

## RELATIONSHIP BETWEEN FOREIGN DIRECT INVESTMENT AND ECONOMIC GROWTH: A COMPREHENSIVE REVIEW OF LITERATURE

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### ABSTRACT

*The globalization of national economies has led to a rise in foreign direct investment (FDI) flows over the last two decades. This surge in FDI flows has in turn resulted in potential gains for the FDI receiving countries, thereby motivating research focused on the nexus between FDI and economic growth. It is in this direction that the present paper makes an attempt to thoroughly review the existing literature in a variable-wise manner focused on the FDI-growth linkages in developing economies particularly. Moreover, a special emphasis has been laid on reviewing some studies conducted so far on identifying the determinants of FDI and studying the FDI-growth nexus in BRICS group of countries which are considered to be the fastest emerging and representative developing economies today having witnessed a spectacular rise in FDI flows. It can be synthesized from the existing literature that the FDI-growth relationship is far from conclusive. The comprehensive review conducted in this paper reveals a mixed evidence regarding the growth performance of FDI which is found to depend on the host country characteristics like trade openness, macroeconomic stability, financial development and economic freedom.*

**Keywords:** Foreign Direct Investment, FDI, economic growth, GDP, BRICS.

### Introduction

Foreign direct investment (FDI) is defined as an investment reflecting a lasting interest and control by a foreign direct investor, resident in one economy, in an enterprise resident in another economy (UNCTAD, 2018). The contribution made by foreign direct investment towards increasing integration of economies is immense. Traditionally, the policies aimed at promoting FDI adopted the quantitative approach where the main focus of countries used to be on maximizing FDI inflows. However, with the advent of Information and Communication Technology (ICT) facilities, Multinational Corporations have gained access to better and adequate information, thereby helping them to decide on which country to invest in. FDI has increasingly been considered as a catalyst for economic growth and development for both developed and developing countries. Due to the wide spread belief that FDI has a potential to impact economic growth, huge efforts have been made across countries to invite inward FDI flows by offering various incentives to foreign investors. Given such efforts by countries across the globe, a sharp rise in FDI flows has been witnessed in the last few decades. FDI has thus gained remarkable attention worldwide. It has emerged as a key topic of interest among researchers, practitioners and policy makers. A

large number of researchers have focused on the relationship between FDI and economic growth taking different countries as their sample. However, a mixed empirical evidence has been found in the literature. While some researchers view FDI as a catalyst of economic growth, others prove just the opposite. In this paper, a review of literature has been conducted in a variable-wise manner with the aim to examine the impact of FDI on economic growth of the recipient economies. As the growth impact of FDI seems to be conditional upon some other variables, this review aims to identify and study those variables that exert an influence on the FDI-growth nexus. Moreover, a special emphasis has been placed on the fastest growing BRICS economies which have shown remarkable performance in attracting foreign direct investment.

### Review of Literature

The relationship between FDI and economic growth has gained enormous importance in the growth literature. The existing literature reveals a mixed evidence regarding the FDI-growth nexus. While some studies indicate a positive growth impact of FDI in the host countries, others yield statistically insignificant, negative or no contribution of FDI towards economic growth, the third strand of literature includes mixed results within the individual studies and the fourth group of studies reveal that FDI does

not exert an independent influence on economic growth. In the following section, we present all the four strands of literature to gain a better and deeper insight on the growth impact of FDI in the host economies. The review is presented in a sequential manner beginning with the studies revealing a positive growth impact of FDI, then the studies yielding negative, insignificant or no impact are presented, followed by the third and fourth strand of literature.

### **I. Foreign Direct Investment and Economic Growth**

Many empirical studies that have analyzed the FDI-growth relationship, using different samples and estimation methods, reveal a positive association between the two variables. Hansen & Rand (2006) examined the causal nexus between FDI and economic growth in 31 developing countries of Asia, Africa and Latin America using Vector Autoregressive (VAR) model. The results of both mean group estimator and fixed effects estimator used in the study reveal a long-run impact of FDI on Gross Domestic Product (GDP) growth. While addressing the issue of heterogeneity, it was found that no systematic differences exist in the total effect of FDI across regions indicating that the growth benefits from FDI to Africa should be equal to the growth-enhancing impact of FDI in Asia and Latin America. Yao (2006) studied the impact of FDI and exports on economic growth using dynamic panel data approach covering 28 Chinese provinces over the period 1978-2000. The findings reveal a strong positive effect of both FDI and exports on economic growth. The paper suggests the developing economies to follow two significant development policies adopted by China to their benefit viz. export promotion policy and adoption of global technology and business practices. Worldwide debates among economists about the growth enhancing impact of FDI motivated further research in this area. Tiwari & Mutascu (2011) suggested that growth in the initial phase can be promoted through exports whereas FDI should be undertaken for enhancing growth in the later stage. de Mello (1999) finds a positive impact of FDI on output growth in a sample of 32 OECD and non-OECD countries while

revealing that the growth-enhancing impact of FDI is dependent on the complementarity effect and the degree of substitution between foreign direct investment and domestic investment. Other studies also found a positive effect of FDI on economic growth (Bouchoucha & Ali, 2019; Pegkas, 2015 and K. H. Zhang, 2001). Feridun & Sissoko (2011) assessed the relationship between FDI and GDP per capita in Singaporean economy. The major finding of the study is that the economic growth in Singapore is caused by the FDI implying a unidirectional causality from FDI to GDP. However, no evidence of bi-directional causality is found between FDI and GDP. Dritsaki et al. (2004) conducted a co-integration analysis revealing a long-run relationship between FDI, exports and economic growth in Greece. Metwally (2004) revealed a feedback effect in the sense that the growth in FDI inflows leads to growth in exports which in turn leads to growth in Gross National Product (GNP) and the GNP growth ultimately attracts more FDI into the country. Sahoo & Mathiyazhagan (2003) revealed a long run relationship between Gross Domestic Product (GDP), FDI and exports in India. Both exports and FDI exert a positive influence on economic growth but exports play a better role than FDI in enhancing the economic growth of India. Szkorupová (2014) also found a long-run relationship between FDI, exports and economic growth in Slovakia. Both FDI as well as exports exert a positive impact on economic growth of the country.

Another group of researchers have found a negative, statistically insignificant or no relationship between FDI and economic growth in the host economies. For instance, Mencinger (2003) found a negative causal relationship between FDI and economic growth and this result is attributed to the chosen form of FDI which is acquisition under the reference period as the sales revenue was largely spent on consumption and imports instead of improving the productivity of local assets. Moreover, a strong link was found between current account and FDI; with the increase in amount of inward FDI flows into a country increases the current account deficit and foreign debt. Herzer (2012) also contradicts many previous studies as the results of his study clearly indicate that the

impact of FDI on economic growth is found to be negative on an average in case of developing countries. Lian & Ma (2013) examined the linkage between FDI and economic growth in the western region of China using time-series data. The results show that FDI inflows do not cause economic growth in the recipient economies and economic growth also does not exert a significant impact on FDI implying exaggeration on part of some researchers regarding the impact of FDI on economic growth. The paper has some policy implications suggesting the host nations to not only attract more and more FDI flows, but also take steps to improve the quality of utilization of FDI in order to promote economic growth in a much better way. The impact of FDI on per capita growth in Russia was studied using Generalized Method of Moments (GMM) technique (Ledyeva & Linden, 2006). The results suggest that there is no significant contribution of FDI in economic growth and the growth is mainly explained by domestic investment, exports and initial level of economic development during the reference period. Carbonell & Werner (2018) employed an improved and robust empirical methodology, General-to-specific (GETS) method for assessing FDI-growth nexus in Spain and found no significant positive impact of FDI on economic growth despite of the fact that Spain is a large FDI recipient having good absorptive capacity required for reaping the growth-enhancing benefits of FDI. Gunby, Jin, & Reed (2017) conducted a meta-analysis to test whether the impact of FDI on growth has been over emphasized in literature. The major finding of the study is that the effect of FDI on Chinese economic growth is much smaller than expected. Earlier estimates tend to be over emphasized which may be due to publication bias or sample characteristics. A study is conducted in the six Gulf Cooperation Council countries (United Arab Emirates, Oman, Qatar, Kingdom of Saudi Arabia, Kuwait and Bahrain) analyzing the growth impact of Foreign Direct Investment (FDI) for the period 1996 to 2007 (Hussein, 2009). The findings reveal a weak relationship between FDI and GDP in these countries. Awolusi et al. (2017) finds a small positive impact of FDI on economic growth in selected African

economies. Zhao & Du (2007) reveal that a bidirectional causality between FDI and economic growth in China is not highly significant, however, a unidirectional causality runs from economic growth to FDI. Christopher (2012) revealed a positive relationship between FDI and economic growth, though the contribution of FDI to GDP growth was very low for the period under review.

The third strand of literature yields mixed results regarding the impact of FDI on economic growth of recipient countries. Lo et al. (2016) revealed a positive impact of FDI on Chinese economic development via improvement in allocative efficiency whereas a negative impact was found via worsening productive efficiency leading to an overall negative impact as loss in productive efficiency dominated the gains in allocative efficiency. Alfaro (2003) reveals that the impact of total FDI on growth is ambiguous. It finds a negative impact of FDI on growth in the primary sector, a positive effect in the manufacturing sector and an ambiguous evidence is found in the service sector. Dua & Rashid (1998) have distinguished between FDI approvals and actual flows to examine the impact of both on the level of economic activity in India, measured by industrial output. The results of Granger Causality test reveal that industrial output affects both FDI approvals and actual flows whereas FDI approvals alone have an impact on industrial output and no such effect is produced by the actual FDI flows. Akpan & Eweke (2017) find that no long-run relationship exists between FDI, Industrial Sector Output and GDP in Nigeria. However, a bidirectional relationship is found to exist between FDI and Industrial Sector Output, GDP and Industrial Sector Output and a unidirectional causality running from FDI to GDP. Zhang (2001) assessed the causal nexus between FDI and economic growth and revealed that FDI tends to promote economic growth more in East Asia than Latin America. Johnson (2006) found that FDI inflows lead to improvement in economic growth in developing countries only and not in the developed ones. Ozturk & Kalyoncu (2007) suggested that FDI and GDP are found to be co-integrated for Turkey and Pakistan. A

unidirectional causality is found in case of Pakistan running from GDP to FDI, while in case of Turkey, the findings reveal a strong bi-directional causal nexus between FDI and GDP. Durairaj (2010) found a long run relationship among exports, economic growth and FDI in India. A unidirectional causality runs from exports to FDI and a bidirectional causality between exports and economic growth is found in the short run. Chowdhury & Mavrotas (2006) finds a bi-directional causal relationship between GDP and FDI in Malaysia and Thailand while in case of Chile, only a unidirectional causality is found to run from GDP to FDI and not vice versa. Frimpong & Oteng-abayie (2006) conducted a study aimed at assessing the causal relationship between FDI and economic growth in Ghana for the pre- and post-SAP (Structural Adjustment Programme) periods. The findings revealed no causal linkage between FDI and growth for the total reference period and the pre-SAP period. However, during the post-SAP period when Ghana faced relatively stable political and economic environment, FDI caused economic growth in the country. The study conducted by Choe (2003) found a bi-directional causal linkage between FDI and economic growth in a set of 80 countries, however, the impact is more robust from economic growth to FDI rather than from FDI to growth.

The fourth group of studies reveal that FDI does not exert an independent influence on economic growth but is affected by other conditions prevalent in the host environment. Carkovic & Levine (2002) found that FDI inflows do not have an independent influence on economic growth of a host country. While sound economic policies may spur both growth and FDI, the results do not support the view that FDI shows positive effect on growth that is independent of other growth determinants. Similar results have been found by Cao & Jariyapan (2012) in case of China. The study investigated the channel through which FDI may be beneficial for growth and the results indicated that the effect of FDI on economic growth is dependent on the level of human capital that is available in the host country (Borensztein et al., 1998). Some other researchers have also found that the growth-enhancing impact of FDI is dependent on the

level of human capital present in the host economy (Balasubramanyam & Mahambare, 2003; Li & Liu, 2005; Iqbal & Mumit, 2017; Wang & Wong, 2009; Bende-Nabende et al., 2001; Jyun-Yi & Chih-Chiang, 2008). The following sections present detailed literature that includes some key variables affecting the growth performance of foreign direct investment like trade openness, macroeconomic stability, financial development and economic freedom.

## II. Foreign Direct Investment, Trade Openness and Economic Growth

There has been a huge debate in the literature regarding the relationship between trade policies adopted by a country and its economic performance. The liberal economists argue that the countries following a free trade regime experience faster economic growth while others believe that it is the protectionist trend that helps an economy grow and not the liberal trade policies. The rationale behind the positive openness-growth nexus is that trade openness results in specialization and division of labor contributing to better resource allocation, thereby improving the productivity in an economy. Some studies prove empirically that more open economies are associated with faster economic growth (Harrison, 1996; Greenaway et al.; Edwards, 1998). It is widely argued that the growth enhancing impact of FDI is not independent but is conditional upon the characteristics of host economy of which trade openness is considered to be very important. Nair-Reichert & Weinhold (2001) suggested that the relationship between investment, both foreign and domestic, and economic growth is highly heterogeneous in developing countries and there is some evidence that the potential of FDI in raising future growth rates is higher in more open economies. Nunnenkamp & Spatz (2003) found a positive relationship between FDI and economic growth in developing countries. However, this relationship is affected by the host country characteristics like GDP per capita, schooling, institutional development and openness to trade. Prüfer & Tondl (2008) analyzed the FDI-growth relationship in Latin American (LA) countries employing Bayesian Model Averaging (BMA) and found FDI to have a strong correlation with

productivity growth in LA subject to a well-developed legal system and macroeconomic stability. In other country contexts, human capital or income threshold as well as trade openness are important channels to reap positive productivity effects of FDI. Athukorala & Chand (2000) investigated the effect of trade orientation of FDI receiving countries on the productivity gains from international production of foreign affiliates by studying the manufacturing affiliates of United States transnational corporations from over 44 countries. The results suggested that the productivity gains from international production are found to be greater under a trade policy regime which is more open in nature. Cinar & Nulambeh (2018) studied the relationship between FDI, trade openness, inflation and economic growth in Sub-Saharan African countries and the findings revealed that foreign direct investment and trade openness show a significant positive impact on economic growth whereas inflation shows a negative impact. The paper recommends the policy making institutions to devise strategies aimed at attracting more FDI to Africa. Basu et al. (2003) examined the causal linkage between FDI and economic growth in a panel of 23 developing countries and found a bidirectional causality between FDI and economic growth in more open economies whereas in closed economies, a unidirectional causality is found running from GDP to FDI. Liu et al. (2002) found a bi-directional causal linkage between economic growth, FDI and exports indicating that economic development, exports and FDI reinforce each other under open trade policy regime. Wijeweera et al. (2010) revealed positive impact of FDI inflows on economic growth in presence of skilled labor force. Moreover, it shows a negative effect of corruption on economic growth whereas trade openness exerts a positive influence on economic growth via efficiency gains. Mehic, Silajdzic, & Babic-Hodovic (2013) found that FDI exerts a significant positive impact on economic growth in the seven southeast European countries and the results are robust when data on domestic investments was included. Moreover, it is found that trade openness and macroeconomic stability are the main determinants of growth in these countries.

As revealed by the studies of Balasubramanyam et al. (1996), Kohpaiboon (2003), and Atique et al. (2004), the growth enhancing impact of FDI tends to be greater in countries that pursue an export-promotion policy than in those adopting an import-substitution one, thus providing support to the famous Bhagwati hypothesis. Another study by Balamurali & Bogahawatte (2004) showed the positive impact of both FDI and trade openness on economic growth of Sri Lanka. Sakyi et al. (2015) revealed that the interaction between FDI and trade openness is highly significant in promoting the economic growth. The paper has policy implications for Ghana recommending that FDI be channelized into such export-oriented sectors of the economy where it has a comparative advantage. Khamphengvong & Srithilat (2017) found a statistically significant positive impact of FDI and trade openness on economic growth in the long-run in Lao PDR. Yusoff & Nuh (2015) revealed that both FDI and international trade are significant determinants of economic growth. Adhikary (2011) assessed the causal nexus between FDI, trade openness, capital formation, and economic growth in Bangladesh. A statistically significant long-run relationship is found among the variables. Unidirectional long-run causality is found to run from changes in FDI, trade openness and capital formation to the economic growth rates. FDI and level of capital formation exert a significant positive impact on changes in GDP whereas trade openness shows a strong negative, but diminishing impact on economic growth. Belloumi (2014) used ARDL model to co-integration to test the long-run relationship among FDI, economic growth and trade openness in Tunisia, and Granger causality to test the causal relationship between these variables. The findings revealed a long-run relationship among the variables while taking FDI as the dependent variable. However, no causal relationship was found between FDI and economic growth in the short-run. Similarly, no causality was found between trade openness and economic growth.

### **III. Foreign Direct Investment, Macroeconomic Stability and Economic Growth**

It is a widespread belief that economic stability at macro level seems to be favorable for economic growth of a country. For instance, high rates of inflation often proxied for macroeconomic instability result in adverse and uncertain business environment leading to reduction in the economic growth rates. By creating an adverse business climate, macroeconomic instability can lead to reduction in foreign capital inflow and productivity of existing foreign investment in a country. Against this backdrop, it becomes interesting to review some empirical studies that have been conducted to study such phenomena. Jallab et al. (2008) found that FDI does not affect economic growth independently in MENA countries and the growth impact of FDI is independent of trade openness and income per capita. It is, however, found that FDI exerts a significant positive impact on economic growth in presence of macroeconomic stability. Alguacil et al. (2011) investigated the FDI-growth relationship in developing countries for the period 1976–2005. To account for the differences in the level of income, two sets of developing countries have been used in this study, that is, the low and lower-middle income countries and the upper-middle income countries as classified by World Bank. The findings reveal a significant positive impact of FDI on economic growth in the low and lower-middle income countries and the same effect persists even after considering structural, institutional and macroeconomic factors in the regression. For the upper-middle income countries, macroeconomic stability has a significant impact on the FDI-growth relationship. Abdelmalki et al. (2012) tested the contribution of macroeconomic stability in the FDI-growth nexus in a sample of 87 developing countries in Africa, Latin America, Caribbean and Asia and found a positive impact of FDI inflows on growth in the countries of Africa, Latin America and Caribbean but not so in Asia. Macroeconomic instability (measured by inflation) affects the economic growth of African countries in a negative manner. The positive effect of inward FDI flows on growth is observed only when

inflation does not exceed a certain level in these countries. A study tested whether a robust macroeconomic policy framework is related with faster economic growth in a set of 41 developing countries at a given investment rate. The findings revealed that macroeconomic instability exerts a negative impact on both investments as well as economic growth in these countries (Bleaney, 1996). Prüfer & Tondl (2008) found that there exists a strong correlation between FDI and productivity growth in Latin America subject to a well-developed legal system and macroeconomic stability. Mehic et al. (2013) found a significant positive growth impact of FDI in the seven southeast European countries and the main determinants of growth were found to be trade openness and macroeconomic stability. Bengoa & Sanchez-Robles (2003) suggest that foreign direct investment has a positive correlation with economic growth in the recipient countries. However, the host country requires a minimum threshold level of human capital, economic stability and liberalized markets in order to reap the long-term benefits of FDI flows.

### **IV. Foreign Direct Investment, Financial Development and Economic Growth**

There is a notable evidence in the literature regarding the significant role played by financial development in the economic growth of a country. It is believed that efficient financial systems lead to improvement in economic growth rates due to better capital allocation and reduction in transaction costs. Beck et al. (2000), King & Levine (1993a, 1993b) reveal that well-developed financial systems enhance economic growth and development. Many researchers argue that successful acquisition of new technology introduced by foreign firms often requires external financing which is possible only if the host economy has a well-developed and efficient financial system in place. Alfaro & Charlton (2007) revealed an association between FDI at the industry level and higher growth, which is found to be stronger for industries which have much greater skill requirements and depend more on external finance. The empirical studies reveal the

significant role played by financial markets in helping the host countries realize the benefits of FDI, thus recommending the policy makers to improve the level of financial market development so as to gain from the spillovers generated by FDI (Alfaro et al., 2004; Alfaro et al., 2009). Kelly (2016) found a long-run relationship between FDI and economic growth only in countries which have achieved a sufficient level of financial sector development. Hermes & Lensink (2003) suggested that the growth enhancing effect of FDI is positive for such countries which have sufficiently developed financial systems. Alfaro & Chauvin (2016) found that the spillover benefits from FDI are more pronounced in financially developed economies which allow domestic firms to gain significantly from the opportunities provided by foreign firms. Durham (2004) did not support a direct, independent positive impact of FDI and EFPI (equity foreign portfolio investment) on growth, but revealed that the growth enhancing effect of FDI and EFPI depends on the financial and institutional development of the host countries. Chee & Nair (2010) revealed the significant role played by financial sector development in generating the positive impact of FDI on economic growth and suggested that the complementary effect of FDI and financial sector development on growth is more pronounced for least developed countries as compared to developing and developed countries. Prasad et al. (2007) revealed that the countries depending on foreign capital grow slower than the ones relying on domestic capital. The relationship between FDI and growth has been assessed through a meta-regression analysis (MRA) while conducting a thorough analysis of 880 estimates reported in 108 publications. The findings revealed that FDI exerts a positive impact on economic growth and the two important absorptive capacity variables for FDI to positively affect growth are financial development and trade openness of the host economy (Iamsiraroj & Ulubaşoğlu, 2015). Azman-Saini et al. (2010) found that the growth-enhancing effect of FDI can be realized only when the host economy exceeds a minimum (threshold) level of financial market development. Lee & Chang (2009) revealed a weak short-run but a strong

long-run interrelationship among FDI, financial development and economic growth. Anwar & Nguyen (2010) revealed a bi-directional linkage between FDI and economic growth in Vietnam. However, the growth impact of FDI tends to be greater when resources are invested in human capital, financial development and reduction of technological gap between domestic and foreign firms. Ljungwall & Li (2007) revealed that financial sector development in host country enhances the growth impact of foreign direct investment. Adeniyi & Omisakin (2012) tested the causality between foreign direct investment and economic growth with the impact of financial sector development on the FDI-growth nexus in the Economic Community of West African States (ECOWAS). The findings support the role of financial sector development in FDI-growth relationship in Ghana, Gambia and Sierra Leone. However, no causal linkage between FDI and economic growth is observed in Nigeria regardless of the level of financial sector development. Kholdy & Sohrabian (2005) found that FDI does not granger cause economic growth even in countries having well-developed financial markets.

#### V. Foreign Direct Investment, Economic Freedom and Economic Growth

A well-developed and investment friendly institutional framework is believed to offer a favorable climate for foreign investment. The domestic investment climate characterized by good governance, market supporting environment, protection of property and sufficient level of freedom to operate in a country becomes a major attraction for foreign investors. Such a supporting environment tends to ease out the business hurdles faced by foreign investors thereby facilitating them in a better manner. The domestic investment climate of an economy is captured by a composite measure, that is, the level of economic freedom present in a country. According to the index proposed by Heritage Foundation, economic freedom comprises of ten components namely property rights, freedom from corruption, tax burden, government spending, business freedom, labor freedom, monetary freedom, trade freedom,

investment freedom and financial freedom. An economically free country provides a favorable investment environment to foreign investors. Imtiaz & Bashir (2017) while analyzing the relationship between domestic investment climate (measured by economic freedom index) and foreign direct investment found economic freedom to play a significant role in attracting inward FDI in South Asia. Quazi (2007) also found economic freedom to be a positive and significant determinant of FDI in East Asian countries. Since FDI is believed to impact economic growth in host economy, this motivates researchers to identify other variables that can enhance the growth impact of FDI. Zghidi, Sghaier, & Abida (2016) found that the growth enhancing effect of FDI is more evident in presence of economic freedom variable. Azman-Saini, Law, & Ahmad (2010) and Burcu (2019) revealed that FDI does not exert an independent influence on economic growth but the growth performance of FDI depends on the level of economic freedom present in a host country. Moreover, some studies found a positive and significant impact of foreign direct investment and economic freedom on the economic growth of developing countries (Sheshgelani & Badri, 2017; Hayrdaroglu, 2016).

## **VI. Foreign Direct Investment in BRICS economies**

The BRICS (Brazil, Russia, India, China and South Africa) economies which are considered to be most developed of the emerging economies are projected to remain the key drivers of growth in the world economy in future. Since the Global Financial Crisis, 2008-2017, the GNP (Gross National Product) per capita growth rate at the global level has dropped to only 1.7% at an average. But the global per capita growth during this period has been largely driven by the BRICS group of countries, averaging 5.4%. These countries account for 30.4% of world GNP at present. BRICS economies have witnessed a spectacular rise in FDI inflows (Nistor, 2015; Kapoor & Tewari, 2010). In order to attract FDI inflows, these offer many benefits to foreign investors like cheap labor, natural resources and huge markets. Ranjan & Agrawal (2011) revealed that trade openness,

market size, macroeconomic stability, labor cost, and growth prospects are the main determinants of FDI inflows in BRIC countries, while Vijayakumar et al. (2010) found in his study that market size, labor cost, infrastructure, currency value and gross capital formation were found to be the potential determinants of inward FDI flows into these economies. However, economic stability, growth prospects and trade openness were found to be insignificant in determining FDI inflows. Duan (2010) undertakes trend and industrial pattern analysis of FDI inflows in BRIC economies and finds the overall increasing trend in FDI inflows in these countries. In Brazil, Russia and India, the tertiary sector is the major recipient of inward FDI flows followed by secondary and primary sectors. In China, secondary sector receives the major portion of total FDI inflows whereas the primary and tertiary sectors receive a little amount of inward FDI. Only a few researchers have focused on the FDI-growth nexus in BRICS economies revealing a positive linkage between the two (Agrawal, 2015; Hayrdaroglu, 2016).

## **Conclusion**

Foreign direct investment is considered to be a panacea for economic growth of countries across the globe. This has motivated researchers to examine the FDI-growth relationship in host countries. From the analysis of literature review conducted in this paper, it is synthesized that a mixed evidence is found in empirical research focusing on the role of FDI in enhancing the economic growth of the host country. Moreover, the growth performance of FDI is found to vary with respect to different countries depending on the host country characteristics like trade openness, macroeconomic stability, financial development and economic freedom. An effective policy framework should be adopted by countries aimed at upgrading the existing absorptive capacities in tandem with the inward FDI flows in order to reap the positive benefits of foreign direct investment. Reforms should be undertaken by host countries that are aimed at improving resource allocation, easing out the complex regulatory procedures for businesses, improving political and economic

environment for better FDI attraction, and diversifying the economy so as to reduce the dependence on primary exports.

The FDI inflows to developing economies have increased tremendously over the last two decades and the BRICS economies have played a significant role in the paradigm shift in global investment. A handful of studies conducted on the FDI-growth nexus in these economies

reveal a positive association between the two variables. It is worthwhile to highlight that the growth trajectory of BRICS economies coupled with their rising share in global FDI flows makes it interesting for future researchers in this field to study the various dimensions of growth performance of FDI in these fastest emerging economies as only a few studies have been conducted in this regard.

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