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Nama Penyelia
(Name of Supervisor) : Prof. Madya Dr. Ahmad Sobri Jaffar

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Tarikh
(Date) : 15 Februari 2001

UNIVERSITI UTARA MALAYSIA
ECONOMICS SCHOOL



**THE DETERMINANTS OF FOREIGN DIRECT
INVESTMENT FLOW TO MALAYSIA**

**A thesis submitted by
NAWIN A/L THARUMARAJAH**

**For the award of
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**GRADUATE SCHOOL
UNIVERSITI UTARA MALAYSIA**

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ABSTRAK

Ekonomi Malaysia telah berkembang pesat disebabkan oleh penjana pelaburan asing semenjak pertengahan 1970 an. Oleh yang demikian, kajian ini bertujuan mengenalpasti faktor-faktor yang mempengaruhi kemasukan modal asing dari tahun 1970 hingga 1998. Analisa regresi akan dijalankan bagi mengenalpasti enam faktor lokasi yang mempengaruhi pelaburan asing di Malaysia. Keputusan kajian mendapati di antara faktor-faktor yang signifikan adalah seperti Keluaran Dalam Negara Kasar (KDNK), pelaburan tempatan, kos buruh dan kadar faedah.

ABSTRACT

As the Malaysian economy continued to record rapid progress on the back of sustained economic growth, the contribution of Foreign Direct Investment to the Malaysian economy expanded at a faster pace since the mid 1970's. Thus, the major concern of this paper is to discuss and assess the determinants or influences that led to the expansion of inward capital inflows to Malaysia over the period of 1970-1998. In this paper, a regression analysis will be carried out to determine the importance of six major locational factors, which was expected to entice foreign firms to locate productions in Malaysia. The result show that factors like Gross Domestic Product, domestic investment, labour cost and interest rates were significant in influencing Foreign Direct Investment to Malaysia.

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1. Introduction

Malaysia is the second fastest growing economy in the South East Asian region with an average Gross National Product (GNP) growth of eight-plus percent per year in the last decade. Since independence in 1957, Malaysia has moved from an agriculturally based economy to a more diversified and export oriented one. This transition had been made possible among other things by a steady and increasing inflow of Foreign Direct Investment (FDI) to this country especially to cater for the saving-investment gap domestically. FDI inflow into Malaysia had increased tremendously in the last three decades from RM 6 billion in 1970 to RM 25.6 billion in 1997, representing almost a four fold increase in inward capital flows to this nation (UNCTAD, 1995:460).

1.1 Problem Statement.

The International Monetary Fund (IMF) defines FDI as “*an investment that is made to acquire a lasting interest in an enterprise operating in an economy other than that of the investor, the investor’s purpose being to have an effective voice in the management of the enterprise*” (IMF, 1997:4).

An important determinant of FDI inflows to a country is its locational factors. The location theory and Dunning’s ‘Eclectic Theory’ both emphasized that for a country to be attractive to foreign direct investment, the country should possess a number of location-specific advantages. A number of studies have examined FDI inflow to Lower Developing Countries (LDC's) by using the

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