**Forum:** Economic and Social Council

**Issue:** Foreign investment in developing nations

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**Introduction**

Foreign direct investments (FDI) play a large role in developed and developing countries’ economies. It is becoming a cornerstone for both governments and multinational corporations (MNC) the result of gaining controlling interest in foreign assets comes with a plethora of advantages. For MNCs this includes: a new and larger market which results in a larger total revenue in addition to, access to new resources, products and technology which can improve their production. Furthermore, investing abroad gives companies a chance to diversify their income and achieve higher growth rates; creating potential for investors.

Apart from the benefit gained by the investors FDI’s are critical in both emerging market and developing countries for economic growth. This is due to the resilient nature of the investment; even during times of financial crisis FDI’s remain relatively stable and provide capital flow. This has been evident in the past during the Mexican crisis (1994-95) and the Latin American debt crisis (1980s). A more recent example FDI in developing nations is in seen in 2017: developing nations received 58% of total global FDI from which they received $649 billion. This also helped with investments made as they received 43% of worldwide investment and investments rose by 8% in the developing regions of Asia who received $502 billion. FDI’s can aid with economic growth as they provide with increased: employment, education/training, tax revenue, savings, free trade, choice in the marketplace. Such investments can also act as a support for the countries own companies as they often require the funds and/or expertise of MNC’s in order to expand international sales. Another crucial factor played by FDI is the investment that is made in water, energy and infrastructure. An MNC setting up for production in a developing country would introduce more advanced and technology which can greatly improve efficiency within the country. These are all reasons why FDI’s are responsible for much of the growth of an emerging market.

Although FDI’s have many advantages, they come with certain risks and disadvantages that may have severe adverse effects such as environmental damage, draining the host countries' resources and overtaking the local market which is why developed nations and their MNC’s should be encouraged to make responsible investments that benefit not only them but also the host country.

**Definition of Key Terms**

**Capital**

Capital can be any means of material quantity that can generate revenue for a business. It is not only money that is invested but also includes: physical capital, human capital, natural capital and financial capital. Capital is also something that is produced or purchased that can provide a future stream of benefits. An example of that would be building an airport (physical capital) which is an investment but can provide benefits such as a means for air travel to take place which will continually generate revenue.

**Economic Growth**

A process by which countries' wealth increases over an extended time period (long run). It is the increase in a country's real gross domestic product (GDP) and can be calculated as “a percentage change in real GDP over a period of time” or “a percentage change in real GDP per capita over a period of time”. Such calculations help determine by how much the wealth generated by a country is changing; and also provides as a means to compare different economies.

**Emergent Markets**

Emergent markets/emerging market economies are economies that are stilling working toward becoming a developed economy. Such economies typically have a unified currency, backing system, stock market and are industrializing. They are recognised as having a relatively rapid GDP growth and a substantial global contribution to production.

This rapid growth makes said economies a viable option for investors making them responsible for over half of the global economic growth.

**Foreign Direct Investment (FDI)**

Foreign direct investment (FDI) is the flow of capital between countries; it is '*investment made to acquire lasting interest in enterprises operating outside of the economy of the investor*. `` according to the United Nations Conference for Trade and Development (UNCTAD). It is an investment by MNCs that are based in one country (home country; typically developed countries) that expand into another country (host country) by either opening branches in the host country or buying a local chain/company. In order to be considered an FDI the MNC must have 10% which qualifies as controlling assets. FDI can be made by both MNCs and Governments.

**Investments**

An investment is the purchase of something that can be used to produce wealth in the future (type of capital). Assets of companies can be bought in order to get the benefits or money generated by the company; the amount of benefit reaped depends on the amount/size of investment made.

**Investors**

Anyone who has made an investment in a company, this can include individuals, other MNCs/organizations and governments. In this context however, individuals do not play as big of a role. This is because the benefit developing countries get can come from very large sums of money and resources which individual investors typically do not invest.

**Special economic zones (SEZ)**

A special economic zone is a designated area within a country that is subject to economic regulations that differ from other regions of said country. The SEZ regulations are typically conducive FDI. Conducting business in an SEZ usually implies that the company will receive tax incentives and the opportunity to pay a potentially lower tariff.

**Background Information**

**Economic and social benefits gained by developing nations**

***Employment Opportunities***

When the government or MNC have set up new firms in the host country, this creates a lot more employment opportunity in the market. A new wave of jobs is available to the public. This is also applicable if a new expansion is not made but local company has been purchased. When local companies are taken over they require employees in order to oversee the changes that will be made to the business, thus creating more jobs. An increase in employment is extremely beneficial for developing economies as this means their economic growth will progress at a faster rate. Having a higher percentage of the population employed can improve the quality of life as people can better afford necessities. It also increases consumer spending. When an individual's income rises they are able to spend more on items even outside of necessities. This means that more money is going toward businesses. Money going into local business is excellent for the economy as the country as a whole would be generating more revenue through its companies. This increase in spending would also encourage more people to start becoming entrepreneurs to further fuel the economy.

***Education and Training***

With a higher employment rate comes a higher number of people who are being trained to do certain jobs. When companies look to hire people, they need a workforce who is specialized in they work their job requires them to do, in order to fulfil this, they often have inductions and training sessions. Furthermore, people also learn more skills as they work, creating a more skilled population as a whole. This is beneficial to the economy as more people are now able to work due to the opportunity they are getting of being trained. Certain individuals are also becoming more employable, meaning that even if the specific job they had at a firm is gone they can still find work elsewhere due to the accumulation of new skills. This training is not only helpful in creating employment opportunity but also helps people get better jobs, promoting them to a higher pay. This can help increase a country's GDP per capita and even help reduce the percentage of the population living below the poverty line.

***Savings***

The rate of saving a country has is a key element in all theories of economic growth. FDIs bring in an inflow which is also a crucial determinant of economic growth but the two works closely together as the inflow brought in by FDIs greatly contributes to the savings made by a country.

***Research, Development and Technology***

MNCs can bring along with them a large scope for research and development of both technology and marketing tools. MNCs are extremely successful at marketing and expanding which is why they are often well established and able to invest overseas. Such tools can greatly benefit companies that are taken over in the host country to expand and move their brand forward; to both open more branches or appeal more to the market. Even if a local company has not been bought and instead a new branch of the MNC has been started there is still exposure to new techniques being made. Employees can learn about them and further enhance their careers, as well as introduce these ideas to more of the population. Also, constant development needs to be done to all aspects of a business ranging from actual technology, infrastructure to methods marketing. All of which are being implemented in the host country and giving them opportunities to learn and use this knowledge to better themselves in such aspects.

***Infrastructure***

This aspect is closely related to the development that comes from MNCs and other organizations. When such firms and organizations are established in the host country they must make workplaces; with their typically large budgets they are able to invest in high quality infrastructure. This allows for more viable workspaces in the country. Apart from areas of work governments often improve their existing infrastructure in order to attract more FDIs from MNCs. There are also instances where such companies contribute towards the betterment of the host country themselves to both give back to the community (a large social cost companies are generally expected to bear) and also improve the lives of their employees (areas around or areas sponsored by the company). This is vital as the process of moving toward becoming a developed country is not only limited to economic development but also improving the quality of life for citizens; having better infrastructure plays a large role in that aspect.

***Lower Price and Choice in Market***

This is a social benefit as locals will be able to purchase things at the lowest possible price allowing them to fully maximize their spending. When there are numerous competitors in the market there will be more competition to get as many consumers as possible. Firms can do that by offering the most valuable deals to customers. There will also be many more options is the market for consumers. These are all factors which could ensure the general population is able to afford more as prices are lower than they would have been which also attracts more people to spend money into the markets; a way in which more revenue is generated by the economy.

Although the practice of having developed nations investing in developing nations can help them achieve faster economic growth the same result is simultaneously being achieved by the investments being made by developing countries and non-profit organisations. Developing countries can make substantial revenue by investing in MNCs in other countries and reap the same benefits as they would had the investments been made in their own country. Additionally, there are non-profit organisations that are working toward the improvement of economies around the world that make investments abroad; these investments bring in the same results as the ones made by other countries.

**Risks of FDI**

Although FDI can have extensive benefits to developing countries, if not done with all factors taken into consideration and planning it can have severe adverse effects on both the investor or country being invested in.  FDI can be a great tool to aid economic growth but is not done responsibly and with the intention of mutual benefit there can be long term consequences. Such consequences include MNCs extracting resources from the host country unsustainably, the host country beginning to rely on MNCs and driving out domestic firms. An example of FDIs having adverse effects can be seen in the hyperinflation caused in Azerbaijan[[1]](#footnote-0).

**Major Countries and Organizations Involved**

**United States of America**

The US had a net FDI of $479.4 billion in 2016, placing it at number 1 in the world for FDI received, even today. Their largest investments came from Canada and the United Kingdom, however there are fast growing investments from developing countries such as Thailand and Argentina, according to the U.S. Department of Commerce's International Trade Administration. Although a developed country they can still benefit from FDI for further economic growth. Additionally, it also provides good opportunities for other countries both developed and developing to invest in order to expand their companies into MNCs.

**United Kingdom**

The UK received $299.7 billion in FDI in 2016 putting them at number 2 in the world for most investment received. Whilst only 1.2% of the companies received foreign direct investment that made up for 18 percent of employment and 33 percent of wages, according to the British Office for National Statistics. Although a developed country the same reasoning applies as for the US.

**China**

FDI in China reached $170.6 billion in 2016. This was an all-time high for the country, as close to 2,500 new foreign-invested enterprises are approved monthly on average. China has taking full advantage of the investment system which could play a major role in China being one of the fastest growing economies in the world with their economic growth reaching up to 7% per annum. China also has one of the most successful SEZ in the world, with an entire province, Hainan, to be an SEZ bringing in the most foreign capital in the world.

**Singapore**

Singapore received $61.6 billion in FDI in 2016 putting them in 7th place worldwide for FDI received. The country has a streamlined interface with the government, *TradeNet*, who process permits at incredible speed and a recently revamped intellectual property program that offers incentives for foreign research and development. They also have the infrastructure that allows for larger MNCs to invest there, but recently the actual space left in the country may be serving as an issue.

**India**

India received $44.4 billion in FDI in 2016 putting them in 9th place worldwide for FDI received. Investments were made mostly in the real estate/infrastructure sector by Canada which is helping India become one of the fastest growing regions for investments worldwide. Such investments may also play a significant role making the nation one of the fastest growing economies. SEZs were introduced to [India](https://en.wikipedia.org/wiki/India) in 2000, following the existing SEZ model used in China. Prior to this India relied on [export processing zones](https://en.wikipedia.org/wiki/Export_processing_zones) (EPZs) which failed to make an impact on foreign investors. By 2005, all EPZs had been converted to SEZs and of 2017, there are 221 SEZs in operation.

**Brazil**

Brazil got $78.9 billion in FDI in 2016 putting it in6th place worldwide in FDI received. On its way, back from a recession and corruption, the President Michel Temer introduced in an investment partnership program in 2017, to oversee $14 billion in infrastructure concession plans for: roadways, ports, railways and power lines in hopes to make the country more attractive to investors

**Timeline of Events**

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| --- | --- |
| **Date** | **Description of Event** |
| 2002 | The world stock of FDI reached $7 trillion in 2002, up more than 14 times since 1980 |
| 2003 | Policy changes were made to improve FDI in different nations |
| 2016 | United states of America receive most FDI in the world |
| 2016 | China receives the most FDI worldwide of all developing countries |
| 2019 | FDI percentages decline in comparison to that in the past therefore national policies are being developed in favor of encouraging/attracting more FDI  |

**Relevant UN Treaties and Events**

The UN itself has not created any treaties between countries or made any official guidelines that must be followed when investing as FDI can be made by any country in any country; the number of countries’ pre-existing laws and economic conditions they would have to keep in mind would be too vast.

* **Treaties and events concerning FDI directly**

The UN (more specifically UNCTAD) has however, published numerous articles, reports, studies and statistical analyses which is concerned with the effect FDI has on countries. There is a large focus on how FDI should be made in order to benefit Less Developed Country (LDC). These include ways for countries to attract FDI as well as highlight precautions investors should take whilst investing.  These are helpful as there is more awareness and general education on this topic. It also means that there are regular analyses/checks being done by a larger organization to oversee how FDI is affecting the masses and not just a single country; allows for treaties to be made if specific regions are greatly suffering.

There has been however, changes made in national policies of countries around the world in from 2003-October 2018, 70% of which were favorable to FDI. These investment related policies have “programs and measures in place to encourage outward FDI flows, including information services on the business environment and opportunities in host countries; financial support for pre-investment activities, fiscal measures and political risk insurance” Such measures are taken with the intention of advancing the interests of the host country along with enhancing the international competitiveness of its firms; this tends to promote FDI in developing nations.

* **Treaties and events concerning related factors**

One of the factors that are closely related with the effect FDI has on developing nations is on labor. As mentioned earlier FDI can increase employment but there are often more lenient regulations on labor for numerous reasons. Policies have to be made when welcoming MCNs to work into the host countries to protect the rights of employees and ensure there are minimal adverse effects on the host country itself. Policies are aligned with the relevant “relevant international standards and agreements, such as the Guiding Principles on Business and Human Rights and the labor standards of ILO, the Convention on the Rights of the Child”. There are also policies set which regulate the effect on the environment. These polices can be both legally binding or non-binding depending on the regulation for all member states of the UN

**Previous Attempts to Solve the Issue**

As mentioned earlier, there are no definitive steps the UN has taken in order to solve the issue of declining global FDI as it an issue that affects a large spectrum of countries, The UN cannot make/conduct laws that fit all counties involved as it may clash with their personal interests and the UN stands strongly for autonomy. The UN does however make tremendous efforts in ensuring people are well educated on why and how FDI can be beneficial. There are also country-specific reports written regularly which can help nations determine how effective their policies are and how they must change in the future. Overall, the UN is not causing direct change and is instead supporting nations in the background and aiding this issue to be solved through intellectual means.

**Possible Solutions**

As mentioned earlier in this report FDI can be greatly beneficial to developing countries in terms of economic growth and advancement in society; there are however, some drawbacks which is why responsible FDI should be encouraged. Such investments should: create employment opportunities, enhance the skills of those in the host country, develop the infrastructure and technology, make domestic firms more competitive and be mindful of the environment. In order to achieve this and increase investments the following can be done.

**Implementation of special economic zones**

SEZs promote rapid economic growth through tax leveraging. This provides an incentive that attracts foreign investors and technological advancement. SEZs also provide tax breaks which allows for business to have more independence making the area more attractive to extended business towards. With all the factors working in favour of MNCs they are more likely to invest in these areas.

**Improving infrastructure to meet the requirements of investors**

If the host country invests in improving their infrastructure they can attract a lot more investors. Investors often spend time and resources improving the infrastructure themselves in order to operate and provide a higher quality of life for their employees. If the host country is already equipped with the infrastructure that can support them this means they spend less trying to creating quality infrastructure, making them more likely to choose said country for investments.

**Encouraging first-time investors**

Attracting new firms or firms that are not already part of a larger global network can be a good way to get a larger number of investors. Such firms are more likely to accept linkage to domestic suppliers which can be beneficial to locals as well as agree to slightly stricter regulations as they are newer and are looking to expand globally.

**Regulating laws/policies regarding environment and labor**

Although reducing regulations was favorable but there should be minimal compromise on regulations and policies regarding labor and the environment as exploiting those can lead to more damage than benefit derived from the FDI

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**Appendices**

1. <https://www.ukessays.com/essays/economics/negative-effects-of-fdi-in-host-countries-economics-essay.php>

This link provides information on the case study which shows the negative impact of FDI on Azerbaijan, the information can be useful to understand how FDI can be risky and what should be avoided by both investors and the host country when making such deals

1. <https://developmentfinance.un.org/encouraging-quality-direct-investment>

This link provides more information, statistics and diagrams of how policy changes improved FDI as well as how other organs who may not be directly associated with this issue are involved to some degree when trying to study and regulate FDI as a whole

1. <https://www.thebalance.com/foreign-direct-investment-fdi-pros-cons-and-importance-3306283>

This link has basic information on what and FDI is and how it works; it’s a good starting point if you have no. prior knowledge on the topic

1. <https://www.usnews.com/news/best-countries/slideshows/10-countries-that-receive-the-most-foreign-direct-investment?slide=12>

This link gives more information on some more countries that are heavily involved with this topic

1. For more information refer to appendix [↑](#footnote-ref-0)