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Attractiveness of Countries for Foreign Direct Investments from the Macro-Economic Perspective

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Abstract: Attractiveness and value adding characteristics of countries for Foreign Direct Investments usually are linked to new customers, upcoming demands, unsatisfied needs, competitive situations, etc. But they are also closely connected to macro-economic factors, which build the focus of this research praper. To make it more differentiable, those factors have been separated into five major dimensions: Political/Legal, Economic, Social, Technological and Intercultural Factors. Each of those factors consists of minimum five sub-factors which have been analyzed and taken into consideration. The aim is to find out, which factors influence the decisions for FDIs. If knowing that, stecific decisions can be set to make a country more attractive or to allow managers to base their decisions on a more fact-oriented basement. Main findings are, that managers allocate for a country selection the highest importance to the political stability and legal transparency. This is followed by the economic health of a country. Also the sub-factor "Infrastructure", which is part of the technological environment, is of essential importance. The Intercultural Dimensions occupy a minor role in influencing the decision process. Derived conclusions from these results are, that countries can increase their attractiveness for foreign direct investments by putting focus to the political stability, more transparency and stable economic conditions.

Keywords: Internationalization, Macro-Economic Factors, Foreign Direct Investment

1 Objectives

Expansion of companies to conquer and enter new markets became more important over the last decades. Internationalization and globalization are terms which are used commonly in many economic contexts (Adler, 2008). Industries, such as the automotive industry, the chemical industry, the clothing industry, the food industry, etc. have business activities all over the world. Reasons therefore can be serving new markets, covering upcoming demands, use of resources (e.g. raw materials,…), reducing transports, stay at customer's site, etc. In such processes, companies are forced with many different influence factors (cf. Held, 2004). These factors can occur from the company's structure, strategic goals and visions (internal factors), these are the so called micro-economic factors (Mussnig, 2007). And also the larger environment of a company plays a very important role by entering new markets, new countries or unknown territories. These factors are defined as the external factors and known as macro-economic factors (McCarthy, 1975; Porter, 2008). This research project focuses to the macro-level of influence factors and measures and analyses the importance of these factors to the decision process of selecting a target country for doing Foreign Direct Investments (FDI).

Fast changing environmental conditions of companies influencing the daily business activities as well as have effects on the long term perspectives (cf. Haas et al., 2006). Business entities have to handle these changes and have to be aware of them. One big impact has the globalization and internationalization to those changes (cf. Hinterhuber, 1997; cf. Welfens, 1997). The competitive situation becomes tougher because of the not any longer limitation by distance. The so called "global competition" (Gerber, 2010) forces the companies to be innovative, to be up-to-date, to understand the customer's needs and to serve the right markets with the right goods.

Even if it is the strategic goal of a company to grow, enter new markets, new countries, to gain more market shares or to serve new customers (cf. Stalk, 1998), the selection of the right country becomes a serious topic which has to be solved. Of course, the micro environmental conditions, such as serving customers, markets, fulfilling demands, enter emerging markets, etc. in the most cases firstly play the biggest role in terms of such ventures. But in such complex projects, managers often come relatively soon to the point where they start thinking about the macro-economic conditions of the countries. Those conditions may have a big and strong influence to the expansion process and can become the essential factor if it will end in a success story or it runs into a disaster.

The aim is to analyse and measure the impact of macro-environmental factors to the country selection in terms of expansion processes. For companies, those results can make it more secure to select the right country and for countries itself it is the basis to put actions in terms of increasing the attractiveness and possibilities for foreign direct investments.

1.1 The Macro-Economic Influence Factors

1.1.1 Description of the Macro-Environment

The macro environment can be defined as the large environmental factors which influence the company often in an indirect way. These factors are mainly long-term oriented and not changeable by the company itself. These influences and developments are important for the selection of site locations of companies or for subsidiaries (cf. Kreutzer, 2006).

According to Kreutzer (2006) and Hofbauer *et al.* (2009) the macro environment contains four dimensions: society, economy, technology and law/politics, as shown in Figure 2, which can’t be changed or influenced by the company in any way. The goal of the macro-environmental analysis should be, to use the opportunities and to minimize the risks.

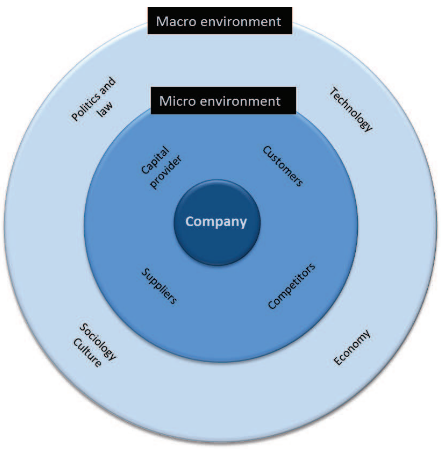

Figure 1
Micro and macro environment of a company (Source: Kreutzer, 2006)

Kotler *et al.* (2007) says that only a company, which recognizes the unsatisfied needs of the market or respectively of the customers, can be successful.

Macro-Economic factors have been tried to explain them in many different ways. One of the most famous definition is the “PEST”-Approach (Pfaff, 2004). Other similar definitions are “PESTLE” and “STEEPLE” approaches.

Both, the PEST(LE) as well as the STEEPLE analysis, help to identify the driving forces of the external environment which influence the company and its business.

The PEST analysis contains following four factors (cf. Pfaff, 2004):

- **P**olitical:
    - Taxation policy, European Union directives, trade regulations, geographical factors like the "war on terror", government stability, employment law, contract law, competition law, etc. (Kew *et al.*, 2005).
- **E**conomical
    - Business cycles, economic growth, interest rates, supply and demand factors, competition factors, public spending, money supply, inflation, unemployment, disposable income (Kew *et al.*, 2005).
- **S**ocio-Cultural
    - Demographic trends, income distribution, social mobility, lifestyle, attitudes to work and leisure, levels of education (Kew *et al.*, 2005).
- **T**echnological
    - Research and development, new inventions or innovations, speed of technology transfer, rates of obsolescence, development of systems (Kew *et al.*, 2005).

In addition to the PEST-abbreviation two more letters, an **L** and an **E**, were included in the mid 90ies. The two additional dimensions are **Legal** (which has been split from the politics) and **Environment** (cf. Kew *et al.*, 2005).

More differentiations about the strategic macro environmental analysis models are summarized by Jeffs (2008):

- STEP or PEST, which stands for Political, Economic, Social and Technological factors.
- SLEPT, which stands for Social, Legal, Economic, Political and Technological factors.
- And as described STEEPLE and PESTLE.

These analyzing methods for identifying external influencing factors describe a structured guideline for detecting opportunities and threats.

The following macro-economic factors have been selected for this research project and include five to six sub-factors to allow a specific analysis:

1. Political/Legal Factors	2. Economic Factors
1.1. Political Stability of the target Country	2.1. Unemployment Rate
1.2. Transparrency and Corruption	2.2. GDP Real Growth Rate
1.3. Trade Regulation	2.3. Inflation Rate
1.4. Employment Law	2.4. GDP per Capita
1.5. Enforcing Contracts	2.5. Starting a Business (Difficulties, Duration, Cost)
	2.6. Tax Rate in % of Profit
3. Social Factors	**4. Technological Environment**
3.1. Household net adjusted disposable income	4.1. Environment (Infrastructure, Electricity, Streets,…)
3.2. Public Spending on Education, total (in % of GDP)	4.2. Technology
3.3. Social Inequality (GINI Index)	4.3. Health
3.4. Growth of Population	4.4. Peace
3.5. Human Development Index (HDI)	4.5. Democracy
3.6. Population below Poverty Line	
5. Intercultural Dimensions / Differences (Hofstede, 2001)	**6. Additional Influence Factors**
5.1. Power Distance (PDI)	6.1. Religion
5.2. Individualism/Collectivism (IND)	6.2. Language Differences
5.3. Masculinity / Femininity (MAS)	6.3. Distance to Origin Country
5.4. Uncertainty Avoidance Index (UAI)	
5.5. Long Term Oriented / Short Term Oriented (LTO)	

Table 1

Selected Macro-Economic Factors for Analysis (Source: Author)

1.1.2 Method and Data Collection

87 High-Level Managers of global acting companies from different industries, such as the automotive industry, the chemical industry, pharmacy sector, clothing industry and food industry have been asked by a structured survey about the importance of five main groups of macro-economic factors, as these were: Political/Legal, Economic, Social, Technological and Intercultural Environment (five main groups with five to six sub-factors each) and had to rate how strong each factor influences the decision in terms of selecting a country during the expansion processes. The survey was built according the Likert-Scale. They could select between 1 = “not important in terms of country selection” to 5 = “has a strong influence to the decision in terms of country selection for expansion”. 87 surveys have been sent out and the participants have been additionally informed by the author about the survey and the basic aim of the research project, namely, to find out which macro-economic factors are able to effectively increase or decrease the attractiveness of countries for foreign direct investments. Knowing specific factors which mainly influence decision processes in terms of country selection allow concentrating more efficiently the resources to increase the attractiveness of the country and increase the possibilities of foreign direct investments. 48 surveys have been returned and fulfilled the “must-have” criteria, which have been defined in the survey in the beginning. The raw data have been summarized by building mean-values to get an overview about the ratings of each macro-economic influence factor.

PARTICIPANTS (Primary Data)			
			Mean-Value
Political/Legal	1.1.	Political Stability	3,54
	1.2.	Transparency, Corruption	3,90
	1.3.	Trade regulation	3,15
	1.4.	Employment law	3,13
	1.5.	Enforcing of contracts	3,02
			3,35
Economic	2.1.	Unemployment rate	2,92
	2.2.	GDP real growth rate	2,96
	2.3.	Inflation rate	2,44
	2.4.	GDP per capita	2,71
	2.5.	Starting a Business	3,79
	2.6.	Tax rate in % of profit	4,19
			3,17
Social	3.1.	Household net adjusted disposable income	3,06
	3.2.	Public spending on education, total (% of GDP)	3,19
	3.3.	Social Inequality (GINI)	3,19
	3.4.	Growth of population	2,92
	3.5.	Human Development Index (HDI)	3,21
	3.6.	Population below poverty line	3,27
			3,14
Technical/ Environment	4.1.	Environment (Infrastructure)	3,56
	4.2.	Technology	2,79
	4.3.	Health	2,56
	4.4.	Peace	3,25
	4.5.	Democracy	3,19
			3,07
Intercultural Dimensions	5.1.	Power Distance	2,25
	5.2.	Indiv./Collectivism	2,19
	5.3.	Masculinity/Femininity	1,83
	5.4.	Uncertainty Avoidance Ind.	2,23
	5.5.	Long/Short Term Oriented	1,85
			2,07
Additional Factors	6.1.	Religion	3,25
	6.2.	Language Differences	3,42
	6.3.	Distance to Origin Company	3,15
			3,27

Table 2

Importance of Macro-Economic Factors for Country Selection in Expansion Processes

(Source: Author)

A mean value out of the 48 single ratings has been calculated for each factor. And in addition for each main group of macro-economic factors has been built again a mean-value to see the main drivers of influence and to be able to derive action for countries to increase their attractiveness in terms of foreign direct investment by business entities.

These primary gained data of measuring the importance of macro-economic factors for manager's decisions in terms of country selection for expansion processes have been enlarged with secondary data, gained from official institutes (data sources please see "References") for a selected group of countries and country agglomerates, as these are: Central Europe, Eastern Europe, USA and China.

All raw data have been classified into a five-classes Likert-Scale (from 1 to 5) to allow a comparability of the data.

The data give an overview about the performance of each country/region for the same selection of macro-economic parameters as it has been used for the survey to analyse the "Importance Indicators".

RATING MATRIX			Ranking by div. Organizations (secondary data) Target Countries [Class 1=positiv; Class 5=negativ]			
			CE*	EE**	China	USA
Political/Legal	1.1.	Political Stability	1,80	3,71	3,00	3,00
	1.2.	Transparency, Corruption	1,60	3,71	5,00	1,00
	1.3.	Trade regulation	1,60	4,14	4,00	1,00
	1.4.	Employment law	1,60	1,86	5,00	1,00
	1.5.	Enforcing of contracts	1,50	2,43	1,00	1,00
Economic	2.1.	Unemployment rate	1,70	2,43	1,00	1,00
	2.2.	GDP real growth rate	3,10	3,57	1,00	2,00
	2.3.	Inflation rate	2,70	3,71	3,00	3,00
	2.4.	GDP per capita	2,78	4,86	5,00	2,00
	2.5.	Starting a Business	2,80	3,43	5,00	1,00
	2.6.	Tax rate in % of profit	2,80	2,57	5,00	3,00
Social	3.1.	Household net adjusted disposable income	2,30	3,80	5,00	1,00
	3.2.	Public spending on education, total (% of GDP)	3,30	4,67	5,00	4,00
	3.3.	Social Inequality (GINI)	1,70	2,43	5,00	5,00
	3.4.	Growth of population	2,20	3,57	2,00	1,00
	3.5.	Human Development Index (HDI)	1,60	3,00	5,00	1,00
	3.6.	Population below poverty line	2,10	4,00	3,00	3,00
Technical/ Environment	4.1.	Environment (Infrastructure, Electricity, Streets, Wa	1,20	2,29	5,00	3,00
	4.2.	Technology	2,70	4,00	1,00	1,00
	4.3.	Health	1,20	2,86	5,00	3,00
	4.4.	Peace	1,50	2,43	5,00	5,00
	4.5.	Democracy	1,20	1,57	5,00	1,00
Intercultural Dimensions	5.1.	Power Distance	2,20	3,71	4,00	2,00
	5.2.	Indiv./Collectivism	3,90	2,57	1,00	5,00
	5.3.	Masculinity/Femininity	2,50	3,14	3,00	3,00
	5.4.	Uncertainty Avoidance Ind.	2,40	3,71	1,00	2,00
	5.5.	Long/Short Term Oriented	1,60	1,50	5,00	1,00
Additional Factors	6.1.	Religion				
	6.2.	Language Differences				
	6.3.	Distance to Origin Company				

* Central Europe: Representative countries for this region which have been taken into evaluation: Austria, Germany, Switzerland, France, Spain, UK, Norway, Sweden, Denmark

** Eastern Europe: As representative countries for this region following have been taken into evaluation: CZ, Slovakia, Romania, Bulgaria, Greece, Poland, Hungary

Table 3

Rating Matrix of Country's Performance in terms of Macro-Economic frameworks

(Source: See Internet Sources under "References")

2 Results and Data Interpretation

2.1 Importance Indicators for Country Selection (Refer to Table 2)

The Importance Indicators are calculated by using the mean value of each macro-economic factor. Each mean value consists of 48 meta data gained by a structured survey. Hereby please refer to Table 2.

The empirical research to find out the strongest influence factors in terms of country selection for Foreign Direct Investments showes especially for the two main groups of macro-economic factors, as they are the *Political/Legal* factors with an Importance Index of *3,35* and the *Economic Factors* (Importance Index of *3,17*) a highly influencing power. Also very important were the *Social* factors which gained an Index of *3,14*. *Technological Environment* has reached an Index of *3,07*. Far behind on the last place are the *Intercultural Dimensions* which have not been that important for their decisions. Therefore the Importance Index only reached *2,07*. The three additional factors, as these are *"Religion", "Language Differences"* and *"Distance to Origin Country"* have also a quite strong influence Index of *3,27*. But these three factors are naturally given and can't be changed by a country actively. Therefore these data are not going to be considered for further considerations and derived actions.

The 48 managers rated the Political/Legal factors and the Economic factors as the most important ones who influence the selection process of a country. What means in other words, that countries, which have a good reputation in those macro-economic areas are more attractive to be selected for Foreign Direct Investments than others. This information gains the possibility to set a special focal point for countries to install specific actions to increase the attractiveness of a country for Foreign Direct Investments. There is also one additional sub-factor which influences the managers' decision of country selection very strong. This is the "*Environment (Infrastructure) Factor*", which gained an Importance Index of *3,56*. This sub-factor also has a strong influence to the country selection beside the Political/Legal and Economic factors. Infrastructure, which means the access to electricity, water, gas, streets, logistics, etc. is an absolute basic criteria and therefore an important factor in terms of selecting the right place for expanding a business.

The Intercultural Differences according to Hofstede's five dimensions are not as important as the other factors (*2,07*). But this is only related to the country selection process from the macro-economic point of view. For the micro-economic point of view it can be totally different (e.g. the organizational structure and the ability of collaboration of the employees within the enterprise).

2.2 Country's Macro-Economic Performance Evaluation (Refer to Table 3)

The data of the secondary research about country's macro-economic performances have been done for four worldwide important economies, as these are: Central Europe, Eastern Europe, USA and China. The data have been collected from different official and well known institutes. A summary of all data please refer to Table 3. The sources therefore can be found under "References".

The aim is building a counterpart to the *Importance Indicators* and to collect "real" data of selected economies about their macro-economic performance. Than, this gives a clear picture about the attractiveness of countries and ability to cover interested foreign direct investor's needs and demands.

The results show in some areas a bit a confusing picture. China, for example, has the highest number of last-places macro-economic factors (of the four analysed country agglomerates). How can it be that China nevertheless is the world's largest and fastest growing economy? Firstly, it depends on in which macro-economic factors a country performs how! There are big differences in the importance of each factor for the country selection – see Table 1. Factors with low importance indicator are not as critical as factors with a high rating. And it can also be seen, that China has reached place number one, for example, at the "Real GDP Growth Rate". This is rated as an important factor for companies who want to install a business in a foreign country and look for a long term successful business model. Therefore this factor is of essential importance for Foreign Direct Investments. Secondly, as it is explained in the beginning of this paper, the ratings of the managers only reflect the macro-economic point of view. Not the micro-economic one. For companies it seems it is more important to immediately have customers, having a new market segment with demand for goods or having a good competitive situation,… Not till then, the companies check about the broader business environment, what in economic definitions is called macro-environment. Both, the USA and China, have mainly extreme positions in this analysis. Either they are number one, or they are on the last place. The Central European Countries perform very well in the Technical Environment and Infrastructure as well as in the Social area. Eastern European Countries are attractive for foreign Investors in terms of Technical Environment and the Employment Law is also very "company friendly". It is important, where countries are less attractive and where they perform really well. The combination of the Importance Index allocated by the managers and the "real" performance of countries can gain a clearer picture what makes it easier to take decision by companies and for countries it is easier to see which factors have to be improved to be more successful and attractive in the future.

2.3 Differences of Requirements of FDI and Macro-Environmental Factors

Managers allocate different importance to one and the same macro-economic influence factor. The prior described results are based on mean values to come to an overall importance index for each factor.

But, it strongly depends in which industries managers work and what their basic product and market requirements are. If the FDI is going to be planned to set-up a production facility to manufacture products where raw materials, machineries, special transports are needed (railway, ship, airport,…), the factors "Technology" and "Infrastructure" are being allocated with an higher importance than for service-related companies, where other facts such as health, security, social development or educational standards are the main drivers for selecting the right country for its own business model. It is the kind of the business model which creates different needs and demands for putting FDIs. And the macro-environmental performances of countries or economic areas play an important role is this matter. Those countries have to match the requirements of the FDI firms. Therefore it is important to divide between the different needs of the different branches. Countries may than can focus to increase attractiveness for special economic sectors.

Managers from the Industry sector (Automotive industry and other heavy industry firms) claiming most imporance to the Technological Factors and Infrastructure (means of transport) as well as access to raw materials. Wheras firms from the service factor allocate main importance to social and economic factors. Hereby especially to Unemployment rate, GDP real growth rate and social development. The Health sector puts great attention to the social factor as well as political requirements. This builds only an overview of different needs and claims to FDI into foreign countries from different economic perspectives, but creates already a differentiatable framework.

3 Conclusions

Not every country can be attractive in the same way and intensity for every branch and business model. On the one hand, companies from the service sector, such as the hotel or bank sector have different claims and demands to macro-environmental factors than industry driven companies. Even companies from the health industry (pharmaceuticals) have again different requirements to these macro-framework and not directly influenceable factors.

Countries on the other hand can observe the requrirements of companies and may try to increase attractiveness for special branches and economic sectors. It may reduces the complexity of requirements and claims and allows countries to put focus to special factors for certain branches. This increases the chance to gain higher FDI or vice versa, namely to outflow FDI to other countries.

There exist a number of Macro-Economic factors which are of essential importance for a country selection process of companies who are going to expand into foreign countries. As a conclusive summary following results can be derived: Countries with a high level of Political Stability, Taxation Policy, Foreseeable Law Regulations and a high level of Economic Performance, as these are: Employment rate, GDP per Capita, Industrial Growth Rate, Inflation, etc. are more likely to be chosen for foreign direct investments in terms of start-up a business entity than countries with lower levels. Also the sub-factor “Infrastructure” plays an important role in this context.

The ranking of the real performance of the four selected economies, as these are Central Europe, Eastern Europe, China and the USA show a complex picture of different performance levels of macro-economic factors. Here it is important to filter the most important influence factors from the managers’ ranking and trying to improve those factors firstly. This kind of knowledge makes it possible, to concentrate the limited resources and necessary forces to a smaller number of macro-economic factors and setting specific actions for improvement. If countries want to be more attractive for FDIs, following these ranks of importance could help gaining new business activities and increasing activities of FDIs.

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