

CHAPTER I

INTRODUCTION

A. Background of the Research

Since the early 19th century, Foreign Direct Investment became popular in various countries around the world. Foreign Direct Investment is usually aimed at developing countries where foreign capital is needed to build infrastructure, facilities and infrastructure, technology and various other things. One of the main objectives of foreign capital flows is Latin America. Interestingly, Latin America is dominated by socialist countries such as Cuba, Chile to Venezuela.

According to Krugman, Foreign Direct Investment is an international capital flow that companies from one country establishing and expanding their companies in other countries. It means that the capital flow does not only transfer the resources but also control the foreign firms abroad.¹ Then he agreed that Foreign Direct Investment gives access to foreign firms to explore domestic management control. It means that both foreign and domestic companies are greatly getting benefit from this investment. Foreign Direct Investment can also promote domestic market competition.

According to Todaro and Smith, FDI is an investment made by international private companies which the funds are used to carry out business activities such as bringing in machinery and buying raw materials for production.² To enter the Foreign Direct Investment in, countries should consider some aspects such as low production cost including transportation, large market, abundant resources, and also the lack of trade barriers and the

¹ Kurniawan, R., & Afrizal, A. (2017). *Pengaruh Foreign Direct Investment Terhadap Perekonomian Masyarakat Dumai Pasca Berlakunya Masyarakat Ekonomi ASEAN* (Doctoral dissertation, Riau University). Page 5.

² Iriani Trisna Rahayu & Ernawati, *Faktor-faktor yang Mempengaruhi Foreign Direct Investment (FDI) di Enam Koridor Ekonomi Indonesia: Market Seeking Atau Resource Seeking*, Jurnal Aplikasi Statistika & Komputasi Statistik, vol. 9, no. 1, 2017. Page 33

level of economic liberalization.³

The concept of Foreign Direct Investment is establishing firms in the recipient country, establishing firms that the home companies own a majority of the company stock, establishing firms in recipient countries that the firms are under the cost of the home firms, establishing a corporation in home country to specifically operate in other countries or putting assets in other countries by national companies from investors.⁴

Foreign Direct Investment has several advantages. First, capital flow reduces the risk of capital ownership by verifying through investment. Second, the global integration of capital markets provides a good way establishing corporate governance, accounting rules, and legality. Third, global capital mobility gives limitations to government's ability for creating wrong policies.⁵

Multinational companies are very interested in investing directly in Latin America. Natural resources and better economic growth every year make Latin America a major destination for foreign investors. This is also supported by the Latin American economy which is increasingly open and integrated with the world economy nowadays. In this region, there are several regional organizations have been formed such as UNASUR (Union of South American Nations), Mercosur (Southern Common Market).⁶ Today, the United States still dominates Foreign Direct Investment in Latin America.

The United States is the biggest investor in Venezuela. Foreign Direct Investment is declined due to the situation that Venezuela take action to avoid relations and intervention by the United States especially in the country. This situation harms America's economy so that the US punish

³ *Ibid* page 34

⁴ Owusu-Antwi, G., Antwi, J., & Poku, P. K. (2013). Foreign direct investment: a journey to economic growth in Ghana-empirical evidence. *International Business & Economics Research Journal (IBER)*, 12(5), 573-584. Page 575.

⁵ *Op.Cit, Pengaruh Foreign Direct Investment Terhadap Perekonomian Masyarakat Dumai Pasca Berlakunya Masyarakat Ekonomi ASEAN*. Page 5

⁶ Pusat Pengkajian dan Pengembangan Kebijakan Kawasan Amerika dan Eropa, 2017, *Peluang dan Tantangan Kerja Sama Perdagangan di Kawasan Amerika Latin*, Badan Pengkajian dan Pengembangan Kebijakan Kementerian Luar Negeri 2017.

Venezuela through economic embargo. The situation is getting hard as most of Latin America's countries against the United States and it forces them to be punished by America within economic embargo similar to Venezuela. This is the reason why the US is the actor that causes the Foreign Direct Investment in Venezuela declined.

Since 2015, Foreign Direct Investment in Latin America has decreased by 9.1% or US\$ 179.1 billion in 2015⁷, furthermore, Foreign Direct Investment in 2016 has decreased by 7.8% or US\$ 167.180.000.000⁸ and 3.6% or US\$ 161.911.000.000 in 2017.⁹

The following data below shows Foreign Direct Investment inflows in Latin America by 2005-2017:¹⁰

Table 1. Foreign Direct Investment Inflows In Latin America Countries 2005-2017

Latin America and the Caribbean: FDI inflows, by recipient country and subregion, 2005–2017
(Millions of dollars and percentages)

Country	2005-2009 ^a	2011	2012	2013	2014	2015	2016	2017	Absolute variation 2017–2016	Relative variation 2017–2016 (percentages)
South America	68 302	168 464	173 392	132 499	152 580	133 524	115 627	111 028	-4 599	-4.0
Argentina	6 204	10 840	15 324	9 822	5 065	11 759	3 260	11 517	8 257	253.3
Bolivia (Plurinational State of)	259	859	1 060	1 750	657	555	335	725	389	116.1
Brazil	32 331	101 158	86 607	69 686	97 180	74 718	78 248	70 685	-7 563	-9.7
Chile	12 170	24 150	30 293	20 825	23 736	21 051	12 374	6 419	-5 955	-48.1
Colombia	8 894	14 647	15 039	16 209	16 167	11 723	13 850	13 924	74	0.5
Ecuador	465	644	567	727	772	1 322	755	606	-149	-19.7
Paraguay	137	581	697	245	412	306	320	356	35	11.1
Peru	4 978	7 341	11 788	9 800	4 441	8 272	6 863	6 769	-93	-1.4
Uruguay	1 461	2 504	6 044	755	3 830	2 435	-379	27	406	107.1
Venezuela (Bolivarian Republic of) ^b	1 403	5 740	5 973	2 680	320	1 383		

Source: Economic Commission for Latin America and the Caribbean (ECLAC) 2018

⁷ Economic Commission for Latin America and The Caribbean (ECLAC), 2016, *Foreign Direct Investment In Latin America and the Caribbean: 2017*, United Nations, Santiago. Page 20.

⁸ Economic Commission for Latin America and The Caribbean (ECLAC), 2017, *Foreign Direct Investment In Latin America and the Caribbean: 2018*, United Nations, Santiago. Page 29.

⁹ *Ibid*, page 29

¹⁰ Economic Commission for Latin America and The Caribbean (ECLAC), 2018, *Foreign Direct Investment In Latin America and the Caribbean: 2018*, United Nations, Santiago. Page 30.

The table shows that Foreign Direct Investment in Latin America declines in most of the Latin American countries where absolute variation in 2017-2016 reaches US\$ -4.599.000 with -4.0 %. By the year 2016-2017, Foreign Direct Investment is only increasing in Argentina, Bolivia, Colombia, and Paraguay while most of the countries' Foreign Direct Investment are declined.

The above data shows the comparison between Foreign Direct Investment and Portfolio Investment in Latin America by the year 2010-2017. Portfolio Investment shows a good graphics by the risen investment in 2015-2017 while the Foreign Direct Investment shows the opposite.

The researcher chose the topic of Foreign Direct Investment in Venezuela because there were no research examines the decline in Foreign Direct Investment from the perspective of the Venezuelan economic crisis. Other studies are focused on the impact of the Venezuelan crisis in immigrants and human security issues. Some research also links the decline in Venezuela's Foreign Direct Investment as a result of the global economic recession. But if it is seen from the Venezuela crisis perspective, the situation is the main cause of the Foreign Direct Investment's decline in Venezuela itself.

The factor above is the reason for researchers to find answers to the problems of the Foreign Direct Investment decline in Venezuela on the period of 2015-2017. According to the above describes, this research focuses in analysing the phenomenon of Foreign Direct Investment's decline in Venezuela and how the situation goes and how it becomes harder since 2015-2017.

B. Research Question

A study must be based on the formulation of the problem. Based on the background that has been described above, the following problem formulation can be drawn: **“Why Venezuela's Foreign Direct Investment in 2015-2017 is declined?”**

C. Objective of the Research

The objective of the research entitled “**Foreign Direct Investment’s Decline in Venezuela 2015-2017**” are as follow:

1. To explain the effect of foreign firms nationalization policy of Venezuela in 2015-2017 that causes the Venezuela economic crisis.
2. To explain Foreign Direct Investment in Latin America that caused by Venezuela economy crisis.

D. Benefit of the Research

D.1 Academic Benefit

This research examines the issue of Global Political Economy related to Venezuela and its regional issues. So the researcher hopes this research can be a reference for developing International Relations study, especially in the Global Political Economy field.

D.2 Practical Benefit

This research gives readers an understanding that Venezuela has a very significant role in Latin America and the nationalization in Venezuela has a direct impact on Foreign Direct Investment in Latin America. So this research is expected to be an advise for the government of Indonesia to avoid the same problem in Venezuela and Latin America countries.

E. Literature Review

E.1 Review of Related Literature

Previous research is very helpful in the validity of the next research. In this research, the researcher takes previous references related to Foreign Direct Investment. The researcher compares five previous research as reference material for this research, they are:

The first research entitled “**Running Hot and Cold: Economic Liberalization and Foreign Direct Investment in Latin America**

by Sector” by R. Douglas Hecock and Eric M. Jepsen.¹¹ This study examines information about the effects of economic market-oriented reforms on Foreign Direct Investment flowing into Latin America in 1985-2006. The results of this research show that Foreign Direct Investment functions are more like a hot portfolio investment and it is almost impossible to have a positive effect associated with more permanent Foreign Direct Investment. Economic reform has a range of implications for economic, development, and industrial policy throughout Latin America and developing countries. This research uses the concept of Foreign Direct Investment. The difference is that previous research discusses what if economic market-oriented reforms are implemented in Latin America and how they affect Foreign Direct Investment in the region. While the author's research discusses the effect of the foreign firms nationalization policy on Foreign Direct Investment in Venezuela by the year 2015-2017.

The second research entitled **“Do Domestic Firm Benefits from Direct Foreign Investment? Evidence from Venezuela”** by Brian J. Aitken and Ann E. Harrison.¹² This research examines information about the benefits of Foreign Direct Investment to domestic companies in recipient countries focusing their research in Venezuela. The analysis was carried out using more than 4.000 factories in Venezuela from 1976-1989. The result of this research is that Foreign Direct Investment harms the productivity of domestic companies. The advantages of Foreign Direct Investment are internalized by the joint venture. It means that Foreign Direct Investment does not provide direct benefits for domestic companies in Venezuela except for companies that directly conduct joint ventures with foreign investors. This research uses Foreign Direct

¹¹ Hecock, R. D., & Jepsen, E. M. (2013). Running Hot and Cold: Economic Liberalization and Foreign Direct Investment in Latin America by Sector. *Latin America Policy*, 4(2), 238-250.

¹² Aitken, B. J., & Harrison, A. E. (1999). Do domestic firms benefit from direct foreign investment? Evidence from Venezuela. *American economic review*, 89(3), 605-618.

Investment theory by the joint venture method. The difference is in the focus of the research. Previous research focused on Foreign Direct Investment benefits on Venezuelan domestic companies. While the authors focusing on the condition of Foreign Direct Investment in Venezuela which was affected by the Venezuelan economic crisis after the nationalization policy implemented.

The third research entitled **“Chinese Foreign Direct Investment in Latin America and the Caribbean: Conditions and Challenges”** by Enrique Dussel Peters.¹³ This study examines how the relationship between China and Latin America, about influence of China on investment in Latin American region. The results of this research are the relations between China and Latin America have become stronger over the past few decades that China being a major trading partner for countries in Latin America in recent years. Chinese companies have also begun investing in Latin America. In other words, countries in the Latin America are very dependent on Chinese investment because it brings benefits to the countries involved. This research uses the Foreign Direct Investment theory. The difference is the focus of the research. Previous research focused on Chinese investment in the Latin American region which is influenced by regional relations or good relations with China. While the author examines the impact of the foreign firms nationalization on Foreign Direct Investment conditions in Venezuela focusing in current issue which is Venezuela economic crisis.

The fourth research entitled **“From Chavez to Maduro: Continuity and Change in Venezuelan Foreign Policy”** by Carlos A. Romero and Victor M. Mijares.¹⁴ This research examines the transition

¹³ Dussel Peters, E. (2019). *China's foreign direct investment in Latin America and the Caribbean: Conditions and challenges*. Universidad Nacional Autonoma de Mexico.. Facultad de Economia; Union de Universidades de America Latina y el Caribe; Centro de Estudios China-Mexico; Red Academica de America Latina y el Caribe sobre China.

¹⁴ Romero, C. A., & Mijares, V. M. (2016). From Chávez to Maduro: Continuity and change in Venezuelan foreign policy. *Contexto internacional*, 38(1), 165-201.

from Hugo Chavez's presidency to Nicolas Maduro. The effects of domestic politics, and Venezuela's foreign policy amendment. How does the Maduro government, during an unpredicted global scenario, deal with international commitments made by his predecessors during Venezuela's complex condition with a crisis and security instability. The result of this research is that during the unstable conditions, unstoppable political turmoil, widespread demonstrations, an economic crisis that has exacerbated Venezuela's situation, regional tensions and energy markets pose difficulties for expansive Venezuelan foreign policy. But on the other hand, the policy act as a stimulus for centralizing greater power internally and politicizing the foreign policy agenda. It is suitable for the goals pursued by the Nicolas Maduro regime. This study uses Foreign Policy theory and the concept of National Interest. The difference is that the previous research discusses the change of Venezuela foreign policy during the Nicolas Maduro regime after Hugo Chavez amidst political instability and the Venezuelan economic crisis. The focus of research lies in the change of foreign policy of the Nicolas Maduro regime. While the author's research focused on foreign firms nationalization policy by the year 2015-2017 which is in the Nicolas Maduro regime.

The fifth research entitled **“Working in Venezuela: How the Crisis Has Affected the Labor Conditions”** by Yohama Caraballo Arias, Jesus Madrid, and Marcial C.¹⁵ Barrios. This research identifies and analyzes the main social factors of the Venezuelan crisis that affect the conditions of workers or laborers and the workers' health. The results of this research show that workers in Venezuela from both the formal and informal sectors struggle to improve the quality of life. The low budget and inflation have reduced the productive power or reduced the purchasing power of the people. The violence that occurred also affected the lives of Venezuelan people. Shortly, the quality of life

¹⁵ Caraballo-Arias, Y., Madrid, J., & Barrios, M. C. (2018). Working in Venezuela: How the Crisis has Affected the Labor Conditions. *Annals of global health*, 84(3), 512.

and well-being of most Venezuelans has been worsened over the past five years. The economic crisis even worsening the lives and health of Venezuelan. This research uses the concept of Personal Security. The difference is the focus of the research. Previous research discusses the impact of the Venezuelan crisis on workers or laborers in Venezuela, which is more directed to the humanity issues. While the author's research is more directed to the economic impact.

E.2 Theoretical Framework

In this research, the author uses the concept of nationalization.

1. Concept of Nationalization

In early 19th century, the dominance of mercantilism or nationalization began to fade along caused by economic liberalism. The perspective of mercantilism and liberalization began to compete to influence state policy. The main character of 19th-century mercantilism is to explain the central role of nation-building and the intervention of countries to develop the economic growth of latecomers. The new era of mercantilism soon known as economic nationalization.¹⁶

According to Lenin, nationalization pointed out the uneven development in global capitalism where the central metropolitan community exploits the people in periphery state which later responded by the national struggle to realize independence from the circle of capitalism.¹⁷

Popular policies in the era of economic nationalization are:¹⁸

- a. Protectionism used to protect domestic producers who have not

¹⁶ Umar Suryadi Bakry, *Ekonomi Politik Internasional*, Pustaka Pelajar, Yogyakarta, Agustus 2015. Page 24

¹⁷ Scott Burchill & Andrew Linklater, *Theories of International Relations*, St. Martin's Press, New York, 1996. Page 174

¹⁸ *Op.cit*, Umar Suryadi Bakry, *Ekonomi Politik Internasional*, Pustaka Pelajar, Yogyakarta, Agustus 2015. Page 25

been able to compete with superior industries.

- b. Protect infant industries to have the ability to compete internationally with mature industries.
- c. Improve the quality of national education to develop the human capital of a country.
- d. The state plays a role to build basic infrastructure for industrial and trade development.

The concept of nationalization developed in many countries which have a similar condition as a latecomers. This condition inspired neo-mercantilists to bring up new development theories, one of them is the dependency theory. This theory is very popular among third world state.

Structuralist Dependency stated that the main factor causing the backwardness of Latin American countries is the exploitation process by foreign parties as a result of unfair economic relations with foreign parties. For structuralists, the free market economy of the world causes more backwardness and poverty than prosperity. The underdevelopment of poor countries and peripheries is caused by the accidental region that is connected with the capitalist and liberal world economic system so that the region becomes the periphery of capitalist countries. This is the reason why periphery states are very dependent on the core state.¹⁹

According to Gunder Frank, an alliance between central dominant class interest and the periphery hampers the economic development in periphery states. Merely, nationalization from the global capitalistic economy will provide independence industrialization for the peripheral state.²⁰

¹⁹ Ruslin, I. T. (2012). Relasi Ekonomi-Politik Dalam Perspektif Dependencia. *Jurnal Sulesana*, 7(2). Page 124.

²⁰ *Op.cit*, Scott Burchill & Andrew Linklater, *Theories of International Relations*, St. Martin's Press, New York, 1996. Page 175

This concept is used to explain the foreign firms' nationalization in Venezuela. According to the concept of nationalization, the latecomers country should strengthen the economy before going out to the global market. As a socialist country, Venezuela is known as an anti-imperialism and intervention of other states. Therefore, nationalization is the solution to release Venezuela from capitalism especially the United States. However, nationalization harms the United State and set Venezuela through an economic embargo. This nationalization policy is the main reason why the Foreign Direct Investment in Venezuela is declined.

2. Concept of Foreign Direct Investment

According to Todaro and Smith, FDI is an investment that made by international private companies, which the funds are used to carry out business activities such as bringing in machinery and buying raw materials for production.²¹ To bring the Foreign Direct Investment in, countries must pay more attention to aspects such as low production cost including transportation, large market, abundant resources, and also the lack of trade barriers and the level of economic liberalization.²²

Foreign Direct Investment can enter a foreign market in number of ways. *Greenfield investment* involves establishing a new plant with its own production abroad. *Brownfield investment* is while a firm purchases an existing firm or plant in a foreign market. The investment can also take form of a joint venture, which implies a partnership between the foreign firm and a firm from the host country.²³

Companies that can make foreign direct investment are companies that meet the following criteria, including:

²¹ *Op.cit*, *Faktor-faktor yang Mempengaruhi Foreign Direct Investment (FDI) di Enam Koridor Ekonomi Indonesia: Market Seeking Atau Resource Seeking*. Page 33

²² *Loc.cit*, *Faktor-faktor yang Mempengaruhi Foreign Direct Investment (FDI) di Enam Koridor Ekonomi Indonesia: Market Seeking Atau Resource Seeking*. Page 33

²³ Ylva Kalin, *FDI in Colombia: Policy and Economic Effects*. Page 4

1. The MNC is large and has a strong presence in the international market
2. These MNCs are often at the forefront of technology and marketing

Multinational companies also pay attention to several things to make foreign direct investment in a country to ensure their companies can run. Besides, the market that is the destination for foreign direct investment has a large market share. The last is the production cost advantages also affect foreign direct investment. Low production costs will further assist foreign companies in producing goods in investment destination countries, so a country with low production costs is very likely to become the main destination for foreign direct investment²⁴

The concept of Foreign Direct Investment is used to explain investment conditions in Venezuela. Based on the criteria for investment objectives, Venezuela doesn't give access to the US to invest in, because Venezuela aimed at take off the US control within its economy. Due to this situation, Foreign Direct Investment in Venezuela slowly begins to decline.

F. Hypotheses

Based on the background and formulation of the problems that have been described previously, the author can take the hypothesis that **Foreign Direct Investment in Venezuela is declined due to the factors below:**

1. The implementation of foreign firms nationalization policy in Venezuela

The nationalization harms the United States because America cannot invest in Venezuela. The United States punished Venezuela within economic embargo. This economic embargo affected the declining of Foreign Direct Investment in Venezuela.

²⁴ Umar Suryadi Bakry, *Ekonomi Politik Internasional: Suatu Pengantar*, Pustaka Pelajar, Yogyakarta, Agustus 2015, hlm. 197-198

2. The inflation experienced by Venezuela regarding to the US sanction named economic embargo

Being punished by the United States have worsened the financial of Venezuela. In this situation, Venezuela faced economic instability. Due to this situation, most of the MNCs think twice to invest in the country.

3. Separatism of the left countries against the US imperialism

President Hugo Chavez is very critical in against the imperialism and the liberalization. This situation has led Venezuela and its allies to fight against and separate from the US control. Finally, the Foreign Direct Investment's decline is not only affecting to Venezuela but also countries that support Venezuela.

G. Research Methodology

G.1 Method of the Research

This research uses a descriptive-analysis method. The purpose of the method is exposure and explanation. The research starts from describing, recording, analysing then describing an analysis of the impact of the nationalization policy on the decline in Foreign Direct Investment in Latin America.

G.2 Object of the Research

The research object is the main concern in the research itself. So the object of this research refers to the declining of Foreign Direct Investment in Latin America by the year 2015-2017.

G.3 Technique of Collecting Data

The data collection technique used in this research is a secondary data collection technique that is obtained through literature review from libraries, reading books, scientific journals, articles, print media or newspapers, and internet media.

G.4 Technique of Analyzing Data

In this research, the author obtained data and explained it with qualitative data analysis methods. The author uses descriptive qualitative techniques obtained from various sources and then processed them systematically. In the data analysis process, the author uses the analysis method according to Miles and Huberman. The data analysis in this research is data collection, data reduction, data presentation, and concluding.²⁵

- a. Data collection is obtained from observations and documentation.
- b. Data reduction including selection, focusing, abstracting, rough data transformation directly or indirectly.²⁶
- c. The presentation of data is obtained from the data selection process. The reduced data then presented to make it easier for researchers to conclude.
- d. Conclusions require the researcher to understand in detail the research conducted. So the conclusion is very dependent on the ability of the author in processing data.

H. Writing System

CHAPTER I INTRODUCTION

In this chapter, the author describes the background of research, question research, the purpose of research, benefits of research consists academic benefit and practical benefit, literature review consists of previous research and conceptual framework, hypotheses, research methods including research designs, research objects, data collection techniques, and data analysis techniques, then writing system.

²⁵ Kuncoro, F. (2012). *Alasan Berubahnya Kebijakan Luar Negeri Amerika Serikat Terhadap EAS (East Asia Summit) Pada Tahun 2010* (Doctoral dissertation, UNIVERSITAS AIRLANGGA). Page 19.

²⁶ *Ibid*, page 37

CHAPTER II THE DYNAMICS OF FEOREIGN DIRECT INVESTMENT IN VENEZUELA

This chapter will explain the Foreign Direct Investment situation in Venezuela in nineteenth until twentieth century and the countries that give effects to the declining of FDI

CHAPTER III ANALYSE FOREIGN DIRECT INVESTMENT'S DECLINE IN VENEZUELA 2015-2017

This chapter will analyse the main research, which will explain the decline of foreign direct investment in Venezuela and the impacts by the year 2015-2017.

CHAPTER IV CLOSING

This chapter contains conclusions from the previous chapters.

