

# National Economic Integration Also Matters: Foreign Direct Investment under Political Risk

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## Abstract

By a game-theoretic approach, this paper analyzes the transfer of the intangible assets such as knowledge through the foreign direct investment under the political risk. It is shown that, if a host government has insufficient commitment capability, it should possess sufficiently productive outside option so as to attract the foreign direct investment that opens the way for the advanced production activity for the developing country. To achieve the development goals successfully, not only an international economic integration but also national one should be considered. And, along with the productivity increase of the outside option, the investment level goes through non-monotonic change, so the relative success in attracting the foreign direct investment in volume does not necessarily lead to learning of sophisticated activity. Moreover, the policy reform that seems to ease the foreign direct investment does not always promote the transfer of the intangible assets. On the contrary, a certain reform can hinder such a transfer.

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