

# Chapter 2: Nature, characteristics and forms of International Investment

- GOAL: Clarify the nature, characteristics and forms of International Investment in the world economy.
- Objectives:
  - To understand features of International investment and how they are defined
  - To capture the differences between international investment and the other capital inflows
  - Understand all forms of international investment
- Contents:
  - The nature of International Investment
  - Characteristics of International Investment
  - Forms of International Investment

# International Investment: A Historical Perspective

- When measured as a proportion of GDP, capital flows in the 1800s were much larger than they are now.
- But, because financial markets were not as developed, international investment was not nearly as diverse as today.
- International investment flows were always subject to occasional defaults and renegotiation.
- Most foreign debt was serviced on schedule by borrowers, and, in the case of Great Britain, the overall returns on foreign bonds were at least as high as they were on domestic British assets.
- International investment came to a complete halt during the 1930s, only to recover toward the end of the 20<sup>th</sup> century.

# International Investment: A Historical Perspective

- International investment grew rapidly after World War II, but this growth was not uniform.
- Immediately after World War II, foreign aid dominated.
- During the 1950s, MNEs began to spread across borders and the eurocurrency market was born.
- International bank lending and FDI accounted for much of the international investment among developed economies.
- In the 1970s the eurocurrency lending to the developing economies grew rapidly, but the 1982 debt crisis slowed bank lending during the 1980s.
- In the 1990s, bank lending was surpassed by FDI and portfolio investment as the largest categories of international investment.

The rapid growth of international investment that we are experiencing raises interesting questions:

- What will be international investment's role in the process of globalization in the future?
- Will future international investment flows be as volatile as they have been over the past 25 years, or will they be more stable?

# Graph 1: The nature and characteristics of Int'l Investment

cuu-duong-than-cong.com

cuu-duong-than-cong.com

# Terms and definitions of Investment

- Investment ???



- International Investment ???



Table 1: Comparisons between Investment and International Investment (*Domestic and Foreign*)

Common	Differences
<ul style="list-style-type: none"><li>➤ Profit/Benefit*</li><li>➤ Return/Interest</li><li>➤ Risk</li></ul>	<ul style="list-style-type: none"><li>➤ Nationality of the investors</li><li>➤ The cross-border movement of production factors</li><li>➤ Payments in foreign currencies (mostly in USD)</li></ul>

Note: \* Profit is the most important factor to distinguish an investment activity with other activities.

# Other capital Inflows

*(in host countries)*

- Official Development Assistance (ODA)
- Commercial Loans (CL):
- Foreign Loans (FL):
- Other capital inflows: Remittances and gifts,...

[cui-duong-than-cong.com](http://cui-duong-than-cong.com)

[cui-duong-than-cong.com](http://cui-duong-than-cong.com)

Table 2: Comparisons between Investment and other capital inflows (*host countries*)

International Investment	Other capital inflows
<ul style="list-style-type: none"><li>➤ From abroad</li><li>➤ Because of benefits</li><li>➤ Unlimited volume</li></ul>	<ul style="list-style-type: none"><li>➤ From abroad</li><li>➤ Not because of benefits</li><li>➤ Limited volume</li></ul>

cuu-duong-than-cong.com

Table 3: Comparisons between Investment and other int'l economic relations

Int'l Investment	Other int'l economic relations
<ul style="list-style-type: none"><li>➤ A branch of int'l economic relations</li><li>➤ Use Comparative Advantages Directly</li><li>➤ Producing</li></ul>	<ul style="list-style-type: none"><li>➤ A branch of int'l economic relations</li><li>➤ Use Comparative Advantages indirectly *</li><li>➤ Trading and Providing Services</li></ul>

Note: \* Int'l trade

# Graph 2: Reviewing

cuu-duong-than-cong.com

cuu-duong-than-cong.com

# Forms of Int'l Investments

- Management-based classification:

- Foreign Direct Investment-FDI (Đầu tư- n- trực ngoại trực tiếp)
- Portfolio Foreign Investment-PFI (Đầu tư- n- trực ngoại gián tiếp)

- Strategy-based classification:

- Greenfield Investment-GI (Đầu tư- mới)
- Mergers and Acquisitions-M&A (Mua lại và sáp nhập)

- Goal-based classification:

- Horizontal Integration-HI (Đầu tư- theo chiều ngang)
- Vertical Integration-VI (Đầu tư- theo chiều dọc)

# Vertical and Horizontal FDI

- Foreign direct investment undertaken by MNEs is often classified as either **vertical** and **horizontal**.
- *Vertical* FDI implies that an MNE owns facilities that fit into different stages of the supply chain.
- *Horizontal* FDI, on the other hand, consists of MNE investments that duplicate facilities and operation in several countries.

# Portfolio Investment

- **Portfolio investment** consists of purchases and sales of securities, such as bonds and stocks, in amounts that do not imply any direct management control or influence on the businesses issuing the securities.
- Portfolio investment has, along with FDI, become one of the two largest categories of international investment.
- The prominence of international portfolio investment is been a very recent phenomenon, however.
- International portfolio investment first required the development of stock and bond markets in other countries.
- Portfolio investment is widely used by investors to spread risk as well as to raise overall returns to savings.

# Forms of Portfolio Investment

- Venture Capital Funds (Quỹ đầu tư mạo hiểm): mostly in emerging market and very risky
- International Equity Investment Funds (Quỹ đầu tư cổ phiếu quốc tế): for small and medium investors
- American Depositary Receipts and Global Depositary Receipts (Biên lai ng- ại gại cậ M hoặc quốc tế)
- Convertible Bonds and Bonds with Equity Warrants (Trỷi khoỷn chuyển ại hoặc cậ bậ ại m bậ g cậ phi)

[cui-duong-than-cong.com](http://cui-duong-than-cong.com)

# Graph 3: Forms of FDI

*(Investment law of Vietnam)*

cuu-duong-than-cong.com

cuu-duong-than-cong.com

In-class Discussion:

# Franchising

Is it a form of Int'l Investment?

[cui-duong-than-cong.com](http://cui-duong-than-cong.com)

# Further Discussion

- The nature of FDI ?
- Transformation of FDI forms ?
- Capital-owned ratio of foreign investors?

# Group Discussion

- Problems:
  - Nature and characteristics of Int'l investment
  - Forms of Int'l investment

[cuu-duong-than-cong.com](http://cuu-duong-than-cong.com)

[cuu-duong-than-cong.com](http://cuu-duong-than-cong.com)

# End of chapter 2

[cuu-duong-than-cong.com](http://cuu-duong-than-cong.com)

[cuu-duong-than-cong.com](http://cuu-duong-than-cong.com)