243.

about the continuation of the financial crisis. However, social and political unrests and the demanding attitude of several less developed countries may affect negatively the FDI inflows.

Several crucial conclusions can be drawn from the analysis of the dynamics of the percentage changes in the FDI capital inflows in the period under investigation. See tables 3 and 4.

Table 3. Change dynamics of FDI inflow by groups of countries in 2007 – 2014 (previous year = 100%)

	2007	2008	2009	2010	2011	2012	2013	2014
Developed countries	100.0	-22.1	-53.7	-52.8	-42.9	-48.2	-46.8	-61.9
EU countries	100.0	-36.5	-58.3	-62.8	-50.7	-53.0	-61.9	-66.3
Developing countries, including	100.0	13.7	-20.2	18.9	10.9	-6.6	5.0	1.5
Asian countries	100.0	8.6	-17.1	21.9	10.2	-5.2	6.7	8.7
African countries	100.0	13.7	-8.6	-18.9	2.3	27.3	-3.6	0.0
Latin American countries	100.0	21.5	-28.2	24.7	16.0	17.9	4.5	-14.5

Source: Author's calculations and research based on: *World Investment Report,* United Nations Conference on Trade and Development (UNCTAD), New York 2012, 2015, Tables number 1.1.. – 1.3. *World, Economy, Years, Countries.*

The change dynamics of the FDI inflow is given in table 3 which also includes calculations based on the figures from table 2. The data concerning the dynamics confirm the argument about a fairly wide range of fluctuation in the case of all countries under investigation starting from 2009 when the effects of the crisis were the deepest and most dramatic, while in 2011 there was an upward trend in FDI inflows which did not last and in the subsequent two years the trend fluctuated again. This fact confirms the argument about the reaction of investors to political and social events. More optimistic projections of the volume of FDI inflows result in the increase of benefits for host countries and the probability that the upward trend will remain is high, which is presented in table 4.

Table 4. Percentage change of FDI inflow by groups of countries in 2007 – 2014 (2007 = 100%)

	2007	2008	2009	2010	2011	2012	2013	2014
Developed countries	100.0	-22.1	-53.7	-52.8	-42.8	-48.2	-46.8	-61.9
EU countries	100.0	-36.5	-58.3	-62.8	-50.7	-53.0	-61.9	-66.3
Developing	100.0	13.2	-9.6	7.5	19.2	11.3	16.9	18.6

countries, including								
Asian countries	100.0	8.6	10.0	9.7	20.9	14.6	22.3	32.0
African countries	100.0	13.7	3.9	-15.7	-13.7	9.8	5.9	5.9
Latin American countries	100.0	21.5	-12.8	8.7	26.2	3.5	8.1	-7.6

Source: Author's calculations and research based on: *World Investment Report*, United Nations Conference on Trade and Development (UNCTAD), New York 2012, 2015, Tables number 1.1.. – 1.3. *World, Economy, Years, Countries.*

The figures in table 4 indicate to a constant downward trend of FDI with reference to 2007, although the pace of the drop shows some improvement in 2011-2013.However, there was a significant trough in 2014 (a drop by almost 62% in comparison to 2007). A reverse trend, i.e. an upward one, is remained as regards the developing countries in Asia (a rise by 18.6% in relation to 2007, with a downward fluctuation in 2009), which have a growth by nearly 33% in the period under investigation and do not experience a decrease in any of the years of that period. However, in Latin America there was a decrease in the period under investigation (by 7.6% in relation to 2007) although till 2013 there was an increase in FDI with a variable pace and a peak in 2011 (+26%). The amplitude of fluctuations was the greatest in the African countries and it is obvious here that the political and social unrest influenced the attitude of foreign investors and the resulting investment climate.

Conclusion

Undoubtedly, FDI – despite several negative features or even hazards – is a chance for the economic development especially of countries that are not fully developed. Investors from better developed economies consider FDI a substantial source of profit.

The article presents a constant trend of an increase of the FDI inflow to the developing countries and of its decrease as regards the developed countries. However, a stable economic, financial, political and social situation in the world is the condition for a substantial and effective capital flow.

The presentation of the dynamics of the FDI inflow to particular countries makes it possible to draw conclusions as regards the reaction of particular groups of countries to the changing economic and political conditions.

Obviously, the developing countries benefited from the financial crisis, particularly the countries in Asia, where the inflow of FDI was especially visible (the FDI inflow rose by almost 1/3 in comparison to the FDI from the period before the crisis).

It is difficult to determine whether this is a long-term trend as every political and economic destabilization may affect international capital flow in a way that is difficult to predict.

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[13.] *World Investment Report*, UNCTAD, New York 2012, 2015, Table 1.1., *Countries*

[14.] *World Investment Report*, United Nations Conference on Trade and Development (UNCTAD), New York 2012, 2015, Tables number 1.1.. – 1.3. *World*, *Economy*, *Years, Countries*

Abstract

International capital flows have been considered for years as the development lever of the global economy. The financial crisis of 2008-2012 resulted in an evident decrease in foreign direct investment (FDI). The aim of the article is to analyze the influence of the crisis phenomena on FDI that was directed to selected groups of countries.