

## The effects of foreign direct investment on the host country

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### Abstract

A corresponds to any flow of foreign direct investment (including loans) granted to foreign companies, provided that residents investing country (in general - enterprise) have an important part of this business property. It is distinguished from short baths capital movements. Direct investment involves mobilization of capital transferred abroad. For this reason, the national statistical departments groups, often under the term direct investment, purchases of shares and long-term loans to the same group of companies that contribute to the industrial capital of the lending company, ie its production capacity.

**Keywords:** foreign direct investment, balance of payments, Monetary Fund

### 1 Introduction

The concept of direct investment aims to deliver a technically defined strictly understood as an acquisition of securities. According to the definition given by the International Monetary Fund in 1977, the Balance of Payments Manual, foreign direct investment "means an investment that aims to acquire a lasting interest in an enterprise operated in a country other than the investor, for the latter influence the actual management of the undertaking concerned"<sup>1</sup>.

Is considered to be a direct foreign investment, foreign investors should have 10% or more of the common shares or voting rights in an enterprise. Thus, once the firm invests at least 10% holding company foreign direct investment includes any investment, be it a new purchase or a simple loan.

I think Romania should, where possible, to ensure domestic needs without resorting to imports, the efficiency of resource investments taking into account the correction of these resources to productive Romanian companies to develop local potential, so that accumulation of capital to produce the country's borders, be kept and used by it.

Also "establish an appropriate ratio between the share of resource allocation to the investment objectives that will contribute to the country's economic revival term generating long-effect in terms of future investment and resource allocation share for targets that do not generate propagated effects in the investment plan, but which are socially necessary"<sup>2</sup>.

In one of his books, French economist P. Joffre says that foreign direct investment by international capital flows is an enterprise in one country creates or develops a subsidiary in another country.

Such an increase direct foreign investment in production capacity abroad, through its subsidiary. The distinguishing feature of direct foreign investment is that it involves not only

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<sup>1</sup> PHLindert-International Economics, Economic Publishing House, Paris, 1997.

<sup>2</sup> Vesca IC, Resource Efficiency Investment, Annals of University "Eftimie Murgu" in Resita Section regional economic development, Ed Eftimie Murgu, 2008

a transfer of resources, but is accompanied by another decisive element: control and power purchase decision on the company investing assets of value added by virtue of a long interest shown by this term. This branch is not just financial obligations in relation to the parent, but it belongs to one and the same organizational structure.

Subsidiary company controlled by the parent receives from it, frequently and directly inputs such as different techniques, trade secrets and various instructions, the use of intellectual property rights, management rules and Intangible assets other type. Consequently, direct investment is not only a movement of capital, direct investment flows, regardless of their destination, is the sum of:

- Net capital contributions provided by investors in the form of acquisition of shares, capital increase or creation of new enterprises;
- Net loans, including loans or advances on short term of the parent to its subsidiary;
- Undistributed profits and reinvested.

The need for capital investment amounting to a level far beyond the current economic condition requires resorting to capital objective of attracting foreign direct investment as capital, a common characteristic of all former communist states. Thus, in this respect is already an interest of both parties, both from investor and foreign capital and domestic investors from.

The imminent integration of countries in Eastern and Central Europe with the Western European Union, driven by strategic interests of both parties, requires the expansion of international cooperation with other countries, especially those developed and accelerating the transition to market economy, open horizons to real international cooperation.

In fact, immediately after the collapse of the socialist system, the countries of Central and Eastern Europe such as Hungary, Poland and former Czechoslovakia, and Bulgaria and Romania have initiated various steps for certain actions such as regional cooperation between countries bordering the Black Sea, creating border economic zones, etc. They also passed at the request of understanding with the European Community, with which signed association agreements or FTAs.

The force required to accelerate this process of transition to market economy and accession to the European Union lies only in the availability of capital. Aware, in turn, that the main obstacle they have to face is the lack of transition states and capital, respectively, private investment, production and services, Western European countries show great interest in financial aid economies in transition.

The transition to a market economy is characterized in all the Eastern and Central European economies to national instability, economic decline, the real crisis of capital and dangerously low rate of investments, especially those productive. Virtually all national economies in transition are marked by deep imbalances due to the decrease in labor productivity and time actually worked, and union pressure on wages and declining management capacity of the new leadership team.

The high rate of interest, which in recent years Romania was among the first countries in transition, was a leading cause of reducing propensity to invest. In these circumstances each national economy is evident inability to cope with the former communist alone equity absolute need to ensure a minimal growth. The need for foreign capital lies, then, precisely in their inability to ex-communist national economy to meet the need, even minimal capital investment recovery, which, if continuing rebound in the years immediately after 1990, likely

to throw these economies in total dependence on the developed world, with serious consequences in the medium and long term.

On the other hand, this need for foreign capital is enhanced and more lagging behind the technological level of industrial production facilities and countries in transition.

## **2 EFFECTS OF FOREIGN INVESTMENTS ON HOST COUNTRY**

Governments must decide by their actions at the national investment policy, which is why their national territory, governments may limit or prohibit direct investments in certain sectors and also different ways to regulate the operations of foreign companies, the to require local participation in new activity, the training of personnel, procurement of components of national origin, common research, access to markets, etc.

Currently, we are witnessing a "yard" hard that many governments do multinational companies, offering various forms of subsidies to encourage them to locate their operations in the country. Basically, now the competition has shifted from firms to the government, which compete in granting substantial incentives to influence foreign investors to choose their countries as multinational location.

Effects on the host country are not necessarily symmetrical with those exerted on the country of origin, in addition, they will not have the same impact as the host country.

Effects on economic activity can be considered, a priori, as good as foreign investment stimulates production, employment and development. By adding new activities or by increasing production companies taken over, and increase national production, Thus, the overall pace of economic growth can accelerate. Direct contribution of foreign saving increases domestic investment opportunities, encouraging growth in the medium-term, often contributing and improving labor productivity due to new knowledge and techniques available to the receiving nation, without additional expenses on its part. Resource allocation is improved, to the extent that foreign firms invest, normally in areas where the nation has a comparative advantage that it could not exploit enough, usually because of low domestic saving potential. Consequently, the overall economic efficiency should increase, in turn, competition could be stimulated by the entry of new producers in the sector, which could lead to a regrouping c ear of local firms.

However, in comparison with local competitors, "the foreign subsidiary is in a privileged position: it benefits from a lower cost and direct access to technical knowledge of the parent company, in part to its resources, better conditions Credit local and international financial markets (the parent company guarantee) usually, it may have managerial skills, marketing or organizational multinational company. But all these are more difficult to adapt national local companies "

On the other hand, multinational companies, seeking to plant a new production unit in a country accepts more easily than national firms to locate in regions in difficulty or whose development is a priority because they can more easily avoid various trade barriers, seeks to take maximum advantage of available public aid and rely primarily on an economic calculation that advantage-Costin their bargaining power allows them to increase benefits (subsidies) and reduce costs. Then, implantation of a new company that allows the host country, while, to increase tax revenues, at least insofar as the tax relief granted is not systematic.

At the same time reducing the risk of receiving the nation's independence and autonomy cannot be ignored, since the policy of increasing production and subsidiary is defined as

mother company interests, interests that may not converge with those of the nation. The codes and investment agreements, the UN and OECD do tend to define and to respect the rules accepted by the company and the nation, although apparently no reasons why a company would sabotage an installation cost on economic grounds.

Effects on balance of payments, the positive effects (entry of foreign currency) are primarily due to capital inflows through acquisition or construction of facilities, hiring staff initially paid by the parent company (as long as NUA branch developed its production activities and sufficient sales to self-financing his expenses) as a result, the trade balance will record exports branch (even at cost of transfer to the parent company) and possibly reduce imports manufactured good from now, locally.

The negative effects are related to the repatriation of dividends, purchase of machinery, parts, intermediate goods imported to ensure its production subsidiary, to pay dividends, royalties paid for the right technology. In general, it is difficult to make overall judgments allowing to say a priori that the host country always benefit or lose in a systematic way with the implementation of a branch of foreign companies, to establish such a court should be able to compare the situation nine with the presence of foreign subsidiary, the situation would have known that a country without direct investment, which is considered to be impossible.

Criticism of foreign direct investment start from the fact that direct investment has negative effects on the balance of payments on short-term investor friendly country in the long term.

From the viewpoint of the host countries, direct investment is considered to be "expensive". A small investment that has weak effects on balance of payments in the early years, is transformed by "game" reinvestment in a company whose returned income (dividends, salaries) can become substantial<sup>3</sup>.

As a fundamental principle, the direct investment that brings high profits is a sign of very weak balance between supply and demand, therefore, the market would be that new "players", so that offer profits to rise until reaching a normal level.

These positive and negative effects on economic activity and balance of payments of the host country will be found, the more nuanced way, the economy, developing countries in which the situation and Romania. Their economic instability may prevent you from benefiting from the favorable effects of implantation of a subsidiary in their territory, and instead to strengthen the unfavorable.

Developing countries generally have a dual economy and disjointed, which makes the development of the subsidiary may not be passed only on the overall economy and weak, some of the effects of domestic product growth of the branch to be transferred to foreign suppliers not for national activities in the upstream production process, there is not such a juxtaposition and interdependency between the "modern" and the branch to which it belongs "traditional" of developing countries

Moreover, the choice of technology and is based on factors of constraints weighing on the economy of the country of origin and, of course, inadequate to the host country factor endowment: appropriate technology would allow a lower employment use of a capital insufficient but the cost of adapting their research or multinational company is excessive.

Due to the relative size ratio of developing countries and multinationals, the host country may lose some of its sovereignty, its economic effectiveness and monetary policy, its development policy. It comes therefore to a situation where a limitation is desired for a multinational company to benefit from its implantation without excessive costs.

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<sup>3</sup> H. Henner - International Commerce, Economic Publishing House, Paris, 1992.

At present, however, host countries, developed or developing, are interested in attracting companies, that it was an auction in the system of subsidies and tax relief, the bargaining power of multinational companies back.

### **3 Conclusions**

Direct investment is a factor of economic development in countries succeeded in entering a surplus capital can be consciously directed benefit effects on macro-economic indicators of a country.

The role of direct investment is just so crucial for developing countries by some government facilities may need to raise capital development, development that benefits both in terms of human resources and in financial terms.

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