

DOI: <https://doi.org/10.36719/2663-4619/100/203-209>

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UNLOCKING THE POTENTIAL: STRATEGIES FOR BOOSTING FOREIGN DIRECT INVESTMENT

Abstract

This article explores the multifaceted strategies nations can employ to enhance their attractiveness to foreign direct investment (FDI). It analyzes global trends, identifies challenges and opportunities, and offers evidence-based solutions for countries seeking to attract and retain FDI.

Through a comprehensive review of literature and global case studies, this work highlights the critical role of policy frameworks, economic stability, regulatory environments, and infrastructure in influencing FDI flows.

In the context of global competition for investment, it is imperative for countries to adopt comprehensive approaches that not only lure but also retain and expand foreign investor participation. The article encompasses an analysis of global experiences, identifying both successful strategies and common challenges. Solutions to overcome these challenges are proposed, highlighting the role of policy reforms, infrastructure development, and the fostering of a stable economic and political environment.

Keywords: *FDI, investment, strategy, solution, problem, global*

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Potensialın açılışı: birbaşa xarici investisiyaların artırılması strategiyaları

Xülasə

Bu məqalə dövlətlərin xaricə birbaşa investisiyalar (XBİ) üçün cəlbediciliyini artırmaq üçün istifadə edə biləcəkləri çoxşaxəli strategiyaları araşdırır. O, qlobal tendensiyaları təhlil edir, çətinlikləri və imkanları müəyyən edir və XBİ-ni cəlb etmək və saxlamaq istəyən ölkələr üçün sübuta əsaslanan həllər təklif edir.

Ədəbiyyatın və qlobal nümunələrin hərtərəfli təhlili vasitəsilə bu iş siyasət çərçivələrinin, iqtisadi sabitliyin, tənzimləyici mühitin və infrastrukturun XBİ axınlarına təsir göstərməkdə mühüm rolunu vurğulayır.

İnvestisiya uğrunda qlobal rəqabət kontekstində ölkələrin xarici investorların iştirakını yalnız cəlb edən deyil, həm də saxlayan və genişləndirən hərtərəfli yanaşmalar qəbul etmələri zəruridir. Məqalə həm uğurlu strategiyaları, həm də ümumi problemləri müəyyən edən qlobal təcrübənin təhlilini əhatə edir. Siyasi islahatların, infrastrukturun inkişafının və sabit iqtisadi və siyasi mühitin dəstəklənməsinin rolunu vurğulayan bu problemlərin aradan qaldırılması üçün həll yolları təklif olunur.

Açar sözlər: *XBİ, investisiya, strategiya, həll, problem, qlobal*

Introduction

In recent years, it has become clear that geopolitical tensions have transformed Foreign Direct Investment (FDI) regulation into a global and growing trend. United States-China tensions, as well as the effects of Russia's invasion of Ukraine, have had an impact on the foreign direct investment

screening process, with countries taking strategic measures to protect their national interests while balancing the demands of an open economy. This increase in foreign direct investment screenings since 2020 has led to a significant increase in the workload of competition lawyers and regulatory authorities in particular.

Foreign Direct Investment (FDI) has emerged as a pivotal source of economic development and industrialization for countries worldwide. Its benefits extend beyond capital influx, fostering job creation, technological advancement, and the development of a competitive business environment. However, attracting FDI requires more than passive policy frameworks. This article delves into the essence of unlocking a country's potential to attract and sustain FDI through strategic initiatives and reforms.

Of course, there is no single type of foreign direct investment. Foreign direct investment is categorized as horizontal, vertical, and conglomerate. Horizontal direct investment refers to investment in a foreign company that has the same type of business operations as the field in which it operates in its home country. For example, a foreign mobile phone manufacturer opened a branch of its store operating in China in the USA.

Vertical direct investment refers to the investments made by investors that are different from their main activity but still related to the main activity. For example, a manufacturing company may receive investment from a foreign company to provide the necessary parts for the manufacturing process or the raw materials it needs.

Conglomerate-style foreign investment is an investment made by a company or individual in a company that is not related to its existing business in its own country. In this type of investment, since the investor enters a sector in which he has no previous experience, the investment takes the form of a joint venture with an already operating foreign company.

Market size is measured by the gross domestic product per capita of the host country. The market volume hypothesis supports the view that a large market is necessary to benefit from economies of scale and use resources effectively (Eiteman, 2001: 96).

There is a strong relationship between foreign direct investments and market size. Because a sufficiently large market provides the company with a satisfactory sales level and, accordingly, the company increases its investments in that region. Companies generally prefer to invest in large markets to benefit from their assets at an optimal level (Asiedu, 2002: 110).

Labor costs are of great importance, especially for foreign investments in labor-intensive industries and for branches established for export purposes. Companies engaged in labor-intensive production will want to invest in regions where cheap labor is available to ensure profit realization. Since the level of unionization in a country creates an obstacle to low wages and administrative freedom, it negatively affects foreign direct investment flows.

However, in cases where labor costs are relatively insignificant and wage differences are very small from one country to another, the ability and productivity of the workforce are effective in foreign direct investment decisions.

Another important factor among the factors affecting direct foreign investments is the trade deficit. Torissi (1985) states that trade surplus is an indicator of a dynamic and healthy economy and therefore encourages foreign direct investments. Other studies conducted in this field have also revealed findings in the same direction. Frey (1985) and Hein (1992) pointed out that there is a strong positive relationship between trade surplus and foreign direct investment (Teng, Jinn, Chern, Maw, Kim, 2001: 63).

Technological Competitiveness.

A country's research and development capabilities and availability of skilled labor contribute highly to that country's competitive advantage for foreign direct investments. The excess of a country's R&D expenditures reveals that country's efforts in technological research, which has a great impact on foreign direct investments.

Countries that have technological capability can attract more investment than countries that do not have this capability.

Quality of Life.

Values such as literacy rate and the ratio of telephone, radio and car owners to the total population are taken into account as quality of life measures. The degree of urbanization of a country is simultaneously related to its industrial capacity and the standard of living of the population. These are both important factors for foreign investors (Moran, 2000: 297).

Geo-Cultural Distance.

Geographical proximity between countries has a significant positive effect on foreign direct investment flows by reducing transportation costs. Likewise, cultural closeness between the countries that are partners in the investment project (for example, French investments in Algeria, German investments in the Czech Republic) facilitates commercial transactions and reduces the degree of uncertainty.

In parallel, foreign direct investment flows are gaining momentum (Braunstein, 2000: 1160).

Political Risk.

Political risk for foreign investors covers fund losses resulting from possible expropriation, disruption of goods, services and labor, and political intervention. Political risk factors pose a different importance for foreign investors trying to enter developing countries.

Global Experiences.

The global landscape of FDI is marked by varied experiences, with some nations achieving remarkable success in attracting foreign investments, while others struggle. Countries like Singapore, Ireland, and the United Arab Emirates exemplify successful FDI attraction, attributed to their robust legal frameworks, investor-friendly tax regimes, and high-quality infrastructure. In contrast, nations grappling with political instability, bureaucratic inefficiencies, and inadequate legal protections often lag in attracting significant FDI (6).

The European Union (EU) has adopted a new regulatory framework to review merger and acquisition deals in 'red flag' sectors (defence, technology and infrastructure) as governments seek to strike a balance between maintaining an open economy and protecting public safety and national defense interests. has been made. After 18 out of twenty-seven European member states adopted the framework, many other European countries, including France, Germany, Italy and the Netherlands, have extended their FDI screening guidelines to other sectors such as consumer goods. This reflects the evolution of foreign direct investment from a niche for defense industry deals to a key part of many deal structures, timelines and regulatory risk assessments, and has been followed by a domino effect (Dunning, 1980).

Two years after Germany expanded its foreign direct investment regulatory regime in October 2020, new foreign direct investment guidelines have been published by France targeting cross-border investments within the EU. But more importantly, the Netherlands (which is the world's third largest recipient of foreign direct investment as of 2019) adopted two new foreign direct investment screening mechanisms applied to domestic and foreign investors; because this was perceived as the country's biggest break from its traditional free trade stance. These expanded screening mechanisms set the tone for subsequent and more serious foreign direct investment restrictions (Moran, Graham, Blomstrom, 2005).

Despite signs that foreign investment into Europe will rebound after the pandemic, the aftershocks of the war in Ukraine, weak economic growth, supply chain disruptions, high inflation and rising energy costs have played a role in the pause. During 2022, companies around the world announced 5,962 greenfield investment and expansion projects in 44 European countries. This represents an annual increase of just 1% compared to 5,877 projects in 2021. A growth of 5% was recorded in 2021. Investments are still 10% lower than the peak reached in 2017.

The 'C-suite' survey, which is part of the research, also reveals that 29% of participating companies postponed their planned investments as a direct result of the energy crisis. As a result of foreign direct investment, the total number of jobs created in Europe fell by 16% annually to 343,634. This decline is also an indication of the cautious approach of investors in an environment of uncertainty in European markets. Participating companies identified the three most important

risks affecting investment across Europe; rising interest rates (45%), high inflation (40%) and rapidly rising public debt levels (36%) (Wei, Shang-Jin, 2000).

The fact that 67% of the companies surveyed stated that they have plans to establish or expand operations in Europe next year shows that there is a margin of optimism. This is a sign that Europe has an important place in current and future business plans. However, expectations are high regarding the responses of both the EU and its member states to global competition (10).

Solutions to Enhance FDI Attractiveness.

Policy Reforms and Incentives: Implementing transparent and streamlined regulatory policies, alongside offering incentives such as tax breaks and grants, can significantly enhance FDI appeal. There must be leadership on climate change and ESG. The survey found that investors recognize the advantages of Europe's environmental leadership, with 61% finding Europe "more attractive" than its rivals when it comes to sustainability. As the EU Green Deal and the US Inflation Reduction Act have come into conflict in recent months, Europe should aim to further increase the share of renewable energy in its energy mix and improve access to decarbonised energy and avoid the US competitive challenge (Buckley, 2000).

Infrastructure Development: Investing in physical and digital infrastructure reduces operational costs and risks for foreign investors, making a country more attractive for investment.

Simultaneously, investment in R&D and production should be encouraged. The survey found that R&D is the top category for new investment in Europe over the next three years, with 64% of executives expecting to increase their R&D footprint in Europe. To realize this potential, policymakers must continue to encourage investment in high-tech, high-value activities that are reshaping the global economy.

Skilled Workforce: Education and vocational training programs can create a skilled labor pool, drawing in companies seeking talented personnel. New generation talents must be developed. While it is thought that artificial intelligence may greatly disrupt the labor market by 2030 and in a period when there are HR constraints in many geographies, the training of new generation talents in critical fields such as technology, energy, engineering, health or data science should turn into a competitive advantage for Europe (Edwin, Lai, 2001: 61).

Political Stability and Governance: Ensuring a stable political environment with effective governance and rule of law is crucial for attracting and retaining foreign investors. Tax and regulatory regimes must be modernized. Providing R&D tax credits, which is investors' top priority in tax policy in 2023.

Market Access and Economic Integration: Engaging in regional trade agreements and economic partnerships can provide foreign investors with broader market access, amplifying a country's attractiveness. Europe must be presented as a hub for the businesses of the future, sending a strong message to investors about how the continent can capitalize on its existing strengths, including R&D, intellectual property and advanced manufacturing.

Support for Small and Medium Enterprises (SMEs) should be strengthened. SMEs, which form the backbone of the European economy and half of its GDP, employ approximately 100 million people across Europe.

Problems and Challenges.

Countries face numerous challenges in attracting FDI, including but not limited to, political instability, corruption, inadequate infrastructure, and restrictive regulatory environments. Additionally, the global competition for FDI means that countries must continuously innovate and improve their value proposition to investors (Emery, Finnerty, Stowe, 1998).

In crafting this article, insights were drawn from a wide range of sources, including the World Bank's reports on FDI, the United Nations Conference on Trade and Development (UNCTAD) publications, and various case studies highlighting national strategies for FDI attraction. These sources provide a comprehensive overview of the factors influencing FDI flows and offer evidence-based analyses of policies and practices that have proven successful in various contexts.

With rising political tensions between China and the United States, there has been a significant decline in U.S. investor interest in Chinese stocks since record-breaking levels last year.

Trading in the most liquid U.S.-listed options, which track Chinese stocks and provide access to China without a presence abroad, has fallen sharply by more than 50% since reaching a record high in November. Moreover, foreign investors, who purchased a net worth of US\$20 billion worth of shares listed in Shanghai and Shenzhen in the first month of 2023 (setting another record), have since added only \$6 billion in the last three months. This dramatic slowdown in direct purchases of Chinese stocks is an indication that investors' confidence in this region is waning.

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Conclusion

Boosting FDI is not a one-size-fits-all solution; it requires a nuanced understanding of the global investment landscape and a country's unique advantages and challenges. By adopting a holistic approach that includes policy reform, infrastructure development, and the fostering of a stable and competitive business environment, countries can unlock their full potential to attract and benefit from foreign direct investment.

There are many alternatives for investors who want to operate internationally. Investors, who try to reduce the effects of the risks and uncertainty that come with doing business internationally as much as possible, first start their activities abroad with exports, continue with licensing agreements and complete this process by starting direct production abroad.

The main reason that drives international investors to foreign direct investment rather than other investments is the desire to adequately benefit from the sales potential of the products they produce.

Foreign direct investments, which have become one of the most important cross-border activities with globalization, support the effective use of limited resources in the world. While these investments increase the competitiveness of capital-exporting countries, they also contribute to economic growth, increased production capacity and exports, employment, technological development, the spread of innovative management and marketing methods, and improving the quality of the workforce in importing countries.

When multinational companies decide on direct foreign investment, they should also carefully analyze the country in which they will invest, in addition to evaluating the profitability of the investment. At this stage, in addition to reviewing the evaluation reports about the countries, they also have to take into account the political and economic stability in the country. Therefore, another duty of governments should be to determine the policies that will enable the creation of a political, economic and social environment that encourages investors, considering that many countries are competing to attract foreign investments. In addition, governments should try to determine the reasons behind the investment decisions of multinational companies in relation to their own countries and determine long-term strategies in this context.

During the development of the investment attraction policy, the existing obstacles and problems (they may be different in different areas) of both the demand and supply factors of the investment process should be revealed, the investment risks should be assessed, and the necessary steps to reduce and eliminate these obstacles and risks should be developed.

In order for the opportunities created by the decisions taken by the government and the numerous measures implemented to become real incentives, they should move the desires of people (business subjects, especially investors) and lead to changes in their behavior.

J. Nye, a professor at George Mason University, believes that, in addition to economic models, institutions in society and government policy should also be taken into account in matters of economic growth and development: "There is such a misconception that the presence of capital in a country is enough for growth: if there is capital, how is the country- will develop. However, the problem of economic growth cannot be solved simply by loading money. The most modern equipment and technology can be bought and brought to the country, but in most cases, the constituent elements of the existing institutional system in the country may not allow their effective use and development may not take place".

It is important that the implemented reforms are aimed at changing behavioral stereotypes that have a negative impact on investment decisions. D. Rodrik writes that "institutional reforms should change not only the parameters of the policy, but also the existing behavioral stereotypes that hinder development." Household behavior and investment decisions are changing in ways that are difficult to monitor and adjust without knowledge of the "deeper parameters" of the economy.

One of the forms of behavior that needs to be changed is the adoption by the government "behind closed doors" of decisions that directly affect the costs and revenues of the business (for example, changing tariff rates, canceling tax incentives, increasing the prices of energy carriers, as well as utility and other service tariffs, etc.) and therefore, the business suffers serious losses. The business cannot plan its activities properly because it cannot be informed about such decisions in time.

Long-term predictability of the business environment is very important. Therefore, the government should abandon the practice of "making decisions in secret", laws and decisions that affect business should be brought to public discussion, and there should be enough time between the adoption and implementation of such decisions, so that the business can adapt to the new rules.

In the period of 1980-2000, the governments of a number of developing countries implemented reforms aimed at economic development. Although a group of them (Singapore, Malaysia, Korea, China, Thailand, Taiwan, Indonesia, Vietnam, Egypt, Tunisia, etc.) have achieved sustainable economic growth, another group of countries (mainly Latin American countries, etc.) have not ensured sustainable growth. they couldn't. According to a group of economists who compared the reform experience of 43 countries, the success of governments aiming at sustainable economic growth depends crucially on the following factors:

1) Prioritizing the export of industrial products - all the countries that ensure sustainable growth have made great progress mainly in the field of exporting industrial products;

2) Avoiding the artificial strengthening of the exchange rate of the national currency - successful countries were able to adjust the exchange rate according to the real income of the country (the real state of the balance of payments), the exchange rate of the national currency was artificially increased in countries that could not achieve sustainable growth;

3) The scale of the public administration sector - in the countries that achieved sustainable growth, the public administration sector was smaller compared to other countries, and they were able to control the inflation process by implementing a more careful tax-budget policy;

4) Liberalization of foreign trade - most of the countries that ensured sustainable economic growth did not go for import liberalization (sharp temporary restrictions were imposed on the import of a number of products), however, they were more open to the world economy thanks to their more active export policy;

5) Access to economic opportunities (for example, the level of education, access to finance, etc.) - all the countries of sustainable growth have been able to achieve a higher level of education of the population (preschool, secondary, secondary and vocational, as well as in the field of higher education).

According to D. Rodrik, the most reliable source of economic growth is industry and industrial exports. It is the growth of industrial production that allows developing countries to catch up with advanced countries and join the ranks of developed countries. He believes that the fundamental way of economic growth is to increase the potential of the economy by improving the quality of human

capital and management (institutions). In his opinion, for the acceleration and sustainability of economic growth, along with increasing the economic potential, more flexible development of the industry should be taken into account.

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Received: 22.01.2024

Accepted: 01.03.2024