



YOUR LOGO

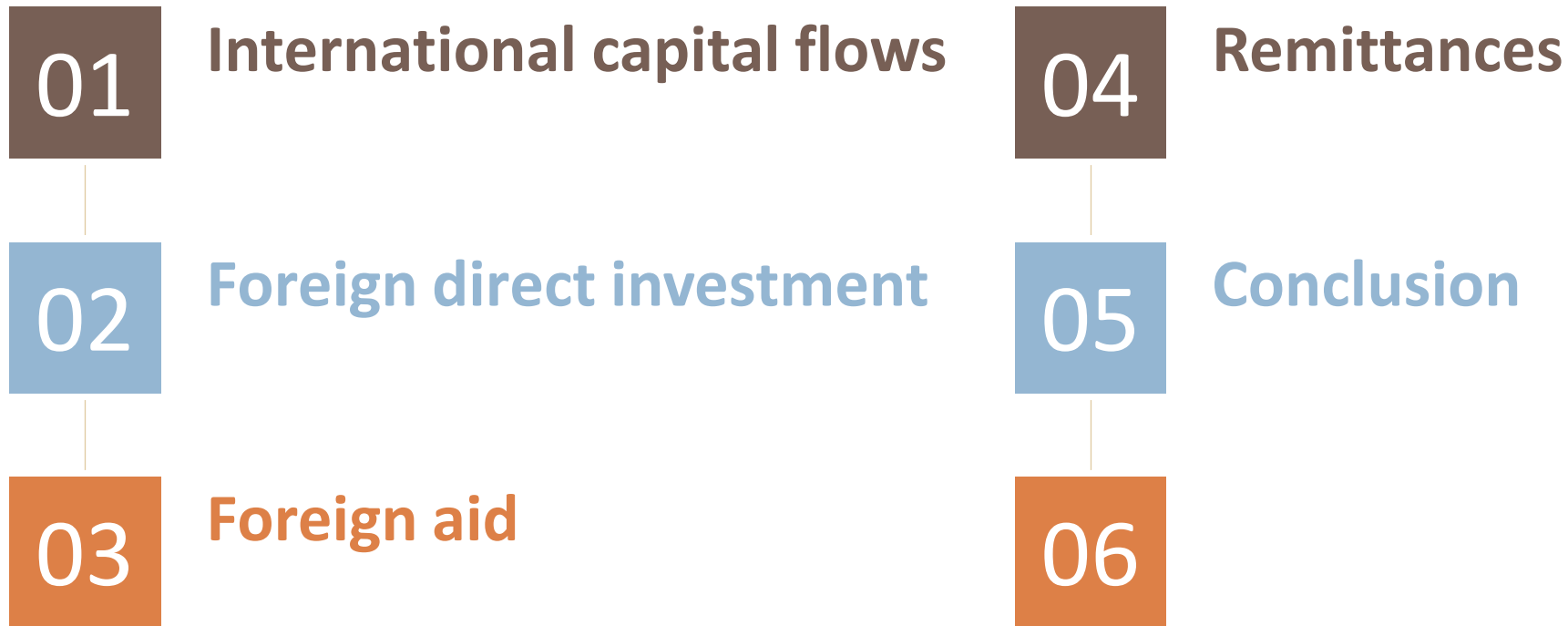
INTERNATIONAL CAPITAL FLOWS

Faculty of Economics, Thammasat University

11/7/2021

EE463 Globalization and International Development

Outline





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INTERNATIONAL CAPITAL FLOWS



Capital flows are transactions involving financial assets between international entities

Forms of international capital flows

Foreign aid

assistance from
bilateral or
multilateral sources
to recipient
governments

Private foreign investments

Investments
through
companies/firms
from abroad

Remittances

earnings by
international
migrants or foreign
workers to their
home country

Military aid

government-to
government
arrangements for
defense and military
purposes



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FOREIGN AID

Design Option #6

What is foreign aid?

- Foreign aid is financial flow, technical assistance and commodities given by residents of one country to another country for development purposes
- Foreign aid is also known as official development assistance (ODA)

Modalities and sources of foreign aid

- Modalities: loans, grants and technical assistance
- Sourced through multilateral or bilateral organizations



What is foreign aid?

- Not all financial flows and technical assistance can be considered as foreign aid
- Depends on who gives it, for what purpose, and the terms and conditions
- Commercial foreign lending, technical assistance for military purposes, and grants from religious groups are not foreign aid



Purpose of foreign aid

- Stimulate economic growth through building infrastructure
- Support productive sectors, introduce new ideas or technologies
- Promote other development objectives, such as strengthening education, health, environment, or political systems



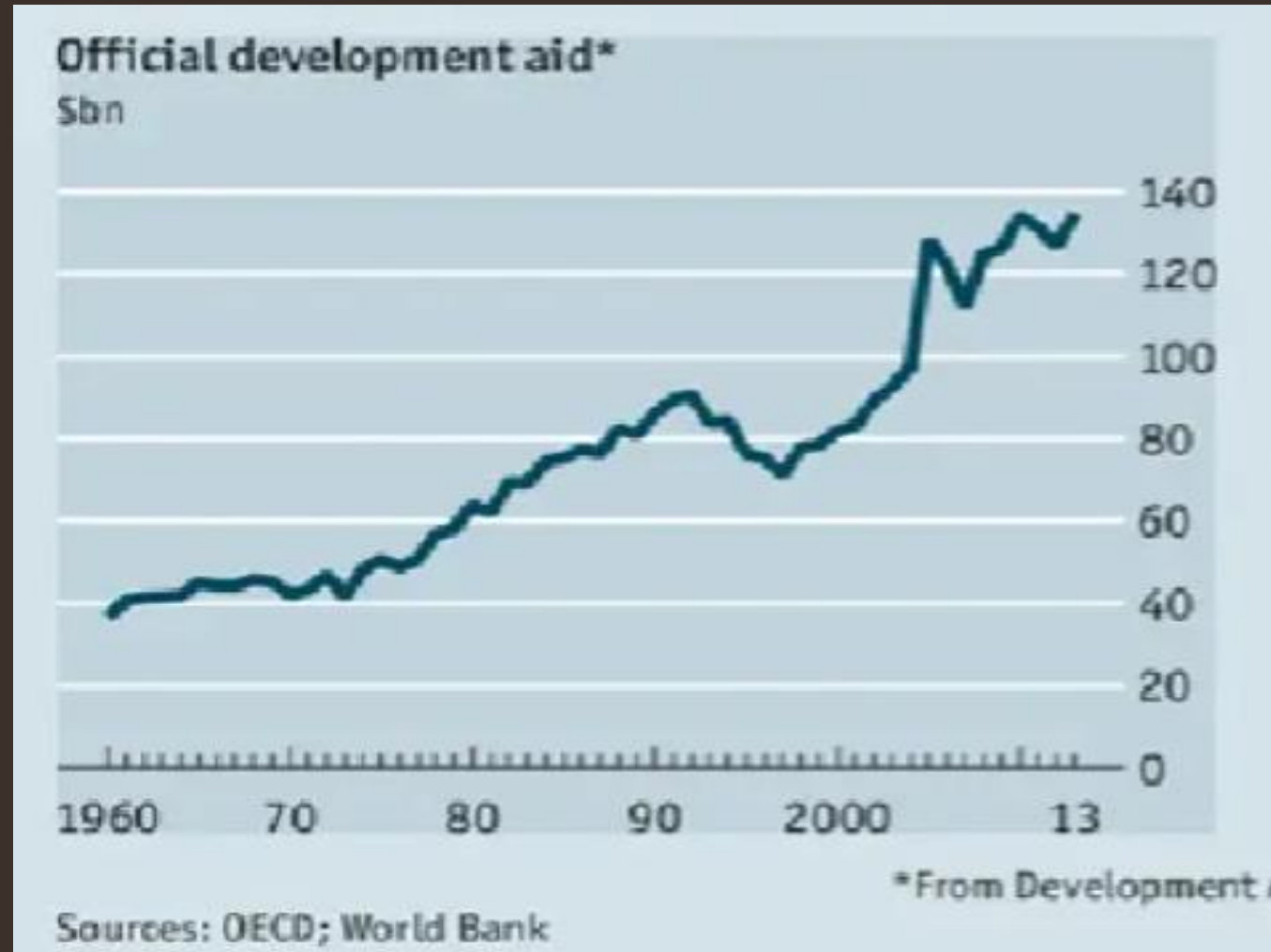
Purpose of foreign aid

- Support subsistence food consumption and other commodities, especially in emergencies after natural disasters or humanitarian crisis
- Help stabilize an economy after economic shocks



Trends in foreign aid

- Global aid rose steadily from the 1960s until it reached a peak of \$90 billion in 1991, after the end of the Cold War
- Global aid declined in the 1990s and started to rebound in the early 2000s
- The global financial crisis in 2008 caused a decline in global aid but rebounded the following year



Sources of ODA: Bilateral aid



- **Bilateral aid:** assistance directly from one country to another; government-to-government
- Supports recipient country governments (government-to-government)
- In some cases aid is disbursed through research organizations, universities, and not-for-profit organizations



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Sources of ODA: Multilateral aid

- **Multilateral aid** is assistance from international institutions which have pooled financial sources provided by their member countries
- Multilateral aid provides larger amounts of aid compared to bilateral aid
- Provides lower bureaucratic costs
- Requires fewer political ties



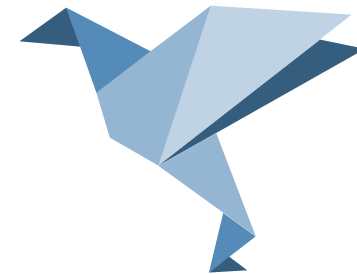
Debate on foreign aid

- Foreign aid enriches elites in recipient countries and therefore does more harm than good
- Reinforces corrupt practices and distorts incentives; example: widespread poverty in Africa and South Asia despite 4 decades of foreign aid
- Accelerates growth, reduces poverty helps achieve development objectives in countries unable to generate resources needed to finance investment; example: Marshall Plan



Aid and economic growth: View 1

Although not always successful, on average aid has a positive impact on economic growth and development



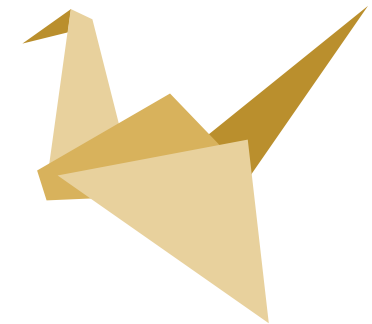
Aid and economic growth: View 1

- Aid promotes growth by financing new investments, especially investments in public goods such as roads, ports, electricity generation and distribution, schools and health facilities
- Aid promotes capital accumulation/ formation as driver for economic growth, and transfer of knowledge/innovation



Aid and economic growth: View 2

Aid has little or no effect on growth,
and could actually undermine growth



Aid and economic growth: View 2

- Aid is spent on large bureaucracies, expensive consultants and corrupt officials of recipient countries
- Aid is not effective if the absorptive capacity of recipient governments is low; implementers lack skills in managing aid
- Aid may crowd out the domestic private sector



Aid and economic growth: View 3

Aid has a conditional relationship with growth, stimulating growth only under certain circumstances



Aid and economic growth: View 3

- Depends on the characteristics of the recipient country and quality of institutions and policies
- Depends on the type of aid: short term (humanitarian assistance); medium term (infrastructure) or long term (education, health)



Aid and economic growth: View 3

- Depends on donor practices; multilateral aid is deemed more effective than bilateral aid because of less influence of political factors





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COFFEE BREAK

Enjoy your 15' pause



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PRIVATE FOREIGN INVESTMENTS

Design Option #9

Private foreign investment

Foreign Direct Investment

Investments by large multinational corporations such as Exxon, Toyota, Hyundai, Coca Cola and



Foreign Portfolio Investment

Investments in the form of stocks, bonds in developing countries' credit and equity markets



Foreign direct investment

- Multinational corporation (MNC): conducts and controls productive activities in more than one country
- Most MNCs are based in North America, Europe and Japan; more recently, PR China, South Korea, Taiwan and Brazil
- MNCs bring development opportunities but may also pose serious problems for developing countries in which they operate



Forms of foreign direct investment

- Historically MNCs focused on extractive and primary industries, mainly petroleum, nonfuel minerals, and agribusiness
- Thereafter MNCs became more involved in export-oriented agriculture and local food processing
- More recently, MNCs operate in manufacturing operations, finance and services



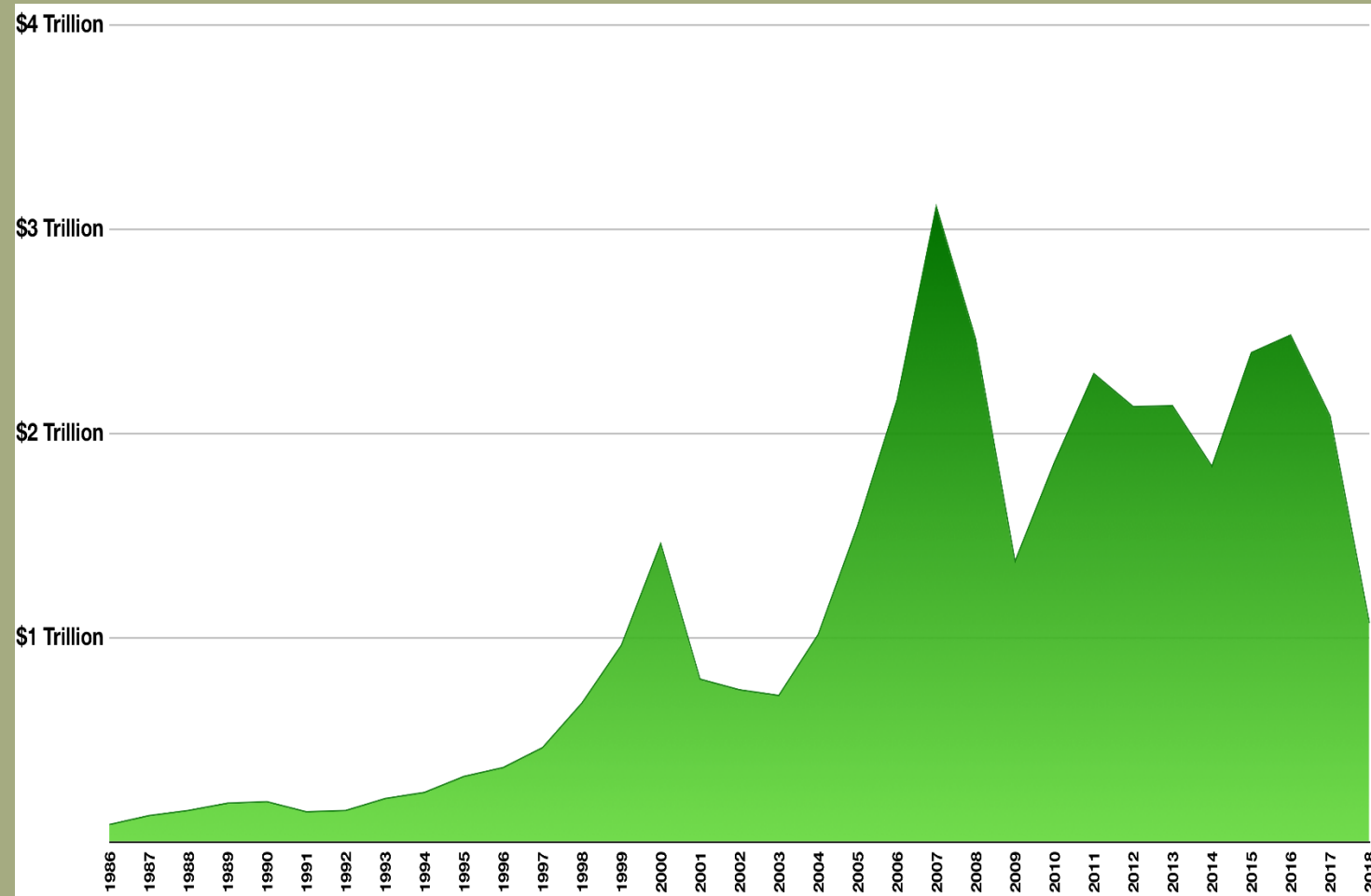
Forms of foreign direct investment

- Production now geared for export to MNCs home country and other developed markets rather than for the host country



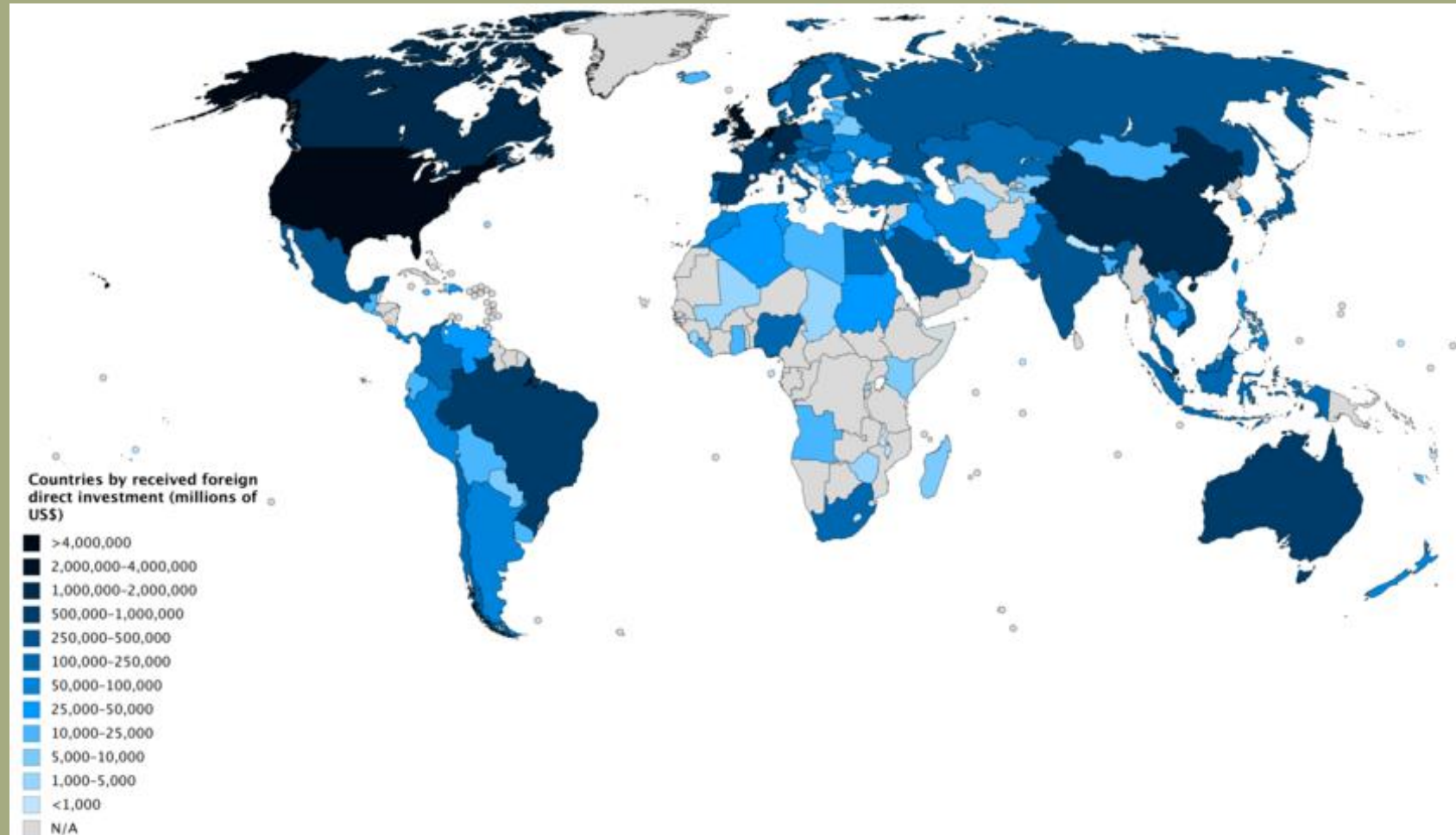
Foreign direct investment trends

- Gradual rise from 1986-2000; decline thereafter, up to 2004 followed by increase up to 2008
- Rebound in 2009; slight dip in 2014 but rebound thereafter
- Developed countries are recipients of a major share of FDI



Major recipients of FDI

- Developed countries are recipients of a major share of FDI
- According to UNCTAD, two thirds of profits from FDI are repatriated back to the home country



Impacts of foreign direct investment

- Fills resource gaps; enables supply of domestic savings, foreign currency, human capital skills
- Fills the gap between foreign exchange requirements and those derived from net export earnings plus net foreign aid
- Generates tax revenues needed and available management and transfer of technology



Impacts of foreign direct investment

- **Crowding out of private businesses**, lower domestic savings and investment rates by substituting private savings
- **Distorts competition** through special arrangements and fails to re-invest profits
- **Reduced foreign exchange earnings** in the long run; failure to improve foreign exchange position of the recipient country



Impacts of foreign direct investment

- **Less-than-expected contribution to public revenues** in reality, contribution through corporate tax is considerably less because of tax holidays, subsidies, and transfer pricing
- **Little impact on developing local resources** MNCs' management, entrepreneurial skills, technology may have little impact on developing local sources



Impacts of foreign direct investment

- **Impact of MNCs on development is uneven;** in some cases MNCs reinforce dualistic economic structures and exacerbate inequalities by promoting the interests of local factory managers above workers
- **MNCs use their economic power to influence government policies** in directions that are unfavorable to development



Foreign portfolio investments

- Private portfolio investments comprise foreign purchases of stocks, bonds, and certificates of deposit and other commercial paper
- Private portfolio investments currently account for a large and rising share of overall net resource flows to developing countries
- Follows liberalization of domestic financial markets and opening up of these markets to foreign investors



Foreign portfolio investments

- Favored destination: middle income countries where risks and returns are higher
- Perspective of recipient country: portfolio investments enables the country to raise capital and domestic investors to diversify their assets
- Perspective of foreign investors: investing in stock markets of developing countries or emerging economies permits them to increase returns while diversify risks





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REMITTANCES

Remittances

- Workers from less developed countries look for jobs overseas because of wage differentials; workers in advanced countries earn 5 times more than in less-developed countries
- This provides incentives for workers to migrate/work temporarily overseas
- **Remittance:** overseas worker send back a portion of wages earned to the home country



Remittances

- Since 1995, remittances have overtaken ODA and portfolio investment flows as a source of capital resource flows to developing countries
- Since 2017 it has overtaken foreign direct investment as a source of capital flow to recipient countries
- Global remittances have grown to a record level of \$613 billion in 2017, a 7% increase from \$573 billion in 2016





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CONCLUSION

Capital flows; foreign aid

- International capital flows take many forms; these include, among others, official development assistance, private foreign investment, remittances and military aid
- Foreign aid is financial flow, technical assistance and commodities given by residents of one country to another country for development purposes



Foreign direct investment

- Foreign direct investment is mainly channeled through multinational corporations; historically MNCs were engaged in extractive/primary commodities, but currently more on manufacturing, finance and services
- Most flows of FDI occur among high income countries



Role of multinational corporations

- MNCs bring advantages as well as disadvantages to the recipient country
- Although MNCs bring capital, technology and skills, they can also use their economic power to influence government policies in directions that are unfavorable to development



Portfolio investments

- Private portfolio investments comprise foreign purchases of stocks, bonds, and certificates of deposit and other commercial paper
- Provide opportunities for domestic investors to diversify their assets and for the foreign investor to generate high returns; naturally follows liberalization of domestic financial markets to foreign investors



Remittances

- Remittances are an important source of capital for developing countries; the figures indicate that remittances are the main source of revenues for the recipient country, exceeding FDI and ODA



THANK **Y**OU!