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FINANCIAL SECTOR DEVELOPMENT AND FOREIGN DIRECT INVESTMENT: A SYNTHESIS OF A RELATIONSHIP

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ABSTRACT

Foreign Direct Investment (FDI) is considered as a business mechanism that brings technology and boost economic development. It is by this sense a crucial factor for those economies that want to improve their performance and strengthen their competitiveness position in the international markets. For that reason, countries present incentives rehabilitate the business environment in such a way to be suitable for doing business and gaining advantages. One of the basic environmental factors that influence the flows of foreign direct investment is the financial system of the hosts. This paper tries to analyze the relationship between the financial system and the foreign direct investment through a survey of different studies.

1. Introduction

The nexus finance and development had been for a long time a debatable issue. The core of the subject is to investigate the nature of this link between these two basic components. The focus also in based on examining the cyclicality of these two factors: is that the financial system which drives the economic or vice-versa and to what extent. Knowing this may pave the way for the conception of the appropriate policy to adopt in improving both factors. In this sense, it is widely recognized that the financial system per se can be an enhancing or an inhibiting factor to the economic development. This paper aims to explore the relationship between the performance of the financial system and the attraction power of the host country to the foreign investment. The issue is multidimensional by the sense that this kind of investment is not conducted only by foreign investments but other variables comprising the economic and the environmental arenas.

2. THE LINK EXTENT BETWEEN FINANCIAL SYSTEM AND FOREIGN DIRECT INVESTMENT

The genesis of the causal link between the financial development and foreign direct investment is found within the debatable issue of the impact of the financial development on economic growth. This line of thought is related to the seminal works of Asli (Asli & Ross , 2001) and (Thorston , Asli, & Ross , 2001) who presented a synthesis of the different indicators that figure out the threshold of the financial development. In this context, the financial development is determined by a package of indicators related especially to the size, scope and depth of the system. In addition to this, it embodies the different financial organs as the intermediaries as well as the financial market. The development sense of the financial sector could be worthy complemented by its capacity to channelize efficiently the necessary funds between savers and investors. This issue is enhanced by the ability of the system to reduce the harsh effects of the information asymmetry. (Nabamita & Sanjukta , 2011) had indicated that the relationship between the financial development and foreign direct investment is not perfectly linear as other imposing variables exert their evident impact on the link between the two variables. According to their study on 97 countries, they showed that the political risk matters most and the attraction of the foreign direct investment is based alongside the development of financial sector

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on how far the political scene is stable. Furthermore, other strands of literature examine the causality of the financial development and FDI via the impact of the former on the economic growth; and as a consequence, a high level of growth and prosperity may constitute an enhancing factor to boost the country attracting effect of FDI. This line of thought is presented by (Maxwell , 1980) who shed light on the link between the saving rate, economic growth and investment level. The study asserted that causal linkage is bi-directional between these variables as a rapid economic growth increases the saving rate which in turn contributes much in releasing the funds necessary to finance the investment projects. The positive picture of the relationship could be reversed as the investment depression leads inevitably to a fall in the economic growth and the same for the saving rate. Additionally, (Oluwatosin, Olusegun, Festus, & Abimbola, 2012) attempted to explore the relationship between the foreign direct investment and economic growth by integrating the role played by the financial sector. By this meaning, the purpose of the study is to demonstrate how far the financial development is beneficial for reaping the advantages and spillovers of FDI. In almost the countries selected by the study, the authors found an interesting impact of the financial development exists. The latter works as push factor to strengthen the capacity of the country in reaping the benefits of FDI. Moreover, (Rodolphe & Wei , 2017) had advocated that the impact of the financial development on the FDI attraction is twofold: direct effect and indirect one. It is meant by the former that the foreign firms' expansion needs a considerable facilitation in acquiring the necessary funds to finance the investment; and this target is made possible by upgrading and developing the financial sector. In this context, the study claimed that the financial development of both the home and the host countries contributes intensely in easing the access to external finance. At the other side, the indirect effect is impact of the restructuring and the development of the financial development on the economic growth which occupies a high position in depicting how far the economy is prosperous and as a consequence, how far it is capable to attract and absorb the benefits of FDI. Besides, (Brealey & Kapalnis, 1996) found in their study that the foreign banking location is strictly related to the extent to which the trade and the capital markets in the host country are developed. This means implicitly that liberalization measures deliver an insight of transparency and efficiency in dealing with the business affairs (snapshot of a favorable environment to do business). This line of thought is emphasized by (Lewis & Stein , 1997) who claimed that financial development and reformation exert a striking positive impact on the overall economy by increasing its efficiency to run its internal and external businesses. However, this fact is no longer possible without taking the institutional and the political development of the country into consideration (institutional and political development are jointly correlated with the financial one to achieve the wanted targets). This assertion is confirmed by their study on the financial liberalization in Nigeria in which they found that the absence of any attempt to reform the political area leads to an evident failure of the financial system reform. Another investigation had been conducted by (Abdullahi & Sandy , 2009) on 25 Sub-Saharan African countries in which they found that the financial openness has a remarkable impact in reducing both the output and the consumption growth. However, this impact is no longer efficient without a background comprising a good institutional quality and a considerable financial development. It is implicitly understood from the study that the liberalization measures and the financial development should go hand in hand to boost the economic growth, reduce the market frictions and diminish the macroeconomic volatility. Within the same framework of analysis, (Arturo , Fabio , & Andrew , 2007) put forward a research question about the extent to which the financial liberalization leads to strengthen the financial sector and allocate efficiently the funds towards more efficient investment projects. The study had been conducted on 25 developing countries in which they found that the financial liberalization and the adoption of the financial reform lead to a more efficient capacity to allocate investment funds. This claim is enhanced by the high levels of screening and supervisory power as well as a fair legal system. (Brou, 2006)undertakes a research focusing on the duration of the financial system under liberalization. The stability by this sense is determined throughout the study by the indicators of performing efficiently the intermediation activity as the good allocation of resources, monitoring and screening power as well as the risk management. A study had been undertaken by applying duration model on 68 countries. The researcher comes up with the result that the banking crises is not an odd phenomenon of the financial system but it needs a permanent vigilance in order to set up good regulatory and supervision policies. The core idea of the paper is that the positive impacts of the financial liberalization in strengthening the financial system and reducing the harsh effects of the crises are not negligible. This fact is possible only under a good financial structure (well-developed financial system) and an efficient prudential supervision. Alongside the researchers undertaken in this field, (Yoon , 1988) had conducted a study on Korean firms during the years 1970, 1980 and 1984. The focus of the research is to analyze the impact of the financial liberalization through the marginal return of capital and marginal cost of credit indicators. The study concluded that the gap of borrowing costs between favored and non-favored sectors had diminished greatly. This reduction was due to the financial liberalization which improves the efficiency of the credit allocation. Furthermore, a study realized by P. (Owen & Otton , 1989) revealed that the efficiency of both the formal and informal credit market has an evident impact on the portfolio allocation. The latter is conducted by the behavior of the deposit rate. The target of the research is to shed light on the role played by the financial liberalization in improving the role of the intermediation both in formal and informal credit market. The study presented a descriptive and analytical investigation of the impact of Unorganized

Money Market (UMM) in financing firms especially in LDCs. According to the new *stucturalists*, the curb markets as an example UMM contributes largely in funding the business activities than the formal financing sector (banking institutions). This fact implies that the increase of deposit rate (as a picture of the financial liberalization) affects the portfolio allocation and may decrease the growth and increase the inflation rate. This assumption is also true in the case when UMM works to finance unproductive assets. It is understood through the study that the role of the financial liberalization may decrease the efficiency gap in the two kinds of markets and the frictions in terms of deposit rates diminish consequently. (Maxwell , 1989) in his turn had advocated in his research conducted on 28 developing countries that there is a link between national saving, foreign debt accumulation and domestic investment responsiveness. The result showed that (Maxwell , 1989) the domestic saving is a crucial factor to finance the rising trend of investment and this outcome has in turn positive reflects on growth improvement and current account performance. (Dani, 2007) at the other side of analysis asserts that the benefits of the liberalization against its costs are measured in terms of sustainability. The latter is considered as the key condition to stimulate growth and meet the targets of the Structural Adjustment Programs. This claim puts forward the idea that the success of the liberalization in improving the quality of the institutions and boosting the economic growth is no longer demarcated from the way of how the process of the liberalization is applied. This idea is also emphasized by (Yoon , 1990) who points out in his study about the financial liberalization between MacKinnon and the *Neostructuralists* that the banking sector can allocate credits more efficiently to lumpy investments than informal markets. This claim is true in case when the interest rate ceilings are eliminated or are reflecting the market conditions. In this context, the divergence between M-S and *Neostructuralists* is not about the financial liberalization itself but on the approaches that underpin it. This assertion reflects evidently that the success or the failure of the financial liberalization depend heavily on the way of how the process is understood and implemented. The link between the financial liberalization and the financial development is also assessed by (Cargill, 1990). In his comparative study between the Korean and Japanese experience of the financial liberalization, he showed that Japan had crossed successful phases in liberalizing its financial sector and it can a model for the Korean economy. He also noted that Korea should take care to the stabilization of prices and the reduction of the government credit allocation as well as the package of non-performing loans. These conditions are of prime importance if the Korean economy wants to take advantage of the liberalization process. (Syahril, 1991) tackled the issue of the Indonesian financial reforms through the banking and the financial markets structures. He presented and analysis and a descriptive assessment of the financial reform phases that Indonesia had witnessed. The phases are indicated by the following years: 1966, 1967, 1970, 1983, 1988, 1989 and 1990. The study delineates the general directions of the financial reforms according to: the liberalization of both the deposit and lending interest rates, the reduction of the priority credits and the intervention of the central bank in setting the policies of the credit allocation, the opening of the financial market and authorizing new banks to enter the Indonesian financial market. The study showed that these reforms had resulted in increasing the bank competition and improving the work of the financial system in general in terms of flexibility, performance and credibility vis-à-vis the customers. The nexus financial liberalization-investment had been also a subject of focus by (Jeffrey , 1992) who adopted Computable General Equilibrium model for Turkey by using 59 variables. The study concluded that the success of the financial liberalization is much dependent on the elasticity of the saving-investment balances. Otherwise, the increase of the deposit interest rate will be followed by an increase in the lending rate, and as a result, the investment decreases. Additionally, in the absence of the saving-investment response of the financial liberalization process, the latter leads to higher inflation rate and higher interest rate. The cause behind this situation is the absence of the elasticity saving-investment leads to credit rationing through the interest rate mechanism. It is evidently shown by the study that the success of the financial liberalization is much dependent on a good response of the nexus saving-investment. In addition to this, (Alvin, 1992) had tackled the extent to which the liberalization regimes could be considered as a push factor to attract foreign direct investment. In his study, he concluded that the fundamental changes of screening functions are necessary if a country wants to implement effectively a policy of liberalizing foreign direct investment regimes. Such changes require the good stand up of the state in order to ensure that changes are not subverted by bureaucratic tendencies within the government. The article indicates that the prudential measures and the supervisory power are basic conditions for an advantageous and a beneficial liberalization regime. The latter had been also a subject of investigation dealt by (Hans & Sharma , 1992). In their study about the economic liberalization and transnational corporation in India, they concluded that the administrative procedures for seeking licensees in India have been lengthy and extensive throughout the liberalization period; and many great ministries and agencies are involved. This means implicitly that the liberalization regime should be conjointly implemented with a good infrastructure characterized by qualified institutions and a fair supervisory regime. The issue of the infrastructure and the interaction between the public sector and the private one has its specific influence on the investment magnitude realized in the economy. In this context, (Morisset , 1993) points out through a study applied on developing countries that there exists a crowding effect between the public sector and the private one in one hand and capital goods and monetary assets on the other when the financial liberalization is implemented. According to the study, he came up to a result that the positive effect of rise in domestic credit could be offset by a portfolio shift from capital goods into monetary assets. In addition to this, the financial liberalization could increase the demand of the public sector for the credit extended by the domestic banking system, therefore limiting the funds available to the private sector. From the above study, it should be noted that a rational synergy between the public and the private sector is a primary condition to preserve the advantages of the financial liberalization. (Diery & Yasim , 1993) had explored the relationship between the deposit rate and the investment under the financial liberalization regime. To serve the target, the study had been undertaken on two samples of the African countries: the first one includes 21 countries while the second one contains 09 countries. The researchers concluded that the effect of real deposit rate on the growth of the gross domestic product is dependent on the efficiency of capital. The cause behind this claim is that the economic growth is related also to other variables like the gross investment to GDP and the level of monetary supply to GDP. In addition to this, they found that the foreign saving has its evident impact on the investment level. The core idea of the analysis is that the effect of the real deposit rate on the monetary supply and the investment level is hampered by the level of the inflation. This fact makes any process to curb the inflation more than a necessity to reap the positive outcomes of the financial liberalization. This study underlines the importance of managing cautiously the macroeconomic indicators in an attempt to ensure the success of the financial liberalization regime. Besides, (Franklin & Douglas , 2007) tried to examine the factors that shape the efficiency of the financial system in both US and Germany. They found that the efficiency consideration of the financial system between these two countries is not only dependent on the regime adopted but also on households' dealings with the system and the firms' sizes. It is implicitly understood that the interaction of the individuals with the financial system as well as the different institutions especially the firms has its remarkable impact on the success or the failure of the financial regime adopted. At the other side of analysis, (Deepak, 1994) tackles the issue of how far the economic liberalization can stimulate investment and enhance growth. In his study, he compared between China and India in terms of economic growth and investment levels. The researcher concluded that the rate of growth in china is higher than in India. This is due to the big magnitude of investment in China. The study reveals that both China and India seek to replace the dirigisme policy by a market oriented one even if the latter remains insecure. The core idea of the research is the liberalization policy when it is fairly managed contributes much in increasing the level of investment both internal and external. This result is confirmed by the study of (Christopher , 1995) who attempted to explore the relationship between the financial liberalization and inflation. He found that the liberalization of foreign exchange and domestic asset markets caused a significant shift in the underlying private sector demand for money. This situation had a result of depriving government of *seignoriage* revenue and correspondingly increasing the inflationary consequences of the growth in the reserve money. According to this study, it is comprehended that the management of the liberalization through the prudential supervision and the respect of the liberalization sequences constitute is a fundamental condition to preserve the economy from unprecedented outcomes of the liberalization process. Another research dealt by (Sang & John , 1995) about the stock market volatility in Korea, Japan and the United States demonstrates clearly that the determination of the stock returns is influenced by the volatilities in the Emerging Markets. The striking evidence of the study is that these volatilities increased after the liberalization of the stock market. The research addresses an implicit indication that the management of the liberalization process according to the particularities of the economy and the targets stated is a worthy step towards the reaping of the liberalization benefits. These benefits are indicated by (Chong , Liu , & Yener , 1996) in their study about the Japanese financial institutions. The research tries to explore the relationship between the universal banking and the risks as well as the returns of the Japanese financial institutions. They concluded that the universal banking process of Japan enacted by the financial system reform of 1992 had positive consequences on the financial institutions. In this sense, the dismantling of the financial entry barriers led to increase competition but exposed the financial institutions to the market risk. In addition to this, the risk of the interest rate became lower as the financial institutions were more flexible. This flexibility and universality of the financial institutions had its positive impacts on the firms' returns. These results are contrasted with what had been found by (Ilene , 1996) who tackled the issue of the relationship between the financial liberalization, risk and portfolio investment. He came up with a result that the dependence on portfolio investment as a consequence of the financial liberalization can constrain the autonomy of the macroeconomic policy and lead to more risk exposure inside the economy. It is asserted from the research that the liberalization embodies negative crowding effects and high levels of risks. This situation could be prevented or at least lessened if the liberalization process is fairly and rationally managed. On the same trend of research, another study about the determinants of the foreign banking location is presented by (Brealey & Kapalnis , The Determinants of Foreign Banking Locations , 1996). They attempted to examine the relationship between the foreign banking branching, trade, foreign direct investment and the capital market activities of the host country. The researchers found that a strong relationship exists between these variables. This result is an evident statement that the liberalization measures enhance the capacity of the host country to attract and absorb the spillovers of the foreign direct investment. A study undertaken by (Erinc, 1997) about the correlation between the financial liberalization and the fiscal repression in Turkey revealed that the fiscal policy had its remarkable effects on the conduct of the financial liberalization. In this sense, the researcher concluded that the adoption of the fiscal policy to finance the public deficit through bond issuing or monetization has significant diverse effects on real output, employment, and the movement of the interest rate as well as the foreign exchange rate. This means implicitly that the public policy could be either a booster or a deleterious factor to the well-functioning of the financial liberalization. Additionally, (Suret & L'Her, 1997) had examined the linkage between the financial liberalization and the gradual opening of the stock market returns. The span of the study covers the period from 1976 to 1994 and combines 20 Emerging Markets. The researchers came up with a result that the financial liberalization and the political risk lead to the existence of hyper-return period. It had been also indicated that the liberalization process conducts positively the stock market and leads to a surge in foreign capital flows. The targets of the financial liberalization are preserved in a case when the process takes into consideration the particularities of the country in which the regime is applied. This assertion had been proclaimed by (Jonah , 1997) in his article about the interactions between globalization, liberalization and national capitalism. He advocated that the liberalization should to be *endogenized* which means to be driven by the national logics. This conceptualization reflects the necessity for the liberalization to the distinct national institutions and the political struggles. This analysis underscores the fact that the liberalization is not as one size fits all but each country has its own recipe according to the degree of development and the level of acceptance. By this meaning, the liberalization is a kind of transforming the divergence of the international economies into a system of convergence through the disemboweling of the national systems of capitalism. If the specific patterns of the countries are not taken into account, this will lead inevitably to high repercussions on the economy. This assertion had been advocated by (Grunberg, 1998) who concluded through his study that the liberalization policies have costly repercussions on public budgets and the social tissue both at national and international levels. The core idea of this conclusion is that the success of the financial liberalization in improving the institutions including the financial ones and enhancing the capacity to attract and absorb the foreign investments is conducted heavily by the extent to which the patterns of the economy are respected. In the same sense, (Linsink , Aljar , & Ilko , 2008) had examined in their study the extent to which the financial liberalization can impact the level of the capital flight in the African countries. They found that the financial liberalization induces a reduction in capital flight; and this reduction is conducted by all the external and the internal measures of the liberalization regime. Additionally, an analysis of the relationship between the financial services and foreign direct investment in Australia had been investigated by (Fariborz , 1998). According to the research he came up with the result that the financial liberalization the size of the Australia's banking system, the bank cost of capital, the real exchange rate and the investment in manufacturing are all major determinants of the foreign investment. What is remarkable is that the financial sector has its distinguished effect on the country attraction to FDI. This result is confirmed by (Ishaq, 1999) who attempted to explore the linkage between the capital movement, the financial flows and foreign direct investment in Ukraine. He concluded that a strong commitment to the economic reform even in the face of tough public opposition and outcry will be essential and will generate a more credible environment for attracting the foreign investment. This means clearly that the host country reforms are a good signal for the foreign investors to set up their businesses. (Nader , 1998) in his turn tried to examine the impact and the determinants of the foreign capital in the Brazilian economy. According to his research, he had revealed that the government policies towards foreign direct investment as well as the privatization ones are considered the major catalysts for foreign direct investment flows. These reforms include the upgrading of the financial sector to meet the requirements of the foreign investors. Besides, (Malcolm , 1998) seeks to clarify how the tissue of the banking sector under globalization affects the functioning of the banks and the financial system in general. The results of his research showed that the imperfect competitive banking sector and a fragile institutional tissue in developing countries hamper the establishment of a sound financial system able to reap the advantages of the globalization. This outcome puts forward the idea that the capacity to benefit from the positive outcome of the globalization depends deeply on the reforms undertaken in the host country. The idea of the host country reforms is also approved by a study presented by (Jackeline & Mohieldin, 1998). They examined the reality of the financial services in Arab countries and found that the Arab countries do not meet the prerequisites for a successful financial liberalization. As a consequence, a clear internal reform of the financial system before opening up the economy to the foreign competition becomes more than a necessity. In the same context, (Huang , Gou, & Wan , 2014) tried to explain the growth effect of the financial repression on the economic growth in a sample comprising 80 countries. This sample had been distinguished according to the income criterion into three blocks: low income countries, middle income countries and high income countries. They found that the financial repressive policies on bank entry, credit allocation, capital account and securities markets had obstructing effects on the economic growth and the capacity of the economy to benefit from the internal and external spillovers of the investment. (Allegret , Courbis , & Dulbecco , 2003) seek to decompose the effects of the financial liberalization into two distinguished effect: the direct effect and the indirect one. According to their analysis, they found that the financial liberalization has positive consequences on the long run growth even if the liberalization leads to occasional financial fragility and crises. The study presented by these researchers implies that liberalizing process has both positive and negative outcome but when it is managed cautiously according to targets assigned, the positive consequences outweigh the negative ones. In addition to this, (Dabo , 2012) seeks to clarify the impact of the liberalization process on the performance of the Nigerian banking system. The researcher adopted the profitability, the operating efficiency, the deposit and lending rate and the capital investments as indicators of the banking performance. The study came up with the result that the liberalization had positive impacts on the banking performance in Nigeria. This is undoubtedly a good signal for the performance of the economy and the foreign investors to engage in economic activities. Moreover, the examination of the liberalization effects on the economic growth under the corruption intensity had been tackled by (Keith & Gonzalo , 2010). The researchers seek to understand the extent to which the positive impacts of the liberalization regime can override the harmful consequences of the corruptive practices. The prominent result of the study showed that the financial liberalization is beneficial for the economic growth only under a good governance practices. This reflects the idea that the governance is a condition to ensure the success of the financial liberalization and take advantage of it. (Silk , Niel , & Robert , 2013) had embarked on a meta-analysis to highlight the relationship between the financial liberalization and economic growth. The study comprises 60 previous empirical studies that tend to explore the level of the impact between these two variables. The research conducted came up with the result that the positive impact of the financial liberalization on economic growth is weak and heterogeneous; and it concluded that the success of the liberalizing process to meets the growth targets is dependent also on other concomitant measures. These are represented by the level of the institutional quality, the economics of the financial markets and the ways of how the monetary and the fiscal policies are managed. Contrarily to what had been advocated by the triggering effects of the financial liberalization on banking crisis, (Helmi & Nabila , 2014) tried to explain this relationship on a sample comprising 58 developing countries. Through the adoption of *dejure* and *defacto* measures of the financial liberalization, they found that the financial liberalization had no considerable effect on the banking crises in the investigated sample. This outcome had been contrasted by the research presented by (Luca & Richard , 2015). They wanted to highlight whether the financial policy adopted increases or decreases the public-debt growth. By using a sample of 89 countries, they found that less strict financial policy contributes in increasing the magnitude of the public debt growth; and the adoption of the financial re-regulation cannot neutralize or reduce the growing trend of the public-debt. In addition to this, (Ang & Warwick, 2007) tried to explain the link between the financial liberalization and the financial development in Malaysia. They found that the financial liberalization stimulates the development of the financial sector. Furthermore, (Abdul , Nienke, & Kenichi, 2008) seek to examine the effect of the financial liberalization on the efficiency in capital allocation. The sample of the study is composed of 5 Emerging Markets and covers the period from 1980 to 1994. The research concluded that the financial liberalization contributes in increasing the efficiency of credit allocation. This means explicitly that the liberalization process leads to improve the quality of the investments funded. Moreover, Clausio E. Radatz (2006) examined the impact of financial development on the reduction of macroeconomic volatility. The study argued that the financial development leads to a stabilization of the output of existing firms and hence the volatility of macroeconomic indicators will be reduced. At the other side, (Péter, Andras, & Viktor, 2006) tackled the issue of the relationship between the saving policy and foreign direct investment in Hungary. The study revealed the importance of saving policy to make the necessary adjustments and to benefit from FDI spillovers. Furthermore, (George , Robert , & Mary, 2005) tried to investigate the interrelationship between foreign bank participation and foreign access to credit across firms in developing countries. The results suggested that all enterprises including small and medium sized ones have lower financing constraints in countries where the foreign bank participation is high. In the same context, (Neeltje, 2007) tried to analyze the foreign banking in developing countries. He found that the financial integration contributes largely in strong entry of foreign banks into developing countries and the majority of these banks are from high income level countries. Additionally, (William & Ramana , 2008) seek to analyze the linkage between banking deregulations, financing constraints and entrepreneurship. The study used micro-data for the period 1976-2001. The data are about entry and exit start-ups from Longitudinal Business Database (LBD) and the technique is Panel Data Analysis. The results of the study suggested that the entrepreneurship grew substantially after interstate banking deregulation. Besides, the reforms through the banking deregulation even they led to better efficiency and better investment choices, they contributed to the emergence of a large amount of churning which is much concentrated in small entrants. The study also revealed that the deregulation permitted the long term entry with large sizes of employment. In the same sense, (Joseph , Randball , Lixlin , & Bernard , 2008) investigated the impact of the institutions on foreign direct investment in China. The study showed that the weak institutions deter domestic investment while special initiatives attract FDI. In addition to this, (Silk , Niel , & Robert , 2013) analyzed the impact of the foreign ownership on bank efficiency. The results of the study revealed that the study showed that foreign ownership affects negatively the banking efficiency and in countries with good governance this effects is lessened. (Alessandra, 2008) in his turn examined the link between the financial integration, productivity and capital accumulation. The study argued that the financial integration has a positive direct effect on productivity, while it does not directly affect capital accumulation. Moreover, (Thomas , Manfrid , & Daniel , 2009) had focused on the linkage between financial deepening, trade openness, and economic development in Sub-Saharan Africa. The results of the study suggested that the financial deepening and trade openness have swayed economic development rather marginally. Besides, (Geert , Campbell , & Christan , 2010) tried to examine the impact of the financial openness on productivity. They found that the financial liberalization is associated with higher rate of economic growth and the financial openness plays a permanent effect on liberalization processes. At the other side, (Alessandra & Simona , 2010) described the relationship between investment, global engagement and financial constraints. The result showed that smaller, younger, and more risky firms; and firms who do not export and are not foreign owned exhibit higher sensitivities displayed by the former categories of firms. This suggests that it shields firms from financial constraints. In addition to this, (Geert , Campbell , & Christan , 2010) examined the relationship between financial openness and productivity. The study indicated that financial openness is associated with higher rates of economic growth through the development of both banking sector, stock markets and to changes in the quality of institutions. Furthermore, (Hiudan , 2011) tried to analyze the link between the foreign bank entry and the firm's access to credit in China. The study indicated that after foreign bank entry, profitable firms used more long term loans. Additionally, (Sajid & Sizhong , 2011) had focused on the linkage between the financial development, foreign direct investment and economic growth. The study revealed that financial development contributes in increasing the level of the domestic capital and foreign investment is affected also by the economy openness and the real exchange rate. In the same sense, (James , 2011) had undertaken a research about the financial development, financial reform and technological deepening. He found that while financial development facilitates the accumulation of new ideas, the implementation of financial reform policies is negatively associated with it. In addition to this, Kenneth S. Chan et al (2012) examined the link between financial reform and financial constraints in the Chinese firms. The study concluded that financial reforms in China lead to a raise in financing constraints especially for large firms while smaller firms display significant constraints..

3. CONCLUSION:

This paper attempts to present a synthesis of the empirical studies that focus on the issue of financial development and its relationship with the foreign investments. What is noted by the results of the studies is that the subject under examination is multi-dimensional as many variables are integrated to exercise an evident impact on the causal link between financial development and foreign investment. In addition to this, it is worthwhile to mention that the attraction of foreign investment does not depend exclusively on the development of the financial sector of the host country but on other factors including economic, political, security and even social criteria. On the other hand, the extent of the study that tackles the effect of financial liberalization on attracting foreign direct investment depends essentially on the analysis of the relationship between the variables that describe each process independently. This approach tries to divide the foreign direct investment and financial liberalization into sub-variables and strive to describe the existed relationship between them. Finally, it should be mentioned that the determination of the positive or the negative relationship is no longer easy because financial liberalization is only a part of a combination including many variables that conduct the investment philosophy in general.

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