Foreign investments and economic growth

- Summary –

Foreign investment flows have become fundamental key drivers of economic growth in the worldwide economy, having an important contribution in gaps decrease among countries. PhD thesis brings under review and debate a topic of great current, controversial and of great importance in the economy. The impact of foreign investments, direct and portfolio, although has been intensively studied and discussed in the theoretical literature, the results obtained are still contradictory. Current work invites the reader to discover the complexity of economic phenomena (globalization, recession, crisis, investments) and transformations that the world economy and foreign investment flows have also suffered economic conditions.

The importance and actuality of research theme is derived, first of all, from the existence of a large volume of papers on this theme, coming from the desire to capture and grind economic fundamentals on foreign investment and economic growth. Although in recent years, both FDI and portfolio investment have had a strong volatile character, we consider that the analysis of the correlations between foreign investments and economic growth rate is a very interesting topic. These capital flows have the potential to boost economic growth in the beneficiary country and to encourage them during the recovery process. Intern and international macroeconomic conditions have significantly influenced the dynamic of foreign investments, generating destabilizing effects and jeopardizing their externalities.

The first chapter, "Theoretical on globalization and economic growth" was meant to be the starting point to provide the theoretical foundations on globalization and its spillovers to the economy. In this respect, highlighting the implications of globalization on growth, with its two forms - economic and financial, allows shaping channels through which this phenomenon drives the development of economies and inhibitory factors on favorable externalities.

Rows of this chapter highlight the controversial nature of globalization, uncertainty around this concept, due to the multitude of definitions of literature which highlight certain features of globalization, such as: boosting the dynamism of the global economy, increased flows mobility and increasing international interdependence of economies. From a conceptual perspective, we find ourselves on a path of uncertainty, due to the large definition given to the term, and the existence of various terms used interchangeably (globalization - mondialization;

globalization - global markets, multinational - transnational company). In our view, globalization is not a trend imposed by multinational companies in their expansion, but rather a complex phenomenon whose repercussions are interconnected in all spheres of economic and social activity.

Our approach has allowed the identification of fundamental channels through which it drives economic growth: international trade, the expansion of multinational companies and financial markets. Increased mobility of commercial flows boosts the company’s access on external markets, production and sales, stimulating the progresses in technology, telecommunications and transport networks.

The contraction of international production activity has generated the restrained of the operations carried out by the multinational corporations, as a consequence of tightening of procuring financial resources workflow. International instability on the market has determined financial resources withdrawal of capital markets. The recovery of international trade delays due to several inhibitory factors, such as: volume decrease of international commercial activities due to the absence of progress in multilateral trade negotiations of the past decade, decreasing the chances of generating new trade flows in the world economy and because of a high level of financial instability, vulnerability and fragility markets and the existence of political risks by the emergence of conflict between Russia and Ukraine.

Amplification interdependencies between national financial markets under the seal of globalization should stimulate the development of domestic markets and enhance their international visibility. The phenomenon of deregulation, consisting in the provision of laws and mitigation in order to stimulate expansion of freedom, was seen as abolition and elimination of any kind of control over the capital.

Thus, since 2008 the world economy is facing volatile, unstable, financial markets causing reactions among investors and contradictory behaviors (evolved into a relatively low in risk appetite, uncertainty, panic, even aversion risk, uncertainty). Also, mutations occurred at the level of investment options, investors abandoning risky investments in favor of safe (bonds and other government securities), financial markets’ credibility as an intermediary financing is strongly affected by international imbalances.

In the second chapter, "The globalization of international investment and their role in stimulating economic growth" we aimed at outlining the theoretical framework for foreign investment, emphasizing both fundamental factors that influence the attractiveness of countries. The theoretical basis for shaping the foreign investment necessary to address the issues we addressed conceptual aspects on investment flows, highlighting similarities or differences and complementarities between FDI and portfolio investments. Briefly, we discussed theoretical problems justifying the existence of FDI in the main typologies (in search of resources, markets, efficiency or strategic assets) and portfolio investment. Research on the determinants of FDI and portfolio investment decision reveals that placement of capital in the economy is directly influenced by the specific host country, domestic economic factors (absorption capacity of capital, macroeconomic stability, domestic economic risks, the development of capital markets). Determinants of the two categories highlight the importance of economic issues (size of the internal market, opening, etc.), along with political and social cultural difference that is oriented portfolio investor in relation to the high rate of interest. Host country's characteristics and the features of domestic capital markets influence and lead to changes in investors' decision placement of capital, investors frequently by focusing stable economies with a sustainable business environment to enable them conduct their business projects and expansion.

Principal Component Analysis on fundamental factors influencing FDI was implemented in the economies of Central and Eastern Europe, over two distinct periods: 2000 – 2007 and 2008 – 2013. The research has revealed that, during 2000 – 2007, in most of the selected economies, foreign investors are encouraged to get in these regions due to investment incentives and their future growth prospects. The development of domestic infrastructure stimulates the entry of a growing volume of foreign capital and development of investment projects in domestic markets. Using advanced equipment purchased from abroad involves organizing training courses and training sessions that encourage the formation of gross human capital. By contrast, in the period 2008 - 2013, the growth in FDI flows in selected economies is strongly influenced by macroeconomic stability (proxy variable inflation rate).

In the case of portfolio investment, the development of the national capital market and interest rate behave as fundamental factors of attractiveness of these flows. Thus, we see that in the period 2000 - 2007, portfolio capital flows are not influenced by selected variables, indicators measuring the development of the capital market and degree of development and stability of internal environment having no impact. By contrast, in the second period selected, we note that there is a positive link, not tight, between inflows of portfolio capital flows and asset value traded on capital markets and loans contracted.

In theory, the link between foreign direct investment and economic growth highlights the presence of channels through which they can foster the development (financial markets, world trade and technology transfer). By contrast, existence of correlations between the financial sector and the real economy, highlight the role of the market capital in boosting economic growth through investment portfolio.

Capital market holds great potential for stimulating economic growth through its involvement in ensuring the effectiveness, competitiveness and solvency of the financial sector to mobilize economic resources surplus (savings), while facilitating their placement and their efficient allocation. In our view, portfolio inflows can boost economic growth by close connections with the capital market. An important role was played by phenomenon of liberalization of capital movements in the context of globalization, market deregulation and elimination of any controls on capital. The high volatility of portfolio investments, the high sensitivity of these capitals to changes in factors that influence them, favors sudden outflows of capital in the economy.

The third chapter, "The dynamics of FDI in the context of globalization and their implications for economic growth", presents an analysis of the dynamics of global FDI, and in the regions, emphasizing the fundamental factors that have had a major impact on developments on foreign capital flows. In this respect, using tables and graphs, we developed reasoning and analyzed the evolution of foreign flows, highlighting also the main influence factors. The analysis carried out in this paper emphasizes a mix of quantitative and qualitative elements.

Global FDI flows have been recording oscillatory dynamics and sometimes, contradictory evolution. The dynamics of foreign capital has frequently been directly influenced by the effectiveness of macroeconomic policies promoted by respective economies, their stability. FDI dynamics analysis reveals an increased interest of investors to emerging economies since 2001, foreign capital inflows are driven by rapid economic growth of these countries in terms of low labor costs and higher qualification thereof.

FDI upward trend continued until the year 2006 - 2007, supported by the enthusiasm and exuberance of foreign investors, the high volume of cross-border mergers and acquisitions. International financial crisis has triggered a strong sense of fragility, vulnerability and volatility, disturbing investors’ confidence in the markets. The difficulties faced by multinational companies in accessing international financial resources, due to constraints in financing through loans, narrowed the range of financing opportunities of multinationals, causing restriction of activities and hence the sharp decline in corporate profits (many investment plans were canceled). Overall macroeconomic instability was felt in a severe contraction of the growth rate of GDP in some economies becoming even negative. Developing economies have been affected by the global turmoil, however, various groups of countries were found to be resistant to shocks and imbalances.

FDI inflows registered a worldwide and regional contraction, due to the dynamic of global economy, characterized by: economic downturn, collapsing stock markets, reducing corporate profitability, completion of privatization, reduced demand on the markets, the increase in funding resources. GDP growth rate by economic region highlights the sinuous evolution of growth in these economies, culminating with strong contractions in real GDP. The presence of regional political and conflict on a global scale associated with a decreased presence of investors in financial markets in these economies (low confidence and high aversion to risk) are fundamental factors that explain the evolution of economic growth since 2010, which creates difficulties for authorities in re-launching in the coming years.

The institutional and legislative reforms, along with the progress of these economies to join the European Union, the economies of Eastern Europe turned in fundamental destinations for FDI. We also appreciate that the volume of FDI inflows in these economies will recover in time as the emergence of political conflict between Russia and Ukraine will negatively influence investors’ confidence in the stability of the region.

Granger Causality Analysis results confirm the existence of a direct unidirectional connections from FDI to GDP (Bulgaria and Romania), while in Poland and the Czech bond is reversed. Expansion of capital and foreign investors' activity has positively contributed to the development of exports and may exert a positive impact on economic development. Granger Causality Analysis emphasizes the challenges and the risks in the global economy during the crisis, such as: macroeconomic instability, vulnerability and turbulence in the market economy generating economic contraction, recession and collapsing business plans.

Flows of foreign capital inflows contribute towards the development of domestic infrastructure, encouraging international growth. Thus, we believe that between FDI and GDP there is an indirect link through the degree of infrastructure development. A high level of infrastructure development stimulates penetration of increased volume of foreign capital, thus creating the conditions recording a higher rate of economic growth.

About Romania, our focus has been channeled to identify factors that stimulate or inhibit the attractiveness of our economy. One key objective of the PhD thesis was represented by the systematic presentation of the main legal regulations in our country and their provisions. The volume of FDI in Romania was strongly driven by tax incentives and facilities regulated by law, enjoyed by foreign investors.

Trends of FDI in Romania has registered an upward trend amid phenomenon of privatization of state companies, it is also encouraged by several factors: changes in regulation of the business environment and investment climate by establishing a special institution to promote FDI, job placement and adoption bankruptcy law and the accelerating pace of economic growth. Strong upward trend of FDI inflows in Romania was disrupted by the outbreak of the global crisis, followed by a sharp decline in capital inflows. Immediate effects of global turmoil have generated a significant decrease of the financial resources available for multinational companies and the worsening the economic condition of investors' home country, but also lower interest multinational companies to invest in emerging economies.

FDI distribution by region reveals their orientation especially in regions that facilitate access to western markets (existence airports) or in regions with high level of development of facilities and services, ensuring in the same time, higher labor productivity.

After a dynamic analysis of FDI in Romania, using the VAR model - Vector Auto regressive we estimated econometric the regression equation of this model, to establish linkages between FDI and economic growth and the implications of selected variables (government stability and external conflict) on the independent variable. Growth performance is directly caused by foreign capital inflows, while the economy is stable. The fragility of the state (government and political stability) significantly disrupts economic growth, causing its contraction. The existence of external conflict increases investors' distrust in the stability of the business environment of the region's economies and jeopardize their attractiveness for foreign capital.

The fourth chapter of the thesis is entitled "Features and portfolio investment implications on economic growth" presents research on the trend and changes in portfolio investment in advanced economies and emerging ones. International economic volatility and turmoil in the markets have had an impact on developments in portfolio investments, which have suffered strong contractions in most economies. As portfolio investment implications on economic growth of recipient economies are reflected by the level of capital market development, we considered necessary to analyze the factors stimulating foreign investments in relation to the development of the internal market. Advanced economies have maintained a long period of institutional investors' favorite destinations. Portfolio flows exuberance ended with the outbreak of the global crisis in 2008, following which, international markets have experienced sharp imbalances, liquidity difficulties, as well as a restriction of activities and plans for expansion of the activities of investors.

Also, portfolio investment growth in advanced economies reflects risk aversion of institutional investors who often resorted to disinvestments (portfolio investment outflows from the economy), increase and strengthen the institutional fragility and the vulnerability of these countries.

The phenomenon of globalization and liberalization of capital movements stimulated a growing volume of portfolio investment and access to investors in other economies. Investors have the opportunity to place their capital in various financial assets with high yields, leading to considerable significant profits. Contraction of these capitals during crisis occurred in both developed economies and emerging economies, it is determined by a combination of factors: the presence and increasing the role of contagion, that favored transmission turmoil on the international stage, risk diversification and expansion they expose investors as well as investors' distrust in skills relevant institutions to manage and remedy the situation.

Consequently, international capital flows are facing a high volatility, reflecting often sudden capital outflows markets. The absence of strict control and supervision over the financial market, the lack of regulations that limit investors' exposure to volatile foreign capital contributed to intensified market contagion and vulnerability.

Among the countries of Central and Eastern Europe, capital market in Poland is characterized by a higher level of development compared with other markets that have smaller economies and exhibit a high degree of dependence on international capital volatility. In terms of market capitalization, the results indicate progress toward higher the development of capital markets, which usually is due to the process of European integration. The capital markets of

Central and Eastern European economies are in a continuous process of development and expansion. Major difficulties faced by the euro area during the crisis, the financial problems that Greece is dealing with, have led to strong disruptions in the markets in Central and Eastern Europe. Tightening of bank lending in these economies jeopardizes investors' opportunities or ongoing expansion of investment projects.

Granger Causality Analysis confirms the high level of development of capital markets in the USA and Austria; portfolio investment inflows of capital in these markets have the capacity and potential to boost national economic growth, leading to a growing volume of transactions. In selected advanced economies in terms of domestic macroeconomic stability (proxy, the inflation rate), capital inflows into the economy will spur higher volume transactions and market capitalization, and the exuberance of the capital market is reflected in rate higher economic growth. The degree of trade openness positively influences the entrance of the domestic capital market investors, enhancing the attractiveness of the capital market and creating the prospects recording a high level of development. The performance of growth is directly influenced by the markets' capitalization in Romania, Bulgaria and Hungary, transaction volume and the level of trade opening. Amplification interdependencies between markets high mobility stimulates trade flows, involving development and business expansion, encouraging investors to the capital market orientation to acquire necessary financial resources. Analysis implemented allows us to say that the stock market has the capacity to boost economic growth. Regarding Eastern Europe economies, the results indicated that higher performance on economic growth may be purchased through the capital market, through an amplified volume traded assets, market capitalization growth and a higher rate of economic growth.

At the same time, we believe that the domestic capital market has some deficiencies, meanwhile others, prevent the penetration of investors: listing and trading process is complex, requires many steps, that are not accepted as official documents in English language is a disadvantage of the domestic capital market which prevents the access of investors, poor technology, legal and regulatory framework precarious investors to make access difficult, and internal systems and procedures fees cumbersome and time consuming. Besides the above factors, in our opinion, the ineffectiveness of the domestic business environment, economic contraction, and underutilization of the authorities to financial resources as loans or structural funds from financial institutions - international banking system amid corruption inhibits the penetration of growing volume of foreign capital and disrupts the development of the capital market.

In conclusion, the regional markets are following modern capital markets' foundation, viable, which offers investors various development opportunities, encouraging their penetration. Adjusting and adapting the transaction (modernization through innovation) and institutional ensuring their stability in the face of future crises, are ways through which destabilizing events such crises can be prevented.