The Role Of A Country’s Infrastructure In Encouraging Inward Foreign Direct Investment

Introduction

By definition, an inward investment involves an external or foreign entity either investing in or purchasing the goods of a local economy. It is foreign money that comes from another country. In other words, foreign direct investment (FDI) refers to an interest in or the acquisition of foreign assets with the goal to control and oversee them. Organizations can make an FDI in a few different ways, including buying the advantages of an outside organization; putting resources into the organization or in new property, plants, or gear; or partaking in a joint endeavor with a remote organization, which normally includes speculation of capital or ability. On the other hand, infrastructure can be defined as the basic physical and organizational structures and facilities of a country. The purpose of this paper is to discuss the role of a country’s infrastructure in encouraging inward foreign direct investment in developing countries and Malaysia as a case study, in my opinion, a country’s infrastructure plays a significant role in encouraging FDI and with some points, I would like to explain why.

How governments encourage FDI

Governments look to encourage FDI when they are anxious to grow their domestic economy and pull in new technologies, business know-how, and capital to their nation. On these occasions, numerous governments despite everything attempt to manage and control the type, quantity, and even the nationality of the FDI to accomplish their domestic, monetary, political, and social objectives.

Financial incentives: Host countries offer organizations a blend of tax incentives and loans to invest in. Home-country governments may likewise offer a mix of insurance, loans, and tax breaks with an end goal to promote their organizations' oversee investments. The initial case of China in Africa illustrated these sorts of motivating forces.

Infrastructure (main focus of this research): Host governments improve or upgrade local infrastructure—in energy, transportation, and communications—to encourage explicit enterprises to contribute. This likewise serves to improve the local conditions for domestic firms.

Administrative procedures and regulatory environment: host-nation governments smooth out the way toward setting up workplaces or creation in their nations. By decreasing administration and administrative conditions, these nations show up increasingly alluring to remote firms.

Invest in education: Nations try to improve their workforce through instruction and occupation preparation. An informed and talented workforce is a significant speculation rule for some worldwide organizations.

Political, economic, and legal stability: host-nation governments try to promise organizations that the neighborhood working conditions are steady, straightforward (i.e., strategies are obviously expressed and in the open area), and improbable to change.

Why infrastructure encourages FDI

The main contribution of FDI to the economic advancement of a nation has been well recognized in the literature. FDI plays a significant role in the economy as it pushes for economic growth by adding domestic capital formation and facilitates the transfer of new technology. Among the huge literature on FDI, few researchers have acknowledged the importance of infrastructure together with other determinants to encourage FDI. Those researchers argue that investors look for markets in which they can get the maximum benefit and lower the cost of production, they illustrated that this can be achieved if the infrastructure is in good conditions and are supportive to investors.

Usually, a country with good physical infrastructures such as highways, ports, bridges, and communications, and so on, will most likely attract more FDI. Coughlin et al. (1991) in their research, analyzed factors that affect the inflows of FDI into the US for a period of 1981-1983. They found that more extensive transportation infrastructures were associated with a high level of FDI. Wheeler and Mody (1992) also found in their study that infrastructure quality is an important factor for developing countries trying to attract FDI from the United States; on the contrary, it is less crucial for developed countries that already have a high quantity of infrastructure.

Advantages of foreign direct investment

- Capital inflows make greater outputs and jobs.
- Capital inflows can help fund a current account deficit.
- Long-term capital inflows are more maintainable than short term portfolio inflows.
- Beneficiary nation can profit by improved knowledge and ability of foreign multinational.
- Investment from abroad could prompt higher wages and improved working conditions,

Potential Problems of Foreign Direct Investment

- Gives multinationals controlling rights within foreign countries. Critics argue powerful MNCs can use their financial clout to influence local politics to gain favorable laws and regulations.
- FDI may be a convenient way to bypass local environmental laws. Developing countries may be tempted to compete on reducing environmental regulation to attract the necessary FDI.
- FDI does not always benefit recipient countries, as it enables foreign multinationals to gain from ownership of raw materials, with little evidence of wealth being distributed throughout society.
- Multinationals have been criticized for poor working conditions in foreign factories (e.g. Apple's factories in China)

Foreign direct investments in developing countries

Direct foreign investments have extended consistently in the course of recent decades. The development in FDI quickened during the 1990s, ascending to $331 billion every 1995 and $1.3 trillion out of 2000 (UNCTAD, 2002). Subsequently, developing countries encountered a sharp increase in the average ratio of FDI to add up to investment during the 1990s. A principal component of the development in FDI has been the rise in foreign investments in the administration division, which is currently the prevailing part of worldwide FDI. For developing countries, FDI in service expanded at a yearly pace of 28 percent over the period 1988 to 1999, and by 1999 represented 37 for each cent of all-out outside speculation inflows.

A significant part of the rise in foreign investments in the service sector has been the development of private capital streams for infrastructure, in light of the general trend towards privatization of infrastructure in developing countries. Conversely, there was a sharp decline in benefactor support for infrastructure projects during the 1990s, with total flows of official development assistance for the infrastructure segment divided over the span of the decade (Willoughby, 2002). Private area support in framework extends in developing countries has risen significantly since 1990 and yearly speculation duties arrived at a pinnacle of $128 billion every 1997. As indicated by the World Bank's Private Participation in Infrastructure (PPI) database, 26 nations granted 72 infrastructure projects with private cooperation in 1984-89, pulling in nearly $19billion in speculation responsibilities. In the 1990s, 132 low-and center salary nations sought after private investment in infrastructure – 57 of them in three or every one of the four of the areas canvassed in the database (transport, vitality, broadcast communications, and water and sewerage). In 1990-2001 developing countries moved to the private area the working danger for right around 2,500 infrastructure projects, drawing in speculation duties of more than $750billion.

Malaysia as a case study

Malaysia has been one of the most successful Southeast Asian countries in pulling in foreign direct investments; Malaysia has consistently attempted to keep up the intensity of FDI determining factors, where numerous strategy instruments have been set up by the Malaysian government to draw in FDI. In the wake of being an independent state, Malaysia has taken advantage of both tangible assets like natural resources, abundant labor, and intangible assets like trade status under a generalized system of preferences (GPS), microeconomics stability, to draw In FDI. The needs of logistics and communications inside the country's boundary have likewise been carried out, for example, the PLUS-highways and KTM railways are both linking the major town. Less expensive ports services in southern Johor and Klang, and budget airline services are likewise available. As far as communication, there are 95% area coverage in peninsular and 77% area coverage in east Malaysia. World investment report (2008). With all the physical infrastructure gave, they can pull in more FDI inflows to Malaysia

Conclusion

In conclusion, this paper discusses the role of infrastructure in pulling in foreign direct investments inflows to developing countries as well as other contributing factors; the reason for focusing on developing countries is that the impact of infrastructure investments is greater in developing countries than that of the developed countries, it has been found that infrastructure has a significant and positive impact on FDI inflows in Malaysia, although there are still other contributing factors, infrastructure still plays a significant role in attracting FDI.