

**FOREIGN DIRECT INVESTMENT, DOMESTIC INVESTMENT AND
ECONOMIC GROWTH: EVIDENCE FROM ASEAN-5**

By

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GSO9457

**Thesis Submitted to the School of Graduate Studies, Universiti Putra Malaysia, in
Fulfilment of the Requirement for the Degree of Doctor of Philosophy**

September 2004

THIS WORK IS DEDICATED TO
MY BELOVED FATHER AND MOTHER
MY DEAREST WIFE INDEA
MY CHILDREN JEHAD, MOHAMMED AND HAYEL

Abstract of thesis presented to the Senate of Universiti Putra Malaysia in fulfilment of the requirement for the degree of Doctor of Philosophy

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Chairman: Professor Ahmad Zubaidi Baharumshah, Ph.D.

Faculty: Economics and Management

This study is an empirical analysis of the impact of domestic investment and FDI on the economic growth of ASEAN-5 namely Indonesia, Malaysia, the Philippines, Thailand and Singapore during the last four decades. Also the study focuses on the FDI inflow into ASEAN-5, and the domestic investment accumulation process in the ASEAN-5.

This research was conducted following recent events such as the decline in the inflow of foreign capital and growth rates of domestic investment and thereafter the economic growth after the Asian financial crisis, and the search for new policy options that could contribute to sustained economic growth.

The growth and FDI models for this study are derived from the endogenous growth model, which can explain the behaviour of ASEAN-5 economies. The theoretical models are based on the previous works of Romer (1991), and developed by

Borensztein, *e. al.* (1998). The domestic investment equation is derived based on the flexible accelerator model, which is an extension of a model established by Fry (1998) and developed by Agrawal (2000a, 2000b).

This study utilized the autoregressive distributed lag approach to cointegration (ARDL) developed by Pesaran *et al.* (1996, 2001). This technique has additional advantages of yielding consistent estimates of the long-run coefficients. It is also free of residual correlation, and can distinguish between dependent and explanatory variables.

The major findings of this study can be summarized as follows: (i) domestic investment, FDI, and financial intermediation significantly affect the economic growth of ASEAN-5; (ii) FDI has positive and significant effect on domestic investment and *vice-versa.* ; (iii) the improvement in the development level of financial intermediation and human capital has a vital role on ASEAN-5's economic growth through FDI and domestic investment channels; (iv) the growth rate of GDP and domestic investment significantly affect FDI inflows to ASEAN-5; (v) outward-looking together with stable exchange rate policies contribute positively to both FDI and domestic investment and thereafter economic growth; (vi) the results reveal that ASEAN-5 can rely on domestic resources such as investment, saving, human capital, financial intermediation as instruments of economic growth, and FDI alone may not be able to sustain economic growth. Hence, economic growth based on domestic resources should be encouraged.

Abstrak tesis yang dikemukakan kepada Senat Universiti Putra Malaysia sebagai memenuhi keperluan untuk ijazah Doktor Falsafah

**PELABURAN LANGSUNG ASING, PELABURAN DOMESTIK DAN
PERTUMBUHAN EKONOMI: BUKTI DARIPADA NEGARA ASEAN-5**

Oleh

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Kajian ini merupakan analisis empirikal bagi kesan-kesan pelaburan domestik dan pelaburan langsung asing (FDI) ke atas pertumbuhan ekonomi ASEAN-5 iaitu Indonesia, Malaysia, Filipina, Thailand dan Singapura, sepanjang empat dekad terakhir ini. Kajian ini juga memberi tumpuan kepada aliran masuk pelaburan langsung asing ke ASEAN-5 dan proses peningkatan pelaburan domestik di dalam ASEAN-5.

Kajian ini dijalankan berikutan peristiwa-peristiwa semasa seperti penurunan di dalam aliran masuk modal asing dan kadar-kadar pertumbuhan pelaburan domestik dan seterusnya penurunan pertumbuhan ekonomi selepas krisis kewangan Asia, serta pengenalan pilihan-pilihan polisi baru yang mampu menyumbang ke arah mengekalkan pertumbuhan ekonomi.

Model-model pertumbuhan dan pelaburan langsung asing yang digunakan di dalam kajian ini diterbitkan daripada model pertumbuhan endogenus, yang mampu

menerangkan gelagat ekonomi ASEAN-5. Model-model teorikal adalah berasaskan kepada kerja-kerja terdahulu oleh Romer (1991) dan dibangunkan oleh Borensztein, *et al.* (1998). Persamaan pelaburan domestik diterbitkan berdasarkan model peningkat fleksibel, yang mana ianya merupakan lanjutan daripada sebuah model yang diasaskan oleh Fry (1998) dan dibangunkan oleh Agrawal (2000a, 2000b).

Kajian ini menggunakan kaedah kointegrasi autoregresi penyebaran tertunda (*the autoregressive distributed lag approach to cointegration*) yang dibangunkan oleh Pesaran *et al.* (1996, 2001). Teknik tersebut mempunyai beberapa kelebihan dalam menghasilkan penganggaran koefisien jangka panjang yang konsisten. Ia juga bebas daripada korelasi residual, dan boleh membezakan di antara pembolehubah dependan dan bebas.

Penemuan utama kajian ini diringkaskan seperti berikut: (i) pelaburan domestik, FDI dan perantaraan kewangan memberi kesan yang signifikan terhadap pertumbuhan ekonomi ASEAN-5; (ii) FDI mempunyai kesan yang positif dan signifikan ke atas pelaburan domestik dan sebaliknya; (iii) kemajuan di dalam tingkat pembangunan perantaraan kewangan dan sumber manusia mempunyai peranan yang penting ke atas pertumbuhan ekonomi ASEAN-5 melalui saluran pelaburan langsung asing dan saluran domestik. (iv) Kadar pertumbuhan KDNK dan pelaburan domestik mempunyai kesan yang signifikan ke atas aliran masuk pelaburan langsung asing ke ASEAN-5; (v) berorientasi pandangan luar (*outward-looking*) beserta polisi kadaran pertukaran yang stabil menyumbang secara positif ke arah kedua-dua pelaburan langsung asing dan pelaburan domestik dan seterusnya terhadap perkembangan ekonomi; (vi)

penemuan kajian mendedahkan bahawa ASEAN-5 boleh mengharapkan sumber domestik seperti pelaburan, tabungan, modal manusia, perantaraan kewangan sebagai instrumen pertumbuhan ekonomi, dan pelaburan langsung asing sahaja tidak mampu untuk mengekalkan pertumbuhan ekonomi. Oleh itu, pertumbuhan ekonomi berasaskan sumber-sumber domestik perlulah digalakkan.

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I certify that the Examination Committee met on 20, September 2004 to conduct the final examination of Suliman Warred Ma'youf Almasaied on his Ph.D. thesis entitle "Foreign Direct Investment, Domestic Investment and Economic Growth: Evidence from ASEAN-5" in accordance with Universiti Pertanian Malaysia (Higher Degree) Act 1980 and Universiti Pertanian Malaysia (Higher Degree) Regulation 1981. The Committee recommends that the candidate be awarded the relevant degree. Members of the Examination Committee are as Follows:

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DECLARATION

I hereby declare that the thesis is based on my original work except for quotations and citations, which have been duly acknowledged. I also declare that it has not been previously or concurrently submitted for any other degree at UPM or other institutions.

SULIMAN WARRED ALMASAIED

Date: 20, September 2004

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