

Foreign Direct Investment and Global Value Chains

Shujiro URATA

ADB I and Waseda University

June 20, 2022

Outline

- 1. Introduction: Global Value Chains and Economic Development
- 2. Global Value Chain (GVCs) : Definition, Participating methods, Benefits, Determinants of GVC participation, etc
- 3. Foreign Direct Investment (FDI): Definition, Modes, Motives, Economic impacts, etc
- 4. Concluding remarks

1. Introduction: Global Value Chains and Economic Development

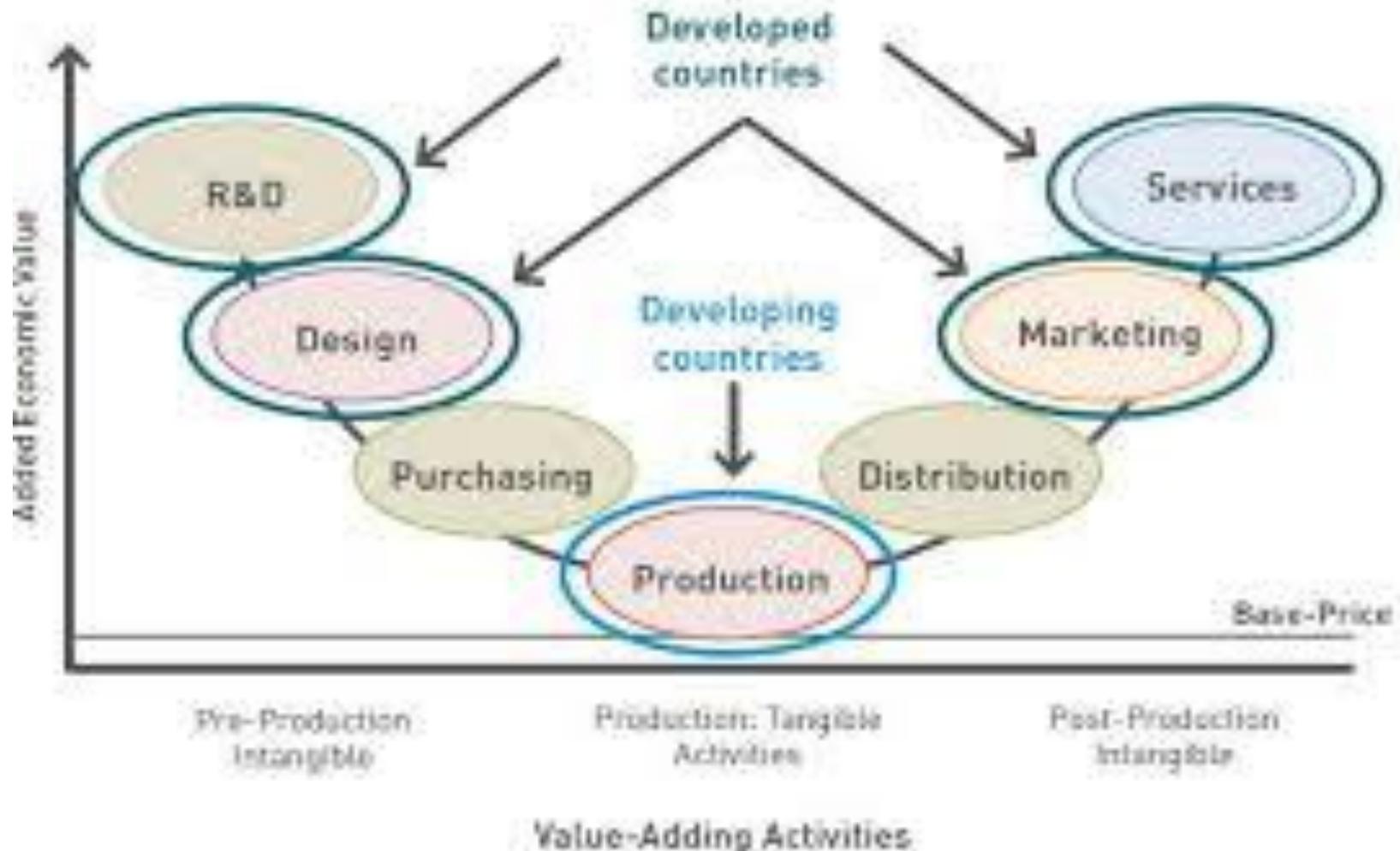
- Global value chains (GVCs) have been attracting attention of policy makers, business people, researchers, and others in recent years because GVCs have been developing and evolving rapidly and because GVCs have contributed to economic development/growth of companies/countries participating in GVCs

2. Global Value Chains (GVCs)

- **What is GVCs?**
- **OECD:**
- International production, trade and investments are increasingly organised within so-called global value chains (GVCs) where the different stages of the production process are located across different countries. Globalisation motivates companies to restructure their operations internationally through outsourcing and offshoring of activities.
<https://www.oecd.org/industry/ind/global-value-chains.htm>

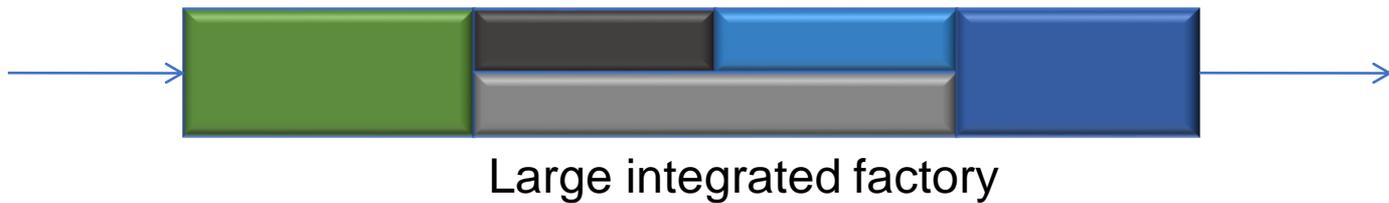
- **World Bank:**
- Companies used to make things primarily in one country. That has all changed. Today, a single finished product often results from manufacturing and assembly in multiple countries, with each step in the process adding value to the end product.
- <https://www.worldbank.org/en/topic/global-value-chains>
- World Development Report 2020
- <https://www.worldbank.org/en/publication/wdr2020>

Global Value Chains (GVC): Smile Curve

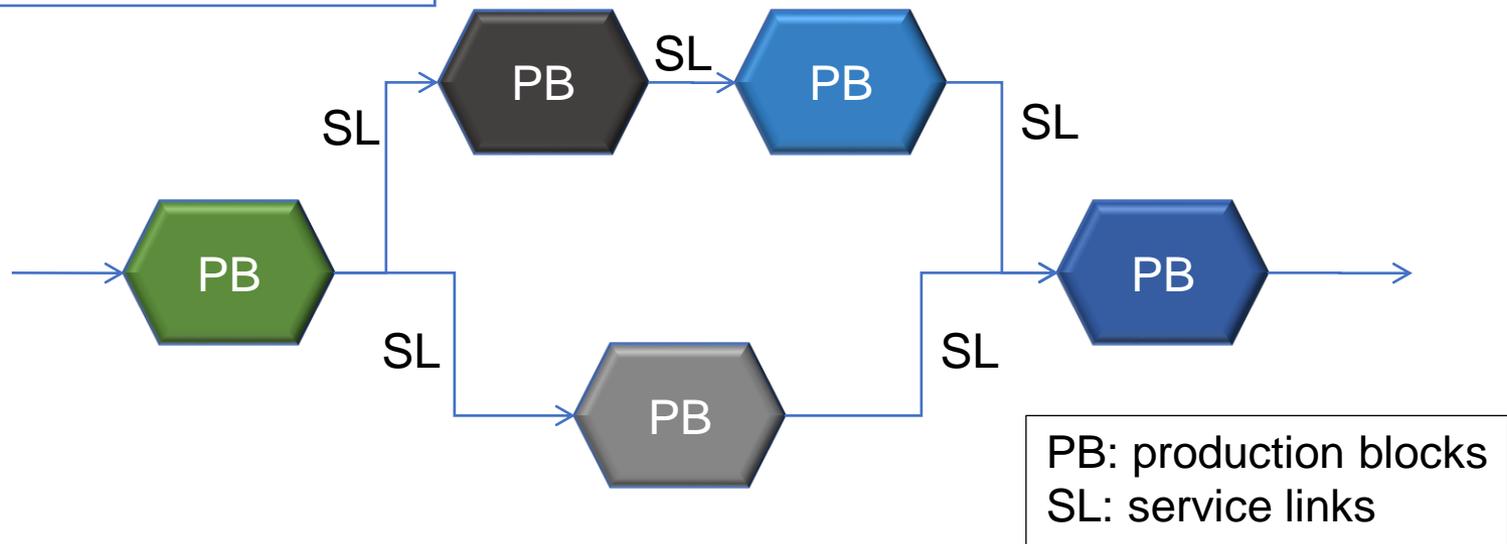


Fragmentation

Before fragmentation



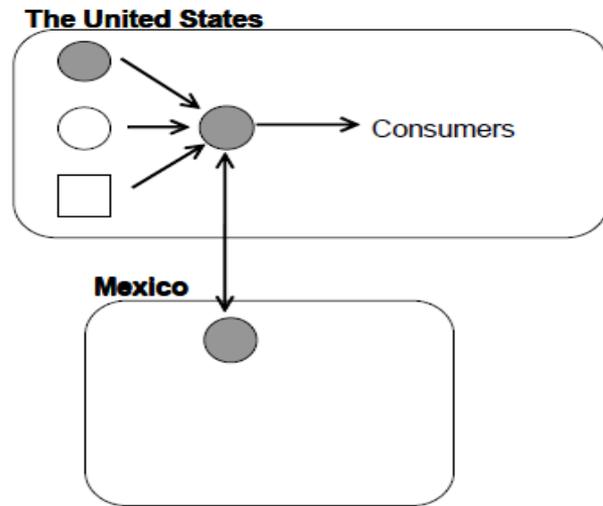
After fragmentation



Fragmentation of production (Jones and Kierzkowski (1990))

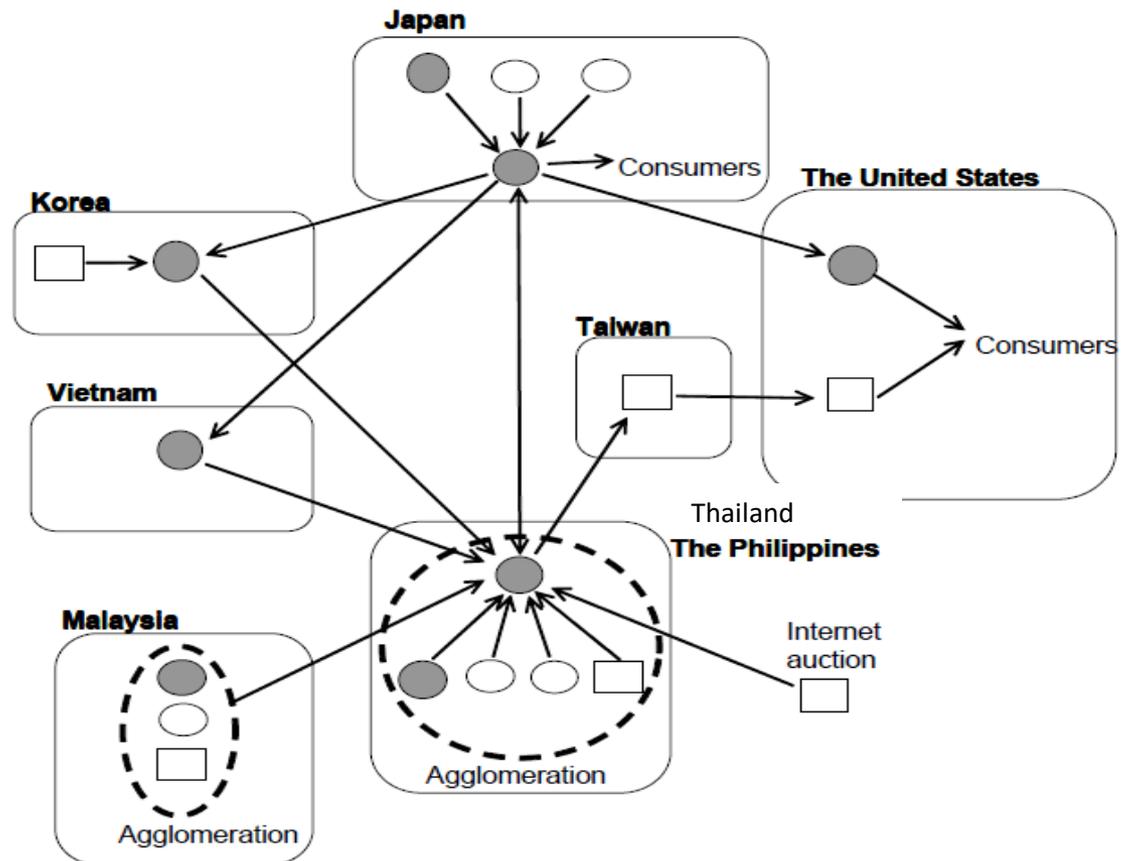
GVC: Production Networks

Cross-border production sharing
(back-and-forth; intra-firm)

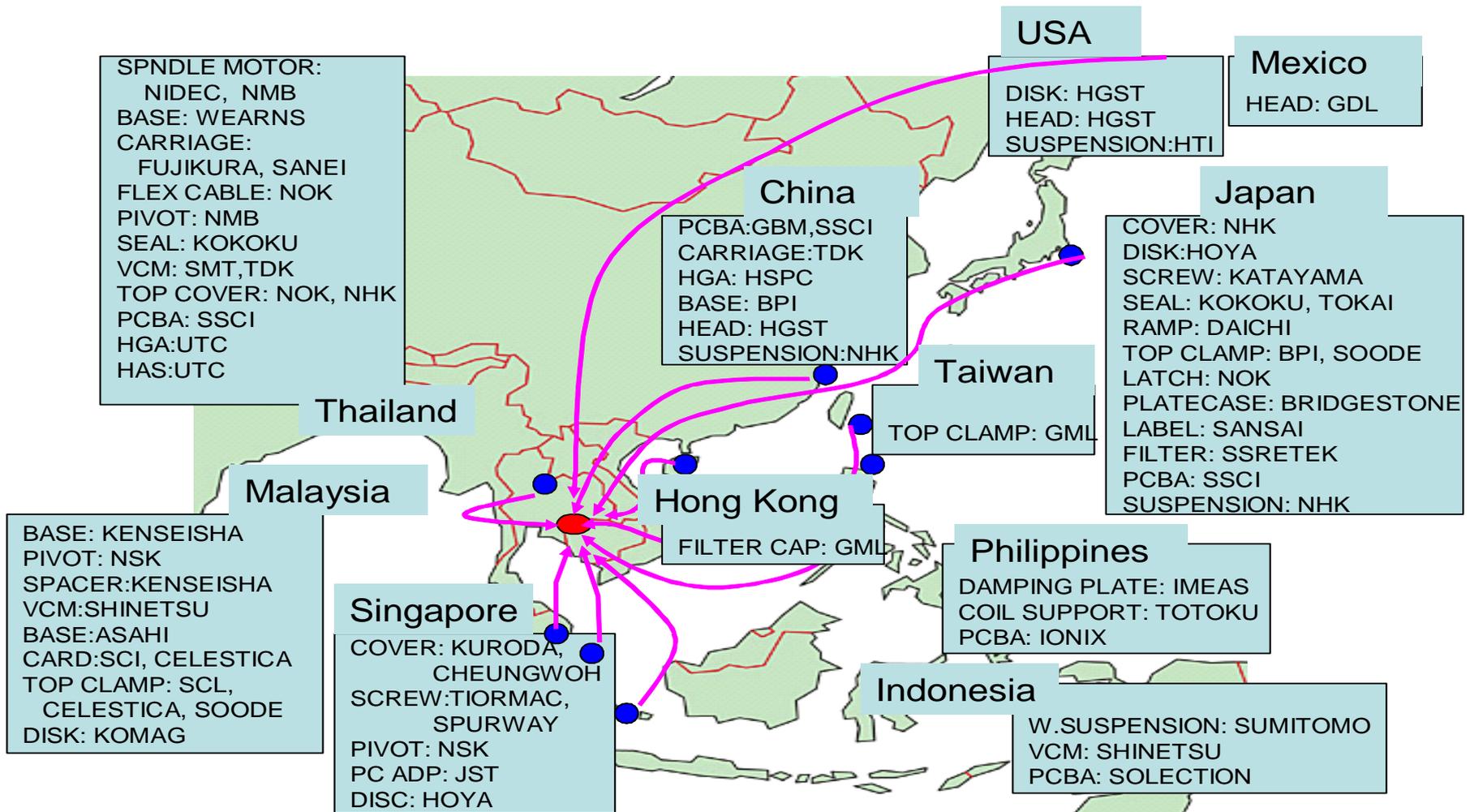


- Headquarters or affiliates
- Unrelated firms with same firm nationality
- Unrelated firms with different firm nationality

Production networks
("networks"; fragmentation and agglomeration;
intra-firm in short distance, arm's length in long distance)



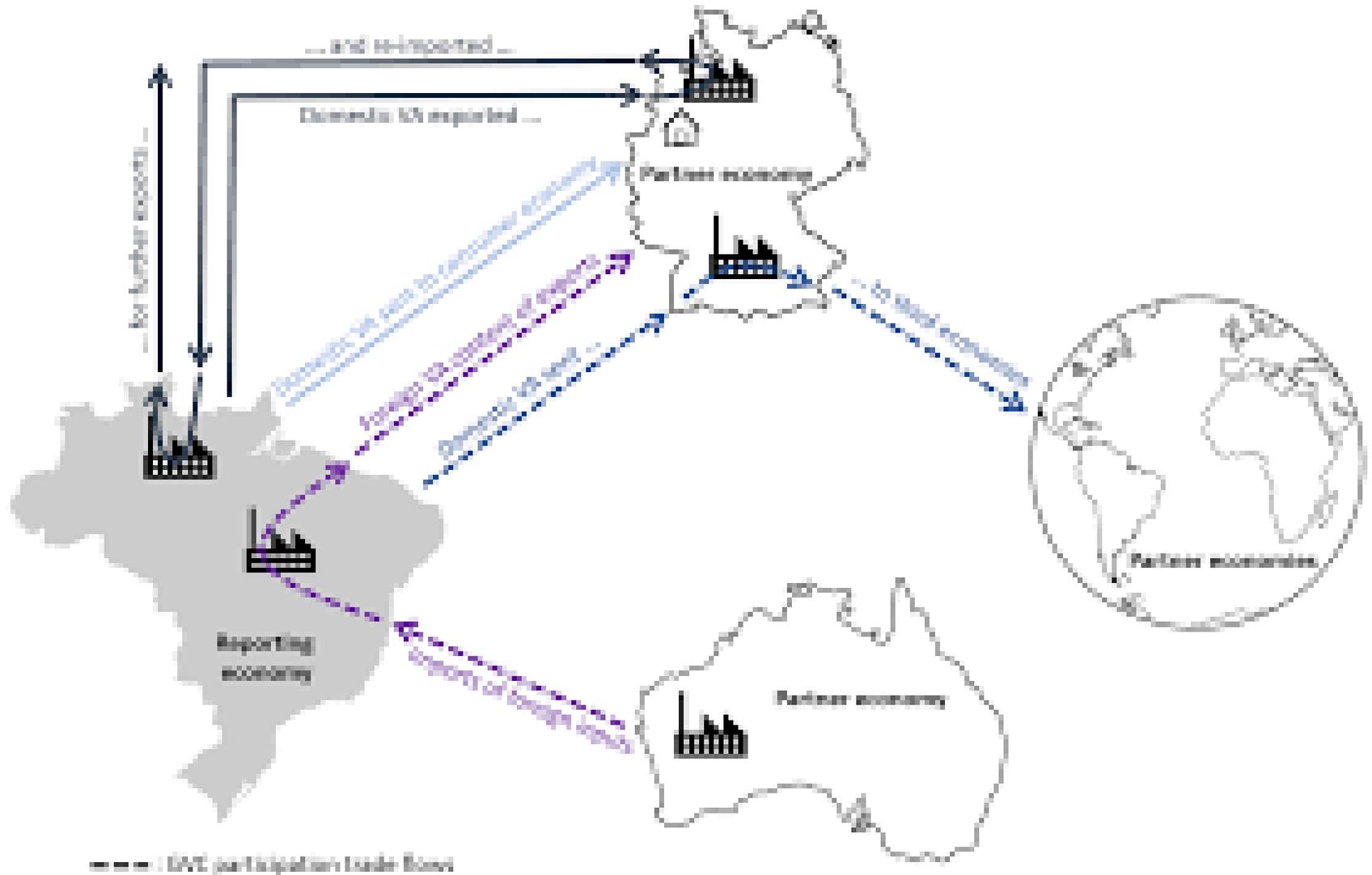
Procurement of Parts by a Hard Disc Drive Producer (Production Network)



GVC Participation I

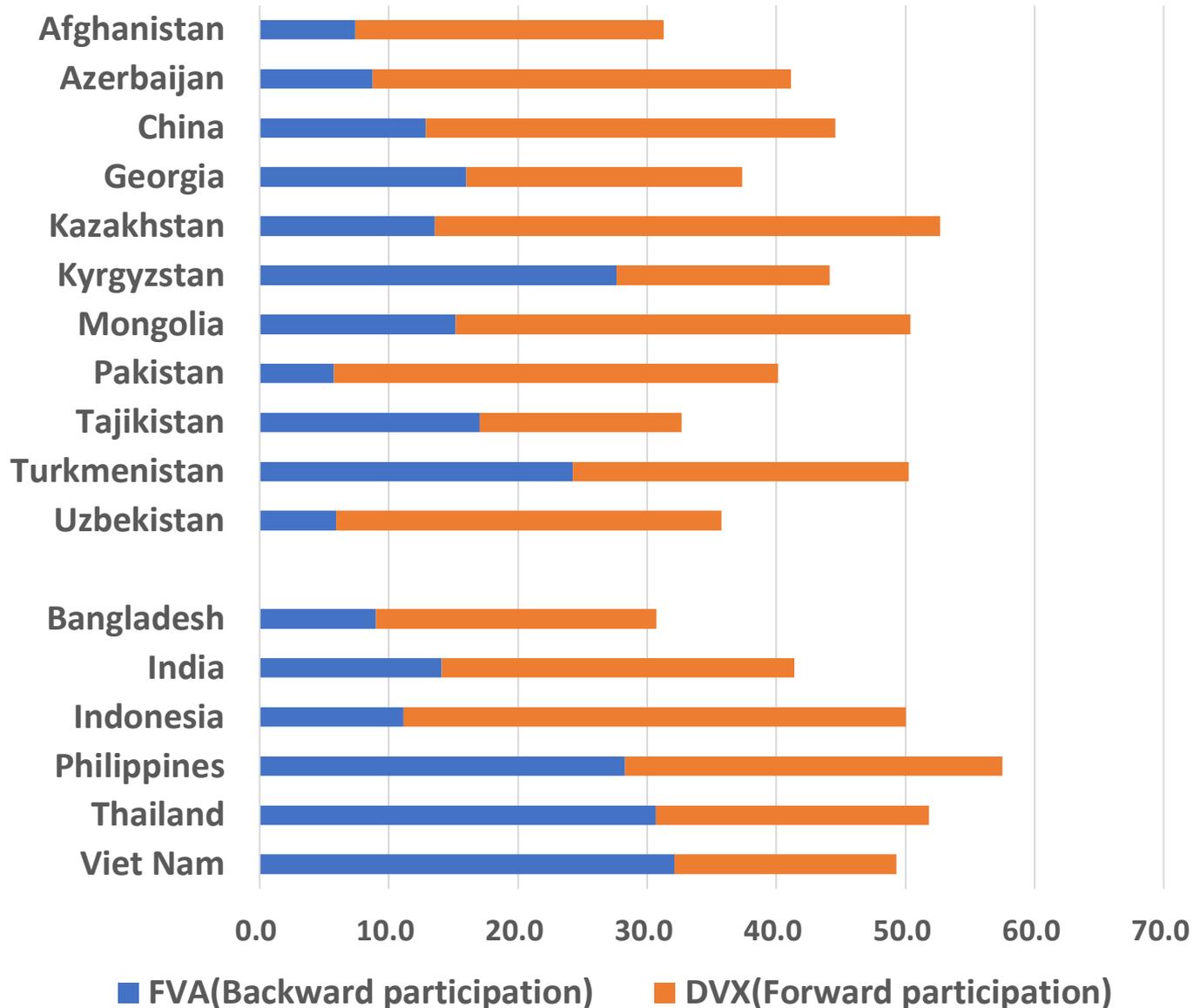
- GVC participation: simultaneous importing and exporting
- Backward Participation: importing foreign inputs to produce the goods and services for export
- Forward Participation: exporting domestically produced inputs to partners in charge of downstream production stages

GVC participation



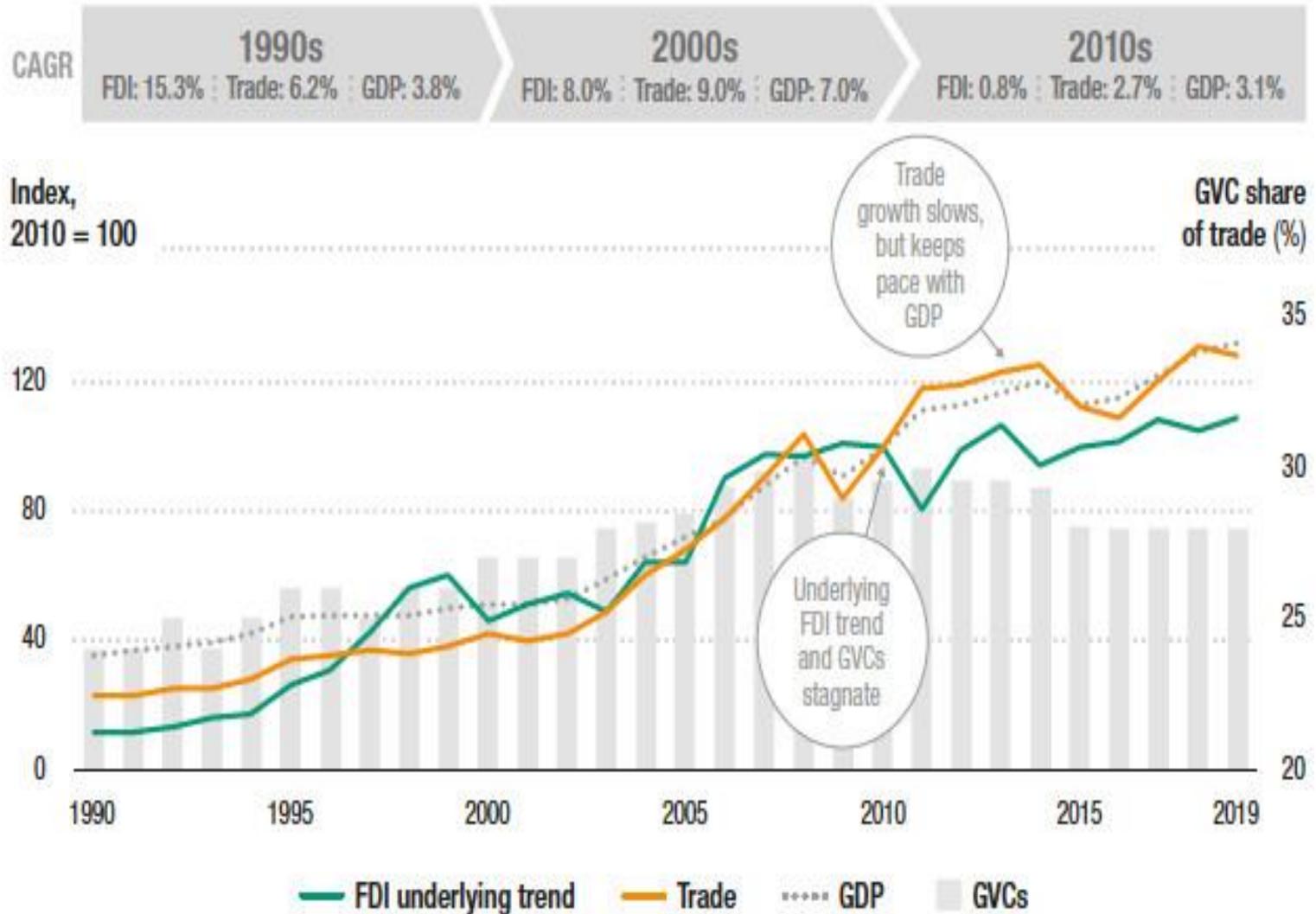
GVC Participation in 2018 (% of Gross exports)

Source: UNCTAD <https://worldmrio.com/unctadgvc/>



The long-term trend of international production

source: VOXEU, CEPR, Aug 13, 2020



GVC Participation II

- **Methods:**
- Participate in foreign trade
- **Attract or involve foreign direct investment (FDI)**
- **Benefits:**
- Engage in foreign trade
- Obtain technology and management know-how
- Improve productivity
- Provide employment opportunity

Factors determining GVC participation:

- **Firms**
- Competitiveness, high productivity
- Technical capability
- Capable workers
- **Foreign ownership**
- Access to finance
- **Countries**
- **Openness to trade and FDI**
- Education
- Infrastructure
- Logistics
- Governance

3. Foreign Direct Investment

- **Definition**
- 10% foreign ownership (IMF definition)
- **Modes**
- Greenfield vs Mergers and acquisitions (M&As)
- Wholly owned vs joint venture
- **Motives**
- Market seeking: horizontal FDI
- Efficiency seeking: vertical FDI => GVCs
- Resource seeking:
- Strategic asset seeking:

- **Benefits of hosting FDI**
- Employment generation
- Involve in trade: GVC
- Technology spillover: backward spillover, forward spillover
- Productivity improvement
- Creation of clusters/agglomeration

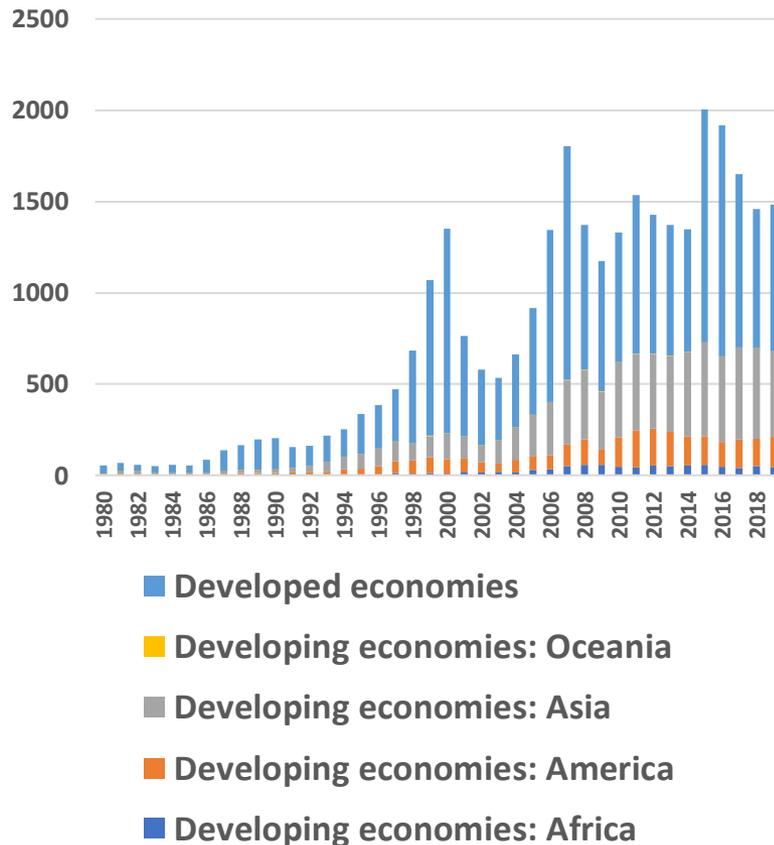
- On FDI, see UNCTAD, World Investment Report 2021
- <https://unctad.org/webflyer/world-investment-report-2021>

- **Factors attracting FDI for developing countries**
- Infrastructure: transportation, communication, electricity supply
- Open trade and FDI environment: international investment agreements (free trade agreements and bilateral investments treaties)
- Good governance: law and order, good regulatory environment
- Capable workers
- Agglomeration
- **For efficiency seeking FDI**
- Low wage workers
- **For market seeking FDI**
- Large market: large regional market (free trade agreement)

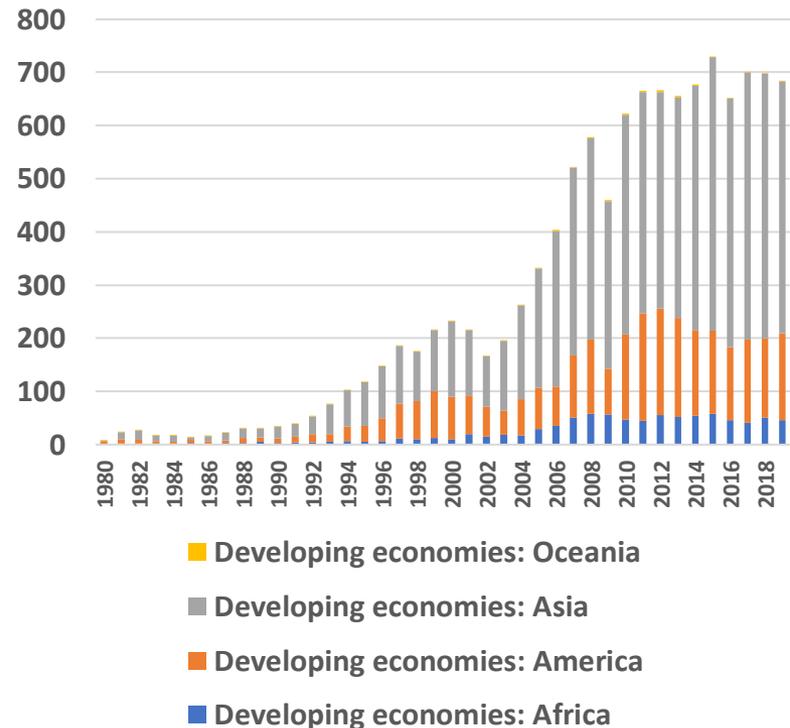
Foreign Direct Investment (FDI) Inflows : \$billion

<https://unctadstat.unctad.org/wds/TableViewer/tableView.aspx?ReportId=96740>

FDI inflows in the world

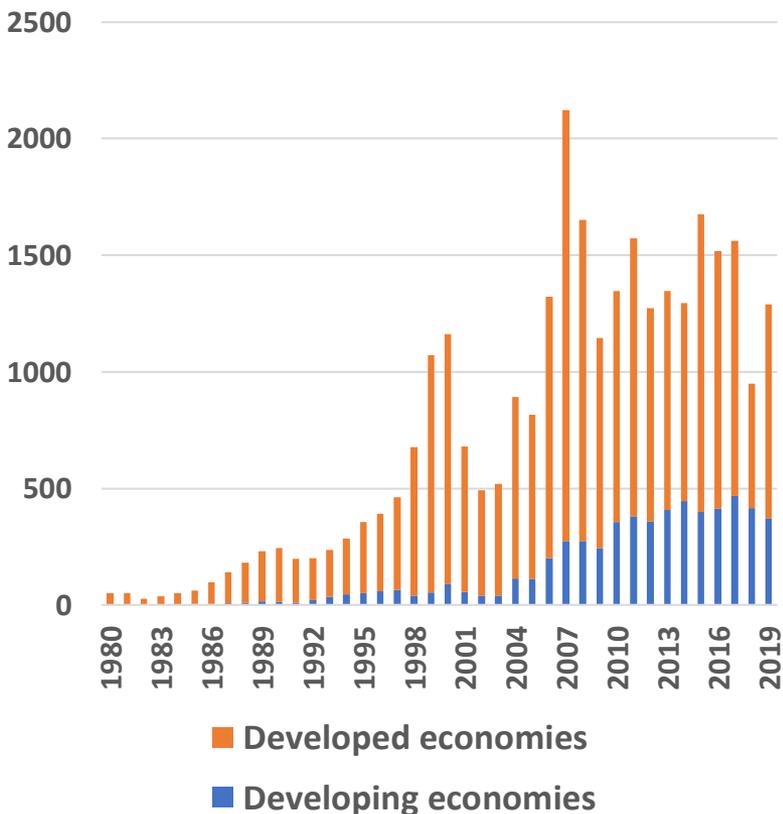


FDI inflows in developing countries

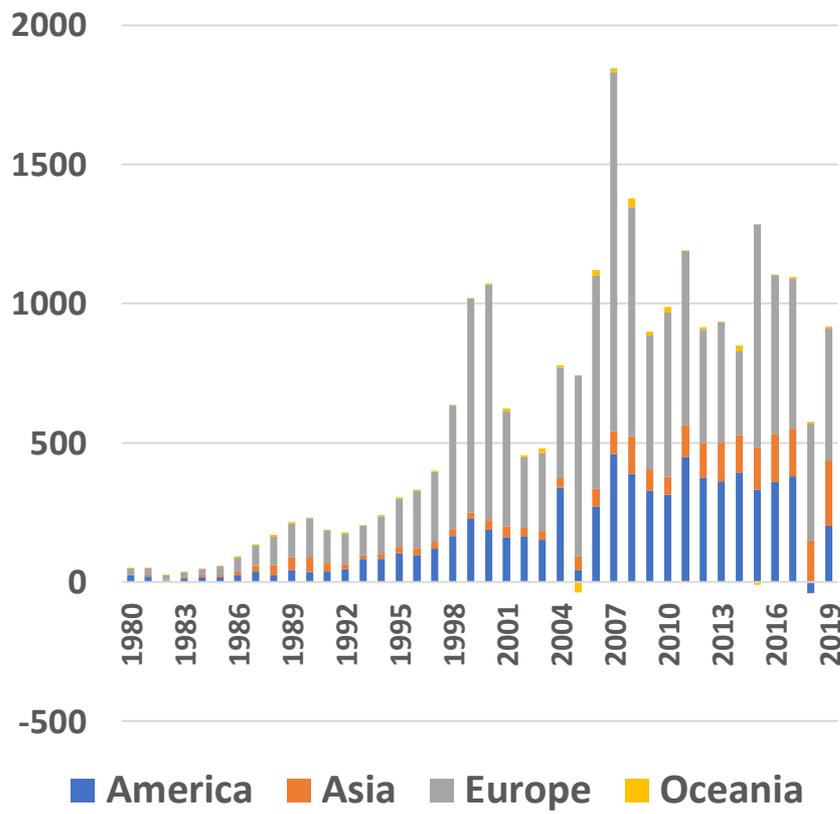


Foreign Direct Investment (FDI) Outflows : \$billion

FDI outflows in the world



FDI outflows from developed countries



4. Concluding Remarks

- GVC and FDI contribute to economic development/economic growth
- For participating in GVCs and attracting FDI, government needs to provide conducive business environment, which includes:
- good infrastructure including both hard and soft infrastructure, open trade and FDI environment, capable workers, etc.
- Government should utilize cooperation with private sector, international cooperation agencies, donor countries

Reference

- Shujiro Urata and Youngmin Baek, *The Determinants of Participation in Global Value Chains: A Cross-Country, Firm-Level Analysis*, ADBI Working Paper No. 1116, Asian Development Bank Institute, April 2020
<https://www.adb.org/sites/default/files/publication/579771/adbi-wp1116.pdf>
- Shujiro Urata ed. *Enhancing SME Participation in Global Value Chains: Determinants, Challenges, and Policy Recommendations*, Asian Development Bank Institute, March 2021
<https://www.adb.org/sites/default/files/publication/682891/adbi-book-enhancing-sme-participation-global-value-chains.pdf>

- Shujiro Urata and Youngmin Baek, *Does GVC Participation Improve Firm Productivity? A Study of Three Developing Asian Countries*, ADBI Working Paper No. 1245, Asian Development Bank Institute, March 2021
<https://www.adb.org/sites/default/files/publication/692486/adbi-wp1245.pdf>
- Shujiro Urata and Youngmin Baek, *Impact of International Investment Agreements on Japanese FDI: A Firm-Level Analysis*, RIETI Discussion Paper Series 22-E-038, Research Institute of Economy, Trade and Industry, April 2022
<https://www.rieti.go.jp/jp/publications/dp/22e038.pdf>