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THE DETERMINANTS OF FOREIGN DIRECT INVESTMENT IN ASIAN COUNTRIES

NUR HIDAYAH BINTI SUKERY

MASTER OF SCIENCE FINANCE
UNIVERSITI UTARA MALAYSIA
2017
THE DETERMINANTS OF FOREIGN DIRECT INVESTMENT IN ASIAN COUNTRIES

By

NUR HIDAYAH BINTI SUKERY

Research Paper Submitted to
School of Economics, Finance and Banking,
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MASTER OF SCIENCE (FINANCE)

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(has presented his/her research paper of the following title)

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by the dissertation).

Nama Penyelidik  : Dr. Sharmilawati Sabki
(Name of Supervisor)

Tandatangan  : 
(Signature)

Tarihk  : 28 Disember 2017
(Date)
DECLARATION

I declare that thesis work described in this research paper is my own work (unless otherwise acknowledged in the text) and that there is no previous work which has been previously submitted for any academic Master’s program. All sources quoted have been acknowledged by reference.

Signature : _____________________
Name : Nur Hidayah Binti Sukery
Date : 28th December 2017
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ABSTRACT

FDI is an investment from the international organizations and individual investors in the host countries to acquire the control on the invested firms and return. In theory, FDI stimulates economic development and improve the well-being of societies. The objectives of this study are to determine the effect of economic growth, inflation, exchange rate, interest rate and financial development on FDI inflows in 26 Asian countries for the duration of 16 years (2000 to 2015). The dependent variable is the FDI net inflows meanwhile the independent variables are economic growth, inflation, exchange rate, interest rate and financial development. This study finds a positive link between financial development and FDI inflows in the 26 Asian countries. This implies that a sound financial development would allow easier accessibility to the international financial market and thereby attract more foreign investors in the domestic financial system, hence improves the FDI inflows in the host country. Moreover, inflation has found to accelerate the FDI inflows while higher economic growth dampens the level of international funds flowing into the host countries. In addition, this study discovers that exchange rate and interest rate are not significant in influencing the inflows of FDI. Thus, this study will assist the policy makers in improving and monitoring the current regulations on the FDI inflows.

Keywords: FDI Inflows, Economic Growth, Inflation, Exchange Rate, Interest Rate, Financial Development.
ABSTRAK


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In the Name of Allah, the Most Forgiving and the Most Merciful

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May Allah bless and may Allah ease everything for you all.
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1.5 Research Objectives
1.6 Significance of the Study
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<tr>
<th>Abbreviation</th>
<th>Meaning</th>
</tr>
</thead>
<tbody>
<tr>
<td>FDI</td>
<td>Foreign Direct Investment</td>
</tr>
<tr>
<td>GDP</td>
<td>Gross Domestic Product</td>
</tr>
<tr>
<td>CPI</td>
<td>Consumer Price Index</td>
</tr>
<tr>
<td>INF</td>
<td>Inflation</td>
</tr>
<tr>
<td>OER</td>
<td>Official Exchange Rate</td>
</tr>
<tr>
<td>INT</td>
<td>Interest Rate</td>
</tr>
<tr>
<td>FD</td>
<td>Financial Development</td>
</tr>
<tr>
<td>USD</td>
<td>United States Dollar</td>
</tr>
</tbody>
</table>
CHAPTER ONE
INTRODUCTION

1.1 BACKGROUND OF THE STUDY

Foreign direct investment (FDI) is defined as an objective of creating a lasting interest by a direct investor in an enterprise and economy which is other than investor’s country. The lasting interest here indicates that a long term relationship exists between direct investors and the enterprise with the significant degree of influence on the enterprise’s management (OECD, 2008). FDI is considered to be an important economic factor because it stimulates economic development and improve the well-being of societies (Ali & Hussain, 2017; Pandya & Sisombat, 2017; Zekarias, 2016). Moreover, with a proper policy framework, FDI can offer financial stability to the participated countries because it is considered to be an important driver of the international economic integration (OECD Report, 2008).

Main components of FDI are debt instruments and equity. Debt instruments include bonds, non-participating preference shares, promissory notes, debentures and commercial paper. In addition, the instruments also comprise of other tradable non-equity securities, trade credit, accounts payable, account receivable, deposits and loans. Meanwhile, equity includes preferred shares, common shares, reinvestment of earnings, reserves and capital contributions.
The contents of the thesis is for internal user only
REFERENCES


Abolghasemi, S. M. S. (2014). Determinants of foreign direct investment in Germany (Doctoral dissertation, Eastern Mediterranean University (EMU)-Doğu Akdeniz Üniversitesi (DAÜ)).


Ponomareva, N. (2000). Are there positive or negative spillovers from foreign-owned to domestic firms.


APPENDIX A

. tsset code year  
  panel variable:  code, 1 to 26  
  time variable:  year, 2000 to 2015  

. regress  fdi x1lngdp x2inf x3lnexch x4int x5fd  

<table>
<thead>
<tr>
<th>Source</th>
<th>SS</th>
<th>df</th>
<th>MS</th>
<th>Number of obs</th>
<th>F( 5, 402)</th>
<th>Prob &gt; F</th>
<th>Adj R-squared</th>
</tr>
</thead>
<tbody>
<tr>
<td>Model</td>
<td>7833.5971</td>
<td>5</td>
<td>1566.71942</td>
<td>408</td>
<td>38.33</td>
<td>0.0000</td>
<td>0.3228</td>
</tr>
<tr>
<td>Residual</td>
<td>16432.9127</td>
<td>402</td>
<td>40.8778922</td>
<td></td>
<td></td>
<td></td>
<td>0.3228</td>
</tr>
<tr>
<td>Total</td>
<td>24266.5098</td>
<td>407</td>
<td>59.6228742</td>
<td></td>
<td></td>
<td></td>
<td>0.3228</td>
</tr>
</tbody>
</table>

| Fdi | Coef. | Std. Err. | t | P>|t| | [95% Conf. Interval] |
|-----|-------|-----------|---|-----|-------------------|
| x1lngdp | -1.456677 | .2251071 | -6.47 | 0.000 | -1.899211 | -1.014143 |
| x2inf | .2143021 | .0778971 | 2.75 | 0.006 | .0611655 | .3674388 |
| x3lnexch | -1.1234209 | .1295968 | -0.95 | 0.341 | -.3781929 | .1313511 |
| x4int | .1405599 | .0773918 | 1.82 | 0.070 | -.0115833 | .2927031 |
| x5fd | .1376796 | .0102809 | 13.39 | 0.000 | .1174684 | .1578907 |
| _cons | 30.74979 | 5.717277 | 5.38 | 0.000 | 19.51029 | 41.98928 |

. vif  

<table>
<thead>
<tr>
<th>Variable</th>
<th>VIF</th>
<th>1/VIF</th>
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</thead>
<tbody>
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<td>x4int</td>
<td>3.04</td>
<td>0.328663</td>
</tr>
<tr>
<td>x1lngdp</td>
<td>2.39</td>
<td>0.418200</td>
</tr>
<tr>
<td>x5fd</td>
<td>1.98</td>
<td>0.506005</td>
</tr>
<tr>
<td>x3lnexch</td>
<td>1.47</td>
<td>0.678888</td>
</tr>
<tr>
<td>x2inf</td>
<td>1.45</td>
<td>0.691354</td>
</tr>
</tbody>
</table>

Mean VIF | 2.07  

. xtreg  fdi x1lngdp x2inf x3lnexch x4int x5fd, fe  

Fixed-effects (within) regression  
Number of obs | 408  
Number of groups | 26  

R-sq:  within = 0.0881  
between = 0.0336  
overall = 0.0401  
Obs per group:  min = 14  
avg = 15.7  
max = 16  
F(5,377) = 7.29  
Prob > F = 0.0000  

corr(u_i, Xb) = -0.3035  

| fdi | Coef. | Std. Err. | t | P>|t| | [95% Conf. Interval] |
|-----|-------|-----------|---|-----|-------------------|
| x1lngdp | .359351 | .513003 | 0.70 | 0.484 | -.6493546 | 1.368057 |
|       | Coef.  | Robust Std. Err. | t     | P>|t|   | [95% Conf. Interval] |
|-------|--------|------------------|-------|-------|----------------------|
| x1lngdp | -1.456677 | .531753          | -2.74 | 0.011 | -2.551843 to -1.3615116 |
| x2inf  | .2143021  | .1182261         | 1.81  | 0.082 | -.029189 to .4577933  |
| x3lnexch | -1.234209 | .3012653         | -0.41 | 0.686 | -.7438884 to .4970465 |
| x4int  | .1405599  | .1404546         | 1.00  | 0.327 | -.1487118 to .4298316 |
| x5fd   | .1376796  | .0510741         | 2.70  | 0.012 | .0324905 to .2428686 |
| _cons  | 30.74979  | 12.05566         | 2.55  | 0.017 | 5.920688 to 55.57889  |

Modified Wald test for groupwise heteroskedasticity in fixed effect regression model:

H0: sigma(i)^2 = sigma^2 for all i

ch2 (26) = 1.3e+05
Prob>chi2 = 0.0000

Wooldridge test for autocorrelation in panel data:

F(1, 25) = 11.076
Prob > F = 0.0027
### APPENDIX B

**Descriptive Statics**

<table>
<thead>
<tr>
<th>Variable</th>
<th>Mean</th>
<th>Minimum</th>
<th>Maximum</th>
<th>Standard Deviation</th>
<th>N</th>
</tr>
</thead>
<tbody>
<tr>
<td>FDI (%)</td>
<td>5.03</td>
<td>-4.70</td>
<td>58.51</td>
<td>7.69</td>
<td>413</td>
</tr>
<tr>
<td>GDP (USD billion)</td>
<td>55,300</td>
<td>43.90</td>
<td>1,110,000</td>
<td>148,000</td>
<td>416</td>
</tr>
<tr>
<td>Inflation (%)</td>
<td>4.57</td>
<td>-18.11</td>
<td>38.60</td>
<td>4.87</td>
<td>413</td>
</tr>
<tr>
<td>Exchange Rate (LCU/USD)</td>
<td>1,190.27</td>
<td>0.27</td>
<td>21,697.57</td>
<td>3,815.55</td>
<td>416</td>
</tr>
<tr>
<td>Interest Rate (%)</td>
<td>10.86</td>
<td>1.14</td>
<td>51.90</td>
<td>7.15</td>
<td>413</td>
</tr>
<tr>
<td>Financial Development (%)</td>
<td>61.91</td>
<td>3.76</td>
<td>233.21</td>
<td>43.29</td>
<td>414</td>
</tr>
</tbody>
</table>

### APPENDIX C

**Correlation Analysis**

<table>
<thead>
<tr>
<th></th>
<th>Y=FDI</th>
<th>X1=GDP</th>
<th>X2=CPI</th>
<th>X3=OER</th>
<th>X4=INT</th>
<th>X5=FD</th>
</tr>
</thead>
<tbody>
<tr>
<td>FDI</td>
<td>1.0000</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>GDP</td>
<td>-0.0509</td>
<td>1.0000</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>CPI</td>
<td>0.0016</td>
<td>-0.2424</td>
<td>1.0000</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>OER</td>
<td>-0.1151</td>
<td>0.0949</td>
<td>0.3004</td>
<td>1.0000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>INT</td>
<td>-0.0514</td>
<td>-0.6245</td>
<td>0.5321</td>
<td>0.3731</td>
<td>1.0000</td>
<td></td>
</tr>
<tr>
<td>FD</td>
<td>0.3920</td>
<td>0.6192</td>
<td>-0.3736</td>
<td>-0.1527</td>
<td>-0.6374</td>
<td>1.0000</td>
</tr>
</tbody>
</table>