HELLENIC REPUBLIC

UNIVERSITY OF MACEDONIA

POLITICAL INSTABILITY, CORRUPTION AND FOREIGN DIRECT INVESTMENT: A COMPARATIVE ANALYSIS OF TRANSITIONAL AND LATIN AMERICAN COUNTRIES.

UNIVERSITY OF MACEDONIA
DEPARTMENT OF BALKAN, SLAVIC AND ORIENTAL STUDIES

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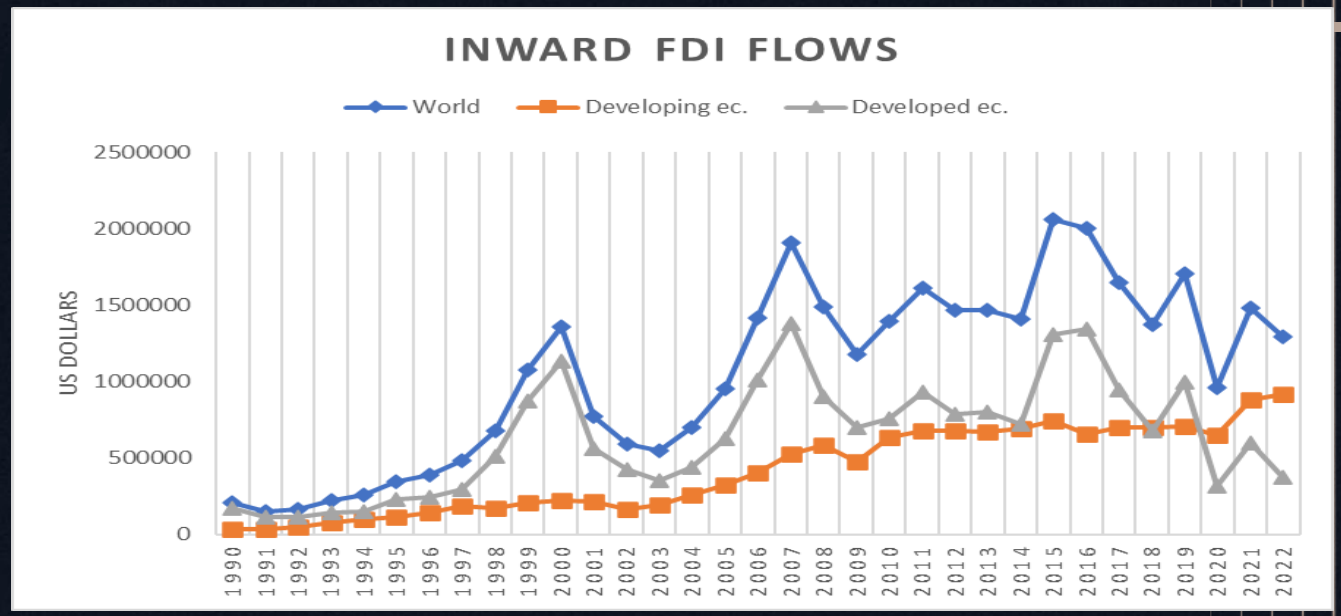
FDI TRENDS THROUGH DECADES

- Traditional view of FDI as an activity conducted between the developed world.

- Economic Rebalancing (Developed to Developing World FDI & Intra-Developing World FDI).



UNCTAD data

INSTITUTIONS & FDI

THE QUALITY OF INSTITUTIONS IS CONSIDERED AS A KEY DETERMINANT IN ATTRACTING FDI. (Busse, & Hefeker,, 2007).

THE INSTITUTIONAL ENVIRONMENT COULD BE ASSESSED THROUGH THE RULE OF LAW, POLITICAL STABILITY & CORRUPTION. (Bailey, 2018).

REVERSE CAUSALITY

(Selowski & Martin, 1997).

SIMILARITY OF INSTITUTIONAL QUALITY BETWEEN HOST & SOURCE COUNTRY. (Egger & Winner, 2006)

INSTITUTIONS & FDI PROBLEMATIC AND KEY QUESTIONS

1.

Does the level of corruption and political instability consist an important determinant of FDI?

2.

Could a specific correlation be concluded?

CORRUPTION AS A DETERMINANT OF FDI

"sand the wheels"

- Implying the slowdown of growth and FDI flows. In this case corruption is a phenomenon with clear negative effects that can be seen in the short and long term.

(BELGIBAYEVA & PLEKHANOV, 2015)

“grease the wheels”

- Approaches corruption not as an a priori positive situation for the economy, but as a “lesser evil”, implying that there is a positive side in corruption. Specifically, corruption can assist in chronic dysfunctions of the economy and improve the status-quo.FDI

(DREHER & GASSEBNER, 2013)

METHODOLOGY

KNOWLEDGE CAPITAL MODEL

Understanding FDI activity through **KK model.**

- Introduction of vertical and horizontal FDI which include efficiency and market seeking motives (Markusen, 2002).

Combined **vertical** and **horizontal** motives create an **equilibrium** in a market. Accordingly, MNEs as well as national firms coexist inside the economy in equilibrium. **Traits** of the **source** and **host** economy like market size, trade freedom and other factor endowments create a specific state of equilibrium (Markusen, 2002).

A deeper understanding of the exact nature of the FDI flows provides better results on **how** they are correlated with institutional factors.

FRAMEWORK

01

KK MODEL

A framework in which the sign of the variable coefficients can indicate horizontal or vertical FDI (Nguyen et al., 2019).

02

BILATERAL THEORETICAL FRAMEWORK

Panel of cross-country observations. Observations consist of a host and a source country.

03

SAMPLE

Source countries consist all countries that IMF provides data. Host countries consist selected countries from S.A. and CEE.

04

TIME & GROUPS

Data reflects the yeas 2009-2021. 3 groups of host countries.

NORTH AMERICA'S GROUP

- "Washington Consensus"
- High corruption
- Organized crime

COUNTRIES:

- Argentina
- Bolivia
- Brazil
- Chile
- Colombia
- Ecuador
- Paraguay
- Peru
- Uruguay
- Venezuela

TRANSITIONAL EUROPE'S GROUP

- "Washington Consensus"
- Endemic corruption
- Bordering EU

COUNTRIES:

- Estonia, Latvia, Lithuania, Czech Rep., Hungary, Poland, Slovak Rep., Slovenia, Belarus, Moldova, Russian Federation, Ukraine, Bulgaria, Croatia, Romania, Albania, Bosnia and Herzegovina, North Macedonia.

HYPOTHESIS

01

Political stability reflects a safe and stable environment for entrepreneurship thus is positively related to FDI (Cieślik & Gurshev, 2020).

02

Corruption delays the investment procedures enforcing risk and cost thus it is negatively related to FDI (Habib & Zurawicki, 2002).

03

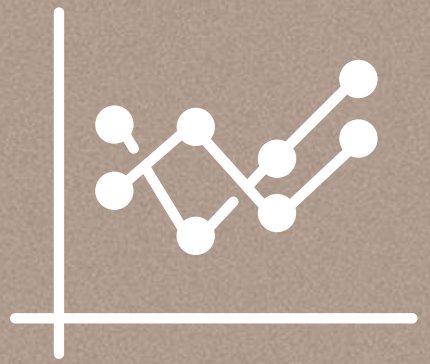
A variable, resulting from the difference between technological endowments from the source and the host squared, that would be statistically significant and positive would indicate vertical FDI (Cieślik & Gurshev, 2020).

DEFINITIONS AND SUMMARY STATISTICS OF DEPENDENT & EXPLANATORY VARIABLES

Variable	Definition	Source	Mean	Std. dev.	Min	Max
	Inward FDI positions (stock)	IMF - CDIS	263	2573	0	136361.2
$DIST_{hs}$	Bilateral distance	CEPII	7133.3	4817.1	59.6	19812
$SUMGDP_{hst}$	GDP HOST + SOURCE in millions (constant $)	UNCTAD	974263.6	2295805	8240.1	25200388
$DGDPPC_{hst}$	Difference between host and source GDP per capita (constant $)	UNCTAD	4311.7	20611.5	-28643	130400.2
$DFTRI_{hst}$	Difference in frontier technological readiness between host and source	UNCTAD	-45.6	364.6	-809	1676
$DSKILLS_{hst}$	Difference in skills development between host and source	UNCTAD	-67.5	330.7	-860	1120
PST_{ht}	Political Stability in host country	WGI	0.069	0.701	-2.021	1.12
COC_{hs}	Control of corruption in host country	WGI	-0.096	0.711	-1.622	1.586
$DGDPSQ_{hst}$	Squared difference between host and source GDP in millions (constant $)	UNCTAD	5403129267527	35741174176321	1.8496	547716634700906
$BITS_{hst}$	Dummy variable, bilateral investment treaty	Investment Policy Hub - UNCTAD	0.33	0.47	0	1
$IMPORTS_{hst}$	Host's imports (value from source)	UNCTAD	198442481.4	1472001072.7	0	84511036822

VARIABLES & CATEGORIZATION

- FDI motives = $f\{(Y_{st}^{pc}\text{-}Y_{ht}^{pc})^2, (Y_{st}\text{-}Y_{ht})^2, (Y_{st}+Y_{ht}), (ftri_{st}\text{-}ftri_{ht}), (skill_{st}\text{-}skill_{ht})\}$
- Bilateral trade costs = $f\{distance_{hs}\}$
- Institutional quality = $f\{stability_{ht}, corruption_{ht}\}$
- Investment barriers = $f\{imports_{hst}, treaty_{hst}\}$



BASIC EQUATION

$$FDI_{hst}^{stock} = e^{\left[\begin{array}{l}\beta_1 DIST_{hs} + \beta_2 SUMGDP_{hs} + \beta_3 DGDPPC_{hst} \\ + \beta_4 DFTRI_{hst} + \beta_5 DSKILLS_{hst} \\ + \beta_6 PST_{ht} + \beta_7 COC_{hs} + \beta_8 DGDPSQ_{hst} \\ + \beta_9 BITS_{hst} + \beta_{10} IMPORTS_{hst} \\ + \mu_{st}\end{array}\right]} \times \varepsilon_{hst}$$

RESULTS

PPML Source-Time Fixed Effects Model on Amount of Inward FDI accumulation – 2009–2021 – simultaneous regressions
*Robust standard errors in parentheses * p < 0.1; **p < 0.05; ***p < 0.01.*

Source-time FE	Aggregate model	Latin	Transitional
$DIST_{hs}$	-0.557*** (19.04)	-0.325*** (5.12)	-0.544*** (10.74)
IMP_{hst}	0.015*** (6.97)	0.021*** (3.92)	0.004* (1.65)
$DGDPSQ_{hst}$	0.088*** (8.13)	0.077*** (4.77)	0.068*** (5.82)
$DGDPPC_{hst}$	-0.020*** (5.32)	-0.015*** (2.73)	-0.017*** (3.98)
$DFTRI_{hst}$	-0.040*** (7.21)	-0.025*** (3.55)	-0.080*** (12.04)
$DSKILLS_{hst}$	-0.015*** (3.45)	-0.027*** (3.06)	-0.029*** (6.67)
$BITs_{hst}$	0.216*** (3.82)	-0.108 (1.41)	0.316*** (4.54)
PST_{ht}	-0.296*** (7.34)	-0.295*** (4.60)	-0.062 (1.36)
COC_{hs}	0.201*** (4.84)	0.239*** (4.58)	-0.119** (2.24)
N	20849	5184	11551
Rsq	0.495	0.642	0.53
$Host - time\ FE$	No	No	No
$Source - time\ FE$	Yes	Yes	Yes
Pseudo log-likelihood	-30545	-7929.6	-18191.5
VIF	1.68	1.61	1.76

COMMENTARY ON RESULTS

1

- The higher the resilience of the political institutions, the more hostile the environment
- Investors seem to take advantage of less stringent economic policies for foreign investment penetration.

2

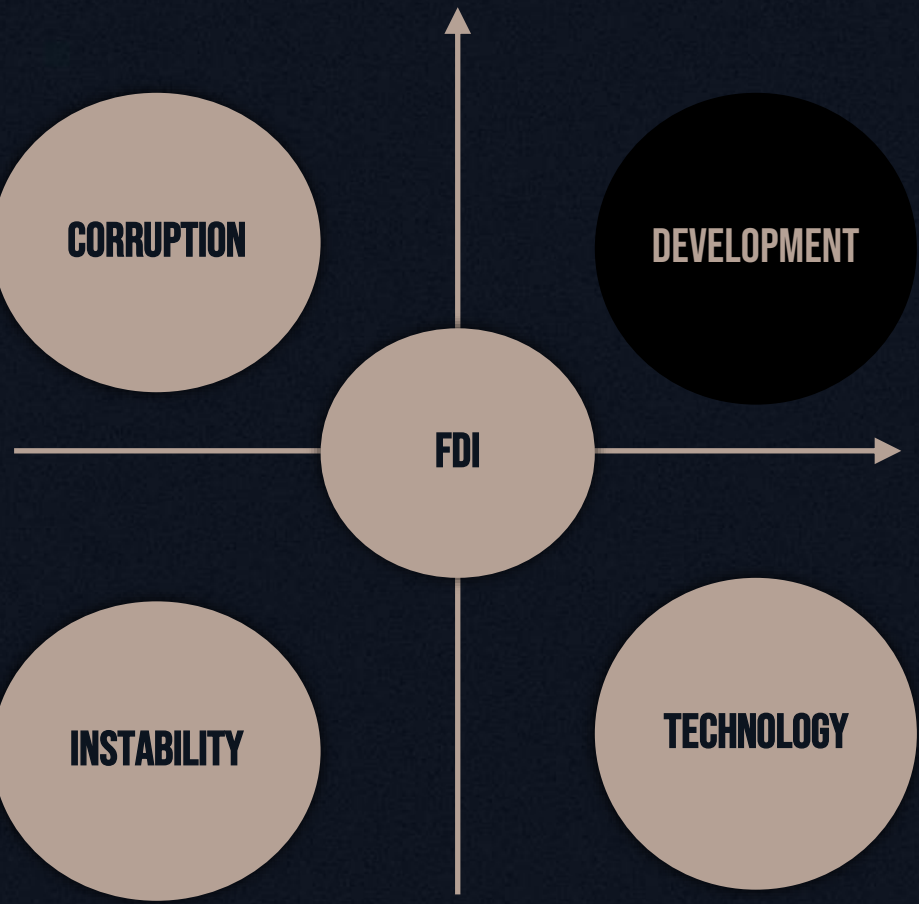
- Higher control of corruption scores tend to increase FDI
- More robust in the Latin American case, even the positive coefficients also prevail in the European case.

3

- The negative sign for the technological readiness coefficient reveals no evidence for vertical FDI.

CONCLUSIONS

- Increased importance of institutions in capital movements
- Increased activity between the South
- Risk of negative externalities from multinational activity



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THANKS !