Department of Management Studies
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6th Lecture

MEANING OF INVESTMENT

In simple terms, Investment refers to purchase of financial assets. While investment goods are those goods, which are used for further production. Investment implies the production of new capital goods, plants and equipments. **John Keynes** refers investment as real investment and not financial investment. Investment is a conscious act of an individual or any entity that involves deployment of money (cash) in securities or assets issued by any financial institution with a view to obtain the target returns over a specified period of time.

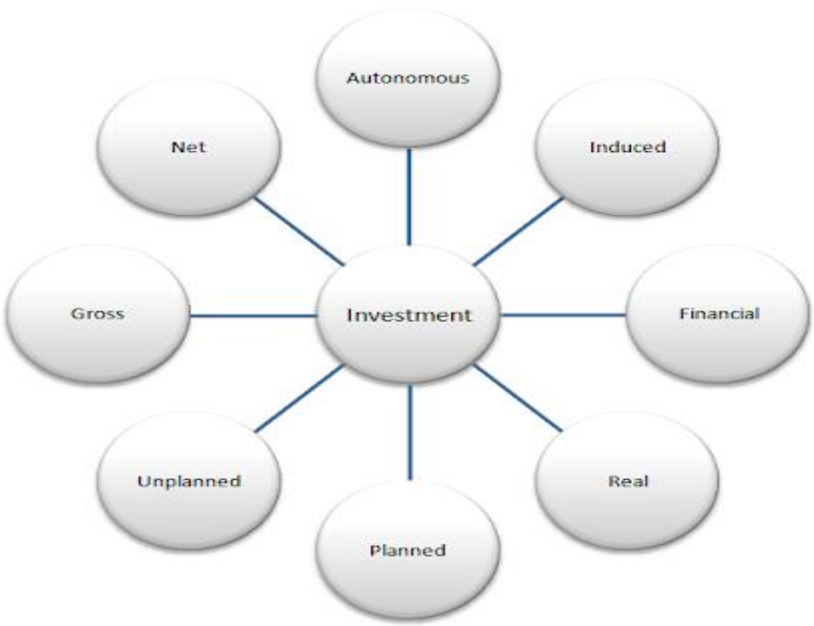
RETURN ON INVESTMENT

Target returns on an investment include:

- Increase in the value of the securities or asset, and/or
- Regular income must be available from the securities or asset.

TYPES OF INVESTMENT

Different types or kinds of investment are discussed in the following points.



- **Autonomous Investment**

Investment which does not change with the changes in income level is called as Autonomous or Government Investment. Autonomous Investment remains constant irrespective of income level. This means even if the income is low, the autonomous investment remains the same. It refers to the investment made on houses, roads, public buildings and other parts of infrastructure. The Government normally makes such a type of investment.

- **Induced Investment**

Investment which changes with the changes in the income level is called as Induced Investment. Induced Investment is positively related to the income level. That is, at high levels of income entrepreneurs are induced to invest more and vice-versa. At a high level of income, Consumption expenditure increases this leads to an increase in investment of capital goods, in order to produce more consumer goods.

- **Financial Investment**

Investment made in buying financial instruments such as new shares, bonds, securities, etc. is considered as a Financial Investment. However, the money used for purchasing existing financial instruments such as old bonds, old shares, etc., cannot be considered as financial investment. It is a mere transfer of a financial asset from one individual to another. In financial investment, money invested for buying of new shares and bonds as well as debentures have a positive impact on employment level, production and economic growth.

- **Real Investment**

Investment made in new plant and equipment, construction of public utilities like schools, roads and railways, etc., is considered as Real Investment. Real investment in new machine tools, plant and equipments purchased factory buildings, etc. increases employment, production and economic growth of the nation. Thus real investment has a direct impact on employment generation, economic growth, etc.

- **Planned Investment**

Investment made with a plan in several sectors of the economy with specific objectives is called as Planned or Intended Investment. Planned Investment can also be called as Intended Investment because an investor while making investment makes a concrete plan of his investment.

- **Unplanned Investment**

Investment done without any planning is called as an Unplanned or Unintended Investment. In unplanned type of investment, investors make investment randomly without making any concrete plans. Hence it can also be called as Unintended Investment. Under this type of investment, the investor may not consider the specific objectives while making an investment decision.

- **Gross Investment**

Gross Investment means the total amount of money spent for creation of new capital assets like Plant and Machinery, Factory Building, etc. It is the total expenditure made on new capital assets in a period.

- **Net Investment**

Net Investment is Gross Investment less (minus) Capital Consumption (Depreciation) during a period of time, usually a year. It must be noted that a part of the investment is meant for depreciation of the capital asset or for replacing a worn-out capital asset. Hence it must be deducted to arrive at net investment.

FOREIGN INVESTMENT

Foreign investment is when a company or individual from one nation invests in assets or ownership stakes of a company based in another nation. As increased globalization in business has occurred, it's become very common for big companies to branch out and invest money in companies located in other countries. These companies may be opening up new manufacturing plants and attracted to cheaper labor, production, and fewer taxes in another country. They may make a foreign investment in another firm outside of their country because the firm being purchased has specific technology, products, or access to additional customers that the purchasing firm wants. Overall, foreign investment in a country is a good sign that often leads to growth of jobs and income. As more foreign investment comes into a country, it can lead to even greater investments because others see the country as economically stable.

DIFFERENT KINDS OF FOREIGN INVESTMENT

COMMERCIAL LOANS: Commercial loans, which primarily take the form of bank loans issued to foreign businesses or governments.

OFFICIAL FLOWS: Official flows, which refer generally to the forms of development assistance that developed nations, give to developing ones.

FOREIGN PORTFOLIO INVESTMENT (FPI): Foreign portfolio investment (FPI), is a category of investment instruments that is more easily traded, may be less permanent, and do not represent a controlling stake in an enterprise. These include investments via equity instruments (stocks) or debt (bonds) of a foreign enterprise which does not necessarily represent a long-term interest.

FOREIGN DIRECT INVESTMENT (FDI): Foreign direct investment (FDI) pertains to international investment in which the investor obtains a lasting interest in an enterprise in another country. Most concretely, it may take the form of buying or constructing a factory in a foreign country or adding improvements to such a facility, in the form of property, plants, or equipment. FDI is calculated to include all kinds of capital contributions, such as the purchases of stocks, as well as the reinvestment of earnings by a wholly owned company incorporated abroad (subsidiary), and the lending of funds to a foreign subsidiary or branch. The reinvestment of earnings and transfer of assets between a parent company and its subsidiary often constitutes a significant part of FDI calculations.

ADVANTAGES OF FDI

- ✓ **ACCESS TO MARKETS:** FDI can be an effective way for you to enter into a foreign market. Some countries may extremely limit foreign company access to their domestic markets. Acquiring or starting a business in the market is a means for you to gain access.

- ✓ **ACCESS TO RESOURCES:** FDI is also an effective way for you to acquire important natural resources, such as precious metals and fossil fuels. Oil companies, for example, often make tremendous FDIs to develop oil fields.

- **REDUCES COST OF PRODUCTION**: FDI is a means for you to reduce your cost of production if the labor market is cheaper and the regulations are less restrictive in the target foreign market. For example, it's a well-known fact that the shoe and clothing industries have been able to drastically reduce their costs of production by moving operations to developing countries.
- **FDI OFFERS A SOURCE OF EXTERNAL CAPITAL AND INCREASED REVENUE.** It can be a tremendous source of external capital for a developing country, which can lead to economic development. For example, if a large factory is constructed in a small developing country, the country will typically have to utilize at least some local labor, equipment, and materials to construct it. This will result in new jobs and foreign money being pumped into the economy. Once the factory is constructed, the factory will have to hire local employees and will probably utilize at least some local materials and services. This will create further jobs and maybe even some new businesses. These new jobs mean that locals have more money to spend, thereby creating even more jobs.

- **TAX REVENUE** is generated from the products and activities of the factory, taxes imposed on factory employee income and purchases, and taxes on the income and purchases now possible because of the added economic activity created by the factory. Developing governments can use this capital infusion and revenue from economic growth to create and improve its physical and economic infrastructure such as building roads, communication systems, educational institutions, and subsidizing the creation of new domestic industries.
- **DEVELOPMENT OF NEW INDUSTRIES.** Remember that an MNE doesn't necessarily own all of the foreign entity. Sometimes a local firm can develop a strategic alliance with a foreign investor to help develop a new industry in the developing country. The developing country gets to establish a new industry and market, and the MNE gets access to a new market through its partnership with the local firm.
- **LEARNING IS AN INDIRECT ADVANTAGE FOR FOREIGN COUNTRIES.** FDI exposes national and local governments, local businesses, and citizens to new business practices, management techniques, economic concepts, and technology that will help them develop local businesses and industries.

TYPES OF FOREIGN DIRECT INVESTMENT (FDI)

- **Inward FDI** is when foreign companies or individuals invest in India.
- **Outward FDI** is when Indian companies or individuals invest in foreign countries

FOREIGN INSTITUTIONAL INVESTMENT (FII)

FII is when foreign institutional investors invest in the shares of a Bangladeshi company, or in bonds offered by a Bangladeshi company. So, if a foreign investor buys shares in Grameen Phone, it is an FII. Only institutional investors like Investment companies, Insurance funds etc. are allowed to invest in Bangladeshi stock market directly. However, if foreign individuals want to invest in Bangladesh's markets, they have to get themselves registered as a sub-account of an FII. The FII will buy shares/ bonds from the Bangladesh markets on their behalf. Bangladesh allows only wealthy foreign individuals or high net worth individuals (HNIs) who have a minimum net worth of $50 million to be registered as a sub-account of a foreign institutional investor (FII). Foreign institutional investors are also known as **'hot money'** because it is not stable in nature. The FIIs can pull out money from a country's stock market/ bond market overnight.

QUALIFIED FOREIGN INVESTMENT (QFI)

As we know, foreign individuals cannot invest directly in Bangladesh's markets without sub-accounts with an FII. As an alternative, QFI was introduced. A Qualified Foreign Investor can invest in Bangladesh without sub-account.

- The Qualified foreign investor (QFI) can be an individual, group or an association.
- The QFI should be resident in a foreign country that is compliant with the standards of Financial Action Task Force (FATF).
- In addition, the QFI must be a signatory to International Organization of Securities Commission's Multilateral Memorandum of Understanding. (MMOU).