FDI AND POVERTY REDUCTION: 
A CRITICAL REAPPRAISAL OF THE ARGUMENTS

Andrew MOLD*

Abstract - Over the last two decades, enormous efforts have been made by developing countries to attract Foreign Direct Investment (FDI). It is commonly agreed upon that, by accelerating economic growth, FDI is a determining feature in poverty reduction. This paper argues that this view needs to be qualified by considering the stylistic facts and existing empirical evidence on the contribution of FDI to growth and poverty reduction. Echoing work by trade economists on the impact of trade on poverty reduction, a simplified framework is suggested which breaks down the influence of FDI into its "growth enhancing" and "distributional" effects. Contrary to the (now) conventional wisdom, little evidence is found that FDI is a major instrument for poverty reduction.

Key Words - FOREIGN DIRECT INVESTMENT, POVERTY REDUCTION, LEAST DEVELOPED COUNTRIES, MULTINATIONALS.

JEL Classification : F21, F23, O19.

The author would like to thank Prof. Van den Bulcke, Filip De Beule, Danny Cassimon and other participants at the Seminar on Foreign Direct Investment and Development at the Institute of Development Policy and Management, University of Antwerp, 23/1/2004, for their useful comments regarding an earlier draft of this paper. He would also like to thank a nameless referee of Region et Développement for some very insightful suggestions to improve the paper. The opinions expressed in this paper are of the author and do not necessarily reflect the opinions of the ECA.

* Trade and Regional Integration Division, Economic Commission for Africa, Addis Ababa; AMold@uneca.org.

Revue Région et Développement n° 20-2004
1. INTRODUCTION

In the 1990s a world-wide boom took place in FDI flows. That boom was especially pronounced in developing countries, where FDI became the primary source of private sector finance. Standing at a record $246 billion in 2000, FDI reached a value over four times higher than international aid flows. Even after the subsequent downturn in FDI in the aftermath of 7/11, the most recent estimate for 2002 puts FDI flows to developing countries at $162 billion, around three times more important than aid (UNCTAD, 2003; Annex Table B.1.). Interpretations of these trends are commonly infused with much enthusiasm, with many authors implying that the private sector is set to take over where the public sector has left off, and that, beyond guaranteeing property rights and providing a basic infrastructure, development is now possible without a substantial role either for the state or for international aid. In this context, it is also often alleged that FDI is making a fundamental contribution to poverty reduction.

It is worth noting that, with a few exceptions, this rosy interpretation of the role of FDI as an instrument for poverty reduction has rarely been supported by much empirical evidence, either at the micro or macro level. Much in the same way as is assumed in the trade literature that trade is good for poverty reduction, it has simply been inferred that, because economic growth is "good for the poor", and FDI is assumed to be good for growth, ceteris paribus FDI must be good for poverty reduction. For instance, in a recent extensive OECD (2002:9) report on the subject of FDI and development, the authors claim that "FDI... contributes to higher economic growth, which is the most potent tool for alleviating poverty in developing countries" (page 9).1

Yet after a decade of emphasis on the benefits of FDI, recently there have been signs of a shift in opinion towards a more critical and, in the opinion of this author, balanced view. This paper takes, as its point of departure, comments by Joseph Stiglitz on the subject in his controversial book "Globalisation and its Critics" (2002). After a lengthy spell at the World Bank (often promoting schemes backed by multinational companies and international financiers), Stiglitz has revealed himself to be surprisingly sceptical about the benefits of FDI. For Stiglitz, FDI frequently turns out to be a mixed blessing – although he accepts the potential of FDI as a source of capital and knowledge transfer, he argues that FDI raises a series of issues essentially related to the abuse by

---

1 In a similar vein, Klein and al. (2001) forthrightly claim that "FDI is a key ingredient for successful economic growth in developing countries... As growth is the single-most important factor affecting poverty reduction, FDI is central to achieving that goal."
multinational corporations of their market power. The crux of his argument is that multinationals exert pressures on developing country governments that they are typically poorly equipped to resist: multinationals distort policy choices, and make control of the domestic economy increasingly difficult. What is remarkable about Stiglitz's observations is not the specialist information he provides (he is not particularly well-known as an expert on the subject), but rather the broad brushstrokes of his arguments: the way he stresses the vices instead of the virtues of FDI.

This article is intended to address these controversies, and review some of the recent literature on the impact of FDI on poverty reduction. It is suggested that a re-examination of the issues is required, and that a return to a more pragmatic approach on the appropriate role of FDI and multinational companies would be advisable – multinationals are neither paragons of economic virtue, nor the *bête noire* of radical thinking. They are unlikely to turn around an economy which is in a dire situation. But providing the right institutional framework is in place, then a cogent argument can be made in favour of using FDI and the activities of MNEs to further goals of national development. Unfortunately, this is not currently the case in many of the poorest developing countries – important legislative deficits exist in areas such as fiscal and competition policy which impede countries from making full use of FDI-developmental potential.

Although evidence is drawn from other developing countries, the paper focuses principally on the perspectives and potential role of FDI in the 49 Least Developed Countries (LDCs), according to the classification of the United Nations. Although the absolute magnitude of the problem of poverty is much greater in countries like China, India, or Nigeria, the LDCs face a series of problems which are quantitatively and qualitatively different: the largest developing countries are able to borrow on international markets, they can attract international investments targeted on their domestic markets and, because of their political and economic clout, enjoy a far better negotiating position vis-à-vis foreign investors. In contrast, for the typical small LDCs, with their restricted access to foreign capital, limited domestic markets, and lack of capacity to resist external political pressures, the situation is far more difficult.

The paper begins with a brief critical review of the stylistic facts of FDI inflows to developing countries, and explains why FDI's potential as a tool for poverty reduction may be limited. The third section provides a summary and discussion of some of the objections that Stiglitz puts forward to an excessive reliance on FDI. In particular, we focus on the controversies related to the growing involvement of multinationals in the provision of public services and utilities in developing countries, an issue which Stiglitz singles out for special criticism. The fourth section outlines a tentative framework which allows a more detailed analysis of how FDI can impact on poverty reduction. Following the burgeoning literature on trade and poverty reduction, and rather than focusing on
the fragmented evidence regarding the contribution of FDI to employment, technological transfer, profit repatriation, etc., it is argued that the overall impact of FDI can be broken down into its growth and distributonal impacts. Finally, section five contains our conclusions.

2. FDI AND DEVELOPMENT IN THE LDCS: THE STYLISTIC FACTS

Since the beginning of the boom of FDI towards developing countries began in the early 1990s, and with the support of many academic economists, the International Financial Institutions (IFIs) have been propagating a highly favourable view of its effects. This positive viewpoint stands out in stark contrast to the received wisdom of the 1970s and 80s, which held that the contribution of FDI to economic development was generally dependent on the form and nature of the foreign investment. As Rodrik (1999:37) has observed, "The attitude of many developing-country policymakers towards Direct Foreign Investment has undergone a remarkable turn-around in the last couple of decades... Multinational enterprises used to be seen as the emblem of dependency; they have now become the saviors of development".

Previously, at one extreme, radical theorists were totally scathing of the role that FDI could play – multinationals were simply equated with foreign exploitation, and it was considered inconceivable that these firms could contribute anything to the development of the host economy. But even among academics less hostile to foreign investment, it was commonly accepted that FDI could impede the development of the national economy if multinational corporations ended up dominating local industry and distorting the domestic policy environment to their favour.

In the aftermath of the Washington Consensus and the fall of the centrally-planned economies, that hard-nosed (and, arguably, more pragmatic) position on FDI faded away rapidly. With the surge in private sector investment towards developing countries, and the relative stagnation of official aid flows, a distinctively up-beat interpretation is given to the role of corporate investment in poverty reduction. As Alain Gillespie (2003), Chief Executive of CDC Capital Partners has recently commented, "in the first world we don't question the link between risk capital generating returns and its benefits for society in terms of employment, etc., so why should we suspend this model when we focus on poor

2 Broadly representative of these views is the work of authors such as Rodney (1972).
3 An article of Lall (1984) is a good example of this shift in attitudes. As one of the most respected experts in the impact of MNEs on host economies, Lall's article represents a kind of mea culpa with regard to his earlier, more critical, stance. The author confesses that he had previously been excessively pessimistic, and now recognises the role MNEs can play in stimulating local economic development.
countries? The World Bank’s Private Sector Development (PSD) Strategy is a tangible manifestation of this new approach to private sector financing in the poorest developing countries.

Against this backdrop, FDI is now contrasted favourably with other forms of capital flows in terms of a number of what are considered intrinsic benefits: It is argued that FDI provides a relatively stable, risk-free, form of finance for development in capital-poor countries. Compared with more speculative flows (bank loans, or portfolio investments), or indeed, international aid, FDI has a relatively low variation coefficient (UNCTAD, 1999). This is a logical consequence of the irreversibility of many investments, especially in a developing country context (where it may be difficult to liquidate an investment in a crisis, when asset prices fall sharply and few alternative buyers are available). Proponents of multinationals also commonly stress the contribution of inbound FDI to technological acquisition and competitive upgrading of national economies (e.g. Dunning and Narula, 1997). Finally, much is made of the capacity of multinationals to facilitate market access for the products produced in the poorest developing countries, such as the horticultural supply-chains set up in African countries like Kenya or Zimbabwe to service British supermarkets (Dolan et. al., 1999).

Although these points have much validity, some of the more extravagant claims for FDI, development and poverty reduction can easily be dismissed, simply by looking at some of the stylistic facts about FDI. There is little doubt that the FDI flows towards developing countries have risen sharply over the last 30 years or so, both in absolute terms and as a percentage of GDP. But this dramatic growth reflects a global up-shift in FDI, rather than an increase in the relative attractiveness of developing countries as a group (Figure 1).

Despite year-on-year variations, the trend line in Figure 1 reveals that there is no clear tendency regarding the share-out of FDI between high income

---

4 In making this statement, it could be argued that Gillespie is guilty of drawing a false dichotomy. It is not an issue of suspending belief in the market mechanism in poor developing countries, but rather, in a context of scarcity and weak institutions, of qualifying it. As Stiglitz (2002:73-74 *inter alia*) stresses, "whenever information is imperfect and markets incomplete, which is to say always, and especially in developing countries, then the invisible hand works most imperfectly." (emphasis in original). In such circumstances, private sector solutions may not always be the most appropriate.

5 The PSD Strategy can be seen as a reaction of the Bank to the acid criticisms directed towards it by the International Financial Institutions Advisory Commission (the "Meltzer Commission"). This new instrument is a joint collaboration between the IFC and the IDA and is intended to accelerate private investment in the poorest developing countries, especially in basic social services.

6 Empirical analysis confirms that foreign investors sat tight during the crises in East Asia in 1997 and Mexico in 1995, while other investors withdrew funds rapidly, only adding to the incipient crises (see Lipsey, 2001).
and developing countries. Typically developing countries take around 20 percent of global inflows, although that figure has increased to over 40 percent before the onset of the debt crisis in 1982, and again rose sharply during the recession in the industrialised countries during the first half of the 1990s, to fall back sharply subsequently. Even the slightly positive long-run trend observed in Figure 1 regarding the share of FDI flowing into developing countries is dependent upon the "China Effect" – the fact that China alone is currently the largest recipient of FDI in the world (if we discount Luxembourg as an atypical case), and that over the last decade it has been attracting in excess of $40 billion annually. If we discount the Chinese case as atypical, the long-term trend of the FDI share to developing countries is downward. This reveals another important characteristic of FDI flows: despite much hubris about the globalisation of markets, multinationals tend to focus their activity on a few select markets.

*Figure 1: FDI world flows and shares to Developing Countries, 1970-2002*

Indeed, one of the most outstanding characteristics of FDI is its uneven distribution in space: just ten developing countries have tended to be the most important destinations for FDI over the past three decades (with the exception of China, which only appeared as a host to FDI in the early 1980s). Those countries are Argentina, Brazil, China, Hong Kong, Indonesia, Malaysia, Mexico, Saudi Arabia, Singapore and Thailand. Together, they have taken in over two thirds of inflows into the developing world since 1970 (Thomson, 2000:16). Moreover,
these concentrations of FDI occurred despite the liberal FDI policies that many developing countries introduced over the last two decades, suggesting that FDI is not generally policy-led, as orthodox economic advice would have us believe, but driven fundamentally by overall economic performance (Chang, 2003:251).

Figure 2: FDI flows to the 49 Least Developed Countries, 1971-2002

It is no coincidence that the aforementioned "success stories" in attracting FDI are typically developing countries with large domestic markets, indicative of the fact that much FDI continues to be market-seeking rather than efficiency or factor seeking. It is thus hardly surprising that the poorest developing countries, typically with small domestic markets and, by definition, low per capita incomes, have been relatively shunned by foreign direct investors. Although inflows have increased substantially in absolute terms since the 1970s (reflecting the worldwide upshift in FDI flows), the overall share of the 49 LDCs in total FDI inflows has been progressively declining, from a maximum of 2.5 percent to just a little over 0.5 percent (Figure 2). Bearing in mind these 49 countries account for around 10 percent of the world population, it is clear that the LDCs are effectively marginalised from FDI inflows.

In addition, FDI inflows are still highly concentrated within the group of 49 LDCs. In 2000, 47 per cent of net FDI flows to all LDCs went to just four oil-exporting LDCs – Angola, Equatorial Guinea, Sudan and Yemen (UNCTAD,
2002-9). These facts in themselves are indicative of the relatively limited role that FDI can play as an instrument for poverty reduction – in spite of the liberalisation of capital inflows undertaken by the vast majority of LDCs, FDI is simply not present in the volume required to make much impact on poverty levels. Nor is it, according to the most optimistic predictions, likely to be so in the near future.

Having said this, it is important to realise that, while net financial flows towards the LDCs have stagnated since the early 1980s, the composition has changed (Table 1). Despite all the rhetoric about the priority to be given to the poorest developing countries, official aid has actually fallen over the last decade. Meanwhile, there has been a notable increment in private investment. Because the LDCs lack the financial markets to attract portfolio investment, and private debt flows have in recent years been negative, most of this increment has come in the form of FDI. Estimated FDI to the LDCs reached in 1999 a record $5.2 billion, equivalent to more than a third of aggregate net resource flows.

Table 1: Long-term net capital flows to LDCs, 1989-2000
(Annual $ millions, annual average)

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Aggregate net resource flows</td>
<td>13 933</td>
<td>13 308</td>
<td>15 039</td>
<td>13 331</td>
</tr>
<tr>
<td>Official net resource flows</td>
<td>12 396</td>
<td>10 719</td>
<td>9 817</td>
<td>9 630</td>
</tr>
<tr>
<td>Grants, excluding technical cooperation</td>
<td>8 392</td>
<td>7 958</td>
<td>7 753</td>
<td>7 578</td>
</tr>
<tr>
<td>Official debt flows</td>
<td>4 004</td>
<td>2 761</td>
<td>2 064</td>
<td>2 053</td>
</tr>
<tr>
<td>-Bilateral</td>
<td>1 009</td>
<td>-36</td>
<td>-439</td>
<td>-327</td>
</tr>
<tr>
<td>-Multilateral</td>
<td>2 995</td>
<td>2 797</td>
<td>2 503</td>
<td>2 379</td>
</tr>
<tr>
<td>Private net resource flows</td>
<td>1 538</td>
<td>2 589</td>
<td>5 222</td>
<td>3 701</td>
</tr>
<tr>
<td>-Foreign direct investment, net inflows</td>
<td>1 132</td>
<td>2 432</td>
<td>5 276</td>
<td>4 315</td>
</tr>
<tr>
<td>as % of aggregate net resource flows</td>
<td>8.1</td>
<td>18.3</td>
<td>35.1</td>
<td>32.4</td>
</tr>
<tr>
<td>-Profit remittances on FDI</td>
<td>661</td>
<td>762</td>
<td>910</td>
<td>993</td>
</tr>
<tr>
<td>as % of total FDI inflows</td>
<td>58.4</td>
<td>31.3</td>
<td>17.2</td>
<td>23.0</td>
</tr>
<tr>
<td>-Portfolio equity flows</td>
<td>0</td>
<td>40</td>
<td>4</td>
<td>3</td>
</tr>
<tr>
<td>-Private debt flows</td>
<td>406</td>
<td>666</td>
<td>-58</td>
<td>-617</td>
</tr>
<tr>
<td>Aggregate net transfers</td>
<td>12 162</td>
<td>11 396</td>
<td>12 979</td>
<td>11 358</td>
</tr>
<tr>
<td>Interest payments on long-term debt</td>
<td>1 110</td>
<td>1 150</td>
<td>1 149</td>
<td>980</td>
</tr>
</tbody>
</table>

Source: Adapted from UNCTAD, 2002:8.

Like it or not, the governments of the LDCs have had to adjust to these new realities. It is also worth noting that the financial cost of these FDI inflows have increased significantly since the late 1980s – at $993 million in 2000, profit

---

7 The top 10 recipient LDC countries in 1999 were Angola, Bangladesh, Cambodia, Lesotho, Mozambique, Myanmar, Sudan, Uganda, the United Republic of Tanzania and Zambia. Together these countries accounted for over 86 per cent of FDI inflows into all LDCs in the period 1998-2000.
repatriation by multinationals actually exceeded interest payments on long-term debt ($980 million). In this sense, although the risk is borne by the foreign investor, FDI does clearly not constitute a "free lunch". Indeed, recently a number of concerns have been raised regarding the rate of profit repatriation and how it can impose significant financial costs on developing countries.8

How do these FDI flows translate into the tangible activity of multinational firms? As Annex Table 1 reveals, the multinationals present in LDCs dedicate themselves to a surprising variety of activities – it is not true that they are purely focussed on the extraction of primary resources.9 Many of the LDCs are resource-poor countries, so it is logical that this pattern of investment emerges. According to the data elaborated by UNCTAD, industries represented include chemical, pharmaceutical, freight transport, tobacco, bottled and canned drinks, trading, insurance, etc. The potential for contributing to export diversification or import-substitution is correspondingly large. Given the enormous costs that dependence on commodities has supposed (see UNCTAD, 2004), this contribution is not to be gainsaid. Indeed, it may constitute one of the major ways in which FDI can accelerate development in the poorest developing countries. What this list does not reveal is the growing tendency for multinationals to become involved in the provision of social services and utilities in LDCs. Because of the central role of basic services in strategies for the reduction of poverty, this issue is especially controversial, and will be discussed in the following section.

Finally, much is made by some analysts of the employment-creating potential of FDI. Unemployment is certainly one of the major challenges facing developing countries, and a consensus exists that creating employment opportunities is one of the most effective ways of rapidly reducing poverty levels. However, the moot point is whether promoting FDI is a very efficient way of reaching this objective. Examining the same ratio for the entire universe of MNEs worldwide in the same year, MNEs employed only 3.5 per cent of the total world economically active population (EAP) and 6 per cent of total people employed around the world (Narula, 2004:21). This is not surprising, given the privileged access that multinationals have to capital, and their well-documented tendency to use capital intensive production techniques10.

---

8 See, for instance, UNCTAD (2003b), Chapter VI.
9 The data in Annex Table 1 have been adapted from UNCTAD (2001), on the basis of firms for which the corresponding data were available. The original table shows the values of sales for affiliates, but the figures were not reliable, and so have been omitted.
10 To cite just one example, Mozal, the aluminium plant located in Mozambique, represents the largest ever single foreign investment in sub-Saharan Africa, totalling some $2.4 billion dollars. Yet Mozal directly employs just 800 workers, equivalent to an average capital intensity of approximately $3 million per worker in one of the poorest countries in the world.
Despite these stylised facts, policymakers in developing countries have often made strenuous efforts, via tax breaks and subsidies, or the establishment of Export Processing Zones (EPZs), to attract FDI on the grounds that it contributes to employment. Yet it has been estimated that total employment in developing country EPZs is no more than 4 million (Dicken, 1998:131). Jobs in EPZs typically represent no more than 5 percent of total employment in the manufacturing sector of developing countries and are tiny compared with the estimated 300 million people who work in the "informal sectors" (Madeley, 1999:113). When one considers that there are an estimated 1,200 million people living on less than $1 a day, it is clear that the potential impact of EPZs on poverty reduction is limited. It is also no coincidence that, with the exception of Mexico and China, the developing countries that have made best use of these practices to attract foreign investment tend to be relatively small island states such as Mauritius. In short, as models which other developing countries could follow, their relevance is limited. Yet governments of developing countries have allocated substantial amounts of scarce funds, and forfeited a considerable amount of tax income, to attract companies into the EPZs, income which could be used for poverty-reduction programmes or essential social expenditures.

3. STIGLITZ'S CRITIQUE OF FDI – REVISITING OLD GHOSTS?

The existence of multinationals sits very uneasily with orthodox economic theory – in a perfect neoclassical world, there would be no need for multinationals or FDI: in the absence of transaction costs, markets could be costlessly and effortlessly supplied from any point of the globe. From this perspective, multinational affiliates arise in situations where barriers to entry are high and imperfect competition is the rule – their presence should correspondingly be more, not less, likely in the least developed countries. As we have seen, this type of a priori theorizing does not correspond well with current patterns of FDI and multinational activity.

The other key issue is whether MNEs will be welfare enhancing for host countries. A purely theoretical reply, based again on orthodox logic, would be "no": they are likely to distort undeveloped markets further, and apply productive techniques which are highly inappropriate in a developing country context. As Moran (1999:2) notes in his extensive review of the literature, "Quite apart from important specific harmful activities (such as permitting pollution, carrying out operations with inadequate health and safety standards, or tolerating the behaviour of abusive subcontractors)... the possibility that FDI

11 Moreover, those jobs are geographically highly concentrated. Mexico alone accounts for 600,000 jobs. China too is responsible for a large share of total employment in EPZs. The vast majority of developing countries have an insignificant participation in the employment generated by EPZs.
might lead to fundamental economic distortion and pervasive damage to the development prospects of the country is ever present."

In this context, the position that Stiglitz takes on the issue of FDI may not stand out for its originality, but the views he puts forward are certainly illustrative of a wider change in opinion regarding FDI. As such, his critique provides a useful starting point in any discussion on the benefits and dangers of adopting a developmental strategy based on FDI, especially in the context of the poorest developing countries.

Stiglitz recognises that FDI has played an important role in many (though not, he stresses, all) cases of successful development, such as Singapore, Malaysia or China. But, he adds, FDI is a mixed blessing, and brings a whole set of problems of its own. Indeed, in a sentence reminiscent of the dependency school literature of the 1970s, he even talks of how the International Financial Institutions (IFIs) have promoted a model of development which betrays a "colonialist-type mentality": instead of persuading developing countries of the importance of producing their own indigenous entrepreneurial class, they are urged by the IFIs to depend on foreigners. The fact that Korea and Japan achieved spectacular success even though foreign investors paid no significant role in their development is ignored (Stiglitz, 2002:72).

Stiglitz made his prestigious reputation as an academic economist with his work on imperfect markets and asymmetric information. Unsurprisingly, therefore, in his critique of the excessive promotion of FDI, he devotes particular attention to the way in which multinationals abuse their market power in developing country, undermining local competitors and charging prices which, from the point of view of Paretian efficiency, are socially non-optimal. In this sense, Stiglitz laments the lack of effective competition laws in many developing countries. But his critique goes far beyond the standard textbook complaint of typical oligopolistic or monopolistic behaviour. Citing various cases where multinationals have used their influence to pressure developing country governments, he goes to the extreme of arguing that "foreign direct investment comes only at the price of undermining democratic processes. This is particularly true for investments in mining, oil, and other natural resources, where foreigners have a real incentive to obtain concessions at low prices." (ibid. 72).

The political power behind many corporate investments is singled out by Stiglitz for criticism: the governments of the industrialised countries frequently commit excesses in defence of the interests of their own MNEs, giving way to a kind of corporate nationalism which squares badly with the idea of free trade and economic liberalism promoted by the IFIs. Stiglitz (ibid.71) cites the example of France Telecom in Ivory Coast, where the French government pressured hard for the concession of a mobile telephone license in favour of Telecom and asked the
Ivory Coast government to exclude their American competitors from the bidding. Another example given is the pressure exercised by the French government to modify a contract signed by the water company Suez Lyonnaise with the Argentinian company Aguas Argentinas, after the former realised that the conditions were not as favourable as they had initially anticipated. When corporate capitalism is manipulated in this way, overpriced utilities and underinvestment in strategically important sectors are typically the result (ibid. 54-59).

Not only does Stiglitz raise concerns over the role of multinationals in the provision of basic utilities, he also critiques the attempts by the IFIs to promote FDI in social services. There is a lot of accumulated evidence that efficient social service provision in developing countries depends fundamentally on the degree of state involvement, particularly at primary levels of attention. Mehrotra et. al. (2001), for instance, study examples of "high-achievers" in social development (countries as diverse as Botswana, Costa Rica, Cuba, and the Democratic Republic of Korea) and conclude that in all, "the state plays an impressive role in the provision of basic services". Indeed, in many of the cases studied, private provision was either actively discouraged or directly prohibited. Yet the privatisation of basic social services in LDCs is now actively encouraged by the IFIs. Representative of the views behind this policy, Klein et. al. (2001) argue that "the delivery of social services to the poor – from insurance schemes to access to basic services such as water and energy – can clearly benefit from reliance on foreign investors."

Stiglitz (ibid.) takes a quite contrary position on this issue, and reminds us that: "many government activities arise because markets have failed to provide essential services. Examples abound... When many European countries created their social security systems and unemployment and disability insurance systems, there were no well-functioning private annuity markets, no private firms that would sell insurance against these risks that played such an important role in individuals' lives... in developing countries, these problems are even worse; eliminating the government enterprise may leave a huge gap – and even if eventually the private sector enters, there can be enormous suffering in the meanwhile."

In its totality, how valid is Stiglitz's critique? The first point to note is that Stiglitz is certainly not alone in his critical evaluation of the role of multinationals in poor countries. Unlike many other contemporary critiques of globalisation and multinational corporations, Stiglitz's comments are not made in a doomatic tone, and he does accept that FDI has an important role to play in economic development. But it is not one that should be placed centre-stage, as some proponents of economic liberalisation and free market radicalism suggest. It is interesting to note that this more pragmatic view of FDI is becoming increasingly widely shared, even from sources hardly suspect of harbouring
heretical views. For instance, in a recent article, IMF economists Prakash Loungani and Assaf Razin stress a number of potential risks associated with large-scale FDI inflows, and argue that "policy recommendations for developing countries should focus on improving the investment climate for all kinds of capital, domestic as well as foreign."

The second point to make is that one does not have to go to the extreme of aligning oneself with the most vociferous critics of the multinational to accept that MNEs have frequently abused their positions of power, particularly in the case of the poorest developing countries which do not necessarily have the negotiating skills or bargaining power to resist the pressures exerted upon them. As Stiglitz points out, this has particularly been the case in the oil and mineral sectors. In an econometric analysis, Ross (2001) provides evidence of a clear association between the dependence on oil and mineral exports on the one hand and the probability of corrupt and antidemocratic regimes. Higher levels of mineral dependence are also strongly correlated with higher poverty rates and low social expenditures, and these countries tend to suffer from exceptionally high rates of child mortality and low life expectancy. Although multinationals are obviously not solely, or even principally, to blame for this situation, their massive presence in these countries clearly implicates them. The fact that there have been a number of recent initiatives to promote greater transparency and accountability in the mineral and oil industries is an explicit acknowledgement of their responsibilities in these cases.12

Thirdly, with regard to Stiglitz's critique of the involvement of FDI in the provision of basic social services and utilities, it is worth recognising the choices open to LDC governments are frequently difficult ones: in cases where state provision has deteriorated to such an extent that many public services have practically ceased to exist, it could be argued that privatization entails few, if any, risks, and could only serve to improve the current situation. Giving the tight budgetary constraints under which most LDC governments operate, public-funded investment programmes are not always feasible. Moreover, some studies suggest that privatised utilities have proved more efficient in extending coverage of services like water or electricity connections.13 On balance, the key questions

---

12 One example is the Extractive Industries Transparency Initiative launched by the UK Prime Minister, Tony Blair, at the World Summit on Sustainable Development, in Johannesburg, September 2002.
13 Barja and Urquiola (2001), for instance, have studied utilities provision in Bolivia under private management, and conclude that foreign investment made possible the increase in access to basic services in urban areas, even though access in rural areas still remains very low. In terms of connection, service expansion in the urban areas did not bypass the poor. On the contrary, in some cases access improvements appear to have been particularly beneficial to low-income households. Even though, Barja and Urquiola do still concede some adverse welfare effects of reform-related price increases.
are therefore whether host governments are prepared to accept tariff increases, with all the distributional consequences that this entails, in return for higher coverage rates, and whether the government is capable of implementing the appropriate regulatory mechanisms to ensure that the private firm does not abuse its position in what are frequently natural monopolies.

Nonetheless, to the extent that social services and utilities facilitated by private sector could undermine the commitment of the government to universal provision, policymakers need to be aware that promoting foreign investment in the social sector or utilities does set a dangerous precedent. As Hertz (2002:239) points out, "There is a real danger that their presence, their taking on of these traditional governmental roles, will create a disincentive for governments to develop appropriate institutions themselves; and that if and when the [foreign investors] pull out, there will be nothing at all to replace them, and no recourse to be had."15

The empirical evidence would seem to offer broad support to this stance. On a number of well-documented occasions, water and energy schemes in which foreign private investors have been present have produced poor results, or provided services at an exorbitantly high cost – something obviously prejudicial to the poor.16 Moreover, there are no guarantees that foreign private investors will respond positively to privatization programmes. As a UN report reminds us, "the growing tendency to leave even LDCs to the mercies of the capital market to build power plants and upgrade their telecommunications facilities has led to growing under provisioning of investments in this sector in the LDCs... Not all LDCs can access FDI in these areas or access it with sufficient urgency to meet their immediate demand for power or water" (UN, 2000:19).

14 For instance, a study of the options for Nairobi's water system by British company Halcrow Group in June 2001 concluded that a 40 percent price increase would be required if any improvements to the capital's infrastructure were to be funded (Ford, 2002:19).
15 Some multinationals themselves admit this. In Nigeria, for instance, Shell spent $52 million in 1999 in the Niger Delta region on a social investment programme building schools, hospitals, roads and bridges, etc., all services which the government had effectively abandoned since the early 1980s. Indeed, the company now employs more development specialists than the government. As one Shell executive comments, "Things are back to front here... the government's in the oil business and we are in local government." (cited in Hert, 2002:220).
16 For discussions on this, see Ford (2002) and Globalization Challenge Initiative (2002). On more than one occasion, the World Bank has itself questioned deals reached between multinationals and developing country governments. Such was the case of Enron's $800 million deal with the Nigerian government. The World Bank itself and other foreign consultants were widely reported to have objected to the terms of the agreement, saying that in haste to solve the electricity supply problem the Nigerian government had offered terms that were excessively favourable to Enron (Economist Intelligence Unit, 2000; 30).
To sum up, in discussing Stiglitz's views, the intention has not been to revisit past controversies, but rather to point out the most salient contemporary debates. It is apparent from this brief discussion that the issue is not only complicated, but also that the list of potential criticisms levelled at foreign investment as a tool for economic development remains a long one.

4. POVERTY REDUCTION AND FDI: TOWARDS A CONCEPTUAL FRAMEWORK

Statistically speaking, there appears to be a weak but existent relationship between the capacity of a country to attract FDI and lower levels of poverty. On the basis of the available data for 60 developing countries, Figure 3 shows the simple regression of FDI stock per capita and the percentage of the population living under $2 a day, with a negative correlation between the two – that is to say, higher levels of FDI are associated with a lower level of poverty. The relationship is weak, with an R² of only 0.15. Nevertheless, it would seem to be a statistically significant one (with a t-statistic for the variable FDI stock per capita significant at the 99% level of confidence).

Figure 3: Poverty and Inward FDI Stock Per capita, 60 Developing Countries

![Figure 3: Poverty and Inward FDI Stock Per capita, 60 Developing Countries](image)

Source: Own elaboration, from UNCTAD and UNDP data (data for the year 2000). T-statistics in brackets.

But what is the direction of causality and through what channels? Is it the case that FDI actively contributes to poverty reduction, or does this relationship simply reflect the propensity of FDI to locate in economies where levels of poverty are already low? A further possibility is that the relationship is a spurious one, due to the omission of other unspecified factors with which both FDI and poverty are correlated. Without the elaboration of a more sophisticated model, it is impossible
to give an answer to these questions. But from existing research it is possible to provide some pointers as to where those interrelationships may reside.

In a recent paper, Warner et. al. (2002:59) identify a number of factors which may be conspiring to constrain the development performance of corporate investments in poor countries:

- Minimum required returns for foreign investors, which in some sectors is approaching 25% per year, making investment in agriculture for example (a key sector for poverty reduction) financially prohibitive\(^\text{17}\);
- Political pressures on operators from host country governments to generate continuous corporate and profit tax contributions that seldom return to the region of operations;
- Operating company reinvesting profits for expansion activities that continue to have little relevance to poor communities;
- Local income earning opportunities (and some labour practices) that tend to exclude access to employment for uneducated communities;
- Products and services affordable only by a few, e.g. bank loans, white goods, utility services (water, transport, electricity, secondary schooling, health care, etc.), crop inputs, etc;
- Value chains (supplies and distribution) inaccessible to domestic small and medium scale enterprises (SMEs);
- The poor level of sustainability of company-led voluntary community development.

It is clear from these points that the relationship between corporate activity and poverty reduction is complex and multifaceted. Some kind of simplifying framework would seem to be required to order and systemise ideas on the subject. With this objective in mind, a tentative framework for evaluating the impact of FDI on poverty reduction is presented in Annex Figures 1 and 2, where we distinguish between a *benign* and a *malign* model of FDI\(^\text{18}\). The diagram attempts only to identify the most immediate effects of FDI on poverty

\(^{17}\) Warner and al. cite the example of CDC Capital Partners, which has began to offload its agricultural assets because of "the need to achieve higher financial returns demanded by the private markets... Our strategy is to dispose of the investment in [our]... historical debt portfolio... which has significant developmental value, but is unlikely to meet the financial hurdles CDC now requires" (Statement by CDC Chairman, 2000, cited in Warner and al. (2002:59).

\(^{18}\) We borrow the terminology of 'benign' and 'malign' models of the interaction between FDI and development from Moran (1998: chapter 1). However, Moran's arguments are based on a comprehensive review of previous studies into the way in which FDI both promotes and impinges on the long-term development prospects. Here we offer a simplifying framework, focusing on the evidence regarding just two dimensions of the issue – how FDI impacts on growth and income distribution.
reduction. In the previous section, we stressed the issue of the political influence of foreign investors. Unfortunately there is no tangible way of measuring such negative pressures. Some studies try to measure, with varying degrees of success, the impact of multinationals on technological acquisition, or the appropriateness of the technologies utilised in a developing country context. Still others, like Stiglitz (2002) or Moran (1999), stress how the multinational can distort policy choices and undermine a local strategy for development. Important as these issues may be, we argue that there is no need to study exhaustively the contribution of multinationals to technological spillovers, or their contribution to the balance of payments or employment. In the final resort, if these factors were decisive, then they should all show up in faster growth rates.

Nonetheless, even if the link between FDI inflows and growth proved to be solid, growth in itself does not guarantee poverty reduction. From the point of view of effective poverty-reduction, distributional considerations are fundamentally important.Echoing earlier (and now largely discredited) theories on the "trickle-down" effect of growth, some authors have argued that over the long run the distribution of income and wealth are unimportant. But, as World Bank economists Martin Ravallion and Shaohua Chen (1997) concede, at any positive rate of growth, the higher the initial inequality, the lower the rate at which income-poverty will subsequently fall. Indeed, if inequality worsens sufficiently, a truly paradoxical situation can arise whereby economic growth can be accompanied by rising poverty. Against this backdrop, a key question is how the presence of multinationals impacts on income and asset distribution.

Consequently, in both the benign and malign models, and following recent literature on poverty reduction, a clear distinction should be made between the growth enhancing and distributional effects. The objective is to disentangle the effects of FDI relative to these two fundamental issues — does FDI increase growth, and how does it effect income and wealth distribution in the host economy? If we can answer these two questions with more or less precision, then the overall contribution of FDI on poverty reduction should be clearer.

19 See, for instance, Harrison (1996). Note that these studies are typically ambiguous about the impact of FDI on spillovers on local firm development and economic growth. Thus the findings of these studies do not significantly modify our conclusions later on in this section regarding the unclear impact of FDI on growth. For a survey, see Saggi (2000).
20 See, in particular, Dollar and Kray (2000).
21 An exhaustive analysis by White and Anderson (2001) of 143 growth episodes found that in over a quarter of the cases changes in distribution played a stronger role than overall growth effect Moreover, even the World Bank now accepts that high levels of inequality not only slow the rate of poverty reduction, but also can negatively affect the rate of economic growth itself (World Bank, 2000). A high degree of inequality impedes the development of markets, slows innovation and limits investment.
4.1. Evidence on the impact of FDI on growth

There have been many studies that analyse the proximate or direct causes of growth, and the list of significant variables is a long one, e.g. the rate of capital formation, higher levels of human capital development, investment in infrastructure, etc. When FDI is included in the regression, however, there is much empirical ambiguity about its influence on economic growth. One intrinsic problem with this kind of analysis is that FDI flows are frequently correlated with other explanatory variables of growth, such as the ratio of investment to GDP and the degree of openness of the economy. An extensive investigation carried out by UNCTAD (1999) on this issue comes to some intriguing conclusions. To avoid as far as possible the contemporaneous correlation effects just cited, the authors used lagged variables, using panel data analysis on data for over 100 countries over five time periods. Of the explanatory variables included, only the past growth rates, the real per capita income relative to the US and the level of schooling were significant. As the study's authors confess, "the effect of past inflows of FDI on the rate of growth of a country... remains elusive, partly because FDI is intertwined with investment ratios and trade ratios. The coefficients for the FDI variable consistently positive in sign from equation to equation, at least when the periods are pooled, but few of them are significant."

In a similar vein, an econometric study using the Holtz-Eakin causality test on panel data for 24 developing countries from 1971 to 1995 found no evidence of a causal relationship between FDI and growth (Nair-Reichert and Weinhold, 2001). To be sure, some studies do purport to show a positive and significant relationship between FDI and growth. Even in these cases, however, the findings do not always produce much solace for policymakers in the LDCs. For instance, Borenstein and al. (1998), analyse the effect of FDI on economic growth in a cross-country regression framework using data on 69 developing countries from 1970-89, and conclude that FDI is an important vehicle for the diffusion of technology. But, crucially, the capacity of a country to take advantage of FDI inflow in this way depends on an initial threshold stock of human capital – something which normally excludes the poorest developing countries.

It is worth reflecting why FDI does not seem to be a robust determinant of economic performance. One reason is that FDI is not a very good measure of the real level of investment carried out by foreign firms; if FDI takes the form of an M&A or through privatization, it may not add to the net capital stock in the country at all, for instance. Furthermore, there is the question of whether FDI
crowds-in or crowds-out domestic development. Using a theoretical model of investment that includes an FDI variable and with panel data for the period 1970-1996, Agosin and Mayer (2000) run regressions for three developing regions (Africa, Asia and Latin America). The results indicate that in Asia – but less so in Africa – there has been strong crowding in of domestic investment by FDI, a clearly desirable outcome; by contrast, strong crowding out has been the norm in Latin America. The authors reach the conclusion that "the effects of FDI on domestic investment are by no means always favourable and that simplistic policies toward FDI are unlikely to be optimal."

Another motive for the weak relationship between FDI and growth might be that, as a single source of investment, the impact of FDI is usually overshadowed by domestic sources of investment, making it difficult to disentangle its effects. It could also be quite plausible that the direction of causality is the reverse of what FDI enthusiasts suggest - that is, causation is from economic growth to FDI rather than the other way around (Singh and Zammitt, 1998:45)24. Finally, it could be simply that FDI does not influence growth significantly – spillovers may be weak or non-existent, and FDI might imply a series of long-term costs which are not outweighed by short-term benefits of the increased capital inflow. As Lall (2000:5) concludes, "Some analyses show a positive impact while others remain agnostic. Since growth depends on many factors whose effects are difficult to disentangle, and since FDI itself affects several of these factors, an agnostic conclusion is probably the most sensible."

It is also worth bearing in mind that this opinion is borne out by micro-based studies of the impact of FDI. Moran (1999: Chapter 1), for instance, reviews three earlier project-based studies covering 183 projects (principally manufacturing, agri-business, and natural resource processing, rather than mineral or petroleum extraction) in more than 30 countries over more than 15 years. The results are sobering – although a majority of projects (55 percent to 75 percent) usually had a positive impact on the host national income, a large minority of the projects (25 percent to 45 percent, and in one study 75 percent) had a clearly negative impact on the economic welfare of the host. Moreover, after reviewing the evidence himself, Moran (1999:25) goes on to argue that "these three assessments far underestimate the direct damages to and lost opportunities for host-country development caused by ill-structured projects".

24 See, for instance, McMillan's (1999) detailed study of the determinants of FDI in six developing countries. She uses a combination of case studies and Granger causality analysis, and concludes "the primary result of this research is that FDI simply is not as important as previously suggested by development theories. FDI may interact with host country conditions, but it is not the single factor that will drive strong growth, nor is it the key factor in explaining low growth and underdevelopment." (ibid., page 144).
4.2. Evidence on the impact of FDI on income and wealth distribution

A few generalisations might help to clarify any possible interrelationships between inequality and FDI. Firstly, it must be borne in mind that multinationals are generally active within the context of oligopolistic market structures and, if anything, tend to increase inequality in developing countries. The profits from the economic activity undertaken by multinationals tend to be distributed in an unequal manner, most of which ultimately flow abroad. Ceteris paribus, high levels of profit share in income will reduce local consumption, something which may directly affect the poor. But a lot also depends on what happens to the profits that stay in the country. In most cases of primary resource extraction in the LDCs, the principal national shareholder will be the State. In some cases (e.g. Botswana), the government has clearly used the revenues from the activity of foreign companies in a wise manner, to finance health and education expenditures for example. This has a broadly positive impact on income distribution. In other cases, however, this has clearly not been so (e.g. Angola), and the income generated from the activities of multinationals has simply served to finance military conflict or prop up corrupt and highly unpopular governments (e.g. Zaire under Mobutu).

Another consideration to bear in mind is that multinationals often set up a segmented labour market. There is quite solid empirical evidence that, on average, multinationals tend to pay considerably more than their domestic counterparts. In this sense, by raising the average wage rate, the impact may be deemed positive. But to the extent that their net contribution to employment is usually small, and that it is often restricted to an enclave of select workers, their presence will tend to increase wage inequality.

Together, these factors imply that enhanced FDI activity is often associated with polarization and growing income inequalities. Tsai (1995) reviewed the evidence on this point, and found that in almost every previous study, FDI was found to be related to growing inequalities in income distri-

---

25 Some evidence of this has been presented in the case of developed countries too. One well-known critic of the Irish government's FDI dependent economic strategy (O'Hearn, 1998) observes that the share of wages in non-agricultural incomes began to fall from around 69 percent in 1987 to 59 percent in 1994, with a corresponding increase in profit share of income to 41 percent. "This shows conclusively that the overwhelming "winners" from economic growth are capitalists, who have enjoyed a rapid rise in their profit incomes – not just absolutely, but also relative to wages... it is largely correct to say that the recent period of growth has been associated with a rapid rise in profits that accrue to foreign capital, at the expense of the consumption of Irish people and even at the expense of reinvestment."

26 As observed in Section II, the level of profit repatriation can be extremely high, especially in the least-developed, highest risk, markets. For Sub-Saharan Africa, for instance, profit repatriation rates have reached in excess of 90 percent of inflows in recent years (UNCTAD, 1999:165).

27 See, for instance, Velde and Morrissey (2002).
Tsai's own regression analysis reveals that, although a statistically significant relationship exists between FDI and income inequality, this result is extremely sensitive to the inclusion of regional dummies, suggesting that the significance of the correlation is due more to geographical differences in inequality than the deleterious influence of FDI. A more recent study by Milanovic (2003) based on data for 88 developing countries finds no evidence of a relationship between FDI and income inequality.

Another issue which needs to be taken into account is the strong association between international cross-border M&As and FDI inflows. Mergers and acquisitions, in all probability, reinforce effects towards a more unequal distribution of income. The benefits of mergers may, for example, go to shareholders whilst the costs may be borne by workers who lose their jobs as a result of rationalisation. Although the importance of these distributional issues is recognised, there is very little empirical literature on the subject (Singh, 2002:17). Privatizations raise similar concerns about the distributional implications. Once again, however, there is little systematic evidence on this point. A recent review by Birdsall and Nellis (2002) of studies into the distributional impact of privatizations in Mexico, Bolivia, Sri Lanka, India, Malaysia, Egypt, China, the Czech Republic, Georgia and Russia concluded that most privatization programs appear to have worsened the distribution of assets and income, at least in the short run. Job losses associated with privatisation policies have also often been substantial, something which can only compound the negative distributional consequences. In the case of Ghana, for instance, more than 150,000 workers lost their jobs in the country's top public enterprises between 1984 and 1991.

Apart from these direct consequences, a large number of enterprises that were privatized in the 1990s operate in monopolistic or quasi-monopolistic markets and produce goods and services that have very important implications for welfare: electricity, telecommunications, water, post, railways and energy. As discussed in Section 3 of this paper, since many of these enterprises are monopolies, the new private owners may raise prices substantially above their marginal costs and reap monopoly profits. This will affect consumers, especially poor social groups, which may be excluded from the consumption of basic goods and services. For instance, the planned privatisation of the Ghana Water

---

28 Nonetheless, these arguments are less clear for utilities such as electricity and telecommunications, where the poor have tended to benefit from much greater access, than for banks, oil companies, and other natural resource producers

29 Concerns have also been raised that privatisation ends up favouring particular ethnic groups, to the detriment of the population as a whole, and increasing horizontal inequalities. Early efforts at privatisation in Nigeria in the late 1980s met with strong complaints from business groups in the north of the country, who argued that public auctions of federal assets through the Nigerian Stock Exchange would result in a high number of assets going to business groups and individuals in the
Company (GWC) has been accompanied by provisions of tariff rises at a rate of 10-15% every six months, provoking outrage among trade unions and the general public (Ford, 2002:17).

That being said, because of the lack of suitable public sector firms for purchase, the bulk of FDI in LDCs (more than 90 per cent) is through greenfield investment rather than through cross-border M&As (including privatizations). Only a few LDCs (notably the United Republic of Tanzania and Zambia) have recorded M&A deals of some importance during 1987-1999 (UNCTAD, 2001). Some of the deals did not target local firms, but existing foreign affiliates. For example, the largest M&A in an LDC so far was the $260 million acquisition of Texaco Inc-Yetagun Natural in Myanmar by Premier Oil Plc from the United Kingdom in 1997. These considerations should moderate any negative evaluation regarding the impact of M&As on income distribution in the poorest developing countries.

5. CONCLUSIONS

This paper presents a simplified framework for understanding the way in which FDI might impact on poverty reduction. In the final resort, the argument is a straightforward one - studies at the microeconomic level on the presence of the multinationals on technological spillovers, on the trade impact, on employment, etc. throw up too many contradictory results to be easily interpreted: they are excessively dependent on data availability, and the results vary too much from one another to draw any firm conclusions. Consequently, it is argued that by focusing specifically on growth and distributional impacts, a clearer idea of the overall balance of costs and benefits accruing to the host country can be attained.

The analysis carried out in this paper is tentative and preliminary, and further work should be done to analyse more exhaustively the causal relationships by, for example, specifying a multi-equation econometric model. Evidently, as a tool for development, multinationals have a potentially important role to play. Apart from the human, technological and financial resources that they can bring to a country, multinationals can contribute in an important way to the structural diversification of an economy, out of primary commodities and into higher value-added services and manufacturing. This constitutes one of the major challenges currently confronting the LDCs.
Nevertheless, from the evidence reviewed, we can safely conclude that, as a tool for poverty reduction *per se*, FDI is likely to disappoint. We find that few of the bolder claims in favour of FDI as an engine of development are borne out by the literature. Statistically, it has proved very difficult to isolate the impact of FDI on overall macroeconomic performance. Moreover, although exceptions undoubtedly exist, FDI is usually associated with a number of economic characteristics which make it ill-suited as an instrument for poverty reduction. Accepting that the evidence is ambiguous on this point, the presence of multinationals may also exacerbate existing income inequalities, with negative implications for poverty reduction. In welcoming the boom in FDI, development practitioners have tended to turn a blind eye to many of these potential difficulties. In this sense, the more critical opinion of Stiglitz would appear to be vindicated.

It is interesting to note that international business specialists have usually been more cautious about the potential benefits of FDI, observing that the overall impact depends greatly on the kind of investment, its sectoral spread, the absorptive capacity of the host country, etc. The international business expert *par excellence*, John Dunning (1994:79), for example, argues that "Policy makers should be cautious about expecting easy generalizations about the consequences of FDI. Not only will its effects vary according to the kind of FDI undertaken, but these effects will also depend on the economic and other objectives set by Governments, the economic policies pursued by them and the alternatives to FDI open to them."

Finally, it is worth stressing the extent to which all these arguments have been played out before. Within the economics profession, there is an unfortunate habit of periodically repeating old controversies. Consider, for instance, these words by a leading development economist:

"Those who worry about the poverty of the world... have to recognise that the problem cannot be solved by leaving it to private investment. Private investment leaves out the poorest and most needy countries... Yet official aid – the other great hope for relieving poverty – is, if anything, declining in real terms on a per capita basis. There is, moreover, widespread disillusionment with the results of aid... The reality seems to be that poverty will be with us for a long time. Any relief will depend far more on the efforts of the poor countries themselves, on their willingness to create conditions in which in which growth is possible and to mobilize effectively their own indigenous resources, than on the flow of aid or international investment."

Wise advice for the future, except that it was advice given almost thirty years ago, by Maxwell Stamp (1974:129). It is perhaps time that some of the lessons, which are readily available in existing research, were learned.
ANNEX

Figure 1: FDI and Poverty Reduction - The Benign Model

FDI Inflow

Income Equality Effects
  - Lower price services and goods
  - MNEs pay higher wages and create employment
  - Positive Spillovers (e.g. technological, competition effects)
  - Improves trade balance (higher exports)
  - Improves current account which facilitates faster growth
  - Higher tax income from greater economic activity (permitting pro-poor social expenditures)

Growth Effects
  - Positive influence on government policy: better institutional standards, incentive to provide better infrastructure, etc.

Poverty

Contributes to gross domestic capital formation
Figure 2: FDI and Poverty Reduction - The Malign Model

FDI Inflow

Income Inequality
- Tax evasion through transfer pricing puts pressure on government to lower overall tax burden and increase social.
- Possibility of monopolistic rents (higher cost products and services) and shareholder concentration, focusing profits in fewer.

Growth Effects
- Adoption of capital intensive techniques plus crowding out of local investment.
- Negative spillovers (e.g., elimination of local firms) resulting in less competition.
- High import intensity, profit repatriation, and excessive royalty payments worsen current account deficit and slow growth.
- Crowding out effects reduce domestic investment.

Negative influence on government policy (e.g., corruption)

Malign social effects of presence of foreign investors (e.g., encouraging inappropriate consumption patterns, etc.)

Poverty
Table 1: The Largest Fifty Foreign Affiliates in LDCs

<table>
<thead>
<tr>
<th>Foreign Affiliate</th>
<th>Host economy</th>
<th>Home economy</th>
<th>Industry</th>
<th>Employment</th>
<th>Year of establishment</th>
</tr>
</thead>
<tbody>
<tr>
<td>Dunlop Zambia Limited</td>
<td>Zambia</td>
<td>United Kingdom</td>
<td>Tires and inner tubes</td>
<td>448</td>
<td>1964</td>
</tr>
<tr>
<td>Brasseries et Limonaderies du Rwanda SA</td>
<td>Rwanda</td>
<td>Netherlands</td>
<td>Malt beverages</td>
<td>1000</td>
<td>..</td>
</tr>
<tr>
<td>Shell Exploration and Development Madagascar BV</td>
<td>Madagascar</td>
<td>Netherlands</td>
<td>Oil and gas exploration</td>
<td>66</td>
<td>..</td>
</tr>
<tr>
<td>Storicklift (Solomon Islands) ltd</td>
<td>Solomon Islands</td>
<td>United Kingdom</td>
<td>..</td>
<td>..</td>
<td>..</td>
</tr>
<tr>
<td>Boral Gas Solomon’s Ltd</td>
<td>Solomon Islands</td>
<td>Australia</td>
<td>Gas exploration</td>
<td>..</td>
<td>..</td>
</tr>
<tr>
<td>U.S. Oil and Gas Services No. Exterior Ltd.</td>
<td>Angola</td>
<td>Brazil</td>
<td>Nonresidential construction</td>
<td>4000</td>
<td>..</td>
</tr>
<tr>
<td>Ashanti Goldfields (T) Ltd.</td>
<td>United Republic of Tanzania</td>
<td>Ghana</td>
<td>Gold ores</td>
<td>20</td>
<td>..</td>
</tr>
<tr>
<td>Pacific Resources Ltd.</td>
<td>Vanuatu</td>
<td>Hong Kong, China</td>
<td>..</td>
<td>..</td>
<td>..</td>
</tr>
<tr>
<td>HWG Steel Building Products New Caledonia SA</td>
<td>Vanuatu</td>
<td>Australia</td>
<td>..</td>
<td>..</td>
<td>..</td>
</tr>
<tr>
<td>La compagnie minière d’Akokou</td>
<td>Niger</td>
<td>Japan</td>
<td>Mining</td>
<td>1255</td>
<td>1978</td>
</tr>
<tr>
<td>Travel Industry Services Ltd.</td>
<td>Solomon Islands</td>
<td>Fiji</td>
<td>Transport</td>
<td>..</td>
<td>..</td>
</tr>
<tr>
<td>Compagnie Shell De Guinée</td>
<td>Guinea</td>
<td>Netherlands</td>
<td>Petroleum products except bulk terminals</td>
<td>33</td>
<td>..</td>
</tr>
<tr>
<td>Manufacture de Tabacs de l’Ouest Africaine</td>
<td>Senegal</td>
<td>France</td>
<td>Tobacco</td>
<td>410</td>
<td>..</td>
</tr>
<tr>
<td>Fisons Bangladesh Ltd.</td>
<td>Bangladesh</td>
<td>France</td>
<td>Pharmaceutical preparations</td>
<td>1300</td>
<td>1964</td>
</tr>
<tr>
<td>Brasseries et Limonaderies Du Burundi Sari</td>
<td>Burundi</td>
<td>Netherlands</td>
<td>Bottled and canned soft drinks</td>
<td>1350</td>
<td>1997</td>
</tr>
<tr>
<td>Myanmar Kasbo Co., Ltd.</td>
<td>Myanmar</td>
<td>Japan</td>
<td>Trading</td>
<td>8</td>
<td>1995</td>
</tr>
<tr>
<td>John Walden And Co.</td>
<td>Benin</td>
<td>United Kingdom</td>
<td>Piece goods</td>
<td>74</td>
<td>..</td>
</tr>
<tr>
<td>Caloil Shipping Co. Inc.</td>
<td>Liberia</td>
<td>Japan</td>
<td>Transport</td>
<td>..</td>
<td>1989</td>
</tr>
<tr>
<td>The坦尚尼亚电力公司</td>
<td>Bangladesh</td>
<td>United Kingdom</td>
<td>Motors and generators</td>
<td>1200</td>
<td>1962</td>
</tr>
<tr>
<td>Nestle Senegal SA</td>
<td>Senegal</td>
<td>Switzerland</td>
<td>Fluid milk</td>
<td>230</td>
<td>..</td>
</tr>
<tr>
<td>Vesperis Shipping Corp.</td>
<td>Liberia</td>
<td>Japan</td>
<td>Transport</td>
<td>..</td>
<td>1993</td>
</tr>
<tr>
<td>Manufacture Burkinabe De Cigarettes SA</td>
<td>Burkina Faso</td>
<td>France</td>
<td>Tobacco</td>
<td>150</td>
<td>..</td>
</tr>
<tr>
<td>Total Togocargo Niger SA</td>
<td>Niger</td>
<td>France</td>
<td>Petroleum products except bulk terminals</td>
<td>45</td>
<td>..</td>
</tr>
<tr>
<td>Togo et Shell SA</td>
<td>Togo</td>
<td>Netherlands</td>
<td>Petroleum products except bulk terminals</td>
<td>96</td>
<td>..</td>
</tr>
<tr>
<td>Spie Batignolles Ltd.</td>
<td>Lesotho</td>
<td>France</td>
<td>Engineering services</td>
<td>1400</td>
<td>1987</td>
</tr>
<tr>
<td>Cica Burkina</td>
<td>Burkina Faso</td>
<td>France</td>
<td>Cars and other motor vehicles</td>
<td>150</td>
<td>1991</td>
</tr>
<tr>
<td>Nouvelles Savonneries de l’Ouest Africain SA</td>
<td>Senegal</td>
<td>United States</td>
<td>Cleaning, pestering and sanitation preparations</td>
<td>200</td>
<td>1994</td>
</tr>
<tr>
<td>Hamahou Trans. Inc.</td>
<td>Liberia</td>
<td>Japan</td>
<td>Transport</td>
<td>..</td>
<td>1986</td>
</tr>
<tr>
<td>MK Tanzania Ltd.</td>
<td>United Rep. of Tanzania</td>
<td>Luxembour</td>
<td>Electronic parts and equipment</td>
<td>150</td>
<td>..</td>
</tr>
<tr>
<td>Mamya-Op (Bangladesh) Ltd.</td>
<td>Bangladesh</td>
<td>Japan</td>
<td>Sporting and athletic goods</td>
<td>600</td>
<td>1991</td>
</tr>
<tr>
<td>Laurel Shipping Corp.</td>
<td>Liberia</td>
<td>Japan</td>
<td>Transport</td>
<td>..</td>
<td>1971</td>
</tr>
<tr>
<td>Standard Chartered Bank Uganda Ltd</td>
<td>Uganda</td>
<td>United Kingdom</td>
<td>Commercial banks</td>
<td>106</td>
<td>..</td>
</tr>
<tr>
<td>Cabinda Gulf Oil Company Ltd.</td>
<td>Angola</td>
<td>United States</td>
<td>Petroleum refining</td>
<td>1800</td>
<td>..</td>
</tr>
<tr>
<td>Compagnie Française de l’Afrique Occidentale</td>
<td>Niger</td>
<td>France</td>
<td>New and used car dealers</td>
<td>45</td>
<td>1963</td>
</tr>
<tr>
<td>Canadian Occidental Yemen Operation Company Ltd.</td>
<td>Yemen</td>
<td>Canada</td>
<td>Oil and gas field services</td>
<td>1000</td>
<td>..</td>
</tr>
<tr>
<td>Qbe Insurance (Vanuatu) Ltd.</td>
<td>Vanuatu</td>
<td>Hong Kong, China</td>
<td>Insurance carriers</td>
<td>..</td>
<td>..</td>
</tr>
<tr>
<td>Organon Bangladesh Ltd.</td>
<td>Bangladesh</td>
<td>Netherlands</td>
<td>Pharmaceutical preparations</td>
<td>1000</td>
<td>1965</td>
</tr>
<tr>
<td>Simon Brewerys Limited</td>
<td>Samoa</td>
<td>Australia</td>
<td>Malt beverages</td>
<td>140</td>
<td>1978</td>
</tr>
<tr>
<td>Pascal (No.1) Tankers Corp.</td>
<td>Liberia</td>
<td>Japan</td>
<td>Transport</td>
<td>..</td>
<td>1987</td>
</tr>
<tr>
<td>Mod-Nei Transport Ltd.</td>
<td>Liberia</td>
<td>Japan</td>
<td>Transport</td>
<td>..</td>
<td>1989</td>
</tr>
<tr>
<td>Foreign Affiliate</td>
<td>Host economy</td>
<td>Home economy</td>
<td>Industry</td>
<td>Employment</td>
<td>Year at establishment</td>
</tr>
<tr>
<td>-------------------</td>
<td>--------------</td>
<td>--------------</td>
<td>-------------------</td>
<td>------------</td>
<td>-----------------------</td>
</tr>
<tr>
<td>Ananda Computers</td>
<td>Bangladesh</td>
<td>United States</td>
<td>Office equipment</td>
<td>40</td>
<td>1987</td>
</tr>
<tr>
<td>Société Sénégalaise d'Oxygène et d'Acétylène</td>
<td>Senegal</td>
<td>France</td>
<td>Natural gas liquids</td>
<td>80</td>
<td>..</td>
</tr>
<tr>
<td>Galian Holdings Ltd.</td>
<td>Zambia</td>
<td>India</td>
<td>Holding companies</td>
<td>100</td>
<td>1995</td>
</tr>
<tr>
<td>Manufacture de Cigarettes Du Tchad</td>
<td>Chad</td>
<td>France</td>
<td>Tobacco</td>
<td>127</td>
<td>..</td>
</tr>
<tr>
<td>Emerald Resort Pvt. Ltd.</td>
<td>Maldives</td>
<td>Japan</td>
<td>Hotel</td>
<td>133</td>
<td>1991</td>
</tr>
<tr>
<td>Horizons Madagascar SA</td>
<td>Madagascar</td>
<td>France</td>
<td>Chemicals</td>
<td>69</td>
<td>1987</td>
</tr>
<tr>
<td>World Car Carrier Inc.</td>
<td>Liberia</td>
<td>Japan</td>
<td>Transport</td>
<td>3</td>
<td>1988</td>
</tr>
<tr>
<td>Scac Delmas Viteku</td>
<td>Burkina Faso</td>
<td>France</td>
<td>Freight Transport arrangers</td>
<td>250</td>
<td>..</td>
</tr>
<tr>
<td>Ned Electricité SA</td>
<td>Senegal</td>
<td>France</td>
<td>Electric services</td>
<td>9</td>
<td>..</td>
</tr>
<tr>
<td>Colgate Palmolive (Zambia) Ltd.</td>
<td>Zambia</td>
<td>United States</td>
<td>Manufacturing industries</td>
<td>150</td>
<td>..</td>
</tr>
</tbody>
</table>

*Source: Elaborated from UNCTAD, 2001.*
REFERENCES

Agosin M., Mayer R., 2000, "Foreign Investment in Developing Countries- Does it Crowd in Domestic Investment?", UNCTAD Discussion Papers, n° 146, February.


Dollar D., Kraay A., 2000, Growth is Good for the Poor, World Bank, Washington DC.


Mehtrotra S., Vandemoortele J., Delamonica E., 2000, *Basic Services for All?*, UNICEF Innocenti Research Centre, Florence, Italy.


Velde D., Morrissey O., 2002, "Foreign Direct Investment, Skills and Wage Inequality in East Asia", paper presented at the DESG conference, Nottingham, April.


IDE ET RÉDUCTION DE LA PAUVRETÉ :
UNE RÉEXAMEN CRITIQUE DES ARGUMENTS

Résumé - Au cours des deux dernières décennies, un effort considérable a été réalisé par les pays en développement pour attirer les investissements directs étrangers. Il est généralement admis qu'en accélérant la croissance, les IDE contribuent de manière déterminante à réduire la pauvreté. Cet article soutient que ce point de vue doit être nuancé au regard des faits et des vérifications empiriques. En réponse à différents travaux sur l'impact du commerce sur la réduction de la pauvreté, un certains nombre d'arguments sont suggérés qui remettent en question le lien entre IDE, "renforcement de la croissance" et effet "redistributif". Contrairement à ce qui est communément admis, rien ne prouve que les IDE constituent un instrument majeur de réduction de la pauvreté.

IED Y REDUCCIÓN DE LA POBREZA :
UN EXAMEN CRÍTICO DE LOS ARGUMENTOS

Resumen - A lo largo de las últimas dos décadas los países en vía de desarrollo han hecho un esfuerzo importante para atraer las inversiones extranjeras directas. Se admite generalmente que si se acelera el crecimiento económico, las IED contribuyen determinadamente a reducir la pobreza. Este artículo defiende que se tiene que relativizar este punto de vista mirando los hechos y las evidencias empíricas existentes sobre la contribución de las IED al crecimiento y a la reducción de la pobreza. Respondiendo a estudios llevados a cabo por economistas del comercio sobre el impacto del comercio sobre la reducción de la pobreza, proponemos un plan sencillo que pone en tela de juicio la influencia de las IED para "reinforzar el crecimiento económico" y los efectos "distributivos". Al contrario de lo que se admite en general, encontramos pocas pruebas de que las IED constituyen un instrumento de reducción de la pobreza.