THE EXPANSION OF FDI FLOWS – A MAJOR FACTOR OF GLOBALIZATION

CLAUDIA ISAC, CODRUȚA DURA, FLORIN CRISTIAN CIURLĂU *

ABSTRACT: Globalization is the process whereby geographical distance becomes a less important factor in establishing and developing cross-border economic, political and socio-cultural relations; therefore production networks and Foreign Direct Investment (FDI) flows represent the main factors that play a key role in the process of getting international and worldwide spreading. Globalization phenomenon involves a process of deepening and widening of interdependence relations between different economic entities and spheres and takes into account international trade relations, the cross-border movement of international production factors, but mostly the expansion of FDI flows, having significant positive effects on the welfare of nations or geographical areas. The impact of the global economic crisis on FDI flows is a heterogeneous one, as the effects of the depression came to light in many different ways, depending on the level of development, the geographical area or the economic field.

The overall fall in global FDI flows during the crisis was accompanied by a significant shift in the traditional pattern of FDI: emerging countries well-endowed with natural resources were becoming a growing source of FDI for developed countries, due to internationalization strategies carried out by their multinational companies (MNCs). Based on recent forecasts, UNCTAD specialists estimate that global FDI will recover to its pre-crisis level in 2011, rising to $1.4-1.6 trillion, approaching its 2007 peak in 2013. However, the business environment remains volatile and MNCs are cautious rather than optimistic regarding their investment plans.

KEY WORDS: globalization; Foreign Direct Investments (FDI); multinational companies (MNCs); FDI flows; the global economic crisis; developed countries; emerging economies; developing and transition countries.

JEL CLASSIFICATION: F21; F23.

* Assoc. Prof., Ph.D., University of Petrosani, Romania, isacclaudia@gmail.com
Assoc. Prof., Ph.D., University of Petrosani, Romania, codrutaradura@yahoo.com
Lecturer, Ph.D., „Dimitrie Cantemir” Christian University, Bucharest, Romania
1. INTRODUCTION

Recent developments in the world economy lie under the sign of globalization, of interdependence between the economic actors and the national states, of multiple interactions. Practically, any economic activity carried out anywhere on the planet will have, sooner or later, certain effects on the world economy as a whole or on some levels of economy.

The phenomenon of globalization has a number of determinants:
- **economically** materialized through trade liberalization, through creating global production networks, free movement of capital;
- **technologically** through the export of technologies, intensification of research and development, the emergence of the information society;
- **socially** through the migration of population and labor force, the improvement of education or health systems, the substantiation of equitable wage policies etc.;
- **from cultural point of view** through the crystallization of cultural values based on the ideas of freedom, equity, equilibrium, tolerance, acceptance;
- **politically** through the processes of the multilateral global cooperation and the harmonization of the interests of States with those of multinational corporations (MNCs), regional or international institutions called to watch over global stability and security etc.

It is a paradox that as it becomes a more obvious and more widely accepted real contemporary issue, globalization is still a controversial concept in economic literature and international politics.

2. DISCUSSIONS REGARDING THE CONCEPT OF GLOBALIZATION WITHIN THE LITERATURE

According to Friedman, one of the most fervent supporters of the thesis of globalization, "globalization is not a simple trend or a fantasy; it is rather an international system. It is the system which now took the place of the Cold War system and, by the way, globalization, has its own laws and logic, it is capable of influencing nowadays, directly or indirectly the environment policy, the geopolitics and the economy of each country in the world". (Friedman, 2000).

In the narrow sense, globalization means a process of expansion of transactions between firms and people across national borders and a process of emphasizing interdependencies among "global entities" which could take the form of private enterprises, public institutions or Governments.

Within Romanian literature, one of the well-known definitions of the globalization concept is given by I. Popescu, A. Bondrea and M. Constantinescu who claim that "globalization is the process whereby geographical distance becomes a less important factor in establishing and developing cross-border economic, political and socio-cultural relations; thus relation networks and interdependencies represent the
main factor that has an absolute potential of getting international and worldwide spreading". (Popescu, et all., 2004).

Liviu Voinea, in his prestigious book "Transnational Corporate Entities and the Global Capitalism" published by Polirom in 2007, draws a synopsis of the concepts of globalization produced by specialized literature; it begins with understanding Glyn’s and Sutcliffe’s concept according to which globalization is “an extension of production capitalist relations”, continuing with Berhman who considers that "globalization is a new world order that transcends the traditional models of capitalism" and ending with the criticism of globalization which draws the attention to its contribution in bringing about the economic crisis in Southeast Asia (1997-1998), Mexico (1994) and Argentina (2001), and to the trend of proliferation of protectionist policies in the United States and the European Union, in the very context of ample theoretical debates regarding the liberalization of world trade (Rodrik, 2002).

The extent of changes which accompany the process of globalization and its overwhelming spreading rate, produced in their turn, a new series of debates about the relation between globalization and the national States. Held and McGrew (2003) have systematized the opinions expressed in the specialized literature into three distinct "sides" (Voinea, 2007):

- The skeptics, who believe that the present circumstances of globalization are not new, and the world economy was at least as marked by the phenomenon of globalization during the Roman Empire or before World War II as it is now. Therefore, the experts in this category do not consider that the national States are threatened today by the danger of disappearance, but on the contrary, their role becomes more important as international relations are amplified;

- Transformers, saying that the phenomenon of globalization is accompanied by new economic, social, political, cultural and technological circumstances, leading inevitably to a transformation of the role of States in the world economy, based on the reconsideration of the coordinates of the environment in which they operate;

- Hyper-globalists who are partisans of a free global market, created against weakening the influences of nation States upon economic activities carried out in a given space.

By entering into the hyper-globalist trend, Robert Reich appreciated that "…we live deep transformations that will rearrange the politics and the economy of the next century. There will no longer be national economies, when this process is completed. All that remains within the borders are the people who represent the Nations ...". According to the same author, the standard of living of the people will depend in the end on the performance of large multinational companies and not on the success of each nation. (Reich, 1996).

This is why the object of the current paper is not the formulation of a universal definition for the concept of globalization nor is the development of macroeconomic policy directions that lead to the activation of this process; the interest of authors is directed instead towards understanding the mechanisms of globalization rapid spreading by the instrumentality of foreign direct investments (FDI).
3. THE DYNAMICS OF FDI FLOWS DURING THE CRISIS

Extremely complex, the phenomenon of globalization involves the process of strengthening and broadening relations of interdependence between different economic sectors and actors and it takes into consideration three important variables, namely international trade, international movement of production factors and last but not least foreign investment flows (Dumitrescu & Bal, 2002). Thus, foreign investments should be viewed not only as a flow of capital between the two entities; they must be analyzed depending on the method of investment which is chosen.

Therefore, the literature shows a number of pros and cons to choosing a certain method of foreign-investment - external credit, joint venture or foreign investment – concluding that the external credit is preferable if the initial investment leveraging is independent in terms of functionality from the host state; the joint venture is implemented when it contributes to the development of a public-private investment project, the association between a pre-existing entity, owned by the host State and the foreign investor; the foreign investment which develops in the form of portfolio international investments through the acquisition on the financial market of securities in the form of shares or bonds and foreign direct investments that allow the investor to purchase the control share package of a firm or to set up new companies.

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Therefore, the literature shows a number of pros and cons to choosing a certain method of foreign-investment - external credit, joint venture or foreign investment – concluding that:

- the external credit is preferable if the initial investment leveraging is independent in terms of functionality from the host state;
- the joint venture is implemented when it contributes to the development of a public-private investment project, the association between a pre-existing entity, owned by the host State and the foreign investor;
- the foreign investment which develops in the form of portfolio international investments through the acquisition on the financial market of securities in the form of shares or bonds and foreign direct investments that allow the investor to purchase the control share package of a firm or to set up new companies (Dumitrescu & Bal, 2002).

In this context, the economic importance of FDI starts from defining them as a long-term relationship reflecting a lasting interest and control of an entity resident in one economy (natural or legal person) upon an economic unit resident in another economy (Voinea, 2007). The expansion of foreign direct investments as a planetary-
scale phenomenon is linked to the important impact on the prosperity of a State or region. The most direct effect of this kind of investment is the economic growth and the creation of new jobs, the increase of production capacity, increase of tax levies specific to the development of economic activities and the stimulation of investments, foreign direct investments contributing to an infusion of technological innovations in the field, the adoption of modern industrial practices and the implementation of managerial strategies which result in an increase in the competitiveness of the sector.

Global economic growth has led to an increase in foreign direct investments in the period 2003-2007; the peak level was attained in 2007 when it reached a level of $2063.4 billion according to UNCTAD statistics. Despite the most acute crisis of the post-war period that broke out in 2007, the increase in the volume of foreign direct investments in the first half of 2007 by 30% as compared to the year 2006 due to, in particular, the growth of reinvested profits and acquisitions and cross-border mergers, attenuates the decline of investments during the second half of the same year.

In 2008, the international financial crisis affected the growth cycle of international investments so that this year there was a sharp reduction by nearly 10% in the volume of investments. In fact, the impact of the international financial crisis upon the flows of FDI is heterogeneous, the strongest feature being that the effects of the crisis have acted differently, depending on the level of development, on the region and sector of activity (table 1 and table 2).

Table 1. FDI flows in 2007-2008

<table>
<thead>
<tr>
<th>Country/Region</th>
<th>FDI flows</th>
<th></th>
<th>Growth (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2007</td>
<td>2008</td>
<td></td>
</tr>
<tr>
<td>Global</td>
<td>2063.4</td>
<td>1868.9</td>
<td>-9.4</td>
</tr>
<tr>
<td>Europe</td>
<td>1270.7</td>
<td>990.3</td>
<td>-22.1</td>
</tr>
<tr>
<td>United States</td>
<td>313.8</td>
<td>298.6</td>
<td>-4.8</td>
</tr>
<tr>
<td>Japan</td>
<td>73.5</td>
<td>127.4</td>
<td>73.2</td>
</tr>
<tr>
<td>Latin America</td>
<td>52.1</td>
<td>36.1</td>
<td>-30.7</td>
</tr>
<tr>
<td>Africa</td>
<td>5.3</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Asia and Oceania</td>
<td>5.3</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>West Asia</td>
<td>44.8</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>East Asia, Southeast Asia and South Asia</td>
<td>166.5</td>
<td>185.2</td>
<td>11.2</td>
</tr>
</tbody>
</table>

Thus, as a result of the problems financial institutions were faced with, of the liquidity crisis or the reduction in the number of international mergers and acquisitions, foreign direct investment flows have decreased by approximately 33% in most of the developed countries. FDI flows attracted in 2008 registered low levels particularly in Finland, Hungary and Italy but also in the United Kingdom, France and the United States as compared with the levels achieved in the year 2007. As regards the group of developing countries, the rate of increase of FDI in 2007 was by 4% lower than in 2007 when the rate of growth exceeded 20%.
Table 2. FDI flow by sector/industry, 2007-2009

<table>
<thead>
<tr>
<th>Sector/Industry</th>
<th>Value ($ billion)</th>
<th>Number of cases</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2007</td>
<td>2008</td>
</tr>
<tr>
<td>Primary</td>
<td>74</td>
<td>90</td>
</tr>
<tr>
<td>Agriculture, hunting, forestry and fishing</td>
<td>2</td>
<td>3</td>
</tr>
<tr>
<td>Mining, quarrying and petroleum</td>
<td>72</td>
<td>87</td>
</tr>
<tr>
<td>Manufacturing</td>
<td>337</td>
<td>326</td>
</tr>
<tr>
<td>Food, beverages and tobacco</td>
<td>50</td>
<td>132</td>
</tr>
<tr>
<td>Chemicals and chemical products</td>
<td>117</td>
<td>74</td>
</tr>
<tr>
<td>Non-metallic mineral products</td>
<td>38</td>
<td>29</td>
</tr>
<tr>
<td>Metal and metal products</td>
<td>70</td>
<td>14</td>
</tr>
<tr>
<td>Machinery and equipment</td>
<td>20</td>
<td>15</td>
</tr>
<tr>
<td>Electrical and electronical equipment</td>
<td>24</td>
<td>14</td>
</tr>
<tr>
<td>Motor vehicles and other transport equipment</td>
<td>3</td>
<td>12</td>
</tr>
<tr>
<td>Services</td>
<td>612</td>
<td>290</td>
</tr>
<tr>
<td>Electricity, gas and water</td>
<td>103</td>
<td>49</td>
</tr>
<tr>
<td>Construction</td>
<td>15</td>
<td>2</td>
</tr>
<tr>
<td>Trade</td>
<td>41</td>
<td>17</td>
</tr>
<tr>
<td>Transport, storage and communications</td>
<td>66</td>
<td>34</td>
</tr>
<tr>
<td>Finance</td>
<td>249</td>
<td>74</td>
</tr>
<tr>
<td>Business services</td>
<td>102</td>
<td>101</td>
</tr>
<tr>
<td>Total</td>
<td>1023</td>
<td>707</td>
</tr>
</tbody>
</table>

Source: UNCTAD, World Investment Report, Global Trend in FDI, 2010, Chapter I

Unlike other regions of the world, investment flows to the developing countries of Asia continued to increase so that for the Group of countries in East Asia, Southeast Asia and South Asia the growth from 2007 to 2008 is of 11.2%, while for the rest of countries in Asia, including Oceania the increase by $ 28.2 trillion represents 13.4%. By including Japan in the Asian assembly, with the largest increase in investment flows for a period of two consecutive years, i.e. 73.2% we can conclude that this region represents a pole of economic concentration.

A structural analysis of investment flows for countries in the Asian region is interesting and it shows a heterogeneous evolution of foreign investments relocation from China which in the past two years registered increases in the cost of labour and thereby production costs to countries such as Vietnam and Bangladesh with cheap labor or India and Taiwan which have earned the reputation of countries with qualified manpower in IT - figure 1.
The Expansion of FDI Flows – A Major Factor of Globalization

Inonesia 9%
Malaysia 14%
Philippines 5%
Thailand 17%
Singapore 45%
Vietnam 8%
Other ASEAN 2%

Source: World Bank

Figure 1. Cumulative FDI inflows in ASEAN 1990-2009, distribution by country (share of total inflows to all ASEAN member states)

This trend is maintained in 2010-2011, even though the volume of FDI in East Asia, Southeast Asia and South Asia increased by 24%. The three sub-regions have recorded very different flows so that if inflows to ASEAN States have doubled, those towards East Asia increased by more than 15% while flows towards the Southeast Asia fell by almost 20%.

Unlike the Asian states, in other regions of the world investment flows recorded negative values in 2008 as compared to the year 2007, such as in Latin America, where the sharp decline is from $ 52.1 billion to $ 36.1 billion, namely more than 30%; Europe registers a decrease of 22.1% and the United States a decrease of $ 15.2 billion.

A retrospective analysis of FDI in the world from sectorial point of view during the crisis, allows us to highlight the following features:

- the most affected segments were those based on services that have had an average decrease of $ 243 bil./year, which has also affected the total volume of foreign direct investments, which fell by $ 773 bil. Services held at the beginning of the crisis 59.82% of the total FDI, while in 2009 their share fell to 50.4% in favor of the primary sector that had a lower rate of decrease in comparison with other sectors - the share of FDI in this sector from the total of FDI increases from 7.23% in 2007 to 19.2% in 2009;

- the declining trend in the service sector continues for all the 6 segments, the most affected being the financial services with a drastic reduction from $ 249 bil. to $ 10 bil., an atypical development being registered in constructions where, after a sharp decline from $ 13 bil. in 2007 to $ 2 bil.
in 2007 it returns to a volume of investments of $ 10 bil., that is to say a drop of 23% from the crisis break-out;

- the trend in manufacturing industry is down for 5 of the 7 segments, the most significant decrease being registered by metallurgy, over 70 times and non-metallic mineral products of 38 times and in terms of value, the chemical industry has decreased by $ 84 bil. An interesting development for consumer behavior during the crisis was registered by food, beverages and tobacco industry and motor vehicles and other transport equipment industry, both recording increases in 2008 and decreases in 2009;

- in the case of the primary sector, agriculture, hunting, forestry and fishing and mining, quarrying and petroleum, the trend is similar in the sense that 2008 is the year of growth of the volume of FDI up to 50% and 20,83% respectively followed by a significant drop in both segments;

- 2009 is the maximum year of the crisis in many fields, such as finance, transport, communications and utilities - in particular in financial services, while in the case of industrial activities fluctuations were heterogeneous so that some industries such as the food industry and the automobile industry record significant rises and others such as the chemical industry, metallurgy and electrical equipment industry have exacerbated declines;

- the level of investments in the energy sector has fallen worldwide, due to the austere financing environment which have diminished the final demand and the available cash flows. The economic crisis results in the decrease of the global use of energy in 2009, a phenomenon which was registered for the first time since 1981. Nevertheless, the energy consumption is expected to resume its long term climbing trend, worldwide. In the oil and gas industries, most firms restricted capital expenditures, not only by drilling fewer wells, but also by postponing and even abandoning exploration projects (UNCTAD, 2010a).

The year 2008 put an end to the growth cycle investment that began in 2004 and we witnessed world FDI inflows climbing to the peak value of 1.9 $ trillion in 2007. The slump in global FDI during 2008-2009 was caused by two major factors which influenced both domestic and international investments. First, firms’ ability to invest has been dramatically shrunk by the fall in access to financial resources, brought about both by internal developments (the dramatic decrease in corporate profits) and by external unfavorable evolutions (low credit availability and high financing costs). Second, the propensity to invest has been negatively influenced by economic forecasts and this trend was more pronounced in developed countries, which were stricken by the most severe recession in the post-war period.

The synergistic impact of the two factors on the investment projects trend was strengthened in 2008 by a high level of risk perception from multinational companies (MNCs) which determined them to rationalize their costs and to cut off their investment plans in order to become more adaptive to any further worsening of the business environment (UNCTAD, 2009a).

As we have already seen, the impact of the crisis on FDI flows varies, depending on region and economic sector. Developed countries have been the most
affected, with a significant decline in FDI flows in 2008, while developing and transition economies have reached a positive growth rate of FDI inflows to developing countries of 7%, although this level was lower than in 2007. This development was entailed by even relatively high economic growth rates that remained dominant in several developing and transition economies including, among others, BRICs (Brazil, China, India and Russia) in 2008 (UNCTAD, 2009a).

The overall fall in global FDI flows during the crisis was accompanied by a significant shift in the traditional pattern of FDI. We have learned from the economic theory that capital should flow from advanced economies to developing or low-income countries. In practice, this has not been the case as emerging countries well-endowed with natural resources were becoming a growing source of FDI for developed countries, due to ambitious internationalization strategies carried out by their MNCs.

According to UNCTAD statistics, global FDI flows amounted moderately to $1.24 trillion in 2010, but they were still 15% below their pre-crisis average level. Based on their forecasts, UNCTAD specialists estimate that global FDI will recover to its pre-crisis level in 2011, rising to $1.4-1.6 trillion, approaching its 2007 peak in 2013. However, the business environment remains unstable and MNCs are cautious rather than optimistic regarding their investment programs. Figure 2 emphasizes baseline and pessimistic scenario for future FDI growth trend.

During the first quarter of 2011, FDI inflows run high compared to the same period of 2010. The recovery trend is likely to lean against the following positive developments which aim to create new investment opportunities for companies across the Globe: the significant increase in MNCs profits, the determination of taking up the running corporate and industrial restructuring anti-crisis measures, the rise of outward FDI from developing Asia, the implementation of Southern MNCs internationalization strategies, the quick deploy of strengthening investment policies etc.

4. CONCLUSION

Against the grim background of the global economic crisis, FDI represent essential vehicles of globalization processes. The 2007-2010 period analyzed in the paper from FDI evolution point of view, does not mark the first time when the world economy goes over the recession, but it certainly represents a downturn after many years, namely after the Great Depression that began in 1929 and after Breton Woods System Fall in 1971.

Moreover, we must lay stress on the fact that was for the first time when a large magnitude crisis is located mainly at the level of developed countries and not only in emerging economies.

The FDI expansion in the world economy was indeed astonishing: in the last decades of the former century, international investment flows followed a spectacular growing trend. During 2003 and 2007, statistical data gave evidence of unprecedented expansion and increase in FDI flows. The global economic crisis which erupted at the end of 2008 has hit the overall world economy, including investment trends. We must highlight two main factors that bore upon FDI shrank: restricted access to financial resources which altered the firms’ capacity to invest and the cautious behavior of
MNCs regarding their future investment plans, because of shadowy prospects for the economy, markets and risks.

However, we can assert FDI that remains an unequivocal vehicle of globalization, even in times of crisis. The issue of globalization is extremely complex and, at the same time, it generates debates in specialized national and international literature. Beyond the confrontation of ideas that are far from being concluded, it comes out the conclusion that globalization is an inevitable process and an irreversible one, if we place a sign of equality between the process of globalization and the intensification and multiplication of interaction processes, which are more obvious both at the level of individuals and at the level of relations among the main actors of the global economy – the nation States, MNCs and international organizations. Therefore, the path of global economic phenomena can no longer be controlled, and the new world economic order must be based on a new model of development that places welfare, dependency and interconnectivity in the limelight.


**Figure 2. Global FDI flows, 2002-2010, and projections for 2011-2013**

(Billions of Dollars)

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