CHAPTER 5

SUMMARY OF THE STUDY

As there are believes that Foreign Direct investment (FDI) is very beneficial for a host country, especially in long run, governments are using FDI as a leading tool for economic development for the countries. Nations are competing each in attracting FDI. Among host nation, East Asia is a region that is very attractive for international investors, besides Triads.

Hence, this study is conducted to investigate the determinants of the bilateral inward Foreign Direct Investment inflows among East Asian nations. Moreover, the study aims to descriptively analyze those factors on how they generally affect FDI. Many characteristics of the nations are discussed as key determinants, compared to the others.

However, the scope of study is limited only in the East Asia region according to the data available from UNCTAD. The study focuses in 8 host sample nations, including China, Hong Kong, Indonesia, Korea, Malaysia, Philippines, Thailand, and Vietnam. In econometric procedure, 9 home nations are studied. The nine are China, Hong Kong, Indonesia, Japan, Korea, Malaysia, Philippines, Singapore, and Thailand. The time horizontal for the study is the year 1996. Meanwhile, dynamic behavior will be described as well by employing data in the eight countries during 1991-2000.

The study of inward FDI in the East Asian economies presents that i) the relative size of the economies, ii) the relative amount of labor, iii) the difference in cost of funding, iv) the difference of the growth of wholesale price, v) the export value of the host country, and vi) the export competitiveness of the host country are determining factors for East Asian inward foreign direct investment. And among the factors, the relative size of the economies and the relative amount of labors are the most significant determinants.

The relative size of the host economy over the home economy is reported as a negative determinant of the value of inward FDI to a host country. This implies that the bigger size of the home economy, compared to the host, is a factor that encourages higher FDI flows from the investing country to the host country. Meanwhile, the study reports that the relative amount of population of the two countries also determines the value of inward investment. By this, the comparatively higher amount of labor of a host country, compared to the home, encourage investments as it implies lower cost of labor. As a result, traditional hypotheses of FDI determinants are still valid. In a linkage, Dunning's Eclectic Model concerning proprietary advantage and location advantage is then reaffirmed. Nevertheless, the gravity model is not supported as the distance between the investing country and the recipient is not reported as a determining factor

However, it is remarkable that the model reports only 25.81% goodness of fit. As a result, further study should be required, for the better understanding on the explanatory factors of the flows. This leads to a further study in dynamic behavior of inward FDI in the region in Chapter 4.

The study of correlation coefficients for the longer period of time, in Chapter 4 support the significance of either market size hypothesis, cost hypothesis, or export competitiveness hypothesis.

The first hypothesis, which is market size hypothesis, is supported by the positive relationship between the proxies and the value of inward FDI in several East Asian countries. However, the proxy is not valid in the case of Hong Kong, Malaysia, and Thailand. Meanwhile, the study cannot reaffirm the positive correlation between market-size and inward FDI in Vietnam, where the data is limited.

The second hypothesis, cost hypothesis, is weakly supported as the cost of lending is reported as a positive indicator of inward FDI only in the case of Korea and Malaysia. Meanwhile, the lending interest rate in the Philippines is reported as a negative indicator of inward FDI. In terms of inflation, the study reports a negative relationship between the proxy and the inward FDI in the case of Hong Kong, Korea, and Thailand. However, by studying the correlation between the growth of inward FDI and the cost, either interest rate or WPI, the study reports either weak or negative correlation between the factors. This relation underlines the fact that a price-stability is required to encourage inward FDI.

The export hypothesis is accepted as having a positive relation to the inward FDI in most of nations, except Malaysia and Thailand. Meanwhile, it is even more strongly supported in Hong Kong, Indonesia, and Korea when growth variables are employed. Besides the exports, currency depreciation is reported with a positive relationship to the value of inward FDI in China, Indonesia, Korea, Thailand, and Vietnam.

In addition, the study reports that each country has its own characteristics that influent inward FDI to the countries differently. In some countries, the country's market size may report a relatively high correlation with the country's inward FDI performance, compared to other factors. However, for some countries, the market size hypothesis reports a weak relationship, compared to cost hypothesis, or export hypothesis.

Beside the hypothesis that are tested and reaffirmed, the study reports that there are other factors that influents the value of inward FDI. For example, In China, its accession to WTO is a major factor that encourages a higher investment in the country. Meanwhile, in Hong Kong, its capability in providing investors with market confidence and price stability, as well as sound financial and capital markets and telecommunication network, are the outstanding factors that influent inward FDI. In contrast, economic instability, civil unrest, and corruption practices in Indonesia and the Philippines discourage inward FDI to the country. In Korea, the skilled labor of the country, the export promotion policies, and FDI deregulation of the government help encouraging more FDI to the country. In Malaysia, the shortage of skilled labor, the increasing cost of labor, and the restrictions on international activities are the major obstacles that kept the FDI value of the country remain low, compared to the others. In Thailand, it is reported that better financial system and reforms are needed. Lastly, in the case of Vietnam, the fresh natural resources, the newly opened economy, and the country's specific economic relations with China and the United States are the major factors that encourage a large amount of FDI to flow into the country during the period. However, restrictions, regulations, and bureaucratic red tape are still the major obstacle on the country's inward FDI.

Policy Recommendation

As present in the model and in the correlation analysis, the size of the host country, the size of the home country, the low and stable production cost, and the country performance on export promotion determine inward FDI. The study would rather refer to the study in Chapter 3 and 4 for suggesting on how to attract more inward FDI.

1. Investor Targeting

Since, the study reports that the market size of the home country, measured by Per Capita Income rather than GDP, is a strong indicator of inward FDI as a push factor, then government agencies should be more proactive on attracting investors from high purchasing power economy. The agency should apply investor-targeting strategy to target the potential investors. The regulations may be eased and incentives might be applied in order to make the country more competitive.

2. Production Development

In the view of pull factors, which refer to location advantage that makes the country become attractive to international investors and pull in the investment, the government should ensure market confidence, provide worthy cost of labor, strengthen relative cost of production efficiency, enhancing national productivity, promote export competitiveness, and develop other factor that support investment climate. This is to provide invester with better environment for investment and make it more advantage to invest in the country, compared to other destinations.

2.1 Market Size Development

The analysis has shown that the market size of the host country, measure by GDP, and PCI, helps attracting FDI. Meanwhile, the growth of the market also has positive impact in attracting FDI. The government should assist the business sector enhancing the growth of the market. The expansion of the economy shall ensure the confidence of investor on market potential and purchasing power, by control the growth of population and increase national income year by year.

2.2 Labor Market Development

Labor market must also be developed to remain its competitiveness against the neighbors. Skilled and productive labor should be created via education support and R&D development. Technical knowledge should be promoted in order to attract specific industries. Information technology and communication skills, in other languages, should be realized as important factors for providing multinational enterprises competitive labor force. Moreover, the government should promote the establishment of labor unions as a tool for Thai labors to bargain with their employees. However, the government must ensure that the actions of the unions will be full of reasons and not over-acting that would harm the economy as a whole. Besides, laws and regulation should be reviewed and enforced to fulfill the needs of entrepreneurs.

Moreover, from the study, it is reported that the low interest rate should be remained. Meanwhile, the inflation must be controlled stable in order to encourage higher inward FDI to the country.

3. Export Development

Export tariff should be reviewed and reduced to lower the cost of exporting. Trade agreements and good relationship with trade partners must be taken with best care. Bilateral agreements and multinational agreements should be considered promptly and carefully. Meanwhile, the country should stimulate the establishment and development of ASEAN Free Trade Area, AFTA in order to encourage value of trade between the members. Also, the free trade should decree the cost of materials imported, and lead to a lower production cost of the country as well.

Meanwhile, the stable and fundamental persistent exchange rate is also required. This is in order to provide international investors with lower exchange rate risk and support the country's growth in inward foreign direct investment.

4. Other Developments

Besides the investor targeting, market and production development, and export development, the government should also put a serious attention on bureaucratic reforms, corruption demolishing, law and regulations enforcement, and intellectual property protection. These are several key areas that affect the decision for investment and trade partnership during the decades.

Moreover, infrastructures must be developed promptly and properly to maintain the country competitiveness. The well-designed infrastructure settlement will help firms reduce costs and increase their competitiveness as well. The construction of Suwanbhum International airport, the development of surrounding facilities, the establishment of new business areas cannot be ignored, otherwise the country will not be able to promote the foreign direct investment efficiently.

For further studies

For the future studies, it is recommended to extend the study in various areas for a better understanding about inward FDI determinants in East Asia. Further studies may investigate the longer-run relationship in order to present another consistent explanation for inward FDI. Also, further studies in a specific industry across the region, or across various industries in a specific country, can be conducted if it is hypothesized that each industry, or in each country, may have different determinants.

In addition, several more hypotheses are also challenging to be tested; such as, effect of tariff rate, effect of degree of economic co-operation. Proxies for cost of labor and technological level can also be developed. And if possible, average tariff rate and fiscal incentives should be measured and added to the model.

Also, as it was found in this study that the relative cost of capital, proxy by the countries' interest rate positively determines the flow. The lower interest rate in the home nation, compared to that in the host, the higher direct investment will be introduced. Hence, it can be studied where international investors generally fund their investment; home country's capital, host country capital, or anywhere else. The study should then provide public more understandings about investors' behavior and impacts of interest rate and exchange rate on inward foreign direct investment of a country.