FDI and Economic Growth: The Role of Local Financial Markets
Alfaro, Chanda, Kaleml-Ozcan, Sayek, forthcoming JIE

FDI: “flows of foreign investment to acquire a lasting management interest (10 percent or more of voting stock) in an enterprise operating in an economy”

**Does FDI induce growth?**
- direct capital transfer
- direct knowledge transfer
- spillovers

**Empirical evidence**
- Aitken and Harrison (1999, AER): Venezuela plant level data
  no spillover from foreign to domestic firms
  no significant impact of FDI on growth
**Motivation:**
Do local conditions matter?
“absorptive capacities”
macroeconomic management (trade openness/inflation)
infrastructure (phone lines/paved roads)
human capital (share of labor with secondary education)

**Case studies**
→ 115 of 130 workers went on to develop own business

India: Suzuki established assembly line plant for small cars 1981
→ initially all parts from Japan, now 90% from Indian firms

Costa-Rica: Intel established semiconductor plant in 1996
→ formation of a software sector
**Data: The extent of Financial Development**

**LLY**: Liquid liabilities of the financial system
currency plus demand and interest bearing liabilities of banks and nonfinancial intermediaries divided by GDP

**BTOT**: Commercial Central Bank Assets
the ratio of commercial bank assets divided by commercial bank plus central bank assets.

**PRIVCR**: Private Sector Credit
the value of credits by financial intermediaries to the private sector divided by GDP

**BANKCR**: Bank Credit
the credit by deposit money banks to the private sector divided by GDP

**SVALT**: the value of stock trading relative to the size of the economy

**SCAPT**: the average value (over a year) of listed domestic shares on domestic exchanges as a share of the size of economy (GDP)