Foreign Direct Investment and its Determinants: A Study on India and Brazil

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ABSTRACT: *International trade builds up through international factor movement (IFM). IFM means movement of labour, capital and other elements of production among different country. It occurs by three ways: first one is immigration or emigration, international borrowing or lending is second way and last one is foreign direct investment (FDI). FDI means controlling ownership of a business enterprise of one country is based on entity of another country. Investment through FDI depends on various factors namely Inflation Rate, Human Development Index (HDI), Global Terrorism Index (GTI), Global Peace Index (GPI), Unemployment, Population; Corruption Perception Index (CPI), Industrial disputes etc. Object of this present study is to identify the effect of these factors on FDI inflow for India and Brazil. Also identify the more important determinants for FDI of these two countries. Ten years data (2005 to 2014) have been used for determining the result of this study. Result reveals that there exist impact of sample factors on FDI Inflow between two countries but strength of different factors varies.*

Keywords: *International Factor Movement, Foreign Direct Investment, Gross Terrorism Index, Gross Peace Index, Corruption Perception Index.*

I. INTRODUCTION

Genesis of Foreign Direct investment (FDI) comes out from the activities of multinational companies during the period of first half of nineteenth century i.e. prior to First World War (Knidleberger, et. al., 1983). Now, inflow of Foreign Direct Investment (FDI) increases globally day to day. In 1970 total worldwide inflow of FDI was 10172528390 US dollar and in 2014 it was reached at 1561365079452.96 US dollar (IMF Report). Significantly it helps to generate economic benefits of host as well as home countries by providing capital, foreign exchange, technological support, enhancing healthy competition among business firms (IMF, 1999; Crespo and Fontura, 2007; Romer, 1993). FDI inflow varies from one to other countries with different objective. Researcher Athukorala (2009) argues that objective of some companies seek large domestic market (market seeking FDI) and some of them seek the supply of natural resources (resource seeking FDI). Another side, some companies want to relocate their plants to reduce their production cost and create a linkage with global market (efficiency seeking FDI). So based on requirement inflow of FDI varies.

Total inflow of FDI depends on different factors like flexibility of labour market, deepness of financial market, better infrastructure, more independent judiciary system, educational attainment etc.(Walsh and Yu, 2010). In another study Singh and Jun (1995) opine that FDI is also influenced by Labour management, strength of export, political stability of country, infrastructural differences etc. So it is clear that inflow of FDI is the function of some factors.

This paper is designed by using following section: section-I represents Introduction, section-II deals with literature reviews which is classified in two parts, part I deals with literature review aim of section-III is to identify the research gap and depicted the objective of the study, section-IV provides Hypothesis development, section-V describes data and methodology, it also categorized as four parts i.e. part I deal with source of data collection, part II relates with Measurement of Variables, part III is devoted for highlights the calculation techniques of dependent variables and part IV contents with research methodology, section-VI is devoted for result analysis which is split up in two parts for two countries and last section i.e. section-VII highlights conclusion of this study.

II. LITERATURE REVIEWS

Foreign Direct Investment has a positive impact of economical growth of a country. Different researcher argues about this. Agosin and Mayer (2000) conduct a study on 32 developing countries of Asia, Latin America and Africa during the period of 1970-1996. They use regression method for analysis purpose. They reveal positive impact of FDI on domestic investment but it is not very strong. In another study Alfaro, Chanda, Kalemil-Ozcan and Sayek (2001) reveal that FDI contributes positive effect on economic growth by analyzing the panel data of 41 countries through OLS model during the period 1981 to 1997. Researchers Blomstrom, Lipsey and Zejan (1994) also establish a relationship between FDI inflows and countries economic

growth by analyzing the relevant data of 78 countries for the period 1960 to 1985.In the year 2001 Carkovic and Levine find out the impact of FDI on GDP by using dynamic panel data estimator for the period 1960 to 1995, they also identify the FDI strongly linked with productivity. Another side researcher Hermes and Lensink (2000) conduct study on relevant data of 67 least developed countries for the period 1970 to 1995 for determining the effect of FDI on growth of country by using cross-country OLS model. They also find out the positive impact of FDI on growth of country's economical position. Another side researcher Zhang (2001) examines the impact of Inward FDI stock on country specific growth. He conducts his study by using Stationarity and cointegration method on relevant data of 11 Latin American and East Asian countries for the period 1970 to 1995.

Research on different unions like ASEAN, OECD etc, regarding FDI and economical growth of countries are also depicted by various researchers. Bende-Nabende, Ford and Slater (2000) examine the effect of FDI on five ASEAN countries over the period 1970 to 1994 by applying least square method. They observe that FDI has positive and significant coefficient in the growth equation of three countries out of five countries. They also argue that FDI inflow promotes the balance between domestic capital and FDI capital. Moreover it has positive effect on human resource development, technological transfer, expansion of trade and learning etc. In the year 1998 Borensztein, de Gregorio and Lee investigate the effect of gross FDI outflow from OECD countries (i.e. 69 countries) on economical growth during the period 1970 to 1979 and 1980 to 1989 by using SUR (seemingly unrelated regression) method. FDI exert a positive effect of economical growth of a country if minimum level of human capital is exists.

Goldberg and Klein (1998) examine the effect of Real Exchange Rate on FDI. They use gravity model and real exchange rate includes as depreciation of the host country. Depreciation reduces the amount of foreign currency which is required to purchase assets in other country, and also reduce the nominal return in term of foreign currency. Result of their study highlights that there is an insignificant impact of real exchange rate on FDI. Researchers Egger and Pfaffermayr (2004) conduct a study on various variables for determining the effect of those on FDI. Variables are individual income, development of country, capital abundance, labour abundance and educational difference etc. Result of their study indicates that there is a significant effect of these variables on FDI. Generally factors act as attractor of FDI. Rodrick(1999) and Lim (2001) argue that GDP growth is the signal of higher return which attract FDI inflow and reduces outflow of FDI of source country. Another side Ekholm, Forslid and Markusen, (2007), Blonigen et al. (2007), and Baltagi, Egger and Pfaffermayr (2007) conduct their study on market proximity i.e. size of market and FDI by using regression model. Results of their studies reveal that there is a positive and significant effect of market size on FDI inflow. Country's Productivity is also a factor which influences the FDI inflows. Result of Cross country analysis on panel data suggest that effect of country's productivity varies between countries (Razin, Rubenstein, and Sadka 2004, and Razin, Sadka, and Tong, 2008). Blonigen (2005) examines the effect of corporate taxes and tax treaties on FDI inflows. He finds out the significant effect of taxes on FDI inflows. While Razin and Sadka (2007, Ch 10) highlight the two fold impact of taxes on FDI inflows and outflows. Higher tax rate of host country creates a negative impact on FDI inflows as well as tax rebate helps to increase FDI inflows. Researchers Blonigen & Davies (2004) and Egger et al. (2006) show highly positive impact of existing tax treaties on FDI inflows, but negative impact of new tax treaties on FDI inflows. But when Di Giovanni (2005) conducts his study for examine the effect of tax treaties only on volatility of FDI inflows, and then positive effects of tax treaties are reflected. Financial and political risks are also taken as factors of FDI inflows by researchers Razin, Sadka, and Tong (2008) for conduct their study. Return on investment and cost of political conflict are considered as proxy of financial risk and political risk. Another set of researchers like Carr et.al (2001) also conduct their study on financial and political risk and reveal significant effect of those on FDI inflows. Regional trade agreement and currency of different unions have an impact on FDI inflows (Petroulas, 2007 and Baldwin et al., 2008).

Another study Jadhav (2012) investigates the relationship FDI inflow and economic, institutional and political factors of BRICS countries. He takes into account Market size, Trade openness, natural resources as economic factor and Political stability/no violence, Macroeconomic stability (Inflation Rate), Government effectiveness, control of corruption, regularity quality, voice and accountability, rule of law as potential political and institutional factor of FDI. This study is conducted by using panel data for the year 2000 to 2009. Result of this study reveals that economic factor is more significant than political and institutional factors in BRICS countries. Hence market size is measured by real GDP and it is a significant determinant of FDI inflow.

Researcher Agarwal (2013), examines the relationship between FDI and economic growth (GDP) of BRICS countries for the period 1989 to 2012. He uses co integration and causality analysis at panel level. Causality tests indicate that there is a long run causality running from FDI to economic growth in these economies. Laskar (2015), conduct a study on FDI and Trade for determining the determinants of those on BRICS countries. She has taken various independent variables such as GDP, GDP Growth, and distance between host and source country, population of host country. Gravity Model is used for this study. Study reveals

that bilateral trade and FDI flows are positively related with market size and negatively related with the distance between the countries.

III. RESEARCH GAP AND OBJECTIVE OF THE STUDY

Previous section depicts the research on different areas of foreign direct investment. As per above researchers findings, FDI act as a important vehicles for generates Gross Domestic Product, enhance productivity growth, mobilize technology, expansion of trade, development of human resources, boost up learning procedure etc. They highlight these results by conducting studies on different countries. This may be on a single country or OECD countries or ASEAN countries or European countries.

Inflow of FDI depends on some factors. Researchers prove it by using different statistical techniques on different relevant data. They highlight different factors which create impact on inflow of FDI. Factors are real exchange rate, individual income, development cost of country, capital abundance, labour abundance, educational difference, rate of return, corporate tax, tax treaty, cost of political conflict, regional trade agreement, Market size, Trade openness, natural resources, Political stability/no violence, Macroeconomic stability , Government effectiveness, control of corruption, regularity quality, voice and accountability, rule of law, GDP, GDP Growth, and distance between host and source country, population of host country etc.

It seems to clear from above discussion there is limited studies which cover the analysis of factors on inflow of FDI. But there is very limited studies on inflow of FDI which relates with only India and Brazil (two developing BRICS country of two continents). As well as which reflect the effect of Human Development Index (HDI), Corruption Perception Index (CPI), Global Peace Index (GPI), Global Terrorism Index (GTI), Market Size (i.e. population), Unemployment Ratio, Inflation Rate and industrial disputes on inflow of Foreign Direct Investment. Objective of the present study is to measure and analysis the effect of these above eight factors on inflow of Foreign Direct Investment of two BRICS countries (i.e. India and Brazil) separately and combined form.

IV. HYPOTHESIS DEVELOPMENT

i) Human Development Index:

The Human Development Index (HDI) is a summary composite index which measures a country's average achievements in basic three aspects of human development i.e. health, knowledge, and income (Reyles, 2011). It is a more comprehensive welfare outcome of a country (Lehnert, Benmamoun, & Zhao, 2013; Sharma & Gani, 2004). HDI is developed through various ways. Foreign direct investment is affected by it (Agosin and Machado, 2005; Al-Sadig, 2013). Researchers Reiter & Steensma, (2010) suggest that Human Development has a positive but small effect on FDI. Hence, following hypothesis can be drawn from this discussion:

H_1: *There is a positive relationship between Foreign Direct Investment and Human Development Index.*

ii) Corruption Perception Index:

Corruption has a negative impact on foreign direct investment inflows (Hines,1995 and Wei,2000). Smarzynska and Wei (2000) suggest that corruption makes local bureaucracy, reduces transparency; hence foreign direct investors are less interested to invest in corrupted country. So generally it is expected that corruption creates a negative impact on FDI. Hypothesis of this determinant can be depicted as follows:

H_2: *There is a negative relationship between foreign direct investment and corruption perception index.*

iii) Unemployment Ratio:

This ratio implies percentage of unemployed person to total population. It has an important impact on trade policy. Dutt et.al. (2009) argue same investigation that, development of trade and unemployment ratio negatively related to each other. Moreover, unemployment and cost for labour negatively related to each other. Enhancement of unemployment reduces wages per hour of labour (Wiczer and Eubanks, 2014**).** Generally, foreign direct investors are more attracted in those countries where labour cost is cheap. This explanation helps to draw the following hypothesis.

H_3: *There is a positive relationship between unemployment ratio and inflow of foreign direct investment.*

iv) Market Size (Population):

Market size has a positive impact on trade development (Lehmijoki and Palokangas,2010). Generally requirement and development of trade simultaneously increases with population growth i.e. growth of market size (Melitz, 2003). It is expected that Foreign Direct Investment varies with the variation of population of country. Hence these arguments can be used as based for determining the following hypothesis.

H_4: *There is a positive relationship between market size and inflow of FDI.*

v) Global Peace Index:
Environmental stability and peacefulness generates trade friendly economic policy (Copeland and Taylor, 2013). Deepness of peace of any country is measured through Global Peace Index (GPI). Hence, it is expected that inflow foreign direct investment depends on country's peacefulness and economic stability. These explanations clear the following hypothesis.
H$_5$: *There is a positive relationship between Global Peace Index and inflow of foreign direct investment.*

vi) Global Terrorism Index (GTI):
Terrorism is the use of violence or threat of violence in order to purport a political, religious, or ideological change (Wikipedia). Intention of terrorism activity measures through **Global Terrorism Index** (GTI). It is an attempt to systematically rank the nations of the **world** according to **terrorist** activity (Fandl, 2003). This activity in a country creates direct negative impact on trade (Nitsch and Schumacher, 2003). Researcher S.W.Polachek (2004) also examines the negative relationship between trade and terrorism activities. It can be concluded that, inflow of FDI is negatively affected by Global Terrorism Index. Following hypothesis can be drawn from the above discussion.
H$_6$: *There is a negative relationship between Global Terrorism Index and inflow of FDI.*

vii) Inflation Rate:
Inflation can be defined as a sustained increase in the general level of prices for goods and services. It is measured as an annual percentage increase. As inflation rises, every dollar you own buys a smaller percentage of a good or service (Wikipedia). High rate of inflation creates many economical problems and hurt the growth of economy. It also slows down the economic growth (Ashra, 2002). In case of highly inflationary situation trade development is dismissed (Ramzan et.al.2013). Hence, it can be argued that highly inflationary condition is unfavorable for inflow of FDI.
So, hypothesis for this element can be drawn as follows.
H$_7$: *There is negative relationship between inflation rate and inflow of foreign direct investment.*

viii) Industrial Disputes:
Industrial dispute reduces country's growth and development (Arputharaj & Gayatriraj, 2014). Generally it also reduces the inflow of FDI. hence following hypothesis can be drawn for this element.
H$_8$: *There is negative relationship between industrial disputes and inflow of foreign direct investment.*

V. DATA AND RESEARCH METHODOLOGY:
Part-I
Data collection
In this study 10 years data (2005 to 2014) are used for empirically examine the above hypothesis. Data for this study are collected from the website of International Monetary Fund (IMF). Others related information are collected from official website of UN, ILO etc.

Part-II
Measurement of Variables:
Here two type variables are considered, namely dependent variable and independent variable. These are as follows:

Dependent Variable:
Inflow of Foreign Direct Investment is taken as dependent variable. Ten years data of two countries varies from one to another year.

Independent Variable:
We are considered eight independent variables for this study and logically these are established in the previous section. These independent variables are calculated in different ways.

Part III
Calculation Techniques of Variables:
Human Development Index:
The Human Development Index (HDI) is a combined measure of average achievement of key dimensions of human development i.e. a long and healthy life, being knowledgeable and have a decent standard of living. The HDI is the geometric mean of normalized indices for each of the three dimensions (Human Development Report). Higher score indicates higher development of human life.

Corruption Perception Index:
The *Corruption Perceptions Index is the result of public sector survey. It* measures the perceived levels of public sector corruption in countries worldwide. It based on expert opinion; countries are scored from 0 (highly corrupt) to 10 (very clean). Some countries score well, but no country scores a perfect 100. (Petrobas, 2012).

Unemployment:
Unemployment refers to the share of the labor force that is without work but available for and seeking employment. Unemployment ratio calculated on total labour force.

Market Size (i.e. Total Population):
Market size means total population of the country. This total population is considered as prospective market.

Global Peace Index:
Higher value of this index represents high peace and vis-a-vis. Value of this index varies from 0 (Zero) to 1 (one). The index gauges global peace using three broad themes: the level of safety and security in society, the extent of domestic and international conflict, and the degree of militarization (Wikipedia).

Global Terrorism Index:
The Global Terrorism Index (GTI) is an attempt to represent systematic rank the nations of the world according to terrorist activity. The index combines a number of factors associated with terrorist attack. Higher value of this index provides high terrorism activity and vis-à-vis. It varies between zero (0) to one (1) (Wikipedia).

Inflation: Inflation rate is calculated by using consumer price index. It reflects the annual percentage change of consumer price index to average consumer price index for goods and services that may be changes or fixed. The Laspeyres formula is generally used for calculation of inflation rate.

Industrial Dispute: According to Section 2 (k) of the Industrial Disputes Act, 1947, the term 'industrial dispute' means "any dispute or difference between employers and employers or between employers and workmen, or between workmen and workmen, which is connected with the employment or non-employment or the terms of employment and conditions of employment of any person. Year wise number of Industrial Disputes is considerable here.

Part: IV
Methodology:
The following multiple regression models have been estimated to investigate the impact of Human Development Index, Corruption Perception Index, Unemployment Ratio, Population (i.e. Market Size), Global Perception Index, Global Terrorism Index, Inflation Rate on Inflow of FDI for five BRICS countries separately. Logarithm is implemented both side for calculation purpose.
Multiple Regression Models are derived by the following way:
$LFDI_{inf} = \beta_0 + \beta_1 L\ HDI + \beta_2 LCPI + \beta_3 LUR + \beta_4 LP + \beta_5 LGPI + \beta_6 LGTI + \beta_7 LIR + \beta_8 LID + \square$
This model is implemented on two countries separately and gets the following results.
Description of variables are presented in table no.1

Table No.1

Variable	Description
$LFDI_{inf}$	Log of Inflow of Foreign Direct Investment.
LHDI	Log of Human Development Index.
LCPI	Log of Corruption Perception Index.
LUR	Log of Unemployment Ratio.
LP	Log of Total Population.
LGPI	Log of Global Perception Index.
LGTI	Log of Global Terrorism Index.
LIR	Log of Inflation Rate.
LID	Log of Industrial Disputes

VI.   EMPIRICAL RESULT ANALYSIS:

Part-I
Country wise Analysis

Result of multiple regression analysis for two countries discussed as follows:

India:
Results of Descriptive Statistics are provided by the table no 9. Average FDI inflow in India is 10.4113. Standard deviation is .21734; diversity from mean point is 10.19396 (i.e.10.4113-.21734). This value indicates that data set of inflows of FDI are not very closure to the mean value. Values of other variables vary from one year to another year.

Table No.2

Descriptive Statistics			
	Mean	Std. Deviation	N
FDI_IN	10.4113	.21734	10
HDI	1.7368	.04321	10
CPI	.5290	.03396	10
Unemployment	7.6671	.02471	10
Market_Size	9.0865	.01810	10
GPI	.3897	.01757	10
GTI	.8891	.01471	10
Inflation_Rate	.9015	.14223	10
Industrial_Dispute	2.5799	.11216	10

Regression Table of India signifies the effect of following seven variables on FDI inflow. Hence HDI, -.734 indicates one percent enhancement of HDI decrease 7.34% percent of FDI inflow and vis-a-vis. Same way 1% increase in CPI helps to increase 15.14% of FDI inflow and vis-à-vis.

Table No.3

Regression Table

Model	Beta	t	Sig.
(Constant)		1.342	.408
HDI	-.738	-1.659	.345
CPI	1.514	3.430	.181
Unemployment	.481	2.078	.286
Market_Size	-.993	-1.295	.419
GPI	2.617	4.109	.152
GTI	-1.760	-3.496	.177
Inflation_Rate	.859	2.402	.251
Industrial_Dispute	-.205	-.817	.564

Result of regression model for India shows coefficient value of Hypothesis 1 (H_1), H_2, H_4, H_7 are not satisfied. Another side H_3, H_5, H_6 and H_8 are satisfied by the coefficient value. But these are not significant. In case of India unemployment is an effective factor for enhancement of FDI inflow. Table no.4 shows the fitness of regression model.

Table No 4

Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.994[a]	.988	.892	.07151

Hence, adjusted R^2 is 89.20% indicates that it is good-fit of regression equation. Another side, it is identified that sample factors have more effect on inflow of FDI rather than other factors which is represented by following ANOVA (Table No.5) table:

Table No.5

ANOVA[a]						
Model		Sum of Squares	Df	Mean Square	F	Sig.
1	Regression	.420	8	.053	10.268	.237[b]
	Residual	.005	1	.005		
	Total	.425	9			

Hence, sample factors of this study are accurate than others factors because, regression value is .420 which covers 98.82% (Approx) of total value and residual value is .425 i.e. 1.18% of total value. So, it can be said that all sample factors affect the inflow of FDI.

Brazil:

Results of Descriptive Statistics show by the table no 6. Average FDI inflow in Brazil is 10.6686. Standard deviation is .26820; diversity from mean point is 10.4004 (i.e.10.6686-.26820). It indicates that values of data set of inflows of FDI are not very closure to the mean value. Values of other variables vary from one year to another year.

Table No.6

Descriptive Statistics			
	Mean	Std. Deviation	N
FDI_INFLOW	10.6686	.26820	10
HDI	1.8216	.04652	10
CPI	.5728	.03494	10
Unemployment_Ratio	7.1681	.04848	10
Population_Size	8.2955	.01296	10
GPI	.3151	.00748	10
GTI	1.7953	.71260	10
Inflatio_Rate	.7312	.08960	10
Industrial_Dispute	2.5799	.11216	10

Regression Table of Brazil signifies the effect of following seven variables on FDI inflow. Here HDI, 0.276 indicates one percent enhancement of HDI increase 27.6 percent of FDI inflow and vis-a-vis.
Regression Table

Table No.7

Model	Beta	t	Sig.
(Constant)		.700	.611
HDI	.276	.503	.704
CPI	.548	.844	.554
Unemployment_Ratio	-.880	-2.069	.287
Population_Size	-.434	-.438	.737
GPI	-.689	-1.380	.399
GTI	.534	1.272	.424
Inflatio_Rate	-.737	-1.497	.375
Industrial_Dispute	-.902	-1.450	.384

Coefficient values of all variables are but these values not satisfy all hypothesis. Hence, Hypothesis (H_1) 1, H_7 and H_8 are satisfied by the above results but results prove that H_2, H_3, H_4, H_5 and H_6 are not true. Result shows that enhancement of unemployment ratio reduces inflow of FDI and vis-à-vis. It also reflected through this result that higher Inflation rate decreases inflow of FDI and vis-à-vis.
Table no.7 shows the fitness of regression model.

Table No 7

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.987[a]	.975	.771	.12823

Hence, adjusted R^2 is 77.1% indicates good-fit of regression equation. Table no 7 shows this result. Another side, it is identified that sample factors have more significant effect on inflow of FDI rather than other factors which is represented by following ANOVA (Table No.8) table:

Table No. 8

ANOVAᵃ						
Model		Sum of Squares	df	Mean Square	F	Sig.
	Regression	.631	8	.079	4.796	.340[b]
	Residual	.016	1	.016		
	Total	.647	9			

So, sample factors of this study are more accurate than other because, regression value is .631 which covers 97.53% (Approx) of total value and residual value is .016 i.e. 2.47% of total value. Hence, all sample factors affects the inflow of FDI.

VII. CONCLUSION

It can be concluded that all variables have been created an effect on inflow of FDI. All sample determinants during the study period (2005 to 2014) create effect on FDI inflow but there is no significant impact. Out of eight hypotheses only four are satisfied by the sample data of India and three are satisfied by the

sample data of Brazil. Hence unemployment ratio, Global Peace Index, Global Terrorism Index and Industrial Disputes rate of India influences FDI inflow in right way. Another side Human Development Index, Inflation Rate and Industrial Disputes of Brazil influence FDI inflow in right way.

This paper clears that all determinants have not similar effect on FDI inflow for all countries. Moreover intensity of effect varies from one to another country. It can be concluded that one determinant is responsible for FDI inflow of all countries.

The result of this study is the signal about the importance of some determinants on FDI inflow. However it would be better to take study with bigger sample in terms of country, variables and period before generalization of result.

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