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Briefing Paper

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A Review of Literature Regarding the Determinants of Foreign Direct Investment (FDI)

1 Introduction

The following paper reviews the literature on FDI determinants. It is the first of a series of papers for the Committee for Enterprise, Trade and Investment that examine Northern Ireland's FDI attractiveness.

The paper begins by outlining a number of definitions and the theory behind FDI determinants.

The later part of the paper looks at available literature from a range of organisations to identify general, sector specific and 'deal breaking' FDI determinants. The paper also looks briefly at how Northern Ireland differs from the rest of the world in terms of the reasons why companies chose to locate here.

Subsequent papers will measure Northern Ireland's performance across the determinants identified in this paper.

2 Definitions and theory

FDI is defined as:

> *Investment from one country into another (normally by companies rather than governments) that involves establishing operations or acquiring tangible assets, including stakes in other businesses.*[1]

It entails:

> *The purchase or establishment of income-generating assets in a foreign country that entails the control of the operation or organisation.*[2]

FDI is considered to bring substantial benefit to host economies according to the **OECD** FDI:

> *…is a key element in international economic integration. FDI creates direct, stable and long-lasting links between economies. It encourages the transfer of technology and know-how between countries, and allows the host economy to promote its products more widely in international markets. FDI is also an additional source of funding for investment and, under the right policy environment, it can be an important vehicle for development*[3]*.*

With these potential benefits in mind creating conditions suitable for FDI is often prominent in the economic goals of policy makers. The Northern Ireland Executive have embedded attracting FDI within their Economic Strategy[4] and are currently seeking devolution of Corporation Tax powers from the UK Government in order to have greater control over fiscal levers which, it is argued, could increase the level of FDI into Northern Ireland.

Economic theory suggests that in order for FDI to take place three types of advantages must be observable. These are ownership advantages, location advantages and internalisation advantages. This is often referred to as the OLI framework which is discussed briefly below:

- Ownership advantages (The 'why' of multinational activity)

  The firm in question must possess advantages over firms in the host country. These may include financial resources, human capital, technological advantages, or size of brand;

- Location advantages (The 'where' of production)

  For companies to engage in FDI there must also be specific locational advantages

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[1] Financial Times Lexicon, Definition of Foreign Direct Investment http://nia1.me/2cj Accessed on 04/10/14

[2] *Ibid*

[3] OECD Factbook 2013, Available at http://nia1.me/29m . Accessed on 27/10/14.

[4] "Northern Ireland Economic Strategy (revised)" (2012). DETI. Available at http://nia1.me/29n . Accessed on 28/10/14.

in a particular country, that could not be gained by expanding in its home country or locating in another overseas country. These can include tax and other incentives, infrastructure[5], labour market advantages, logistics or access to markets, regulations or government policy, amongst other factors.

- Internalisation advantages (The 'how' of involvement)

  Not only must firms possess these advantages, but it also must be more advantageous for firms to 'internalise' these advantages by integrating in foreign markets rather than selling or licensing its products to firms in the host country. This reduces transactions cost and removes the uncertainty of the market.[6]

The 'why' question regarding ownership advantages is a decision based on a firm's assessment of its own capabilities, the 'how' question regarding internalisation is also an assessment by a firm of how best to use its resources to increase profits in another country. These two decisions are largely ones which firms make introspectively. It is the 'where' question regarding advantages of location which policy makers are in a position to influence in order to attract FDI. However, multinational enterprises (MNEs) are diverse, heterogeneous and therefore will seek different characteristics from national economies. To generalise over a 'typical' MNE is unwise due to the range of companies which operate on a multinational basis.

While MNEs globalise in order to seek higher or longer-term profits there is a distinction that can be made between those which are 'cost-orientated' and 'market-orientated'. Cost-orientated MNEs look to increase efficiency by seeking:

- Reduced labour costs;
- Increased labour productivity;
- Cheaper or more secure inputs; and
- Lower tax burden/ government incentives.

Whereas, Market-orientated MNEs look to increase revenue by seeking:

- Access to larger and emerging markets;
- A more favourable regulatory environment;
- Technology and information transfer; and
- To preclude or counteract moves taken by competitors.

[5] Infrastructure is used throughout this paper in a general sense to refer to the physical assets which make up a region's energy management, transport, digital communications, flood management, water and waste networks and the intellectual capital. The significance of each of these elements to a business' decision to locate in a particularly economy will vary from business to business (a communications business may have different priorities than a logistics business for example). The next paper in this series will look at Northern Ireland's infrastructure 'performance' in a micro sense, considering each of these factors.

[6] Dunning. J.H, (1993) "Re-evaluating the benefits of Foreign Direct Investment". Available online at http://nia1.me/29o (Accessed 06/10/14)

These underpinning motivations for FDI are not exclusive or indeed exhaustive and other factors can also play a role. This Briefing Paper seeks to review the literature which has been written on FDI and assess what determinants are important for firms engaging in FDI, with a particular focus on FDI into developed economies which is of greater relevance for Northern Ireland. The conclusions are written with a view to appraise the role of multiple factors, rather than arriving at a definitive answer to what determinant is the main driver of FDI.

3 FDI Determinants by Sector

A working paper commissioned by the **IMF** studied FDI in a number of developing and advanced economies[7]. Its dataset broke FDI inflows down into three sectors[8].

- Primary: Acquisition of resources e.g. mining, fishing, agriculture, oil extraction.
- Secondary: Manufacturing or assembly e.g. automobiles, aerospace, engineering.
- Tertiary: Service provision e.g. information technology, finance, and transport.

Assessing FDI by sector is useful in that it enables analysis on what macroeconomic factors attract what types of FDI and if there are differences worth noting between what determines FDI inflows between the three different sectors of the economy, given the heterogeneous nature of firms that engage in FDI.

3.1 Macroeconomic variables

The paper evaluates the relationship between FDI and certain macroeconomic variables, such as, inflation, current FDI stock, openness, real exchange rate and GDP per capita. To clarify, openness is a measure of how open a country is to trade and investment, based on what barriers to entry exist.

- Primary sector
  - FDI in this sector only had a relationship with the current stock of FDI, which was revealed to be a positive determinant. This can be explained by how the primary sector is chiefly concerned with the location of natural resources rather than the broader economic environment.
- Secondary sector

[7] Walsh. J,P, and Yu. J, (2010). "Determinants of Foreign Direct Investment: A Sectoral and Institutional Approach." Available at https://www.imf.org/external/pubs/cat/longres.cfm?sk=24135.0 . Accessed on 07/10/14.

[8] The three sectors referred to here and throughout the paper correspond to the basic categorisations of industry sectors used in economic theory – primary, secondary, and tertiary. They are broad division of business activity related to but distinct from the sectors referred to in the Northern Ireland Economic Strategy. Those sectors are more specific and are in a sense a subsector of three broader categorisations used in this paper (although it is possible for a business sector to cross a number of these three broad sector classifications – for example the agri-food sector can be defined to include primary, secondary and tertiary activities). These more specific sectors will be addressed in more detail in subsequent papers.

    - FDI in this sector has a much stronger relationship with macroeconomic variables.
    - Current FDI stock proved a positive determinant of FDI.
    - A weaker exchange rate leads to more FDI in manufacturing.
    - Richer countries get a lower share of manufacturing FDI compared to poorer countries relative to GDP. This can be explained somewhat by the preference for lower labour costs in manufacturing.

- Tertiary sector
    - There are some relationships with macroeconomic variables, though not in the same areas.
    - Current FDI stock proved a positive determinant of FDI inflows.
    - The openness of the economy is a strong determinant to tertiary FDI inflows. This has no direct explanation, but could be linked to broader economic liberalisation which is generally positive for the service sector.
    - A strong exchange rate is a positive determinant of FDI in the tertiary sector. This may be associated with the high profits and relative high wages which tend to exist in countries with strong exchange rates.

3.2 Qualitative variables

The paper also evaluates the role of qualitative variables in attracting FDI such as a measure of labour flexibility (based on hiring and firing costs), infrastructure quality, financial depth, judicial independence, legal system efficiency, and enrolment rates for primary, secondary, and tertiary education.

- Primary sector
    - Like was the case with macroeconomic variables FDI in the primary sector showed little relationship with qualitative variables.
    - This is unsurprising as the acquisition of natural resources is unlikely to be related to factors such as the development of a financial system, or the quality of the legal system.
- Secondary sector
    - FDI in the secondary sector demonstrates a greater relationship with qualitative variables, with labour market flexibility and financial depth proving a strong positive determinant of manufacturing FDI.
- Tertiary sector

- FDI in the tertiary sector is also demonstrated to have relationships with qualitative variables.
- Judicial independence has a strong effect on levels of FDI in the tertiary sector.
- Quality of infrastructure also has a strong positive impact on tertiary FDI.

3.3 Advanced v Developing economies

The paper then goes on to differentiate how factors differ between the advanced and developing economies.

3.3a Macroeconomic variables

- Primary sector
  - Primary sector FDI in developing or advanced economies shows little relationship with macroeconomic variables.
- Secondary sector
  - For secondary sector FDI the relationships with macroeconomic variables remain unchanged when the data is split to differentiate between advanced and developing economies.
- Tertiary sector
  - When the data is split to differentiate between advanced and developing economies we find that macroeconomic conditions have a strong effect on tertiary FDI in advanced economies.
  - A strong exchange rate and a greater stock of current FDI lead to significantly more services FDI inflows amongst advanced economies, and have little effect on developing economies.

3.3b Qualitative variables

- Primary sector
  - As has been the case throughout this analysis, primary sector FDI shows little relation with qualitative variables, even when split by advanced and developing economies.
- Secondary sector
  - There are differences that emerge in qualitative variables between advanced and developing economies in the secondary sector. Labour flexibility and financial depth was shown to be a positive determinant initially, when split by economy type, it only remains important for developing economies.

- Tertiary sector
    - There are some observable differences in the relationship between tertiary FDI when split by advanced and developing economies.
    - In advanced economies an independent judiciary leads to more FDI.
    - Interestingly a more flexible labour market leads to less FDI, but only in advanced economies.
    - Better infrastructure remains important for attracting tertiary FDI in both advanced and developing economies.

3.4 Overview

The IMF working paper demonstrated a number of interesting salient points which are worth considering about the determinants of FDI.

- FDI is not homogenous and can take place across different sectors of the economy.
- FDI is attracted to different characteristics of host economies depending on what sector the inflows take place in.
- Not only is FDI from different sectors attracted to different characteristics, but it also behaves differently within sectors when engaging with advanced and developing economies.

3.5 Policy Implications

Based on the results of their analysis the authors suggest maintaining prudent macroeconomic management, such as strong growth, openness and low inflation. This is especially true for FDI in services in advanced economies. Having an independent judiciary and good infrastructure are also considered positive for services FDI, therefore this is something which should be strived for by policymakers if services FDI is considered desirable. From the perspective of an advanced economy, the research offers little guidance on how to attract FDI in the secondary sector and even less so in the primary sector.

4 The role of Tax and Incentives

A report of determinants of FDI location by fDi intelligence found that regulations/business climate was cited as a motive in 20.6% of cases, while Investment Promotion Agencies (IPAs) or government support was cited in 4.8% of cases. It is important to note that multiple motivations could be potentially cited, however it does highlight tax and incentives as motivating factor for businesses[9].

[9] “The fDi Report” (2014)”.Pg 16. fDi Intelligence.

A study conducted on behalf of the **World Bank** analysed the role of tax and other incentives in determining FDI.

4.1 Key findings

- Tax incentives will generally neither make up for serious deficiencies in the investment environment, nor generate the desired positive externalities.
- The importance of fundamental factors like economic conditions and political climate is underlined by the fact that most investors are often unaware of the full range of incentives when they invest.
- However when factors such as human capital or political stability are equal, then taxes and incentives may exert a significant impact.
- While tax incentives may bring significant increases in investment flows, it may have a negative impact on fiscal revenues and could create opportunities for illicit tax behaviour by multinational companies, such as profit shifting.
- Much of the impact of tax policy is firm specific. Mobile firms or firms which engage in multiple markets would tend to be attracted by such tax incentives as it gives them an opportunity to exploit different tax regimes across countries[10].

4.2 Overview

The paper mentioned illustrates that FDI may respond to taxation and incentives in different ways and policy makers must guard against automatic assumptions about the relationships between lower tax, increased investment and higher tax revenues. However, it does suggest that all things remaining equal such tax and incentives can serve a role as a 'tie breaker' amongst countries with similar levels of human and physical capital.

A policy analysis conducted by the **OECD** comes to similar conclusions noting that

> *Inbound FDI is recognised as being attracted by macroeconomic stability; a supportive legal and regulatory framework; skilled labour and labour market flexibility well developed infrastructure; and business opportunities tied to market size (with profitability of the domestic market tied to the purchasing power of the population, and foreign markets reached via an extensive network of trade agreements). In other words, a number of non-tax factors are central drivers to FDI decisions. Sound tax policy establishes a basis for fiscal stability which strengthens the business*

[10] Morisset. J, and Pirnia. N,. (2000) "How Tax Policy and Incentives Affect Foreign Direct Investment". Available at http://nia1.me/29q . Accessed on 13/10/14

> *climate. Additionally, in certain cases, tax may be an important factor influencing location decisions[11].*

In gathering together several different empirical studies, the results found a strong negative relationship between FDI and taxation. In broad terms a 1% increase in the tax rate was found to lead to a 3.72% change in FDI. However, this comes with a qualification that sensitivity of FDI to taxation may differ dependent on firm, industry and national conditions and may be subject to diminishing returns.

Alongside the assessment of the influence that tax plays in FDI decision making, the paper also enters a discussion around the factors which policy makers must take into account when making decisions regarding tax levels. Some key points arise out of that.

- It is not only the statutory ‘headline’ rate which is important when assessing the relationship between tax and FDI but the average ‘effective’ tax rate, which takes a view that the broader fiscal picture is the most important for investors making location decisions regarding FDI.
- While much preoccupation is given to corporate tax, other taxes such as environmental taxes are said to be “becoming much more important” by tax officials. This is explained by the tax planning powers that MNEs have at their disposal. Corporate tax is said to be already “taken care” of, in that companies have a great degree of freedom in deciding the level of tax they will pay on profits in the host country. This is due to the capacity of large firms to shift profits using complex tax avoidance and accounting measures, which allows for sales in countries with higher corporate tax to be accounted for in countries with lower rates of corporation tax, therefore creating a lower tax burden for the firm in question.
- Like other studies mentioned it notes the fundamental nature of non-tax factors.
  - Competition from low tax countries without developed infrastructure or public services is not considered a serious threat to countries with these advantages, regardless of higher taxes.
  - Large OECD countries with relatively high taxes are amongst the most successful at attracting FDI.
  - The study notes that of empirical studies into the relationship between FDI and tax some find a strong negative relationship, others do not, which somewhat outlines the complexity of the matter at hand.
- The study notes that governments have a responsibility to balance fairness, investor attractiveness and revenue raising in the tax system.

[11] OECD (2007) “Tax Effects on Foreign Direct Investment”. Available at http://nia1.me/29r Accessed on 13/10/14.

- In decision making policy makers must assess the legitimacy of claims made by business interests of locating elsewhere because of more favourable tax regimes.
- In contrast an over eagerness to attract investment could have negative impacts on revenue.
- In terms of public opinion there may be a perceived unfairness if highly profitable MNEs are granted lower taxes and other financial incentives.

5 Clustering and Embedding

The location of an industry cluster/ critical mass was cited as a motive in 6.4% of FDI projects (119 projects) in 2013 by **fDi intelligence**[12]. This makes it a worthy factor for appraisal, particularly as the existence of a cluster is often considered to improve the quality of FDI.

A policy paper by **OECD** outlines the importance of not only attracting FDI but maximising the benefits of FDI by embedding it with regional policy. FDI can be seen as more or less advantageous in how it responds to these challenges[13].

- In terms of finance, foreign investment is often criticised for 'financial leakage' out of the host region through the remittance of earnings and profits back to the parent company and use of transfer pricing to reduce taxes paid in the host region.
- In terms of technology, foreign investors are accused of not making available their technology to potential users outside the firm, either directly, through linkages with indigenous firms, or indirectly via the demonstration effect. Another issue is the appropriateness of the technology transferred, with the argument put forward that multinationals do not adapt their process technology for use in developing countries to make it more appropriate to a low-skilled labour environment.
- In terms of linkages, it is often argued that there is little sourcing of materials and services locally, and so positive spin-offs for local suppliers are limited, whilst there are often few forward sales linkages or strategic collaborations in the regional economy.
- In terms of vulnerability to closure, the fact that a foreign affiliate is often a replica of another operation elsewhere within the parent group and that overseas headquarters often have a wide choice of possible locations for any investment, leads many commentators to the view that foreign operations attracted by investment incentives are relatively vulnerable to closure.

[12] "The fDi Report" (2014)".Pg 16. fDi Intelligence.

[13] Potter. J, (2003) "Embedding Foreign Direct Investment". Available at http://www1.oecd.org/regional/regional-policy/2489910.pdf . Accessed on 14/10/14.

In order to improve the impacts of FDI, it is therefore important to adopt policies to improve the quality of the FDI attracted. This can be achieved through better targeting in marketing, promotion and incentive provision and making improvements in the quality of local business environment in terms of local skills, infrastructure, technology base and so on.

In giving examples of successful regional embedding of FDI the paper cites Wales where restructuring away from dependency from coal and steel has been led by FDI, with foreign firms becoming more embedded by engaging in local purchasing and tutoring local firms adding to a diffusion of knowledge and sharing of best practice. The paper also points to Baden-Württemberg in Germany (home to Audi, Porsche and Mercedes-Benz)[14] as another successful region where FDI has been successfully embedded.

Perhaps the most notable example of FDI having real positive externalities in a local economy is the example of Nissan in the North-East of England where "technology transfer" led to revitalising the UK automobile industry and through "demonstration effects" increased the quality of the local supply chain.[15]

As former BBC Economics editor Evan Davis notes:

…when Nissan opened in Sunderland it didn't just create one factory's worth of new jobs in the north-east of England, it revamped the supply chains. It shook the UK parts makers out of their low standards and, in doing so, gave the entire British motor industry a future[16].

5.1 Policy Implications

In order to maximise the effects of FDI it is important that after the initial attraction of FDI there is subsequent after care, which links local firms with new entrants. Knowledge transfer to domestic actors can help build endogenous growth, which in turn can help reduce long-term reliance on incentives to attract FDI.

Academic research published in the **Cambridge Journal of Economics** looked closely at the relationship between FDI and clusters. Its econometric analysis makes several interesting conclusions [17].

- Firms in clusters gain significant spill over benefits from FDI in their region.
- Such advantages are not experienced by non-cluster firms which merely suffer 'crowding out' without the off-setting benefits of FDI.

[14] "The Automotive Cluster in Baden- Württemberg" (2004). Available at http://nia1.me/29s . Accessed on 28/10/14.
[15] Griffith, A.Wall. S, (2012) "Applied Economics", Pearson, London.
[16] "Davis, E. (2011). "Made in Britain", Little Brown, London.
[17] De Propris, L. and Driffield, N. (2005). "The Importance of Clusters for Spill overs from Foreign Direct Investment and Technology Sourcing", Cambridge Journal of Economics. Available at http://nia1.me/29c .Accessed on 14/10/14.

- Technology transfer, alongside new management techniques can lead to higher productivity within domestic firms within a cluster.
- Both private and social benefit from FDI is greatest when MNEs enter pre-existing clusters. This is explained by foreign to domestic spill overs and technology sourcing.
- This paper suggests that FDI generated clusters can be fragile given that MNEs have the capacity to relocate.

5.2 Overview

Given these points it is suggested that basing a region's competitiveness on international capital is unwise. Rather in order to attract and maximise the potential of FDI the authors argue that regions should support and encourage endogenous cluster development through encouraging cooperation between local firms and developing new SMEs. If a region becomes a centre of accumulated knowledge it will soon become an attractive locality for MNE investment, rather than being attractive through lower cost factors. These steps have the potential to increase the quantity and quality of FDI. The authors suggest a strategy of developing local clusters in order to attract FDI, rather than trying to create FDI based clusters from an originally weak position.

6 Market Size

Another potential factor determining FDI location is access to larger markets.

The importance of this determinant is exemplified by research carried out by **fDi intelligence** which states that of FDI projects in 2013, "domestic market growth potential" was cited as a motive in 45.4% of projects, while "proximity to markets or customers" was cited as a motive in 33% of projects. It is worth noting that multiple motives can be cited for individual projects, so there may be crossover between these two figures, nevertheless the report characterises FDI in 2013 as "primarily market seeking[18]."

The importance of market size is identified as a determinant in a policy paper commissioned by the World Bank, which states;

> *OECD countries are more likely to invest in countries whose market size is big, are closer in terms of bilateral distance, and with which they share a colonial and linguistic heritage".*

[18] "The fDi Report" (2014)".Pg 16. fDi Intelligence.

The same paper notes that "Obviously BRIC (Brazil, Russia, India, and China) offers conspicuous advantages like market size to investors[19].

Market size is therefore broadly considered an important determinant of FDI.

A review conducted on behalf of the UK Government into the UK's suitability for FDI finds that;

Larger, fast growing markets are associated with higher FDI inflows. The literature generally captures these market characteristics by using GDP, GDP per capita, GDP growth, or (at sectoral or firm level) market size measured in terms of industry output. The initial and potential future demand conditions in a market act as a signal to inward investors on the attractiveness of a location. Furthermore, it allows investors to locate where they can take advantage of scale economies. The UK market size, and industry growth performance compares well with its other advanced countries signalling significant potential for inward investors[20].

It is worth considering the attractiveness to FDI of Northern Ireland's position within the United Kingdom, the world's 6th largest economy, and subsequently the UK's membership of the European Union, the world's largest trading bloc.

An UK Government publication assesses the role that EU membership has contributed to UK successes at attracting FDI[21]. The key findings of which are:

- The UK has seen substantial growth in both inward and outward FDI since accession to the EU, although determining how far the EU was responsible for this is complicated by other factors – in particular the global surge in FDI at the same time. However, the stylised facts support the theory that membership of the EU is a key factor in attracting investment to the UK, and demonstrates the importance of this investment for the UK.
- EU membership has contributed to FDI growth in the UK by reducing access costs to a larger market, enabling greater economies of scale and returns on investment, increasing competition and facilitating agglomeration.
- The UK has been a major beneficiary of FDI flows in the EU, but integration has also enabled growth in outward FDI to EU countries, and increasing returns on this investment.
- Important potential future FDI gains are possible from further integration, particularly following successful liberalisation of services industries. The long-term FDI cost of withdrawal would be significant.

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[19] Wagle, S. (2011). "Investing across Borders with Heterogeneous Firms. Do FDI- specific Regulations Matter?" Policy Research Working Paper, The World Bank.

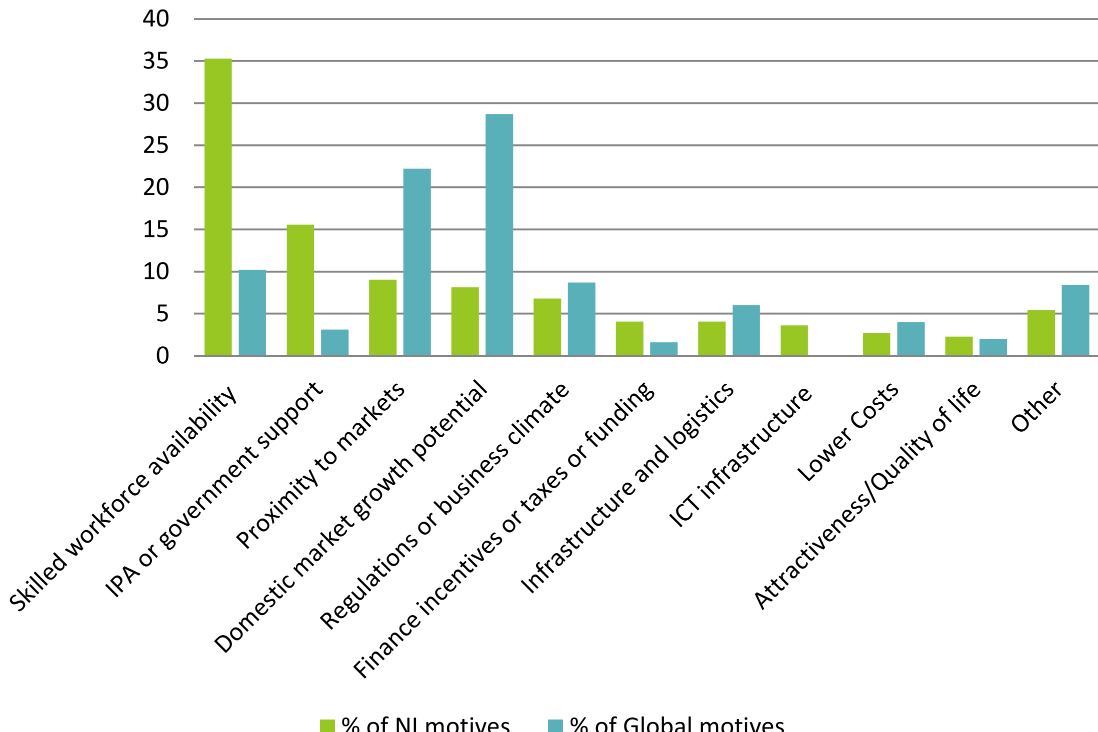
[20] Driffield, N. et al (2013). "How attractive is the UK for future manufacturing foreign direct investment?" .Government Office for Science. Available at http://nia1.me/299 . Accessed on 23/10/14.

[21] "EU membership and FDI". UK Government. Available at http://nia1.me/29a .Accessed on 23/10/14.

7 Variation between Northern Ireland and Global Determinants

So far, this paper has evaluated factors which are important for FDI globally. This section evaluates the differences that exist between the motivations for FDI globally and in the specific case of Northern Ireland.

Figure 1: Motives of FDI in NI v Motives of FDI Globally



[22]

The above chart extracted from data provided by **fDi Intelligence** at the Northern Ireland Economic Conference 2014 contrasts motivations cited by firms engaging in FDI globally with those cited by firms engaging in FDI in Northern Ireland.

There are notable factors which are cited much more extensively in the Northern Ireland example in comparison to the global study. The existence of an Investment Promotion Agency (IPA) of which Invest NI is a prime example, and/or government support is cited 5 times more in the Northern Ireland case. This can be viewed positively in terms of the performance of Invest NI in contributing to bringing inward investment into Northern Ireland. Also, firms engaging in FDI in Northern Ireland cited the importance of "skilled workforce availability" more than three times as much

[22]Figure 1. Created with data from Barklie, G (2014). "Why are firms establishing a presence in NI?" fDi Markets.

compared to the global study. This again is something which can be viewed as a positive endorsement of skill levels amongst the local workforce, though this matter as well as other factors will be addressed in more depth in further research.

There are other areas where motivations feature much less in the Northern Ireland study compared to the global study. The motive categorised as "domestic market growth potential" is cited more than three times more in the global study. This is somewhat unsurprising given the small population of Northern Ireland (1.8 million) and the fact that it contributes only 2% of UK Gross Value Added (GVA) compared to the global study which considers FDI in some of the world's largest emerging economies such as the BRIC countries (Brazil, Russia, India, China) where market size is a key selling point to inward investment. "Proximity to markets" is another factor which was cited considerably more in the global study than in the Northern Ireland case. This figure is somewhat surprising given Northern Ireland's position within the UK which brings with it, as outlined above, membership of the European Union and also the Northern Ireland specific advantage of sharing a land border with the Republic of Ireland, which can be advantageous for investors.

We can view similarities on a number of the determinants such as "regulations or business climate" showing roughly equal import both globally and in the specific Northern Ireland case. This is also the case for "infrastructure and logistics" and with regards "attractiveness/quality of life". In regards to these factors Northern Ireland is in line with the global trends in motivations for investment.

Interestingly "lower costs" is only cited as a motivation in a small percentage of FDI projects in both the global and Northern Ireland specific study. This is somewhat counter intuitive, as earlier in the paper I indicated the cost-orientated, efficiency seeking motivations which often drive some firms to engage in inward investment. Therefore it is surprising that "lower costs" isn't more highly cited as a motive, especially as competitive costs on wages and property is an advantage of investing in Northern Ireland stressed by Invest NI[23]. Glenn Barklie of **fDi intelligence**, the organisation behind the survey, accounted for these results at the Northern Ireland Economic Conference 2014[24] by explaining that firms often stress positive aspects, such as skill levels, when outlining why they have located in a particular country, rather than citing cheaper inputs into the production cycle, such as comparatively cheap labour or low prices of land. Motivations categorised as "finance incentives or taxes or funding" also score very low in both studies, though in the Northern Ireland case it scores slightly higher, this perhaps is a result of incentives granted by Invest NI. This category may be subject to the same understatement as the "lower costs" category, though this is ultimately speculation.

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[23] Written Evidence from Invest NI. Corporation Tax in Northern Ireland- Northern Ireland Affairs Select Committee. Available at http://nia1.me/2al. Accessed on 12/11/14.

[24] Barklie, G. (2014). Talk on "Examining the importance of economic drivers- foreign direct investment". Delivered on 07/10/14.

Table 1: Motivations of FDI globally compared with NI[25]

	% of NI motives	% of Global motives
Skilled workforce availability	35.29	10.21
IPA of government support	15.55	3.11
Proximity to market	9.05	22.22
Domestic market growth potential	8.14	28.71
Regulations or business climate	6.79	8.71
Finance incentives of taxes or funding	4.07	1.58
Infrastructure and logistics	4.07	5.99
ICT Infrastructure	3.62	-
Lower costs	2.71	3.97
Attractiveness/Quality of life	2.26	2
Other	5.43	8.43

8 Conclusion

Overall this Briefing Paper has examined a range of literature on the determinants of FDI. FDI is highly diverse and as Section Two demonstrated can be attracted by different factors dependent on whether it takes place in the primary, secondary or tertiary sectors. It was also revealed that FDI in the same sector is attracted to different aspects dependent on whether an economy is advanced or developing. Section Three examined the role of tax and incentives in attracting FDI, it stressed the importance of the tax burden as a whole, particularly the effective tax rate, rather than the statutory 'headline' rate and also noted the fundamental nature of non-tax factors such as infrastructure and public services over low taxes. However it was noted that tax and incentives could become more important in situations when non-tax factors were roughly equal. Section Four discussed not only how the location of an industry cluster can attract FDI, but also how clusters can actually amplify the benefits which FDI can bring to the host economy. Section Five entered a brief discussion of the role that market size plays in determining FDI, whilst also noting the benefits which the UK has received regarding FDI from membership of the EU. Section Six outlined the differences between the factors that motivate FDI in Northern Ireland and how these differ in importance compared to factors which typically motivate FDI globally.

The table below summarises the different factors identified throughout this Briefing Paper which are attractive to FDI. Column one shows the factors which are positive for FDI generally, although as has been noted Northern Ireland's general factors are different from the typical motivations for FDI globally. Column two illustrates factors which are attractive for FDI and aligns them with the specific sector in which they are

[25] Detailed Figures from fDi Intelligence. (2014) "Why are firms establishing a presence in Northern Ireland?"

most favoured. Column three outlines factors which can play important deciding roles in FDI location, particularly in cases were all other factors are roughly equal.

Table 2: Factors identified which are attractive for FDI

1 Generic Factors →	2 Sector Specific →	3 Deal Breakers/ Other Desirables →
Global ▪ Access to markets ▪ Business climate	**Extraction Industries:** ▪ Natural resources	▪ Tax levels
	Low Value Added Manufacturing: ▪ Low labour costs ▪ Labour market flexibility	▪ Government incentives
Northern Ireland ▪ Skilled workforce availability	**High Value Added Manufacturing:** ▪ Specific local skills base ▪ Existence of an industry specific cluster	▪ Investment Promotion Agency support
	Service Industries: ▪ Infrastructure ▪ Low barriers to market entry	▪ Quality of Life