The Effect of Corruption on FDI Inflow: Empirical Evidence from Panel Data of East Asian Economies

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Abstract
This study has made fresh insights and investigates the effects of corruption on FDI inflow for a panel of 16 Asian economies from 1995-2009. The empirical result suggests a one unit increase in the level of corruption triggers a decrease in FDI inflow by approximately 3.4 percentage points. Thus, some of the arguments that corruption does not keep FDI out of those corrupt countries were either flawed or invalid. In fact it is reasonable to claim that some of the countries that are characterized by high level of corruption but also with a remarkable FDI inflow could even double their inward FDI if they manage to reduce the present pervasive level of corruption.

Key Words:
Corruption; FDI Inflow; Panel Data; REM, FGLS; Economic Growth; Openness; Human Capital

Introduction
Until recently, there was a strong consensus in the literature that multinational corporations (MNCs) invest in specific locations mainly because of strong economic fundamentals in the host countries for example, large market size, stable macroeconomic environment, availability of skilled labor, infrastructure etc and thereby influence the attractiveness of the country to FDI inflows (Dunning 1993, Globerman and Shapiro 1999, Shapiro and Globerman 2001). However, the host country’s economic fundamentals may not be sufficient for inward FDI. Therefore it now becomes important to study afresh what determines inflow of FDI. In this regard, one of the most damaging risks that TNCs must consider in entering emerging market economies is the threat of corruption, which undermines economic reform and, ultimately, national economic stability. Moreover, corruption raises the cost of doing business, distorts the allocation of