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## Foreign Direct Investment, Finance, and Economic Development

*Chapter for the Encyclopedia of International Economics and Global Trade, Forthcoming*

33 Pages

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### Abstract

Research has sought to understand how foreign direct investment affects host economies. This paper reviews the empirical literature, specifically addressing the question: How does FDI affect economic development of host countries and what is the role of local financial markets in mediating the potential benefits? We first define FDI and discuss general theories on types and drivers of FDI. This review takes a host-country perspective rather than a firm perspective and thus only highlights the key insights from the rich firm-level literature on MNCs. We then focus on how financial conditions in host countries affect the extent of FDI-related capital inflows, shape the operations of foreign firms, and mediate the extent of productivity spillovers from FDI to local firms. The survey focuses mainly on work related to developing countries.

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