

Host Country-Specific Factors Causing Outwards Foreign Direct Investment from Malaysia

(Faktor Spesifik di Negara Tuan Rumah Yang Mendorong Pelaburan Langsung Asing dari Malaysia)

Gul Andaman
Zulkornain Yusop
Zaleha Mohd Noor
Shive Ranjane Kaliappan
Universiti Putra Malaysia

ABSTRACT

This study analyzes macroeconomic and institutional factors of the host countries in attracting outwards foreign direct investment (OFDI) from Malaysia. Results show that primary motives behind Malaysian OFDI are to seek growing markets and natural resources. Foreign economy's depreciating currency with respect to Ringgit Malaysia, lower private sector lending rate, shorter geographical distance from Malaysia and government accountability are also important pull factors. Malaysian OFDI is significantly low in ASEAN Member States (AMS) and in the developed states. Policy implications thus include generation of higher OFDI towards AMS given the strategic importance of ASEAN Economic Community and in developed regions to access foreign technology.

Keywords: Institutions; macroeconomic factors; Malaysian overseas investments; outwards foreign direct investment

ABSTRAK

Kajian ini menganalisa faktor ekonomi makro dan institusi bagi negara tuan rumah yang menyebabkan berlakunya pelaburan langsung asing keluar daripada Malaysia (PLAK). Keputusan kajian menunjukkan motif utama PLAK adalah untuk mencari pasaran baharu yang sedang berkembang serta kewujudan sumber asli. Kejatuhan nilai matawang bagi negara tuan rumah berbanding dengan ringgit, kadar pinjaman yang rendah di negara tuan rumah, jarak geografi, tahap akauntabiliti pihak kerajaan adalah faktor penarik yang penting. Setakat ini, PLAK daripada Malaysia adalah masih rendah di kalangan Negara ASEAN dan negara maju. Polisi yang dicadang ialah peningkatan PLAK oleh Malaysia di kalangan negara ASEAN dan juga negara maju yang lain bagi membolehkan Malaysia mempelajari teknologi yang terbaru.

Kata kunci: Institusi; faktor makroekonomi; pelaburan Malaysia di luar negara; pelaburan langsung asing keluar daripada Malaysia (PLAK).

INTRODUCTION

Since the beginning of this millennium, there has been a big leap in the OFDI emanating from developing countries (Das 2013). The increase in OFDI has been recorded from \$134.19 billion in 2000 to \$327.56 billion in 2010 and this figure continues to increase. Although the bulk of the outward FDI is still shared by the spectrum of developed nations, developing countries have nonetheless shown impressive numbers; and thus caught the interest of various researchers (Figure 1).

Malaysia's OFDI flows have been increasing and the economy is currently labeled as a net capital exporter (Figure 2) whereby inwards foreign direct investment (IFDI) is lower than OFDI. Being a rapidly developing economy, it has lost its low-cost advantage; and thus the IFDI has decreased over time (Diaconu 2014; Goh & Wong 2011). Other emerging economies such as China

and India have become more attractive destinations for foreign investors. Therefore, it has become imperative for Malaysia in the era of globalization to continue increasing its overseas and local investments so that the disadvantage of competition from lower-wage countries can be compensated. As a response, Malaysia's OFDI has been building up rapidly. However, despite the growing OFDI from Malaysia and its diversity in sectors and regions worldwide, there is a very limited literature and in fact no quantitative study has explored pull factors behind bilateral Malaysian OFDI. This study fills the vacuum in the literature by scrutinizing the host country-specific macroeconomic and institutional factors (i.e. the pull factors) responsible for attracting OFDI from Malaysia via gravity model. It also draws fresh perspective on the factors and policies that can further increase the OFDI; and thereby contribute to the growing literature on OFDI from Malaysia.



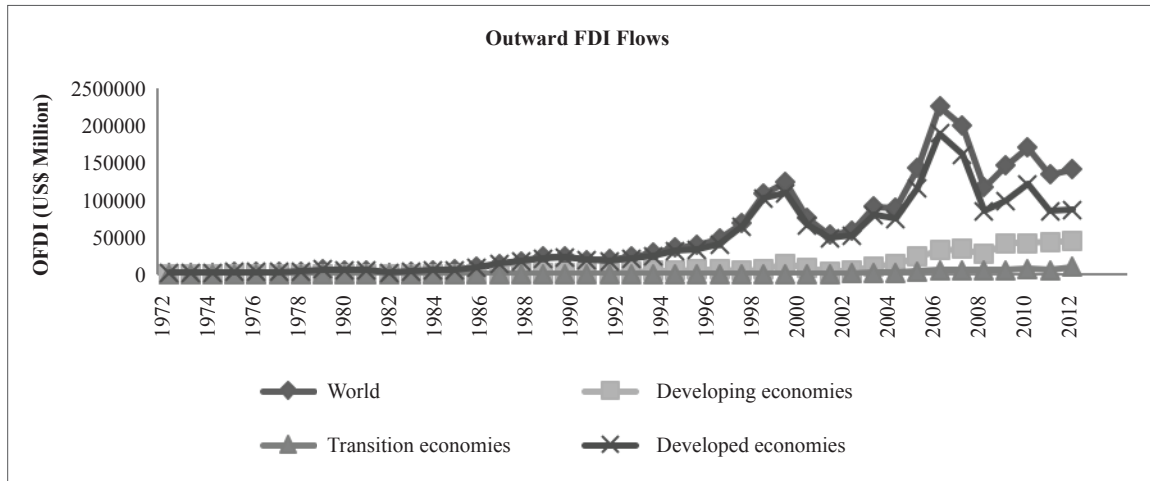


FIGURE 1. OFDI
Source: UNCTAD Database, 2015

Rest of the paper is organized as follows. Section 2 presents an overview of the Malaysian OFDI. Section 3 describes the literature review. Section 4 develops conceptual framework and hypothesis development, and followed by description of variables and methodology in Section 5. Section 6 presents the results and analysis and Section 7 concludes with policy implications and limitations of the study.

LITERATURE REVIEW

Theoretically stating, a firm invests abroad for various reasons as specified in Dunning’s eclectic paradigm or OLI Theory (Dunning 1993, 1995, 1998, 2001). The theory states that firstly, competitive or ownership advantages such as possession of tangible and intangible assets of the firm enable local investors to invest abroad. Secondly, location-specific advantages such as availability of cheap

factor inputs or better transportation, infrastructure, and human and natural resources in the foreign economy and thirdly, internalization advantages (owning production rather than selling or licensing) are the main reasons for firms to engage in OFDI. Dunning’s Investment Development Path (IDP) (Dunning 1981, 1986; Narula and Dunning 2010) is also one of the most cited models that identifies the determinants for OFDI. These include home country’s GNP, technological development and technology transfer from IFDI that make it possible for the domestic firms to invest abroad. Firms also invest abroad to access foreign markets, foreign technology or strategic assets, seek natural resources, and gain diversification. As put forward by Amal, Raboch and Tomio (2009), Stoian and Filipaios (2008), Stoian (2013), and De Beule and Duanmu (2012), macroeconomic factors embodied in OLI Theory and IDP are important but not sufficient determinants of OFDI. Institutional factors such as control of corruption, bureaucracy quality, political stability,

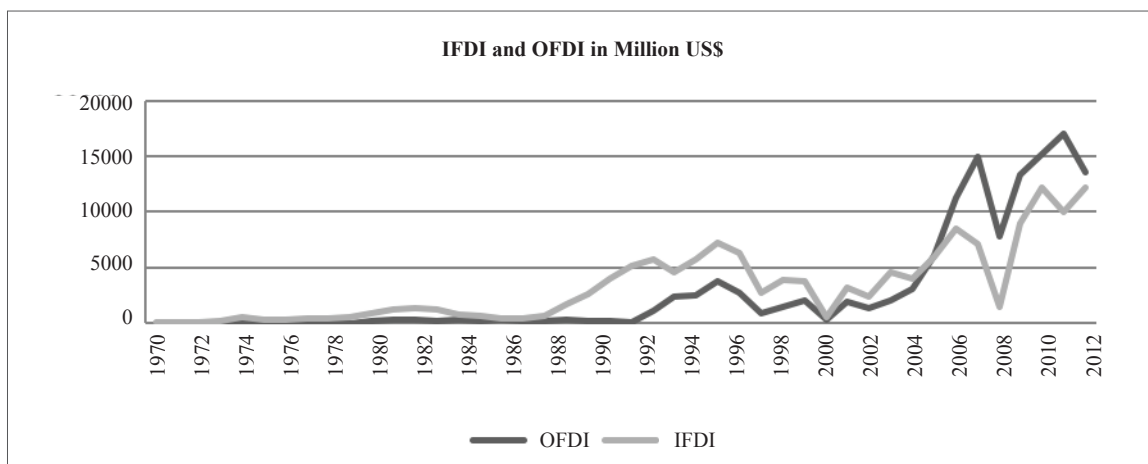


FIGURE 2. IFDI and OFDI in Malaysia
Source: UNCTAD Database, 2015

and governance quality are also crucial variables that propel investors to execute cross-border investments. An obvious case in point is that such macroeconomic and institutional factors exist in both home and host countries and act as 'push' factors and 'pull' factors for the investors, respectively.

Empirically speaking, there is a plethora of analyses on factors causing OFDI from developing countries, especially China, India, South East Asia and Central and Eastern European Countries (CEEC). Main factor leading to establishment of third world multinationals is technological transfer resulting from IFDI, as highlighted by Tolentino (1993). Similarly, Apergis (2009) declared that IFDI and domestic GDP are the primary determinants of OFDI. Technological developments which encompass innovative capabilities, higher productivity or R&D growth in the local firms act as competitive advantages and drive local investors to engage in overseas investments (Intarakumnerd 2013). Other studies that stress on the same idea are done by Pantelidis and Kyrkilis (2005), Torrecillas and Alvarez (2013) and Duran and Ubeda (2010).

With respect to specific countries and regions, the following studies provide us with robust evidence of how crucial competitive advantages are for generation of OFDI from developing countries. Das (2013) said that higher R&D growth, trade openness and lower political risk attracted OFDI from developing Asian region. Possession of scale economies or technological superiority in the Chinese firm made them more productive (Bhaumik, Driffield and Zhou 2015). Indian OFDI also evolved over time from sluggish to an accelerating trend (Chandrawanshi and Banerji 2011) because Indian firms gained the ability to develop cost-effective techniques especially in Pharmaceuticals industry (Athukorala 2009; Kedron and Bagchi-Sen 2012). Similarly, Indian IT firms also possessed managerial and labor low-cost advantages (Narayanan and Bhat 2011) which acted as their ownership advantages. For Turkish firms, such ownership advantages have been identified as operation-related, product-related, marketing-related and management-related competitive advantages (Kaya and Erden 2008).

Home country macroeconomic determinants acting as push factors for OFDI from South Asia, South East Asian, East Asian and other developing economies have too been examined by many authors. Bhasin and Jain (2013) said that higher GDP, indicating higher domestic market size, low capital controls and open FDI policy enabled higher OFDI. Empirical evidences by Aykut and Ratha (2004), Kim and Rhe (2009) specifically for South Korea, Tolentino (2010), Cheung and Qian (2009) particularly for China also state that traditional macroeconomic factors such as savings rate and GDP growth lead to more OFDI.

Presence of certain factors in foreign countries acts as pull factors attracting OFDI from developing nations.

Gammeltoft (2008) proved in his empirical study that cheap labor and production costs in other emerging and developing countries, and their geographical and cultural proximity cause higher OFDI. Local companies also invest abroad to acquire technology, managerial know-how and knowledge. The latter aim is also fulfilled by GCC's cross border investments (Ramady 2014). Seeking cheap labor, low production costs and strategic assets are also primary motives behind Thailand garment industry's OFDI (Passakonjaras 2012). Likewise, Indian firms also invest abroad to seek resources, technology & R&D markets, risk-diversification, efficiency and also acquisition of foreign brand names and expansion of product mixes. Such motives are also found behind Chinese investment abroad (Deng 2003; Hong and Sun 2006; Wu and Chen 2001; Deng, 2007; Du and Boateng 2014). Zhang and Daly (2011) shared similar results but they also added higher host country GDP, exports, and openness to FDI as other determinant factors.

The motives to invest abroad depend on the destination and source of OFDI as well. Chinese firms have been investing in developed countries to access the technology and in developing countries to access markets (Chang 2014). Disaggregation of Chinese OFDI also show that market seeking is the main motive for investing in OECD countries, whereas resource seeking and working in poor institutions motives hold for investing in non-OECD countries (Kolstad and Wiig 2012). Another interesting feature of OFDI structure from China is that privately owned firms go global because of their ownership advantage in terms of organizational capabilities whereas state owned firms invest abroad because they have government support (Liang, Lu and Wang 2012).

Favorable government policies are also crucial in enabling firms to invest abroad (Hattari and Rajan 2010; Kumar and Chadha 2009; Sun, Peng, Lee and Tan 2015). China's 2001 go-global policy and Indian government's supportive reforms and easy access to finance for emerging multinationals are all examples of such policies (Hong and Sun 2006). Promotional measures such as financing and taxation assistance and concession, reduction of political and environmental risks and other monitoring policies help in increasing OFDI (Luo, Xue and Han 2010). Chowdhury (2011) also highlighted the importance of financial and trade liberalization policies in facilitating Indian firms to invest abroad.

Gao (2005) and Nissan and Niroomand (2010) proved that OFDI is a positive function of host country's GDP and lower distance between host and home country. Shen and Lin (2011) also concluded that higher distance between host and home country discouraged cross-border consolidation among eight Asian economies in pre and post 1997 financial crisis era. Hattari and Rajan (2009) also shared similar views about bilateral OFDI in developing Asia. They augmented the gravity model approach and concluded that bilateral exports, exchange rate appreciation, host country's financial openness,

lower political risk and free trade agreement encourage bilateral OFDI. Similarly, Kalotay and Sulstarova (2010) also suggested that higher bilateral OFDI from Russia is caused by higher domestic and host economy GDP, CIS membership and possession of natural resources by host economies. Such links are also considered before decision to invest abroad is finalized. For example, the ethnic networks such as presence of Chinese in other countries will force the local Chinese investors to form business relationships with them. This is basically termed as ‘low cultural distance’ (Quer, Claver and Rienda 2012). A similar concept discussed by Gao, Liu and Zoh (2013) stated that higher human mobility or the number of local students who go abroad and stay there help in creating international network which result in positive knowledge flows over time and eventually enable OFDI.

Few studies stress on the home and host country’s institutional infrastructure apart from conventional macroeconomic factors responsible for higher OFDI. These include Rammal and Zurbruegg (2006), Stal and Cazorra (2011) and Deng and Yang (2014) for both developed and developing countries. Mishra and Daly (2007), Stoian (2013), Stoian and Filippaios (2008), Buckley, Forsans and Munjal (2012) and Kalotay (2008) clearly established the fact that Dunning’s OLI framework has a missing leg which they refer to as ‘institutional leg’. Home country’s overall institutional reforms and competition reforms significantly explain the generation of OFDI. Amal et al. (2009) also highlighted the positive impact of higher globalization index and economic freedom in causing OFDI from Latin America. Ramasamy, Yeung and Laforet (2012) claimed that higher OFDI by China is not affected due to host country’s political risk. In fact, and on the other side, Kang and Jiang (2012) concluded that economic factors are less important determinants than institutional factors, measured by economic freedom, political

influence, FDI restriction, cultural distance, bilateral distance, and bilateral trade.

In Malaysia, higher OFDI is generated by higher level of exports, IFDI, and higher labor productivity (Saad, Noor and Nor 2011). Higher openness of the Malaysian economy and higher income level also increase OFDI from Malaysia (Kueh, Puah and Apoi 2008). Furthermore, seeking growing markets (Saad, Noor and Nor 2014 and Ragayah 1999) and seeking lower wages (Jomo 2002) are the relevant push factors for Malaysian OFDI. Goh and Wong (2011) claimed in their empirical study that liberalization policies of 1980s and higher GDP of the foreign country acted as push and pull factors respectively. Government has been encouraging local firms to invest abroad irrespective of their local competitiveness. The formation of Government-Linked Corporations (GLCs) such as Petronas Sdn Bhd and Malaysian Multinationals are indications of the fact that government has been actively involved in increasing OFDI (Ariff and Lopez 2008; Tham 2007; Zainal 2005).

It can be observed that although Malaysian macroeconomic factors helping in OFDI generation have been explored to an extent but the application of gravity model showcasing the effects of host countries’ institutional and macroeconomic factors causing bilateral OFDI from Malaysia to major recipients have not been examined and that is the primary objective of the study.

Within developing Asia, OFDI from South East and East Asia has grown remarkably well. The UNCTAD (2014) database shows that OFDI flows from the region have increased from US\$ 94,925 Million in 2000 to US\$ 326,012 Million in 2013, an increase of almost 243%. It can be seen from Figure 3 that the highest contribution in the region is by East Asia followed by South East Asia. Malaysia is part of the South East Asian region and its OFDI has also been continuously increasing over time (Figure 2). A closer analysis shows that OFDI

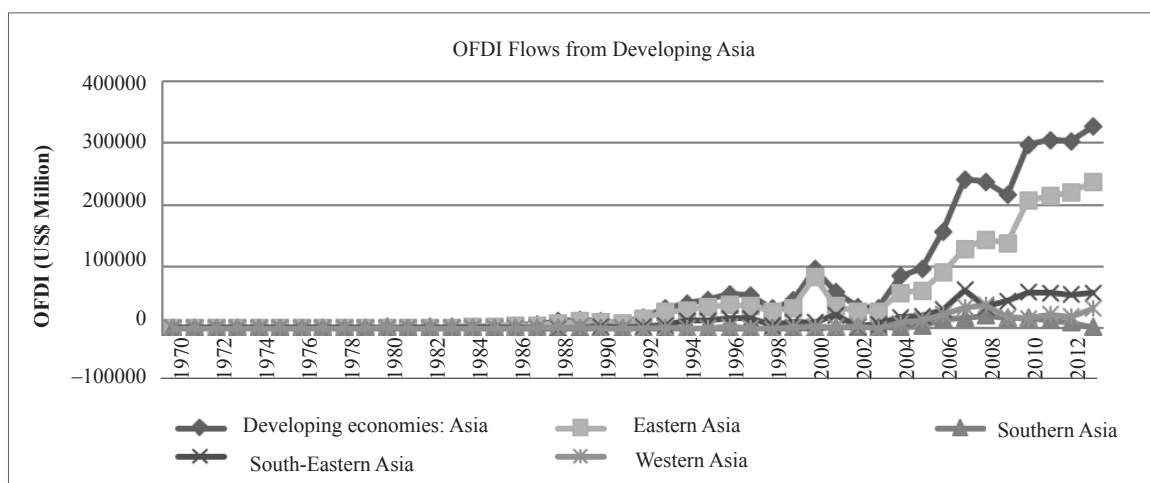


FIGURE 3. OFDI from Developing Asia

Source: UNCTAD Database, 2015

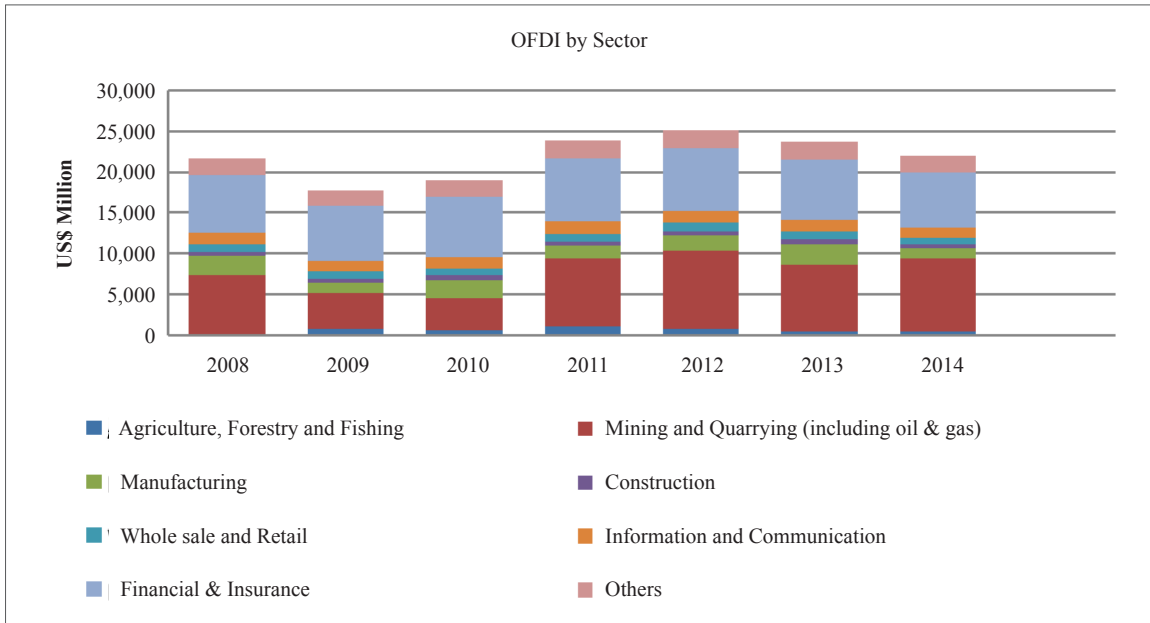


FIGURE 4. Outflows in Major Sectors
 Source: Department of Statistics, 2015

from Malaysia has been most prominent in Mining and Quarrying (including oil and gas) sector followed by Financial and Insurance sector (Figure 4). Hence, it seems that Malaysia has been investing abroad seeking natural resources and accessing foreign markets in the services sector as opposed to other objectives such as technology seeking, or diversification seeking. On the other hand, ASEAN’s Indonesia and Singapore and developed economies such as UK and Australia are the

highest recipients of Malaysian investment outflows (Figure 5). Indeed, such observations require a systematic investigation of the factors forcing Malaysian investors to invest abroad.

The details of company profiles (Mavroeidi 2013) show that the major players investing overseas are Petronas and YTL Corporation Bhd in ‘energy’ sector. Uzma Bhd is also an ‘oil and gas’ sector company. Another company, Tanjong PLC operates in the fields of power generation,

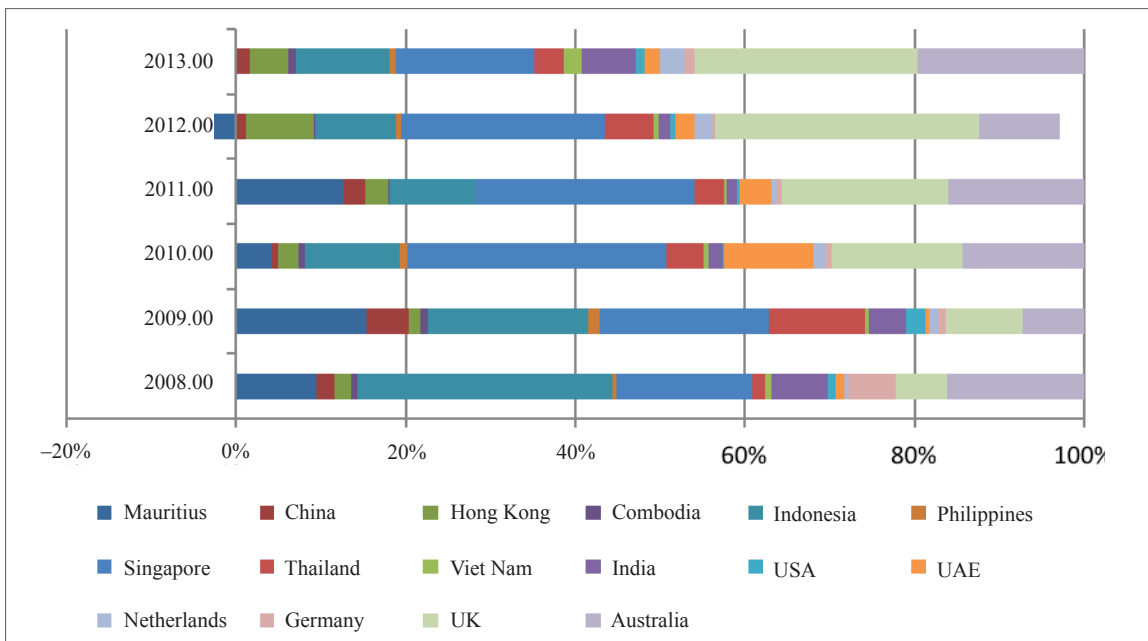


FIGURE 5. Major Recipients of the Outflows from Malaysia
 Source: Department of Statistics, Malaysia 2015

gaming, leisure and property investments. Ranhill Bhd supplies construction, engineering, environment-related, power and petrochemicals services. Melewar Industrial Group Bhd also has power generation setups in Thailand and the group plans to expand further. Sime Darby is a multinational company representing diversified operations overseas.

Financial services sector is also a major investor in overseas markets. Banks such as CIMB Group, Maybank, Public Bank, RHB Bank, Hong Leong Bank, Ambank, Affin Bank have worldwide operations. OSK Holdings offers financial, advisory and investment services and has diversified into South East Asia. In the 'Information and Telecommunications' sector, Axiata Group Bhd, Telekom Malaysia Bhd (TM), Maxis Communications, Nextnation, MNC Wireless Bhd, Billadam, and Iscistech (IT Services Company) are the various mobile and mobile services companies that have subsidiaries and ownerships abroad. Similarly, 'Property and Hotels' sector also has range of multinationals. Few major companies are The Employee Provident Fund (EPF), Genting Malaysia Bhd, SP Setia, TA Global, Selangor Dredging Bhd (SDB), Permodalan Nasional Bhd (PNB), Malayan United Industries (MUI), IOI Corp, Berjaya Group, Sunway and Advanced Synergy.

Construction companies have also been involved in overseas investments, especially in Middle East. United Engineers Malaysia, Sunway, Wah Seong, Bina Puri and Muhibbah are the main companies providing various construction services in different countries. Multinationals in 'Manufacturing' sector comprise of PPB Group Bhd, KNM Group, Press Metal Bhd, Unisem Group, Formosa Prosonic Industries Bhd, Mega First, EP Manufacturing Berhad (EPMB), Pantech Group Holdings Bhd, Asia File Corporation, Abric Bhd, Triplus industries, Hui Holdings, Alpha Biologics and Catenate.

METHODS

CONCEPTUAL FRAMEWORK

As stated in the theoretical and empirical literatures, countries engage in overseas investment due to various motives such as market seeking, foreign technology seeking, natural resource seeking, diversification and strategic asset seeking. With respect to Malaysia, it is hypothesized that following motives hold more importance.

As discussed by Saad et al. (2014) and Goh and Wong (2011), primary motive behind Malaysian OFDI is to access foreign markets. Theoretically speaking, bigger markets provide more opportunities for foreigners to invest in various regions and hence, there is a greater chance of making profit. Larger market size also helps investors to expand their businesses. Most of the overseas investments done by Malaysian investors are in the 'Energy' sector (Figure 5). For example, Petronas

and YTL Corporation Bhd have executed investments worldwide, targeting growing markets. Literature takes GDP per capita or GDP growth rates to capture the effects of large and growing market size in the host countries (Kang and Jiang 2012; Goh and Wong 2011; Bhasin and Jain 2013).

One of the major motives of investing abroad is to seek a consistent supply of natural resources as put forward by Dunning's OLI theory. As far as Malaysia is concerned, it has been primarily investing in countries with oil and gas reserves such as UAE, USA, Australia, Indonesia and China. Apart from Petronas and YTL Corporation Bhd, Uzma Bhd (oil and gas sector), Tanjong PLC, Ranhill Bhd, Melewar Industrial Group Bhd, and Sime Darby are also power generating companies and have an interest in investing abroad for securing energy supplies. Hence, a major hypothesis of this study is that Malaysian investors seek natural resources when investing abroad.

Another major motive of investing overseas is to seek strategic assets and acquiring technology. Firms invest in foreign countries to acquire companies via mergers and takeovers that possess better techniques and are technologically more advanced. Possession of such assets have the potential of transferring technology back to the home country which eventually is expected to raise labor and factor productivity growth rates. Although graphical analysis and overview of the company profiles do not rigorously support that Malaysian investors have been investing abroad for seeking technology, but nonetheless it is an important factor and needs to be tested.

For local firms that invest abroad, their subsidiaries or foreign affiliates will also tend to expand their businesses over time in the foreign economy. For that, the investors will borrow from foreign country's banking institutions and hence, their lending rates will be an important determinant of Malaysian overseas direct investments. Higher the lending rate, higher will be the cost of borrowing capital, and lower will be the OFDI.

Theoretically speaking, if Malaysian currency is depreciating and creates an expectation of further depreciation with respect to foreign currency, Malaysian exports will increase as they will become cheaper. Hence, local firms will establish links with the foreign firms through international market for goods and services rather than by investing abroad. Secondly, it will be more expensive to invest abroad if foreign currency is appreciating and hence, local firms would prefer to export more than invest. Therefore, a depreciating value of Ringgit Malaysia (RM) per unit of foreign currency will lead to lower OFDI (Udomkerdmongkol, Morrissey and Gorg 2009).

More trade openness and more bilateral trade with the foreign economies would indicate that there are mechanisms in place for trade and capital account liberalization. Hence, local firms will be propelled to invest in such economies (Kang and Jiang 2012).

Analysis of economic and political freedom in the host economy is an integral part of decision making process of the investors before overseas investments are finalized. As put forward by Kang and Jiang (2012), institutions' friendly attitude towards FDI or economies where there is protection of property rights, less ownership restriction and low corruption or higher bureaucracy quality, more FDI's will take place. According to Worldwide Governance Indicators (WGI), 'Voice and Accountability' measure captures the extent to which citizens are able to participate in selecting their government, the extent of freedom of expression, freedom of association and free media. It is intuitively argued in this study that such freedom level in the host economy is likely to attract more investors from Malaysia. This is because investors are bound to feel more secure with their investments if the society has strong democratic forces conducive to business environment. A high ranking on this measure also indicates strong governance.

Another important institutional variable is the political stability and absence of violence. If there are perceptions and expectations that there will be violence or terrorism and that can cause instability, local investors would not feel secure to invest. Political risk has actually been used in many studies to analyze how it affects the OFDI (De Beule and Duanmu 2012; Duanmu 2012; Quer, Claver and Rienda 2012; Ramasamy, Yeung and Laforet 2012). It will be used in this study as well and it is expected that higher political instability will lower OFDI.

Cultural perspective is captured by linguistic proximity of Malaysian official language with the official languages of respective host economies. It is also a standard variable used in the gravity model. The idea behind the factor is that investors prefer to invest in countries where common spoken language or common official language is the same. In other words, higher linguistic proximity will lead to higher investment from Malaysia.

Other control factors and dummy variables are also considered to be relevant. Firstly, it is believed that there is major bilateral OFDI taking place within the ASEAN region. From Figure 5, it can be seen that Singapore and Indonesia are consistently receiving higher OFDI from Malaysia. Hence, ASEAN region is likely to be the preferred area for Malaysian investors. Secondly, lower distance and common border with the respective host country will also attract higher investment from Malaysia as that makes the investments cost-effective. Thirdly, it is also observed from the data that about 33.6% of the major bilateral OFDI is received by UK and Australia. Hence, it will be interesting to check if Malaysian OFDI is higher in the developed states.

MEASUREMENT OF OFDI

According to IMF's definition of OFDI, direct investment abroad is a form of direct investment whereby companies

investing abroad with the intention of obtaining a lasting interest and the threshold level is 'holdings of at least 10% ownership' in an enterprise resident of another economy. In line with this definition, data is compiled by Department of Statistics, Malaysia (DOSM) on quarterly basis in the Balance of Payments statistics section. Bank Negara Malaysia also compiles data on investment abroad by country over time based on Cash Balance of Payments Reporting System (CBOP) but this data is different from IMF definition and only includes equity investment, inter-company loans and real estate acquisitions. Hence, that data has not been used in the study. DOSM has on the other hand started recording bilateral data on Direct Investment Abroad (DIA, also known as OFDI) since 2008 on quarterly basis by country and by sector. Due to lack of available bilateral data on OFDI for earlier time periods, this study has taken into account yearly FDI outflows from 2008 to 2013. The series are measured in US\$ Million for all the major recipients reported in Figure 5 and is titled as *OUTFLOWS*. Also, natural logarithm of the variable has been generated to cater for non-linear relationship and labeled as *LOUTFLOWS*. Since there were negative values, the data had been transformed by using Equation 1 following Busse and Hefeker (2007).

$$y = \ln(x + \sqrt{x^2 + 1}) \quad (1)$$

INDEPENDENT VARIABLES

GDP per capita (*GDP_PC*), measured in US\$, reflects market wealth. As described above, natural resource seeking is one of the major motives behind Malaysian OFDI. It is measured using the proxy of 'ratio of ores and metals as percentage of merchandise exports' in the host country and it is titled as *RESOURCES* (Amighini, Rabellotti and Sanfilippo 2013; Buckley et al. 2012; Chang 2014; Deng and Yang 2014; Kang and Jiang 2012; Ramasamy et al. 2012). Technological development in the host country can attract Malaysian investors if one of the primary motives is to seek assets or R&D. To capture the technological advancements in the host country, the variable of R&D as percentage of GDP in the host economy has been taken into account (*R&D*). *R&D* has been recorded as a dummy variable assuming the value of 1 if R&D expenditures are more than 2% of GDP, and 0 if otherwise. Bilateral Trade reflects the amount of exports and imports between Malaysia and the relevant host economy (Bevan and Estrin 2004; Buckley et al. 2007; Kang and Jiang 2012). Department of Statistics, Malaysia compiles data on bilateral exports and imports on quarterly basis. The data points have been converted to US\$ Million by using the exchange rate for respective years and then the absolute values of imports and exports are added to reflect total bilateral trade (*BIL_TRADE*). Relative exchange rate is bilateral official exchange rate of host economy currency per unit of Ringgit Malaysia, RM (*REL_EX*). The data for the official value of exchange rate is reported by World

Development Indicators, 2014 database but it is defined as foreign currency per unit of US\$. To obtain the required variable for the study, the exchange rate has been divided by the official exchange rate of RM/US\$. Lending rate (*LEND_RATE*) is defined as rate that meets the short- and medium-term financing needs of the private sector by the World Bank. It is the interest rate on which loans are disbursed to private sector.

The data representing strong governance has been taken from World Governance Indicators 2013 (WGI). WGI reports data on 'Voice and Accountability' in which higher value of the index indicates strong democratic forces, freedom of expression and higher government accountability. This variable has been titled as governance measure, *GOV_WGI*. Another aspect of institutional perspective is captured by political stability and absence of violence. Index points for this variable have been taken from WGI, 2013 database's indicator titled 'Political Stability an Absence of Violence'. Higher values on this index (*POL_STAB*) indicate political instability and more incidences of politically motivated terrorism. To capture cultural dimension, which is also part of institutional outlook, linguistic proximity (*LANG_PROX*) data has been recorded from French Research Center in International Economics (CEPII) database.

CEPII dataset also contains information on bilateral distance (*BIL_DIST*) between two capital cities of various countries. *ASEAN* is a dummy variable taking the value of 1 if the host economy is a member of ASEAN region quantifying the impact of free trade agreements and AEC formation on Malaysian FDI outflows. Secondly, if the host country shares same border with Malaysia, it is also given a value of 1. This variable is titled as *COMM_BOR*. Lastly, if the host country is a developed state, which means that it has GNI per capita of \$12, 746 or above, it receives a value of 1 and it is represented as *DEV_STATE* in this study.

$$\begin{aligned} OUTFLOWS_{it} = & \alpha_0 + \beta_1 GDP_PC_{it} + \\ & \beta_2 RESOURCES_{it} + \beta_3 R\&D_{it} + \beta_4 BIL_TRADE_{it} + \\ & \beta_5 REL_EX_{it} + \beta_6 LEND_RATE_{it} + \beta_7 GOV_WGI_{it} + \\ & \beta_8 POL_STAB_{it} + \beta_9 BIL_DIST_{it} + \\ & \beta_{10} LANG_PROX_{it} + \beta_{11} ASEAN_{it} + \\ & \beta_{12} COMM_BOR_{it} + \beta_{13} DEV_STATE_{it} + \mu_i + v_{it} \quad (2) \end{aligned}$$

where '*i*' = host economy, $i = 1, 2, 3, \dots, n$ and '*t*' stands for annual time period changes from 2008 till 2013, μ_i is country-specific error term and v_{it} is standard random error term.

The regression model stated above is a panel data estimation strategy. Based on Breusch-Pagan Lagrangian Multiplier test, random effects GLS regression model is finalized for quantifying the effects of macroeconomic and institutional variables of the foreign economies on Malaysian bilateral OFDI to the major recipients in which the data is available for the stated time period (Amal et al. 2009; Durán and Úbeda 2010; Kalotay and Sulstarova 2010).

RESULTS AND DISCUSSION

The first two models in Table 1 do not take the natural logarithm of the OFDI and also have lower values of R-square as compared to third model where it increases to 72.6%. It is important to reveal that all models pass the diagnostics checks and do not suffer from problems such as autocorrelation as robust standard errors of the coefficients have been used. Pesaran cross sectional dependence test has been used due to large N and small T characteristics of the panel data. It can be seen that cross sectional dependence is also not significant.

Malaysian OFDI is higher in countries with higher GDP per capita. This result is in line with Ragayah (1999) and Hiratsuka (2006). Also, the assertion that the primary motive behind Malaysian overseas investment is seeking natural resources has been proved as the relevant variable is coming out to be significant with very high magnitudes as well. However, the presence of R&D expenditures in the economy does not propel investment from Malaysia indicating that technology seeking motive may carry lower importance as compared to other factors before investment decisions are finalized.

Higher lending rate in the respective economies decreases the investment from Malaysia. Appreciated RM or relatively cheaper foreign currency attracts more investments as it is more cost effective to invest. On the other hand, higher bilateral trade is not significantly attracting Malaysian investments. Malaysian investment should be higher in economies more open to trade with respect to Malaysia. Nonetheless, this study does not support that line of argument. In fact, higher bilateral trade does not translate significantly into higher investment.

Amongst the variables capturing institutional aspects, the governance indicator of WGI turns out to be positive and significantly explain the pattern of investment from Malaysian investors. Secondly, higher outflows are also experienced in countries with low political instability index, although the variable lacks significance. Another feature in the analysis is that not much of the Malaysian investment is being done in the ASEAN region. This is a cause of concern especially after the announcement that ASEAN will be an economically integrated area by the end of 2015. ASEAN Economic Community (AEC) will become a single market and production base which would enable goods, labor, services and technology to move freely within the ASEAN community and manufacturers (local and foreign) can set up various stages of the production cycle in the market where it is economically most efficient. This reflects that there should be more intra-ASEAN investment in the stated time period but it is not the case. Rather than that, a significantly negative sign is witnessed in Models 1 and 3 which means that Malaysian OFDI is focusing on non-ASEAN economies.

TABLE 1. Estimation Results

Variables	Model 1	Model 2	Model 3
	Dep. Variable: OUTFLOWS		Dep. Variable: LOUTFLOWS
GDP_PC	0.0315 ** (.01475)	0.0310** (0.0154675)	0.0000181 (0.0000174)
RESOURCES	21.7589* (11.4675)	22.85482* (12.61598)	0.0305395* (0.0180287)
R&D	519.9542 (487.8356)		0.7673017** (0.3964245)
BIL_TRADE	0.0331 (0.02591)	0.0346266 (0.0243246)	0.00000638 (0.0000136)
LEND_RATE	-1063.342* (632.8111)	-1042.81* (621.6167)	-0.5196958 (0.4484322)
BIL_EX	0.3556128 ** (0.1522324)	0.335423** (0.1430121)	0.0003352* (0.000204)
GOV_WGI	29.27512 ** (13.79538)	27.13209** (13.37064)	0.0209228* (0.0116199)
POL_STAB	-1.848878 (16.1551)	-1.57939 (15.41896)	-0.0008014 (0.0129757)
LANG_PROX	244.9527 (257.1299)	216.0864 (272.584)	0.1817749 (0.1893743)
ASEAN	-1164.051* (700.5034)	-1101.801 (745.8267)	-2.427065*** (0.6246336)
BIL_DIST	-0.2594816*** (0.079438)	-0.22483*** (0.0877437)	-0.000259*** (0.0000729)
COMM_BOR	1033.013 ** (445.2061)	1100.497** (466.8948)	2.548367*** (0.322431)
DEV_STATE	-1640.917 * (941.5597)	-1316.162 (925.6465)	-1.147568* (0.6171701)
Constant	570.8708 (1362.946)	408.6313 (1187.915)	6.779342*** (0.8545183)
Observations	96	96	96
R-Sq	50.05%	47.44%	72.60%
Cross Sectional Independence	-0.072 Pr: 0.9423	-0.059 Pr: 0.9530	0.596 Pr: 0.5512

*Standard Errors reported in Parenthesis * p<0.1; **p<0.05; ***p<0.01*

Malaysian overseas investment outflows are also positive and significant in countries which share common border. Similarly, and as expected, nearby countries attract more investments. There is evidence found in this study that the direction of outflows is significantly lower in developed states indicating the fact that south-south investment flows are more evident. The results of this study are broadly in line with Gao (2005), Hattari and Rajan (2009) and Amal et al. (2009) who stated that investment increases in countries which have lower bilateral distance, bigger markets and better governance.

CONCLUSION AND POLICY IMPLICATIONS

Malaysian OFDI has been continuously increasing over time showing an accelerating trend since 2004. Despite that, there is a dearth of quantitative studies on factors raising bilateral OFDI from Malaysia to other regions mainly due to lack of secondary data. From 2008 onwards, Department of Statistics, Malaysia, started compiling the bilateral OFDI in accordance to the IMF definition on quarterly basis. The data is segregated into OFDI by country and by sector. This study makes use of

that data and takes into account the outward investment outflows by Malaysia to major recipient economies and investigates the pull factors or foreign country-specific factors responsible for it. Results show that Malaysian investment outflows are higher in countries where GDP per capita and natural resource endowments are high. Secondly, appreciating RM and lower lending rates in the host economy also pull the domestic investors to execute cross border investments. Amongst the other variables, Malaysian foreign investment outflows are higher in countries that have lower bilateral distance and share common border. There is enough evidence that Malaysian investment outflows are lower in developed states and AMS.

Hence, Malaysian investors are mainly concerned with securing natural resource supplies and accessing larger markets. Other potential economies for investment could therefore be African states, parts of Latin America and Middle Eastern countries. Recent bearish trend in oil prices depreciated RM as Malaysia is an oil exporting economy. This has a potential of further decreasing outwards investments, thus, the policy makers and the central bank must take appropriate action to control the falling value of RM before the decreasing trend in OFDI (since 2013) continues. ASEAN is a free trade area and the member states have cultural proximity as well. Bilateral investments with AMS have been expected to be significant as ASEAN heads into becoming an economically integrated area by the end of 2015. AEC has the potential of not only providing a large market for foreign investors but also providing the AMS the opportunity of setting up production chains in the markets where it is economically most efficient. Hence, it is expected that intra ASEAN investments and partnerships will increase. However, in this study, there is no evidence that Malaysia is investing significantly more in ASEAN states. This has important policy implications and the policy makers need to introduce more incentives so that outward investment flows in ASEAN region can increase and positive use of AEC can be made by Malaysia. As far as institutions are concerned, Malaysian investors are significantly investing more in countries with voice and accountability. There is weak evidence that high political stability in the host economy is preferred by the domestic investors. Hence, other countries with strong institutions can be targeted for higher investments in the future. Also, since it is evident that Malaysian investment is more of a south-south nature, it is time that the policy should take a new turn in this regard by initiating investments in developed states to seek foreign technology and R&D as done by China, India, Russia and Latin America.

Exploring the significance of factors pulling investment from Malaysia at disaggregated level could be a basis for future research. A particular limitation of this study is that the data points are not large enough for definite patterns of foreign investment outflows to emerge, e.g. with respect to developed and developing

states, mergers/acquisitions and Greenfield investments, hi-tech and low-tech industries, and so on. As more data, especially firm-level or industry level, is released, further work can be done to counter this weakness. Also, other sources of data measuring institutional quality variables should also be explored before more concrete implications about institutions and OFDI are made.

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- Gul Andaman*
Universiti Putra Malaysia
Faculty of Economics and Management
Department of Economics
Universiti Putra Malaysia
43400 Serdang Selangor
gul.andaman@gmail.com
- Zulkornain Yusop
Universiti Putra Malaysia
Faculty of Economics and Management
Department of Economics
Universiti Putra Malaysia
43400 Serdang Selangor
zulkornain@upm.edu.my

Zaleha Mohd Noor
Universiti Putra Malaysia
Faculty of Economics and Management
Department of Economics
Universiti Putra Malaysia
43400 Serdang Selangor
lehnoor@upm.edu.my

Shivee Ranjane Kaliappan
Universiti Putra Malaysia
Faculty of Economics and Management
Department of Economics
Universiti Putra Malaysia
43400 Serdang Selangor
shivee@upm.edu.my

*Corresponding author

