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IMPACT OF FOREIGN DIRECT INVESTMENT INFLOWS ON BRAZILIAN ECONOMY

ROBIN INDERPAL SINGH
RESEARCH SCHOLAR
I.K. GUJRAL PUNJAB TECHNICAL UNIVERSITY
JALANDHAR

DR. SANJEEV BANSAL
ASST. PROFESSOR (COMMERCE)
I.K. GUJRAL PUNJAB TECHNICAL UNIVERSITY
JALANDHAR

DR. JAGWANT SINGH
FORMER HEAD & ASSOCIATE PROFESSOR (COMMERCE)
GGDSD COLLEGE
CHANDIGARH

ABSTRACT

Finance is the major economic problem for the developing economies as they do not have the money for the investments which is necessary for the development of the nation. Developing nations tries to get direct and indirect investments to solve the finance problems in the form of foreign capital and reform their investment policies to get the foreign investments in their country. Due to the changes, there has been changes in the of Foreign Direct Investment inflows in the Brazilian economy. The study is conducted to know the determinants for FDI inflow in Brazil and its impact on economic growth of the country. The study revealed that R&D GDP and EXR are the determinants which significantly influence the FDI inflows in Brazil. They act as the important macroeconomic determinants and pull factors of FDI inflows in Brazil. The study also reveals that FDI is not a significant factor influencing the level of economic growth in Brazil. The results of Economic Growth Model and Foreign Direct Investment Model show that FDI plays a limited role in enhancing the level of economic growth in the country.

KEYWORDS

Brazilian economy, foreign direct investment (FDI).

INTRODUCTION

Finance is the major economic problem for the developing economies as they do not have the money for the investments which is necessary for the development of the nation. Developing nations tries to get direct and indirect investments to solve the finance problems in the form of foreign capital. Earlier commercial banks provide them loans, but after 1980s, after drying up of capital these banks also refused to give loans to countries which forced developing nations to reform their investment policies to get the foreign investments in their country.

Foreign direct investment (FDI) is a process whereby the residents of the source country attain ownership of assets with the intention to control the production, distribution and other activities of a firm in the host country. The International Monetary Fund's Balance of Payments Manual defines FDI as, "an investment that is made to acquire a lasting interest in an enterprise operating in an economy other than that of the investor, the investor's purpose being to have an effective voice in the management of the enterprise". The United Nations World Investment Report (UNCTAD, 1999) defines FDI as, "an investment involving a long-term relationship and reflecting a lasting interest and control of a resident entity in one economy (foreign direct investor or parent enterprise) in an enterprise resident in an economy other than that of the foreign direct investor (FDI enterprise, affiliate enterprise or foreign affiliate)".

Direct investment across national borders is a distinct feature of international economics, which has gained intense attention of all the countries of the world recently. Foreign direct investment is deemed to be a growth catalyst since it is usually accompanied by entrepreneurial, managerial and technical skills which are indispensable for economic growth (Humphrey, 1960). Foreign direct investment is one of the most strategic and vital tools for developing a country's competitiveness and efforts must be made to garner huge share of FDI in the country (Badar, 2006). Going by this ideology FDI is being sought by most of the developing countries of the world for promoting the cause of economic development.

FDI to developing countries in the 1990s was the leading source of external financing and has become a key component of national development strategies for almost all the countries in the world as a vehicle for technology flows and an important source of non-debt inflows for attaining competitive efficiency by creating a meaningful network of global interconnections. FDI provide opportunities to host countries to enhance their economic development and opens new opportunities to home countries to optimize their earnings by employing their ideal resources.

Many developing countries including Brazil made significant progress due to lower barriers of trade, easy finance availability and FDI liberalization along with decreased transport and communications costs and made options available to the firms where to produce and sell.

From the recent past, it has been perceived that foreign direct investment plays a developmental role. Governments are of point of view that foreign direct investment can help the countries to pass through the phase of stagnation and bypass poverty. Since mid-eighties, there has been huge growth of foreign direct investment resulting into changes in the particular's countries attributes such as changes in technology, privatization, change in trade norms, managerial expertise, etc. The role of Foreign Direct Investment is very crucial in enhancing the welfare of host country as of the benefits like innovation, better technology, better managerial techniques, development of skills, enhanced capital, creation of more job opportunities and improvement in the working condition of employees and development of industrial sector in the host country (Caves, 1974; Haddad and Harrison, 1993; Perez, 1997; and Markusen and Venables, 1999). Foreign Direct Investment inflow, which comes as a composite bundle of tangible and intangible asset, which along with the domestic investments increases the growth of the country by efficiently using resources and expands markets by increasing exports.

REVIEW OF LITERATURE

To increase the flow of FDI inflows, so far many studies have been conducted around the globe over the different period of time for exploring the determinants of FDI inflows in an economy. **Bhagwati, J.N (1978),** in his study analyzed the impact of FDI on international trade. He concluded that countries actively pursuing export led growth strategy can reap enormous benefits from FDI. **Cho (2004)** points out that the attractiveness of the economic conditions in host countries; the policy framework towards the private sector, trade and industry, and FDI and its implementation by host governments; and the investment strategies of multinational enterprises are three factors influencing FDI inflows in an economy. **Singh (2005)** in his study explores the uneven beginnings of FDI, in India and examines the developments (economic and political) relating to the trends in two sectors: industry and infrastructure. The study concludes that the impact of the reforms

in India on the policy environment for FDI presents a mixed picture. The industrial reforms have gone far, though they need to be supplemented by more infra-structure reforms, which are a critical missing link. **Chowdhury and Mavrotas (2006)** examines the causal relationship between FDI and economic growth by using an innovative econometric methodology to study the direction of causality between the two variables and found that it is GDP that causes FDI in the case of Chile and not vice versa, while for both Malaysia and Thailand, there is a strong evidence of a bi-directional causality between the two variables. **Khaliq and Noy (2007)** investigates the impact of foreign direct investment (FDI) on economic growth using detailed sectoral data for FDI inflows to Indonesia over the period 1997-2006 and found in the aggregate level, FDI is observed to have a positive effect on economic growth. However, when accounting for the different average growth performance across sectors, the beneficial impact of FDI is no longer apparent. When examining different impacts across sectors, estimation results show that the composition of FDI matters for its effect on economic growth with very few sectors showing positive impact of FDI and one sector even showing a robust negative impact of FDI inflows. **Crespo and Fontoura (2007)** in their paper analyze the factors determining the existence, dimensions and sign of FDI spillovers. They identify that FDI spillovers depend on many factors like absorptive capacities of domestic firms and regions, the technological gap, or the export capacity. **Sharma (2011)** also identifies that complexity in doing business, insufficient growth of service sector, lack of adequate infrastructure and lack of skilled manpower are significant factors influencing FDI inflows. **Solomon (2011)** analyses how the levels of economic development, human capital, financial development and the qualities of the economic and political environments in host countries simultaneously affects the impact of aggregate inflows of Foreign Direct Investment (FDI) on economic growth. The results show that the level of economic development, human capital and quality of the political environment all significantly affect the relationship between inward FDI and growth. **Almfraji and Almsafir (2014)** examined the relationships between FDI and EG, especially the effects of FDI on EG, from 1994 up to 2012 and found that FDI-EG relation is significantly positive, but in some cases it is negative or even null. And within the relation, there exist several influencing factors such as the adequate levels of human capital, the well-developed financial markets, the complementarity between domestic and foreign investment and the open trade regimes, etc. **Melnyk, et al. (2014)** investigates the impact of foreign direct investing on economic development of post Comecon transition econ-omy countries by using Neoclassical growth theory model is used to analyze the effects of FDI on economic growth and the results showed significant FDI influence on economic growth of host countries. **Zekarias (2016)** analyzed the impact of Foreign Direct Investment (FDI) on Economic growth in 14 Eastern Africa countries by employing 34 years (1980-2013) panel data, using dynamic GMM estimators after checking for autocorrelation and model specification tests and confirms that FDI has positive and marginally significant effect of FDI on economic growth, the rate of economic conditional convergence at 5%, absence of significant crowding out effect moving from FDI to domestic investment, interdependence of domestic investment and trade openness in the sub-region.

OBJECTIVES OF THE STUDY

The objective of the study is to evaluate the impact of FDI on the economy. To achieve the objectives of the paper, the study has been done for the period of 1991-2014.

RESEARCH METHODOLOGY

DATA COLLECTION

This study is based on secondary data. The required data have been collected from various sources i.e. World Investment Reports, United Nations, Country Reports on Economic Policy and Trade Practice- Bureau of Economic and Business Affairs, U.S. Department of State and from websites of World Bank, IMF, WTO, UNCTAD, etc. It is a time series data and the relevant data have been collected for the period 1991 to 2014**.**

SELECTION OF VARIABLES

Existing literature was used to choose the right group of variables that clarifies the differences in the flow of the country. As per specifications of UNCTAD, different variable combinations were made. Simple and multiple regression methods are applied to find out the explanatory variables of the FDI inflows in the country in two steps. In the first step, all variables are taken into consideration in the estimable model and in the second stage, few variables which are insignificant are dropped to avoid the problem of multi-co linearity, otherwise the results would have been biased and untrue. Following are the macroeconomic indicators which are considered as the pull factors like: total trade (TRADEGDP), research and development expenditure (R&D GDP), financial position (FIN. Position), exchange rate (EXR), foreign exchange reserves (RESERVES GDP), and foreign direct investment (FDI), foreign direct investment growth rate (FDIG) and level of economic growth (GDPG) are used in the model to gauge the impact.

MODEL BUILDING

Further, to study the impact of foreign direct investment on economic growth, two models were framed and fitted. The foreign direct investment model shows the factors influencing the foreign direct investment in Brazil. The economic growth model depicts the contribution of foreign direct investment to economic growth. The two model equations are expressed below:

FDI = f [TRADEGDP, RESGDP, R&DGDP, FIN. Position, EXR.]

GDPG = f [FDIG]

Where,

FDI	=	Foreign Direct Investment
GDP	=	Gross Domestic Product
TRADE GDP	=	Total Trade as percentage of GDP.
RES GDP	=	Foreign Exchange Reserves as percentage of GDP.
R&D GDP	=	Research & development expenditure as percentage of GDP.
FIN. Position	=	Ratio of external debts to exports (Financial Position)
EXR	=	Exchange rate
GDPG	=	Level of Economic Growth
FDIG	=	Foreign Direct Investment Growth.

Regression analysis (Simple & Multiple Regression) was carried out using relevant econometric techniques. Simple regression method was used to measure the impact of FDI flows on economic growth (proxied by GDP growth). Further, multiple regression analysis was used to identify the major variables which have impact on foreign direct investment. Relevant econometric tests such as coefficient of determination R2, Durbin–Watson [D-W] statistic, Standard error of coefficients, T Statistics and F- ratio were carried out in order to assess the relative significance, desirability and reliability of model estimation parameters.

FINDINGS AND DISCUSSION

MODEL – I

FDI = f [TRADEGDP, RESGDP, R&DGDP, FIN. Position, EXR.]

HYPOTHESIS

H1: There exists a significant impact between FDI and determinants of FDI.

TABLE 1: CORRELATION MATRIX OF FDI AND DETERMINANTS OF FDI

Correlations[a]								
		FDI	GDP	FIN Pos	TRADE GDP	RES GDP	R&D GDP	EXR
FDI	Pearson Correlation	1						
	Sig. (2-tailed)							
	N	24						
GDP	Pearson Correlation	.912**	1					
	Sig. (2-tailed)	.000						
	N	24	24					
FIN Pos	Pearson Correlation	-.536**	-.730**	1				
	Sig. (2-tailed)	.007	.000					
	N	24	24	24				
TRADE GDP	Pearson Correlation	.373	.271	-.554**	1			
	Sig. (2-tailed)	.072	.200	.005				
	N	24	24	24	24			
RES GDP	Pearson Correlation	.809**	.904**	-.723**	.413*	1		
	Sig. (2-tailed)	.000	.000	.000	.045			
	N	24	24	24	24	24		
R&D GDP	Pearson Correlation	.875**	.828**	-.671**	.624**	.814**	1	
	Sig. (2-tailed)	.000	.000	.000	.001	.000		
	N	24	24	24	24	24	24	
EXR	Pearson Correlation	.407*	.287	-.407*	.847**	.373	.712**	1
	Sig. (2-tailed)	.048	.174	.049	.000	.072	.000	
	N	24	24	24	24	24	24	24
**. Correlation is significant at the 0.01 level (2-tailed).								
*. Correlation is significant at the 0.05 level (2-tailed).								
a. Stat =Brazil								

A total of five sub hypothesis are tested with the help of regression analysis and explained statistically.

TABLE 2: MODEL SUMMARY FDI AND DETERMINANTS OF FDI

Model Summary[a]					
Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Durbin-Watson
1	.938[b]	.881	.847	8409.59830525	1.403
a. State = Brazil					
b. Predictors: (Constant), EXR, RES GDP, TRADE GDP, FIN Pos, R&D GDP					

In the above table (Table 2), the R value represents the association that the dependent variable (FDI) has with all independent variable or predictors. The R^2 value (.881) depicts the amount of variance explained by all the independent variables (determinants) accounting in for Foreign Direct Investment (FDI). In case where the number of independent variables is more than 1, the adjusted R square values are considered which comes out to be.847 in this case. The value of adjusted R square depicts that determinants of FDI influence 84.7% of FDI.

TABLE 3: ANNOVA TABLE - FDI AND DETERMINANTS OF FDI

ANOVA[a,b]						
Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	9388717599.615	5	1877743519.923	26.551	.000[c]
	Residual	1272984185.803	18	70721343.656		
	Total	10661701785.418	23			
a. State = Brazil						
b. Dependent Variable: FDI						
c. Predictors: (Constant), EXR, RES GDP, TRADE GDP, FIN Pos, R&D GDP						

The above table (Table 3) talks about the significance of the model. The Significance value (less than.05) confirms that the model is significant at 95% degree of freedom. In other words, it depicts that various determinants of FDI influences FDI. Further, in the analysis (B) values are calculated to check which determinant of FDI significantly influences the FDI.

TABLE 4: COEFFICIENTS SUMMARY: FDI AND DETERMINANTS OF FDI

Coefficients[a,b]								
Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.	Collinearity Statistics	
		B	Std. Error	Beta			Tol	VIF
1	(Constant)	-167742.869	34977.471		-4.796	.000		
	FIN Pos.	5285.820	2991.041	.238	1.767	.094	.367	2.725
	TRADE GDP	690.256	877.316	.139	.787	.442	.211	4.736
	RES GDP	650.853	920.542	.126	.707	.489	.209	4.784
	R&D GDP	**184568.936**	**33594.248**	**1.223**	**5.494**	**.000**	**.134**	**7.476**
	EXR	**-12827.381**	**5051.743**	**-.532**	**-2.539**	**.021**	**.151**	**6.615**
a. State = Brazil								
b. Dependent Variable: FDI								

The above table (Table 4) shows that R&D GDP and EXR are the determinants (p value <.05) which significantly influence the Foreign Direct Investment in Brazil. In other words, we can say that there are only two determinants of FDI named that R&D GDP and EXR which influence the FDI in Brazil.

A regression equation, thus has been drawn after eliminating the insignificant variables from the regression and thus the regression equation thus can be written as:

$Y = B_1X_1 + B_2X_2 + C$

FDI = 184568.936 (R&D GDP)+ -12827.381 (EXR) + (-167742.869)

TABLE 5: SUMMARY OF SUB HYPOTHESIS FORMULATED

Hypothesis Formulated	Status of Acceptance
$H_1$1a : There is a significant impact between FDI and FIN Pos	Not Accepted
$H_1$1b : There is a significant impact between FDI and TRADE GDP	Not Accepted
$H_1$1c : There is a significant impact between FDI and RES GDP	Not Accepted
$H_1$1d : There is a significant impact between FDI and R&D GDP	Accepted
$H_1$1e : There is a significant impact between FDI and EXR	Accepted

MODEL – II

GDP G = f [FDI G]

HYPOTHESIS

H2: There exists a significant impact *between GDP G and determinants of FDI G.*

TABLE 6: CORRELATION MATRIX OF GDP G AND FDI G

Correlations[a]			
		GDP G	FDI G
GDP G	Pearson Correlation	1	
	Sig. (2-tailed)		
	N	24	
FDI G	Pearson Correlation	.377	1
	Sig. (2-tailed)	.070	
	N	24	24
**. Correlation is significant at the 0.01 level (2-tailed).			
*. Correlation is significant at the 0.05 level (2-tailed).			
a. Stat = Brazil			

TABLE 7: MODEL SUMMARY GDP G AND FDI G

Model Summary[a]					
Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Durbin-Watson
1	.377[b]	.142	.103	2.16635338	1.561
a. State = Brazil					
b. Predictors: (Constant), FDI G					

In the above table (Table 7), the R value represents the association that the dependent variable (GDP) has with independent variable or predictor. The R^2 value (.142) depicts the amount of variance explained by the independent variables (FDI G) accounting in for GDP growth.

TABLE 8: ANNOVA TABLE – GDP G AND FDI G

ANOVA[a,b]						
Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	17.087	1	17.087	3.641	.070[c]
	Residual	103.248	22	4.693		
	Total	120.335	23			
a. State = Brazil						
b. Dependent Variable: GDP G						
c. Predictors: (Constant), FDI G						

The above table (Table 8) talks about the significance of the model. The Significance value (more than.05) confirms that the model is not significant at 95% degree of freedom. In other words, it depicts that FDI Growth does not scientifically influence GDP Growth. Further, in the analysis (B) values are calculated to check the level of insignificance.

TABLE 9: COEFFICIENTS SUMMARY: FDI AND DETERMINANTS OF FDI

Coefficients[a,b]								
Model		Unstandardized Coefficients		Standardized Coefficients	T	Sig.	Collinearity Statistics	
		B	Std. Error	Beta			Tol	VIF
1	(Constant)	2.369	.509		4.655	.000		
	FDI G	.016	.009	.377	1.908	.070	1.000	1.000
a. State = Brazil								
b. Dependent Variable: GDP G								

The above table (Table 9) shows that FDI Growth is the factor (p value >.05) which significantly does not influence the GDP Growth in Brazil. In other words, we can say that that FDI Growth does not scientifically influence the GDP Growth in Brazil.

TABLE 10: SUMMARY OF SUB HYPOTHESIS FORMULATED

Hypothesis Formulated	Status of Acceptance
$H_1$2a : There is a significant impact between GDP G and FDI G	Not Accepted

CONCLUSION

It has been found that R&D GDP and EXR are the determinants which significantly influence the FDI inflows in Brazil. They act as the important macroeconomic determinants and pull factors of FDI inflows in Brazil. Thus, it is concluded that the above analysis is successful in identifying those variables which are important in attracting FDI inflows to the country. The study also reveals that FDI is not a significant factor influencing the level of economic growth in Brazil. The results of Economic Growth Model and Foreign Direct Investment Model show that FDI plays a limited role in enhancing the level of economic growth in the country.

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