



**UNIVERSITI PUTRA MALAYSIA**

**INTERPLAY BETWEEN FOREIGN DIRECT INVESTMENT,  
INSTITUTIONAL QUALITY AND ECONOMIC GROWTH**

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**INTERPLAY BETWEEN FOREIGN DIRECT INVESTMENT,  
INSTITUTIONAL QUALITY AND ECONOMIC GROWTH**

**By**

**TUN YIN LI**

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**October 2011**

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Foreign direct investment (FDI) is considered as one of the key ingredients in the development process for many countries. It is viewed as one of the important channels for the transfer of new knowledge across borders. Based on these potential positive spillovers, many countries have eased restrictions on the flows of foreign capital. As a result, FDI inflows increased significantly over the past few decades. However, increase in FDI is not uniform across countries as few countries are able to attract more FDI than the others. Another important issue related to FDI is that not all FDI recipients seem to benefit from FDI inflows. Evidence shows that the impact of multinational corporations (MNCs) presence on the growth of host economies is ambiguous. In some cases, FDI exerts positive impacts on growth but in some other cases there is no or even negative impacts. One of the key explanations for this ambiguity that appears in recent

literatures is the impact of FDI on growth depends on other intervening factors, broadly called “absorptive capacity”. Although evidence on the impact of FDI on economic growth is ambiguous, there is broad theoretical and empirical support for the positive contribution of institutional development in sustaining and promoting economic growth. This study takes a step further by exploring the role of institution in attracting FDI inflows as well as in mediating the positive growth-effects of FDI. It argues that good institutional quality not only able to attract more FDI inflows but also allow the host countries to benefit from MNCs presence through the absorption and internalization of new knowledge that they bring. To test these hypotheses, it uses a generalized method of moments panel estimator and data from 78 countries. Two important conclusions emerge. First, good institutional quality is found to be important pre-condition for host countries to attract more FDI inflows. Secondly, the impact of FDI on growth actually depends on the quality of institution in the host countries. Countries that promote good institutional quality benefit more from MNCs presence.

Abstrak tesis yang dikemukakan kepada Senat Universiti Putra Malaysia sebagai memenuhi keperluan untuk ijazah Master Sains.

**INTERAKSI ANTARA PELABURAN ASING LANGSUNG, KUALITI  
INSTITUSI DAN PERTUBUHAN EKONOMI**

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Pelaburan asing langsung (FDI) dianggap sebagai salah satu faktor utama dalam proses pembangunan bagi kebanyakan negara. Ianya juga dianggap sebagai salah satu saluran penting untuk pemindahan pengetahuan baru antara negara-negara. Dengan manfaat yang berpotensi, kebanyakan negara telah mengurangkan sekatan terhadap aliran modal asing. Akibatnya, aliran masuk FDI meningkat secara mendadak bagi tempoh beberapa dekad yang lepas. Namun, peningkatan FDI adalah tidak seragam antara negara kerana terdapat beberapa negara yang mampu menarik lebih banyak FDI berbanding dengan negara lain. Satu lagi isu penting yang berkaitan dengan FDI adalah bahawa bukan semua penerima FDI mendapat manfaat daripada aliran masuk FDI. Bukti-bukti menunjukkan bahawa kesan daripada kehadiran syarikat multinasional terhadap pertumbuhan ekonomi negara yang menerima FDI adalah kabur. Dalam sesetengah

keadaan, FDI memberikan kesan positif terhadap pertumbuhan ekonomi tetapi dalam keadaan yang lain, FDI langsung tidak memberi kesan atau memberi kesan yang negatif terhadap pertumbuhan ekonomi. Kajian baru-baru ini menjelaskan bahawa kesan FDI terhadap pertumbuhan ekonomi bergantung dengan “daya serapan”. Walaupun bukti-bukti tentang kesan FDI terhadap pertumbuhan ekonomi adalah kabur, terdapatnya sokongan teori and empirik terhadap kesan positif daripada pembangunan institusi dalam meningkatkan dan mengekalkan pertumbuhan ekonomi. Sehubungan dengan itu, kajian ini mengambil langkah lebih lanjut dengan mengkaji peranan institusi dalam menarik FDI serta menjadi pengantaraan bagi mewujudkan kesan positif daripada FDI. Dengan berpendapat bahawa institusi yang baik bukan sahaja mampu menarik lebih banyak aliran masuk FDI, tetapi juga membolehkan penerima FDI mendapat manfaat daripada kehadiran MNC melalui penyerapan dan internalisasi pengetahuan baru. Bagi menguji kedua-dua hipotesis ini, kaedah “generalized method of moments” digunakan dengan data daripada 78 negara. Terdapat dua kesimpulan penting yang diperolehi. Pertama, institusi yang baik menjadi pra-syarat penting bagi negara-negara untuk menarik lebih banyak FDI. Kedua, kesan FDI adalah bergantung kepada tahap kualiti institusi yang terdapat di negara penerima FDI. Negara-negara yang mempunyai kualiti institusi yang baik akan mendapat lebih banyak manfaat daripada kehadiran syarikat multinasional.

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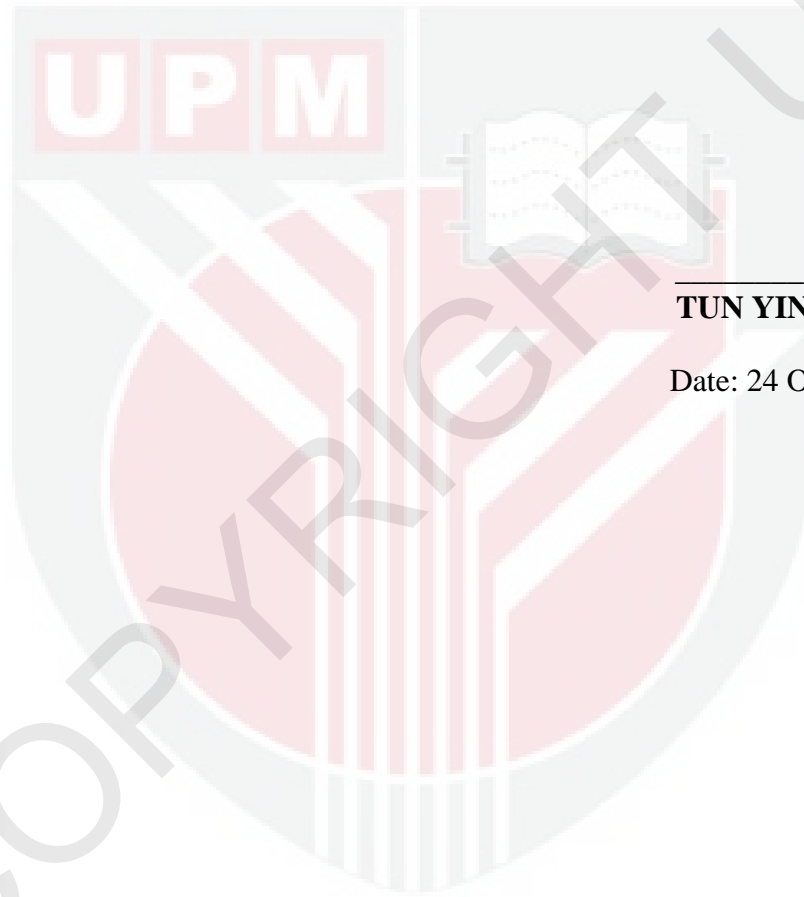
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## DECLARATION

I declare that the thesis is my original work except for quotations and citations which have been duly acknowledged. I also declare that it has not been previously, and is not concurrently, submitted for any other degree at Universiti Putra Malaysia or at any institution.



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