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Effectiveness of Foreign Portfolio Investment with regard to Multinational Corporations in the Long Run

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Abstract - This study was conducted to exploretheapplicationofPortfolio Investments in situations where Foreign Direct Investment (FDI), although stable, does not seem to be compatible with the conductofMultinationalcorporations within a country. In this study the research question that appears would be, “Is it possible to use portfolio investment by multinational corporations in the long run when direct investment is chosen to be withdrawn?”. This study aims to discuss variousbenefitsandascertainthe effectiveness of the Portfolio Investment by including world examples of developing countries and at the same time investigates the position of portfolio investment by the statepartiesandthemultinational corporations when difficulties arise on FDI in the long run. To collect data for the study, secondary data will be gathered using the Black Letter method. FDI and Portfolio Investment are two different types under InternationalInvestmentLaw.FDIis covered bycustomary international law whereas Portfolio is not. While FDI tends to be more stable, Portfolio measures up to it by having benefits with regards to income, liquidity etc. This study mainly analyzes the situationsinMalaysiaandIndia.In conclusion, after analyzing the positive and negative aspects of both types of Investment, it can be when difficulties arise with FDI, the use of portfolio Investment can help mitigate issues that arise. It is recommended for developingcountriestomakeuseof PortfolioInvestmentinamoreliberal manner to take advantage of its benefits for the further development of the country's economy.

Keywords: **Direct, Portfolio, Investment, Multinational**

RESEARCH PROBLEM AND OBJECTIVES

Research Problem

Foreign Direct Investment is considered to becomparativelystablethanForeign Portfolio Investment. However, there is a tendency that multinational corporations withdraw from Foreign Direct Investment in the long run. In such a backdrop is it possible to use Foreign Portfolio Investment which is considered to be less stable than Foreign Direct Investment.

Research Objectives

- To identify the benefits of Foreign portfolio Investment
- To investigate the position of Foreign Portfolio Investment among multinationalcorporationsand between states
- Toidentifythereasonsfor withdrawalfromForeignDirect Investment in the long run

METHODOLOGY

The studyisbasedonForeignDirect Investments and Portfolio Investment and discussed the effectiveness of using Portfolio Investment when there are withdrawals of Direct Investment. Basically, it means to mitigate the negative effects that could arise from direct investment and

to ensure the smoothflowofeconomywithoutany distractions. This study was done using library research and to collect data for the study it used several secondary sources to clarify the question “Would it be possible to use Portfolio Investment by multinational corporations in the long run when Direct Investment is chosen to be withdrawn?”. For data analysis in this study, qualitative data wasanalyzed.Thisdatawasgathered throughinternetarticles,books,judicial decisions,treatiesandsomeother information supplied by websites as well. Thelimitationsofthestudyarethat quantitative data is not deeply analyzed and it only g two major examples as Malaysia and India.

I.INTRODUCTION

International investment law has two parts which can be divided as Foreign Direct Investment and Portfolio Investment. In the internationalspherethenatureof investment is more focused on FDI and Portfolio investments are not taken into consideration. Accordingly, Foreign Direct Investments are protected under customary international law because there are enough treaties and laws to govern it. At the same time Portfolio Investments are not under customary international law.Thereare arguments on these as well. In history there are instances where portfolio investments are identified by treaties. Therefore, it is a proved fact that FDI is more stable than the portfolioinvestments.Toclarifythe problem,itisnecessarytoknowabout definitions of both FDI and FPI. Accordingly, the issue here takes the view that, when there are difficulties with FDI, the host states can mitigate the position through several statepoliciesaccordingtothestate’s economy and can choose the way of Portfolio investments”. Here it mainly considers about two countries as examples; one which once ledtoeconomiccrises (Malaysia) and another which has fast growing economy (India). Both these states use state policies towards the FDI and even though FDI is more stable use portfolio investment in a moreliberalwaytotakecompatible advantages.

II.FOREIGN DIRECT INVESTMENT

Simply this is defined as investment of physical assets or the money which passes by the home state which is the state of the investorpassestohoststateasan investment. As mentioned by the IMF and OECD, direct investment means obtaining a lasting interest by a resident entity of one economy (direct investor) in an enterprise that is resident in another economy (the direct investment enterprise). These are utilized in the open market economies. FDI’s influences to the host state more likely a capital investment. Mergers, acquisitions, logistics, retail and other forms of areas suppliestheexamplesfortheFDI.
Traditionally FDI includes only the physical assets but in the modern context it has been expanded to several non-physical assets and intangiblerights.Moreover,theseare protected under customary international law and Intellectual property, Contractual and Administrative rights are discussed in them.

III.PORTFOLIO INVESTMENT

Portfolio investment is based on shares, debentures, bonds, etc. With regard to IMF, portfolio investment is defined as cross-border transactions and positions involving debt or equity securities, other than those include in direct investment or reserve assets. On the other hand, it is known as hot money as well.

In terms of the international investment law FDI or FPI investments protected under several treaties. Among those treaties’ portfolio investments are included in some. Portfolio investments have distinguished features from primary shares in certain companies which use foreign investment as

a vehicle. These are not under shares which are ordinarily traded but are instruments that directly connected with the companies assharesorindirectlyconnectedas promissorynotesandbonds.Amajor purpose of having portfolio investment is to raise capital for ventures. It can be done by savingorcirculatingaboveinstruments through stock exchange or through other markets.Thisshouldbeencouragedto include under investment treaties because to increase the capital flows, and also it is the interest of the developing countries to encourage their flows. On the other hand, there is an argument against to include portfolioinvestmentsinthetreaties. Accordingly host state has a duty to protect theseunascertainableholdersofthe instrumentsanditcontinuouslychange their identities. In fact, they can pull out of a state. Therefore, value of these instruments can be questioned in view of the financial crises which caused in the previous mass departure of portfolio capital.

In the case of *Fedax vs. Venezuela* domestic holders of promissory notes, who were not entitled to protections have transferred the notes to another foreign citizens of a country with an investment treaty. After that they becomeentitletoclaimagainstthe particular state because the treaty protected portfolio investments.

IV.COMPARISON OF FDI AND FPI

Both FDI and portfolio investments involve the situations funding in another country but these two have distinguish features in nature of holding, the degree of control and term etc. Accordingly, in FDI the degree of control is high as investor obtaining both management rights and ownership rights, portfolioinvestmentshaveonlythe ownership rights the control is very less. Role of investors in FDI is active and in portfolio it is passive. FDI is a long-term investmentwithphysicalassetsand portfolioinvestmentisashort-term investment with financial assets. Moreover, the management of project are efficient in FDI than the portfolio investments. With all these facts entry and exit are not easy thing for FDI but it is relatively easy for portfolio investments. FDI results in transfer of funds, technologyandotherresourcesbut portfolios are results in capital inflow.

V.EFFECTIVENESSOFPORTFOLIO INVESTMENT IN HOST STATES

Sudden withdrawal of portfolio funds from Asian countries has been affected to the Asian Economic crises which held in 1997.It proves the fact that portfolio investment is unstable in the meaning of FDI and it can be withdrawn at any time as investor wishes. On the other hand, FPI is lacking some characteristics that can be protected under the international policy protection as well. Although these facts are established when there are difficulties towards the FDI then host states are mitigating those difficulties and using portfolio investments to their economic systems. Countries such as China, Malaysia, India and Sri Lanka are using portfolio investments in the above manner.

Malaysia uses three types of capital control measures. They are indirect capital controls, control on the capital account and direct capital control. The beginning of the East Asia's financial crises was serious thing which happend in 1997 on Thai baht. Here they invested short term investments and after they pulled out all the money exposure had led to gushing default and after that currency devaluations started. Malaysian ringgit, Indonesian rupiah and Philippine peso were affected as a result of this issue. In the post-crisis's era both FDI and portfolio have helped to overcome the issue and balance payment theory which determined the mobility differentiate hot money and FDI. The statistics for Dependent Variables (1991-2004) proved that introduction of capital controls was helped to promote

soundenvironmentforportfolio investments. Without portfolio investment it isnoteasyforMalaysiatogrow economically solely with the use of FDI.

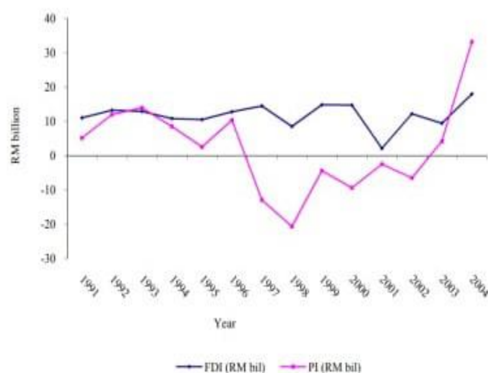

Figure 1 : The Flows of FDI and PI 1991 Through 2004

Normally in developing countries they need money to their own growth. All Asian countries have same features on this section. India is known as the fast-growing major economy in the world and they have 7.4% GDP rate for 2019 as well. Here India has taken several steps to liberalize their foreign investments and as a result of that can improvetheirbusinesses.Inbound investment routes are there that global investors can go beforetheirattractive destination points. FPI framework investors given chance to make their investments in listed equities and other securities. For this they need to register and take the license which were granted by Indian custodian in its manner specified as a DDP through regulations, 2014. Each investor needs to obtain a tax file. India recently change their tax exemptions as long-term capital gain tax wereremovedwithSingaporeand Mauritius. India has a restrictive FDI regime. With regard to Indian ventures it was ranked 57th in the GCR 1999.Even the banking sector needs to use reciprocal investment rights but government pauses restrictions on FDI. Lack of clear cut and transparent sectoral policies for FDI and high tariff rates on imported capital good used for export, limited scale of export processing zones can be known as difficulties in FDI sector. Specially there is no liberalization in exit barriers as well. So, that means they have their own state policies with difficulties towards FDI. Therefore, they have given more liberal way to FPI.

In respect of these examples it can be justified that sound economic states such as USA, England, France can use 100% FDI but if the states having difficulties on FDI they can mitigate their positions and can use portfolio investments as well.

VI.BENEFITSOFPORTFOLIO INVESTMENT

Benefiting by using portfolio investment is a far-reachingandfutureadvantage.
Sometimes, it would give advantages to another generation. On the investors side a wise investment can guard his initial investment and state parties can grow their economies within a short term. Not only the profits gained through shares, there are certain privileges.

A.Diversification

When investing an investor needs to allocate capital in a correct manner in order to reach the benefits in financial market. In a creation of diversified PI it can spread capital across more than one investment category. On the other hand, can diversified into multiple asset classes will help safeguard investors capital and at the same time host states can develop several industries in a short period of time by using hot money.

B.Potential

It is known as a major advantage to the investor. Individuals may be unprepared for their investments. Basically, what they do is placing money in bank saving accounts. It is a protected way but compared to share market and other portfolio investments they cannot grow profits in the financial market. By having PI the position is to potentially earn sizable profits and individuals can prepared for their own future targets. Accordingly, to the host states also can make taxes and safeguard

the investments by attracting investors by providing more facilities.

C.Income

Stocks will create steady income stream for many distributions. Investing in bonds and securities are other ways to make income through PI.

D.Liquidity

Unlike investing in real estates, equities or other fixed income instruments such as shares, securities and etc. can be traded based on supply and demand. Therefore, in PI's both investor and the host states can convert these instruments to cash if necessary.

VII.CONCLUSION

FDI is an investment basically used physical assets and other intangible rights in another country.Hereittransferredfunds, resources, technology etc. Accordingly, the investors have active management on these investments. Foreign Portfolio investment means investment which made through financial assets. From portfolio investments it can gain short term profits and investors do not have control over the investment. Direct investments are more stable than the portfolio investments there are some instances that portfolio investments are recognized by treaties. *Fedax vs. Venezuela* case is an example for the above recognition which has done to promissory notes. Even if the FDI is more stable than portfolio investments, multinational companies can withdraw the direct investment in the long run. Therefore, when there are difficulties towards the FDI the host states can mitigate the position by using their states policies and can make considerations on the portfolio investments as done by the Malaysia and India as an example. Thus, portfolio investment can make replacements in terms of FDI and it has more hidden advantages in short term.

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