Foreign direct Investments and diplomacy

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Abstract- An essential condition for the development of entrepreneurship is an innovative culture, climate and tradition. There is no doubt that these factors depend on the industrial culture, the mentality of the people, as well as on the climate created in the society. This climate depends on the global policy that is conducted in society, on the created material assumptions, but also on numerous other factors: sociological, psychological, ethical, normative, etc.

Index Terms- foreign direct investment, markets, transnational corporations, entrepreneurial economics.

I. Introduction

The development of entrepreneurship is influenced by many factors that can be systematized into: objective and subjective, internal and external, personal and environmental factors, etc. They can also be divided into economic, psychological, sociological, legal, informational, technical-technological, etc. A deregulated economy is also very important for the development of entrepreneurship. The state may not limit the autonomy of economic entities with its measures, nor prescribe the conditions and methods of mutual cooperation. Also, the state should not use various measures of monetary, tax, customs, credit or any other policy to favor some branches and disincentivize others. In this way, unequal conditions for the development of entrepreneurship would be created.

II. Foreign direct investments

Foreign direct investments (hereinafter referred to as FDI) represent one of the basic models of capital movement in the world and, along with trade, one of the driving engines of the globalization of the world economy in the second half of the twentieth century, with a clear tendency for such a trend to continue in the new millennium. FDI represents a model by which companies deploy their production processes around the world, in order to obtain the necessary raw materials, labor and energy under the most favorable conditions, on the one hand, and the most profitable use of the technology and experience they possess in business, on the other hand. There is a complementarity between international trade and direct investment. Namely, regardless of the increase in foreign direct investments that production is carried out for import into their own country, companies carry out significant exports to their branches abroad. Therefore, FDI is not a substitute for international trade. In fact, one-third of the world's trade is between controlled affiliates, such as business-to-business, business-to-business, and business-to-business. Numerous trade flows between enterprises and affiliates would not have occurred without FDI.

Countries in which these investments are made, are interested in economic growth and employment, in better use of certain resources and in improving the quality of products and services. Of course, they seek to regulate the flow of capital by requiring partial local ownership of the company's assets. Some countries still prefer higher loans, fearing that foreign owners do not control basic sectors of the economy. Every national economy enters into international economic relations through several forms of foreign economic transactions. These transactions can be very different and can relate to:

1. import and export of goods and services,
2. import and export of capital and money and
3. certain unilateral transfers (economic aid, gifts).

The international movement of capital represents the transfer of real and financial assets between subjects of different countries, with a counter-transfer postponed for a certain period, in order to realize the economic and political interests of the participants in that transfer. The three main forms of international capital movement are:

1. international movement of loan capital,
2. portfolio investments i
3. direct investments abroad.

Depending on the time of observation, the acquisition of financial assets abroad can be divided into: short-term financial investments and long-term financial investments or portfolio investments. Portfolio investments come in two basic forms:

1. A traditional type of portfolio investment is investing in bonds, bonds, and generally securities issued by a foreign government, or other institutions and even companies in order to raise loan funds on an international capital market. Due to large fluctuations in interest rates, interest is not determined in a fixed amount, but in a variable amount, as a margin that is added to the base interest rate (Libor or prime rate). The owner of the capital does not decide on the way of using the funds, but within the stipulated period, regardless of the achieved results of the

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work, he receives the borrowed funds together with the interest. This is a capital transfer with minimal risk.

2. Another type of portfolio investment is very similar to direct investment, because it is about investing capital in foreign companies. However, the stake moves to a height that does not ensure control and management, and thus does not include influence on the company's way of doing business. Given that the investor cannot influence the way the funds are used, the objective of the placement is to acquire financial assets that will be able to be sold in the future at a higher price than it was purchased, with a capital gain for the investor. In this case, there is no return of the invested capital within a certain period, but it is returned at the moment when the investor judges that it is the best time to sell the assets he owns. The amount of profit (or loss) depends on the success of the business of the invested company, because now the investor participates in the distribution of the realized profit.

Compared to other types of investment, portfolio investments have a favorable relationship between the level of risk assumed by the investor and the amount of profit that can be realized. Portfolio investments carry a higher risk and a higher return on invested funds than bank deposits, but the risk and return are lower than with direct investment.

The basis for defining the difference between portfolio and direct investments is the right of control and management in the company in which the investment is made. If the investor acquires the right of ownership and thus the right of direct control and management of the company on the basis of shares in the company, that investment is a direct investment. Conversely, if the stake invested does not provide the right to control and manage the entity in which it is invested, then it is a portfolio investment. The differences between direct and portfolio investments can be divided into three basic categories:

1. the motive of investing, the prevailing motive of portfolio investors is participation in the profits of local companies in which they have invested through capital gains and dividends. They are not interested in participating in company management, which is the primary preoccupation and motive of foreign direct investors.
2. investment time horizon, unlike FDI, portfolio investments are investments for a short period of a few weeks or months, although it can be extended to 10 years or more, especially in the case when they are realized through the so-called "Venture Capital". Typical venture funds in the USA amount to 75 to 200 million dollars and invest in 20 to 30 companies for a period of 3 to 5 years,
3. type of investors, mainly financial institutions, institutional investors, or individuals primarily interested in achieving financial profit on their roles. Companies involved in the production of goods and services usually appear as FDI investors on the other hand.

In the case of direct investments, the complete influence of the investor is not necessary, but the degree of control and management should be such that the way of management and business policy of the company depend on it.

III. Motives for foreign direct investment

The starting point and basic motive of all subjects undertaking FDI is to maximize profits in the long term. Transnational corporations (hereinafter referred to as TNCs), as holders of FDI through their corporate strategies, must integrate the operations of individual parts into a single system in order to achieve profit maximization at the corporate level. Contrary to this strategy, there is a possibility of trying to reach the maximum profit at the corporate level through profit maximization, which can lead to situations of conflicting interests and thereby reduce the profit at the corporate level. In the literature, the motives for undertaking FDI are divided into:

1. strategic,
2. behavioral (subjective) and
3. economic motives.

Strategic motives can be divided into:

1. production to secure resources,
2. production to secure the market,
3. production to achieve greater efficiency,
4. production for the purpose of acquiring strategic resources/advantages.

TNCs undertake investments abroad in order to secure resources at a lower price than would be possible in the home country. The achieved production is usually exported to the home country where the investor gains a certain competitive advantage based on cheaper inputs. Three types of resources can be a motive for undertaking FDI:

1. physical resources: raw materials, minerals, agricultural products. Investments to secure natural raw materials are usually undertaken by companies from the primary or industrial sector of developed or developing countries to provide a cheap and secure source of supply of resources for which they have the appropriate processing capacity. For those investments, it is characteristic that in the initial phase significant expenses of the investor's company are assumed,
2. cheap unskilled or semi-skilled labor. The investor is usually a company from the industrial or service sector, which locates the production of labor-intensive intermediate products or final products in a country rich in cheap labor. In that case, the host country is somewhat more developed and most often establishes free trade zones in order to attract that type of investment.
3. technological, managerial, marketing and organizational knowledge. FDI motivated by the provision of such sophisticated resources is usually undertaken in the form of strategic alliances or other non-property forms of cooperation (licenses, franchising, contracted management, turn-key contracts) and is linked to technologically intensive branches.

Investments motivated by maintaining existing or conquering new markets are usually directed to countries whose markets were served by exports until the moment when the host country introduced certain trade restrictions, most often in the form of customs barriers. With such an investment, we want to achieve the continuation of serving the local market and possible

expansion to the markets of neighboring countries. When talking about the market as a motive for foreign investments, it is possible to single out four basic reasons for undertaking FDI:

1. when the main suppliers or customers establish their affiliations in some foreign market, it is necessary to follow them in order to maintain the business,
2. when there is a need to adapt products to local tastes and needs, it is necessary to have close contact with the market and well get to know the local culture, customs and habits, so that the foreign supplier does not have less opportunities than the domestic supplier,
3. when serving a local market from a more closely located capacity is more cost-effective than serving from a distance. This type of market orientation is closely related to the characteristics of the industry branch itself, i.e. the country of the supplier. For products that are expensive to transport and can be produced in small batches, production will be located closer to the market being served. On the other hand, if transport costs are low and economies of scale are possible in production, the proximity of the market being served is not so significant,
4. a motive that becomes especially important in the conditions of the global production and marketing strategy of transnational corporations is the need to achieve a physical presence in all markets where all the most important competitors are present.

When greater efficiency is the motive for undertaking FDI, it means that there is a need to rationalize already existing partnerships in such a way that the TNC can realize the benefits of joint management of geographically dislocated capacities. Those advantages of joint management are mainly related to the achievement of economies of scale and economies of diversity (economies of scale in conditions of differentiated products), and to the diversification of risks. This type of investment is most often realized through the mechanisms of purchasing the assets of an existing company, usually a competitor. The motive is not to take advantage of possible cost and marketing advantages that a certain company possesses, but to combine common potentials and advantages in order to achieve a long-term strategic goal, which is constant or greater international competitiveness or the elimination, by joint forces, of the remaining competitors.

The category of economic motives of international business is directly related to the imperfection of the market of goods and factors of production, and includes most of the motives listed in the group of strategic and subjective motives of investment. By establishing partner companies in foreign markets, TNK achieves some of the following economic advantages: economy of scale, marketing and management experience, superior technology, financial potential and product differentiation.

IV. Conclusion

Today, small and medium-sized enterprises form the backbone of the economy of developed and many other countries. In the economic structure of the EU, there are as many as 25 million such companies employing 95 million people, which is 55% of the total number of employees in the private sector. Private enterprise consumption and private investments in Serbia are still not at a satisfactory level. The business climate in Serbia has been improving for the past few years, but not fast enough to stimulate faster development of the corporate sector, as well as the sector of small and medium enterprises. The main limitation, when it comes to institutions and regulations, lies in the non-implementation of regulations and in the inadequate functioning of institutions.

Entrepreneurial economics uses modern theories to understand entrepreneurship. These theories differ from those of the past in that they abandon many of the old neoclassical assumptions that were difficult to apply in practice. Neo-classical economics usually starts from the assumption of perfect information, a tendency towards autonomy and optimization. Abandoning these assumptions makes it possible to incorporate the entrepreneur into the economic theory as a decision-maker in the conditions of uncertainty provided by the boundary conditions of business. Abandoning certain assumptions in neo-classical economic theory gives today's entrepreneurship an intellectual approach.

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