Erasmus University Rotterdam
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Human Rights Violations and Foreign Direct Investment Inflows in Southeast Asia

What is the effect?

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Abstract

Foreign direct investment (FDI) is an essential factor for the development of countries, especially for developing countries. These developing countries aim to attract FDI, as much as possible. Therefore, it is interesting to look at which factors determine an increase or decrease in FDI inflows. The primary independent variable in this research is human rights violations. The main question asked is whether human rights violations affect FDI inflows in Southeast Asian countries. Especially in Southeast Asia, human rights are interesting because of the relatively poor record of countries there in this regard. If it is true that human rights do have an impact on FDI inflows, then there are incentives for local governments to improve their human rights record.

This research compares the influence of the political determinant human rights with two other political/institutional determinants, the rule of law and democracy. It tests which political/institutional determinant has the most influence on FDI inflows. In order to investigate these relationships, quantitative research is used to analyse 15 Southeast Asian countries over the course of 15 years, from 2003 to 2017. This research uses a panel data analysis in STATA to answer the research question. This paper aims to test the relationship of these three independent variables on the dependent variable with the help of five control variables: market size, economic growth, inflation, trade openness and balance of payments.

The results of this paper show that the expectations are not verified. According to this research, human rights do not affect foreign direct investment inflows. In addition, the other independent variables of this research, the rule of law and democracy, do not have a significant impact on foreign direct investment inflows in Southeast Asia either.

Acknowledgement

As a 22-year old master's student at the Erasmus University Rotterdam, I already have had a lot of luck and happiness in my life so far. I feel blessed with the possibilities and freedoms that I have experienced here in the Netherlands. However, this happiness is not experienced by everyone in the world. Many people do not have the same possibilities and opportunities in their life as me. Therefore, I have always had an interest in poorer countries. How can they escape from their reality? How can they improve their economic situation? Can they improve their economic situation?

This Master's program (International Public Management and Policy) increased my interest in human rights in the world. This academic year, I visited the United Nations Human Rights Council (UNHCR) and the International Committee of the Red Cross (ICRC), which were really interesting for me. These visits and the awareness of my luck in my life were the main reasons to focus my thesis on an underdeveloped region of the world, Southeast Asia. I have a profound interest in human rights conditions in this region and what motivates governments to improve their human rights records in order to attract more FDI. Although the outcome is not what I expected and was hoping for, human rights violations are still an important topic for me as a researcher and as a human being.

I am very grateful for the support and guidance of several people since this thesis could not have been conducted without their help. I would like to express my gratitude to Dr. Grand, my thesis supervisor, for guiding me through my thesis project. His input and expertise helped in understanding some crucial components of research. I would like to thank Dr. Zhelyazkova as well for being my second reader. Her practical comments helped me a lot in executing my research project. Furthermore, I cannot thank my family, especially my parents, enough for always supporting me through my studies, and, of course, my girlfriend Sanne, for encouraging me during this hard period.

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List of abbreviations

BoP	Balance of payments
GDP	Gross Domestic Product
US$	US dollars
PTS	Political Terror Scale
EIU	Economist Intelligence Unit
FDI	Foreign direct investment
VIF	Variance Inflation Factor
FE	Fixed estimates
RE	Random estimates
WB	World Bank
ICRC	International Committee of the Red Cross
UNHRC	United Nations Human Rights Council

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Chapter 1. Introduction

1.1 Problem definition

Foreign direct investment (FDI) has a vital role for different reasons. One of the reasons is that FDI is an essential factor for the economic growth of countries in general, but especially for poorer countries, also described as developing countries, of which most Southeast Asian countries are (Chowdhury & Mavrotas, 2006). There are more reasons why FDI is important to the development of countries. The first reason is related to the crucial role of host countries as a source of capital, which stimulates the economy. Second, FDI in host countries can create jobs and opportunities for citizens; these would not exist without foreign investors. Third, an increase in FDI inflows can lead to an increase in technical knowledge, which can further contribute to the development of a country (Chowdhury & Mavrotas, 2006).

In order to boost the economy of the host countries, it is crucial to have a look at the factors, which may explain an increase or decrease in FDI inflows. Different factors have an impact on these flows, which can be divided into two main categories. The first consists of political/institutional factors — for example, the rule of law, democracy and human rights. The second category consists of more economic factors, such as economic growth, inflation, and the balance of payments.

Since the advent of the 21st century, FDI has increased a lot in developing countries (Shah, 2017). Figure 1 illustrates the increase in total FDI flows in Asia. In most years, the inflows have exceeded the outflows, which have ensured a positive net flow of investment capital to Asia. The graph depicts an upward sloping line, which means that during the last 18 years or so, inflows to Asian countries have climbed. Furthermore, the net flows have also climbed over time but not in every year. Southeast Asia is one of the region's most dependent on foreign investors (Chowdhury & Mavrotas, 2006). The region receives relatively more FDI than other developing regions in the world, for example, African regions. According to the World Bank, China alone already receives 25 per cent of the total FDI in the world (World Bank, 2002).

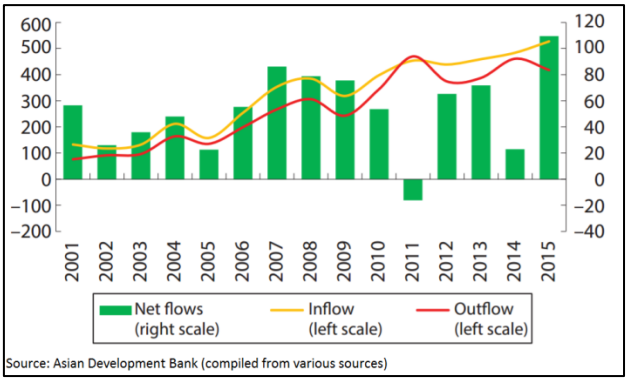

Figure 1: Total FDI flows Asia ($ billion)

However, according to the World Bank (2019), most of the Southeast Asian countries are still developing countries, which means their GNI (Gross national income) per capita is less than 3,895 US dollars. Below this amount of GNI per capita, countries are classified by the World Bank as low-income or lower middle-income countries. This means that despite the increasing trend of FDI flows, FDI inflows in particular, most Southeast Asian countries remain 'developing countries'. As a consequence, these countries still require more FDI inflows to boost their economy and to increase their wealth per capita (Shah, 2017).

From a historical perspective, human rights records of Asian countries score relatively worse than the records of western countries (Kim, 2018). What is most responsible for these human rights issues, though, it economic backwardness. Adverse economic circumstances in Asia were the main reason for the national governments to prefer economic development over the human rights of its citizens (Ghai, 1994). That is why civil and political rights are not the priority of the different national governments in Asia.

In addition to governments, foreign investors deal with these dilemmas as well, since they desire economic profit and cope with respect for human rights in other parts of the world. Different approaches to this dilemma are possible for these investors. They can respect the human rights of the local citizens for different reasons. For example, they can choose not to invest in countries with poor human rights records so as not to put their reputation at stake. On the other hand, they can choose not to do so because of their own norms and values (Janz & Berntsen, 2018). Alternatively, because their main interest is in expanding profits, they can choose to ignore human rights concerns entirely (Bolyard, & Ippolito, 1999).

1.2 Objectives

The problem statement explained the importance of FDI inflows for Southeast Asian countries. In order to determine which factors influence the level of these FDI inflows, this research aims to measure different political factors. It seeks to explain the relationship between human rights violations and FDI inflows in Southeast Asian countries. Furthermore, it seeks to compare the influence of human rights to other political influences on FDI inflows. The other political determinants are the rule of law and democracy. In the end, this research tries to understand which factor has the most significant impact on FDI inflows in Southeast Asian countries.

1.3 Research Question(s)

This paper focuses on the relationship between human rights circumstances and foreign direct investment inflows in Southeast Asian countries. The research question explored is:
What is the effect of human rights violations on the foreign direct investment inflows in Southeast Asian countries?
The following sub-questions try to compare the influence of other political/institutional factors with human rights violations:

1. What is the effect of the rule of law on the foreign direct investment inflows in Southeast Asian countries?
2. What is the effect of democracy on the foreign direct investment inflows in Southeast Asian countries?

1.4 Research Design

This research focuses on 15 developing Southeast Asian countries. The 15 countries are Afghanistan, Bangladesh, Bhutan, Cambodia, China, India, Indonesia, Laos, Myanmar, Nepal, Pakistan, Philippines, Thailand, Timor-Leste and Vietnam. Other Southeast Asian countries do not provide enough data for this research, for example Sri Lanka. Furthermore, this paper does not include developed countries, such as Malaysia, since economic backwardness is the main cause of human rights issues, as discussed in section 1.1 (Ghai, 1994 & Kim, 2018). This figure illustrates the high representation of almost all Southeast Asian countries in this research.

Figure 2: Research countries

1.5 Societal & Academic relevance

The societal relevance of this research consists of two parts: to attract FDI and to reduce human rights violations. First, this paper will contribute towards national governments and human rights proponents interests since they aim to understand which factors determine high FDI inflows in Southeast Asia. Especially for developing countries in Southeast Asia, which are not the wealthiest countries in the world, it is important to receive high FDI inflows to boost their economy and development. Therefore, they must attract and keep foreign investors doing businesses within their borders. Second, it is important to understand whether political determinants such as human rights violations reduce FDI inflows. This would be societally relevant because if this is the case, the governments of Southeast Asian countries have strong incentives to improve the human rights circumstances of their citizens. This improvement would benefit the citizens of the host countries towards a tradition with a greater respect for the rights of human beings. In practice, this means no violations of human rights or at least few violations of human rights than the situation is at this moment. Alternatively, the research may demonstrate these Southeast Asian countries have incentives to improve other political determinants, which deter foreign investors, such as the rule of law and democracy.

The main contribution of this research to the academic world is the composition of the dataset. The data has been updated to include the most recent years that are available in a specific region, namely Southeast Asian countries. It includes many new control variables compared to earlier research (Evans, 1979; Rudel, 1989; Lydenberg, 2005; Dalsrud, 2008; Peterson, Murdie & Asal, 2016). Hopefully, this updated data set provides new insights on the influence of human rights violations on FDI inflows. Furthermore, by taking the most recent years available, it is possible to test the most recent theory about the relationship between human rights violations and FDI inflows, which is the Risk Mitigation model theory (Chapter 3). Earlier research investigating the presence of a relationship between human rights violations and FDI inflows did not test this most recent model. There is the possibility that this updated data set, by including most recent years, will yield different results.

Furthermore, it is relevant for the current literature to add a comparison regarding the impact of two other prominent political/institutional determinants, the rule of law and democracy. This comparison may provide new insights of which political/institutional determinant has the most impact on the decision of foreign investors to invest or not invest in Southeast Asian countries. Researchers are divided as to which factor has the most significant influence on FDI inflows. Most research focuses on one specific political determinant on FDI inflows without also measuring other political determinants

as independent variables (Habib & Zurawicki, 2002; Davenport & Armstrong, 2004; Daniele & Marani, 2006).

1.6 Reading Guide

This research tries to answer the research question through the course of six chapters. The introduction, this chapter, describes the problem definition, outlines the research question that the thesis will explore, and explains the societal and academic relevance of this research. Chapter Two is an essential chapter in this paper because it describes the current literature about the different factors that explain FDI inflows. Two categories divide these different factors, economic and political/institutional factors. This chapter is the basis for the rest of this paper. Chapter 3 narrows the scope towards the two leading theories about the relationship between human rights violations and FDI inflows; these theories (Profit Maximization model and Risk Mitigating model) will be presented in Chapter 3, based on the literature review from Chapter 2. Chapter 4 explains the methodology and the underlying choices that are necessary to execute this research properly. This chapter also explains the choice of a panel data research design and what this kind of research means for the validity and reliability of this paper. Following that, Chapter 5 explains the results and analysis of the data. Chapter 6 concludes the thesis by trying to answer the research question, then discussing its implications and recommendations for future research.

Chapter 2. Literature review

2.1 Foreign Direct Investment (FDI)

First, it is relevant to explain the concept of FDI, the dependent variable in this research. According to Lipsey (2001), FDI exists in two different forms, macro and micro form. The first form explains FDI from a macro view. From this perspective, FDI is viewed from a broad perspective, namely the transactions/investments across national borders. The second form explains FDI from a micro view. From this perspective, FDI is viewed from an individual level. Which individual circumstances have determined the choice for a specific investment? This research mainly focuses on the motivations for foreign investors. However, this focus will include cross border flows, which makes this research a combination of a micro and macro level. The concept of FDI that is used for this research comes from the International Monetary Fund (2008), p 86, "Direct investment is the category of international investment that reflects the objective of a resident entity in one economy, obtaining a lasting interest in an enterprise resident in another economy. (The resident entity is the direct investor, and the enterprise is the direct investment enterprise). The lasting interest implies the existence of a long-term relationship between the direct investor and the enterprise and a significant degree of influence by the investor on the management of the enterprise".

There are many different variables, which may determine the amount of FDI inflows in a country. This part describes different kinds of factors that cause change in the FDI inflows, which consists of two categories: Economic factors and political factors/institutional factors.

2.2 Economic factors

Economic factors can explain the reason to invest or not to invest in another country (Schneider & Frey, 1985). The most well-known proponent of economic explanation for FDI in other countries is Dunning (1973). Economic factors are vital concerning the financial risk for foreign investors instead of the reputational risk, which can be more relevant to the political/institutional factors. Dunning (1973) argues three main economic areas are responsible for the change in FDI: market factors, cost factors and investment climate.

2.2.1 Market size and Market growth

The first main economic area is market factors. For example, the size and growth of the market is an influential factor. Market size (or size of the economy) is the size of the Gross Domestic Product (GDP) (Kaldor, 1954). Historically, researchers agree that there is a positive relationship between market size and FDI (Schmitz & Bieri, 1975; Schneider & Frey, 1985 Papanastassiou, 1990; Tsai, 1994; Pistoresi, 2000). This positive relationship seems to be logical because of the benefits of economies of scale. A broader financial market provides more opportunities for international investors because their production and distribution costs will be lower per unit (Mengistu & Adhikary, 2011).

Market growth (or economic growth) is the growth of the Gross Domestic Product (GDP) per year. Another term for this short-term economic growth is cyclical growth (Kaldor, 1954). The growth rate is a factor that most researchers agree on, namely that it has a positive relationship with FDI (Schneider & Frey; Culem, 1988; Billington, 1999). There are a few researchers, though, that do not find a significant relationship between these variables (Nigh, 1985; Tsai, 1994). One of the reasons for this positive relationship is that a high GDP growth rate indicates growing wealth and, hence, disposal income, for a specific country (Globerman & Shapiro, 2003). Another important reason is that a high growth rate means the existence of stable economic policy and efficient government institutions (Mengistu & Adhikary, 2011). The last and most important reason is that if foreign investors see a growing market, they assume it is possible to earn money in that particular country (Billington, 1999).

2.2.2 Economic stability and labour costs

The second economic area is the cost factor for international investors (Dunning, 1973) because of direct foreign investment. Relevant cost factors include economic stability and low labour costs. Labour costs are a controversial topic because there are researchers that found different relationships between labour costs and FDI inflows. It is essential to understand that different approaches to the influence of labour costs on FDI inflows are possible: positive, negative and neutral relationships. First, some argue a positive relationship between labour costs and FDI exists (Swedenborg, 1979; Weeler & Mody, 1992). Foreign investors search for well-skilled workers abroad, who logically demand higher wages (Jaumotte, 2004). Second, other researchers have found a negative relationship between labour costs and FDI inflows(Schneider & Frey, 1985; Shamsuddin, 1994; Pistoresi, 2000). Low labour costs mean fewer production costs for foreign investors (Jaumotte, 2004; Mengistu & Adhikary, 2011). When cheap labour costs are the main reason for FDI inflows, this is known as ‘vertical FDI’. This ‘vertical FDI’ is the case when large international corporations offshore their labour production costs to receive gains that are more substantial. This

phenomenon occurs if corporations prefer low skilled labour. Thus, the demanded labour is not too difficult for local employees, which makes them suitable to execute these jobs. Third, there are researchers that did not find a significant relationship between labour costs and FDI inflows (Owen, 1982; Tsai, 1994). This phenomenon is a result of a combination of a positive and negative relationship between labour costs and FDI inflows. Different preferences may explain this insignificant relationship: some investors search for cheap labour and other investors for well-skilled workers abroad, who demand higher wages. In the end, these different approaches can outweigh each other, which results in a neutral relationship.

Inflation is a sufficient quantitative measure of a country's economic stability. Inflation in this research means price inflation. According to Flemming (1976) p. 5 price inflation is, "the rate at which the general level of prices in [the] economy is changing". Inflation can indicate financial risk for foreign investors (Charkrabarti, 2001). These investors search for host countries that have stable economies because this means low risk for the investors. Researchers agree that inflation has a negative influence on FDI inflows, which means an increase in inflation should lead to a decrease in FDI inflows (Al-Sadig, 2009).

2.2.3 Balance of payments

The third economic area, according to Dunning (1973), is the investment climate. Dunning measured the investment climate by looking at the balance of payments of the host countries. The balance of payments concept refers to current and capital accounts. A general definition of the balance of payments is, "…given by the algebraic sum of the current and capital accounts." (Velaco, 1987, p.272). If there is a significant deficit in the balance of payments, the expenditures exceed the income of the particular country (Schneider & Frey, 1985). This deficit can be dangerous for the movement of free capital; in this case, it is possible that foreign investors will not receive their investments back. These foreign investors are averse to this kind of financial risk. In addition, this financial risk for foreign investors exists because the balance of payments in host countries is a currency risk. For example, significant deficits in Southeast Asian countries can lead to a decrease in value of their currencies. Therefore, some researchers found a positive relationship between investment climate and FDI inflows (Dunning, 1973; Schneider & Frey, 1985). If this is the case when a balance of payments of a country is positive, and perhaps this positive result increases, FDI inflows increase as well (Dunning, 1973; Schneider & Frey, 1985).

2.2.4 Trade openness

Trade openness or openness of the economy is a popular concept in the world of FDI. The concept of trade openness is sufficiently explained by Harrison (1996) p. 420-421, "The concept of openness, applied to trade policy, could be synonymous with the idea of neutrality. Neutrality means that incentives are neutral between saving a unit of foreign exchange through import substitution and earning a unit of foreign exchange through exports. Clearly, a highly export-oriented economy may not be neutral in this sense, particularly if it shifts incentives in favour of export production through instruments such as export subsidies. It is also possible for a regime to be neutral on average, and yet intervene in specific sectors….". It is related to the extent that countries trade with foreign countries (Singh & Jun, 1999). Export orientation is found to be necessary in order to attract FDI. Sekkat & Veganzones-Varoudakis (2007) concur and support that the openness of the economy should be enlarged by host countries to make their economies more attractive to foreign investors. They make this recommendation based on the outcome of their research that indicates that trade openness increases the amount of FDI inflows (Sekkat & Veganzones-Varoudakis (2007). Thus, there is a positive relationship between the openness of the economy of host countries and the FDI inflows from other countries.

2.2.5 Return on investment

The last crucial economic factor that influences the final destination of FDI inflows is a return on investment. Researchers are divided on the relationship between these two variables. On one side, some researchers argue in favour of a positive relationship between FDI inflows and return on investment (Schneider & Frey, 1985; Tsai, 1994; Lipsey, 1999). The explanation for a positive relationship is the most obvious one, namely that international investors search for host countries with potential high rates of return. On the other side, some researchers showed a negative relationship between FDI inflows and return on investment (Edwards, 1990; Jaspersen, Aylward & Knox, 2000). This negative relationship is a consequence of the way the relationship was measured. They measured this relationship by taking the real GDP per capita where they assume that a higher GDP per capita should yield less return on investment and therefore GDP per capita and FDI are linked (Asiedu, 2002). This explanation assumes that the relationship is inverse, which leads to a negative relationship. There are also researchers who did not find a significant relationship (Loree & Guisinger, 1995; Wei, 2000). It is worth noting that return on investment is similar to labour costs, this will be explained more extensively further in this research. These two determinants are mentioned separately but return on investment is a method of measuring labour costs or labour productivity.

2.3 Political/institutional factors

2.3.1 Democracy

According to Campbell (2008), there is no consensus about what democracy means. This research follows a general concept that is mainly about the political rights of the citizens regarding the choice of the government. This definition comes from Bühlmann et al. (2008) and has three main concepts: equality, freedom and control. "We define freedom, equality and control as the three core principles of democracy. To qualify as a democracy, a given political system has to guarantee freedom and equality. Moreover, it has to optimise the interdependence between these two principles through control. Control is understood as control by the government as well as control of the government" (Bühlmann et al., 2008, p. 15).

A democratic society is one political factor that is a determinant of FDI inflows. Democratic countries are more able to provide a safe environment for international investors (Jensen, 2003). Jensen (2008) also found that democratic countries are capable of receiving 70 per cent more FDI than non-democratic countries. The main reason is that foreign investors foresee less danger of losing their investments in democratic countries than in non-democratic countries (Shah, 2017). This argument assumes that there is a positive relationship between democracy and FDI. However, there are also reasons to assume that there is a negative relationship. Other research found a negative relationship between these variables. For example, Li & Resnick (2003) showed that under certain circumstances democracy could lead to less FDI inflows, for example, democratic governments are less open to foreign investors because they prefer to protect their domestic industries from foreign interests from meeting the interests of the domestic voters. These outcomes are examples of the influence of democracy on FDI.

On the contrary, Oneal (1994) measured no influence of democracy on FDI inflows. An explanation for this outcome could be the positive and negative influences of democracy on FDI in flows outweigh each other. Busse (2003) found that there was no relationship between democracy and FDI inflows in the 1970s. An explanation for this could be that FDI inflows was more driven by profit reasons than political reasons. He demonstrated that after the 1970s, there was a positive relationship between democracy and FDI inflows.

2.3.2 The rule of law

The rule of law is an important variable to determine the FDI inflows in a country. According to Stein (2009), the definition of the rule of law is, *"1. The law is superior to all members of society, including*

government officials vested with either executive, legislative, or judicial power. 2. The law is known, stable, and predictable. Laws are applied equally to all persons in like circumstances. Laws are sufficiently defined and government discretion sufficiently limited to ensure the law is applied non-arbitrarily. 3. Members of society have the right to participate in the creation and refinement of laws that regulate their behaviors. 4. The law is just and protects the human rights and dignity of all members of society. Legal processes are sufficiently robust and accessible to ensure enforcement of these protections by an independent legal profession. 5. Judicial power is exercised independently of either the executive or legislative powers and individual judges base their decisions solely on facts and law of individual cases." These rule of law principles have to make sure that individuals have the best chance offered for fulfilling their maximum potential (Stein, 2009). Stein 2009 also mentioned that these principles are 'an ideal' or 'a goal', which is never fully achieved.

For the relationship between the rule of law and FDI to attract FDI inflows, it is crucial to be able to offer investors contract enforcement and property rights (Mina, 2007). When the rule of law is strong, there is less financial risk for foreign investors, so consequently FDI is more likely to increase (Kaufmann et al., 2000). The main reason for this is that foreign investors are deterred enormously if there is any political volatility that may risk the investments of the multinationals. Therefore, a developed administrative set-up that promises stable rules and laws is crucial for foreign investors (Shah, 2017). Globerman & Shapiro (2003) investigated the determinants of United States investors. They demonstrated that the critical determinant on FDI decisions is whether there is an appropriate 'governance infrastructure' including legislation, regulation and legal systems. In practice, when there is a 'good governance infrastructure', less financial and reputational risks for foreign investors exist. Nobody will steal their property because the law protects the corporate property (Globerman & Shapiro, 2003). This argument means that a stronger rule of law attracts more FDI inflows, which means a positive relationship.

An important note I would like to make is about the relationship between the rule of law and human rights because there seems to be an overlap between these two concepts. The fact that human rights are a part of the rule of law became clear in principle number 4 of the definition by Stein (2009): "*4. The law is just and protects the human rights and dignity of all members of society. Legal processes are sufficiently robust and accessible to ensure enforcement of these protections by an independent legal profession."* Peerenboom (2004) investigated the relationship amongst the rule of law and human rights and economic performance. He found that a strong rule of law does not have to promote human rights in a country. Just because it is written down does not mean it is a reality. A strong rule of law does not guarantee anything regarding human rights. Peerenboom (2004) mentioned that this relationship is not about causality, he argues that the rule of law is more

related with economic development (e.g., FDI inflows) instead of human rights and other indicators of well-being, which is why the rule of law and human rights are two separate determinants of FDI.

2.3.3 Human rights violations

The academic literature is quite extensive in explaining the relationship between human rights and FDI. Human rights violations might have an impact on FDI inflows in Southeast Asian countries (Peterson, Murdie & Asal, 2016). There are two main models explaining whether human rights violations affect FDI inflows: the Profit Maximization model and the Risk Mitigating model.

The first explanation, the Profit Maximization model, is more similar to the previously discussed determinants. This explanation assumes that human rights circumstances do not have an influence on the amount of FDI inflows or even have a negative influence on such inflows. This is based upon the idea that foreign investors only care about maximizing their profit. The idea of the conventional wisdom fits within this model. Conventional wisdom argues that investors are well-known to keep down host countries that feature cheap labour and provide freedom for businesses (Hymer, 1982; Smith, Bolyard, & Ippolito, 1999). The industries of developing countries are mostly associated with poor human rights conditions, which make these investors complicit in human rights violations. This Profit Maximization model is a more traditional explanation. It tries to argue that the main aim of international investors is earning as much as possible regardless of local circumstances (Hymer, 1982; Smith, Bolyard, & Ippolito, 1999).

Furthermore, according the Profit Maximization model, it may be advantageous for international firms if human rights of the local citizens are violated (Blanton & Blanton, 2007). These large firms can have an enormous influence on local communities concerning their living conditions when human rights are not protected (Rudel, 1989). Mostly, investors choose countries based on lower-cost manufacturing and resource extraction (UNCTAD several years). The aim of doing this is sometimes to export back to the developed world (Barry et al., 2013). Conventional wisdom argues that investors are well-known to keep down host countries that provide cheap labour and freedom for businesses (Hymer, 1982; Smith, Bolyard, & Ippolito, 1999). The costs for human rights violations do not restrain investors from their nonobservance. The industries of developing countries are mostly associated with poor human rights conditions, which make these investors complicit regarding human rights violations. Therefore, based on this model, the relationship between human rights violations and FDI inflows in Southeast Asian countries is supposed to be negative. This model will be explained more extensively in the theoretical framework chapter. This model was dominant until the early 1990s. After this period, the Risk Mitigating model became more popular.

The second explanation does not only concern financial risk but also reputational risk (Fiordelisi et al., 2014). All the previously discussed economic determinants of FDI inflows focus on financial risk. The Risk Mitigating model is not only concerned with financial risk. According to this model, human rights are entangled with financial and reputational risks because foreign investors do not want to be associated with countries that have poor human rights records (Barry et al., 2013).

If foreign investors are complicit in human rights violations, then it is vital for them to not appear to be in violation. Connections between foreign investors and human rights violations could bring reputational costs for international investors, which is why human rights conditions can be significant (Vadlamannati, Janz & Berntsen, 2018; Barry et al., 2013). Besides, this can lead to a willingness for citizens to change the governments' trade agreements with developed states (Peterson, Murdie & Asal, 2016). However, when a country has negative human rights conditions, there is an elevated reputational risk for foreign investors, which can lead to less foreign investment for a particular country. This danger can be crucial in the final investment decisions of foreign investors (Janz & Berntsen, 2018). This line of reasoning fits within the Risk Mitigating model. From this perspective, international investors are concerned about the living conditions of local communities (Spar, 1998). This means that there should be a positive relationship between human rights conditions and FDI inflows. This model will be explained further in the theoretical framework chapter.

2.3.4 Corruption

Another important institutional factor to take into account is corruption because it is a severe obstruction for FDI (Wei, 2000). The research of Bénassy-Quéré, Coupet & Mayer (2007) confirmed the theory of Wei (2000). The conclusion is that more corruption within a country has a negative influence on FDI. Because this research is similar to the research of Blanton & Blanton (2007), it is valuable to mention that they did not consider corruption as a control variable.

Corruption appears to overlap with the rule of law. Other studies demonstrated that effects of corruption depend on a country's rule of law (Houston, 2007; Stansel, 2007). In addition, Houston (2007) confirmed that corruption could have a positive effect on economic growth if there is a weak rule of law within a country. Al-Sadig (2009) revealed the negative impacts of corruption on FDI inflows. However, Al-Sadig (2009) suggests that a negative relationship disappears when he controls for the institutional quality and the rule of law. The disappearance of a negative relationship means that international investors value the rule of law more than corruption, which does not exclude corruption from being an important control variable.

Chapter 3. Theoretical Framework

3.1 Theories

As discussed previously, two main models describe the relationship between human rights and the attractiveness for FDI inflows. The first model, the Profit Maximization model argues for a negative relationship between human rights and FDI inflows. The second model, the Risk Mitigating model states there is a positive relationship between human rights and FDI inflows. These two models will be explained more extensively in this chapter.

3.1.1 Profit Maximization model

For a very long time, human rights were not a reputational risk for foreign investors. The reputational risk was not an issue for determining where to invest. Lenin (1999) argues that firms are forced to invest abroad if the home market stagnates. The main aim of this was earning as much profit as possible without regard for local citizens. In other words, the absence of human rights conditions is useful for economic gains of foreign investors (Blanton & Blanton, 2007). In order to achieve this, companies chose countries to invest in based on their estimation of whether the citizens are easy to control. Capital globalisation is essential for establishing that local citizens become dependent on the large international firms, which used all the resources and labour for their profit (Santos, 1970). The factor dependency is crucial, because by keeping the poorest and most vulnerable people under control, these firms can keep their dominance (Hymer, 1971). This led to a situation where local communities lost their independence because foreign investors and local elites preferred economic profit more than the rights of local people (Evans, 1979). This phenomenon connects with the dependency theory, where developing countries became dependent on the more developed countries because the system focuses on maintaining the power of the rich countries, which is known as 'neo-colonialism' (Shohat, 1992). The elites also benefit from the gains of the foreign investors, which is why these foreign investors can enjoy a favoured position -- their interests and concerns are taken more seriously than those of local communities (Evans, 1979).

Firms prefer to avoid rebellions against injustices of the capitalist system. Therefore, they conspire with repressive regimes of host countries. In the end, this will lead to support of repressive regimes that are responsible for violations of human rights in host countries by international firms (Blanton & Blanton, 2007). This situation is the opposite of corporate social responsibility, which is explained by the Risk Mitigating model. Often, certain domestic groups in a host country receive a disproportionate gain from FDI, which is why this group is also willing to listen to the interests of the

foreign investors to maintain the foreign investment (Maxfield, 1998). From another point of view, authoritarian regimes mostly keep down the opposition to protect the cooperation with foreign investors (Rudel, 1989). Consequently, foreign investors primarily choose which countries to invest in based on the political possibilities and public participation. These possibilities are the greatest in countries that repress the human rights of its citizens. Furthermore, foreign investors may fear political opportunities for local citizens (e.g. freedom to protest) because this may affect the power of foreign investors. For example, local citizens may protest against their repression in order to give less power to international corporations, which can lead to less influence of foreign investors. This uncertainty of foreign investors will not exist if citizens are repressed and controlled. The abuse of human rights is helpful to encourage foreign investors. Furthermore, the abuse of human rights is helpful to maintain the power of these foreign investors (Blanton & Blanton, 2007). This situation will lead to what is called a 'haven for international firms'.

When firms have deeply invested themselves in countries based on low labour costs, this is often surrounded by circumstances of human rights violations. However, firms can have a loud voice in order to maintain the neglect of human rights. At this stage, some researchers argue that FDI inflows became an independent variable instead of a dependent variable. If this is true, this means that FDI inflows can influence abuse of human rights (Kim & Trumbore, 2010). Although the impact of FDI inflows on human rights is not within the scope of this thesis, it is crucial to take into account how relationships can go both ways. This is called a 'reverse relationship', which means that the independent variable may affect the dependent variable, and vice versa.

To conclude, the Profit Maximization model suggests the existence of a negative/neutral relationship between human rights conditions and FDI inflows within the borders of a country. This theory was dominant until the early 1990s. Human rights were not commonly discussed during this period. The economic importance of production and labour costs were viewed as more essential than human rights circumstances during this period (Spar, 1999).

3.1.2 Risk Mitigating model

Compared to the previous model, the Risk Mitigating model is currently more applicable because it shows a detrimental side of the Profit Maximization model (Blanton & Blanton, 2007). A negative aspect is when large international investors become associated with human rights violations in the host countries. In a worst-case scenario, the international investor may be responsible for maintaining human rights violations (Dalsrud, 2008). In that case, reputational risk becomes reputational damage for the foreign investors. For example, the market can determine to not

support these foreign investors, which will lead to less profit. This signal from society can also lead to reputational damage (Spar, 1998).

The Risk Mitigating model acknowledges risks firms will face if they abuse human rights. There is a lot of evidence that foreign investors are responsive when they have to deal with condemnations regarding their attitude about human rights, which helps support this theory (Lydenberg, 2005). It is important to note that human rights became more important since the 1990s because that period is more applicable to this thesis (2003 to 2017). Human rights became more important for investors and customers. Consequently, customers are less likely to buy products from firms that support abuse of human rights, which is why firms have a huge problem when they are associated with human rights violations (Blanton & Blanton, 2007).

So far, this section explaining the Risk Mitigating model was about the danger for investors to become associated with human rights violations. However, there is also another motivation for foreign investors to avoid investing in countries where human rights are not respected. This motivation is more intrinsically sound, international investors firmly believe that they should not encourage human rights abuses by investing in countries with poor human rights records (Dalsrud, 2008). A well-known term is associated with this conviction, namely 'corporate social responsibility'. According to the Commission of the European Communities (2001), the explanation of corporate social responsibility is, "A concept whereby companies integrate social and environmental concerns in their business operations and their interaction with their stakeholders voluntarily". This concept relates to the Risk Mitigating model because it assumes that international firms have respect for human rights of local citizens. However, most researchers use the concept from the World Business Council for Sustainable Development (1999), "The commitment of business to contribute to sustainable economic development, working with employees, their families, the local community and society at large to improve their quality of life". This concept pays closer attention to the society and local community. This concept is perfectly imbedded within the Risk Mitigating model since it assumes that international investors emphatically believe that they should act in a moral way. In order to act in morally, it is essential for an international investor to understand their social responsibility; especially, because their behaviours can affect the lives of many local citizens.

In the previous section, it was stated that the Profit Maximization model was more applicable until the early 1990s. Currently, the Risk Mitigating model is more applicable because the attitude of society and the foreign investors towards human rights issues has changed. As a consequence the risk for reputational damage for the foreign investors has increased. (Lydenberg, 2005). Until the

1990s, corporate social responsibility was not commonly discussed; firms did not carry out activities that helped local communities. However, this attitude changed since the late 1990s since many parts of society, including governments, investors, citizens and non-governmental institutions have started to support corporate social responsibility. Furthermore, the majority of these groups agreed that international corporations have to care for local citizens (Lydenberg, 2005). Labour costs became a less important component of production costs because manufacturing has increased which requires well-educated and high-skilled labour (Spar, 1998). Quality became more important compared to the previous century (Spar, 1998). Corporations are now more interested in countries with high quality of labour instead of countries with that offer cheaper wages. A motivating factor is that the success of international investors in a country is higher if no violation of human rights occurs (Blanton & Blanton, 2007). When a country respects the human rights of its citizens, the people's willingness to contribute to the performance of their country is increased. Different researchers showed that respect of human rights of citizens improves the economic performance (Isham et al., 1997). Respect of human rights has several advantages, such as the improvement of the efficiency of work activities and level of education. Furthermore, respect for human rights in host countries increases the FDI inflows by promoting the quality of human capital (Jensen, 2003).

Overall, according to this Risk Mitigating Model, the relationship between human rights and FDI inflows, is supposed to be positive. Therefore, the better human rights conditions are within a country, the higher the FDI inflows are. The concept of human rights includes human rights violations, which is essential for the direction of the relationship within the conceptual model. According to the theory, this research assumes that the Risk Mitigating model is correct in present circumstances, the relationship should be positive between human rights and FDI inflows because better human rights circumstances mean higher FDI inflows. However, this research uses human rights violations as the concept of human rights, which assumes that more human rights violations mean less FDI inflows. Therefore, the relationship, which is still based on the Risk Mitigating model, is changed from positive to negative.

In order to avoid an extensive debate regarding the existence of human rights and when human rights violations take place, this research uses a legal basis to define human rights. This legal basis comes from the United Nations, the Universal Declaration of Human Rights (UNDHR, 1948), which is in the International Human Rights Documents (2018). This declaration consists of thirty articles that describe all rights human beings have. If states do not respect one of the articles in this declaration, then the human rights of its citizens are violated.

3.2 Conceptual Model

This research investigates the relationship between human rights conditions and the FDI inflows in developing countries. The main aim of this research is to determine which theory: Profit Maximization model or Risk Mitigating model, explains the findings of this analysis.

The economic determinants: market size, market growth, economic stability, the balance of payments and trade openness are viewed as control variables. It is valuable to mention that this research does not view the return on investment as a control variable because there are measurement problems. Many researchers chose to measure the return on investment by the real GDP or real GDP per capita (Edwards, 1990; Jaspersen, Aylward & Knox, 2000; Asiedu, 2002). However, this is similar to the measurement of market size, which is also measured by GDP. Therefore, return on investment will not be used further in this research.

In addition, labour costs will not be included in this research. Two reasons are responsible for this exclusion: unclear literature and lack of data. First, the literature is not clear regarding the relation between labour costs and foreign investors. There are too many reasons why investors consider labour costs when investing in a country. Second, there is a lack of data, which makes it impossible to measure the labour costs of all the developing Asian countries. Furthermore, the concept of economic stability will be called inflation because the direction of the relationship is inverse when it becomes inflation that is why the conceptual model uses inflation, which gives a negative relationship instead of a positive relationship.

Another important note is related to the function of the political/institutional variables. First, this research does not use corruption as a control variable because of the overlap between corruption and the rule of law. Therefore, it should be sufficient to use the rule of law within this research because corruption is already a part of the rule of law. Second, the remaining two political/institutional variables, democracy and the rule of law, are other independent variables in this research. The reason to use them as an independent variable instead of as dependent variables is because of the possibility that they co-vary with human rights conditions. Therefore, the decision is made to not use all the political/institutional variables as control variables but as independent variables, which will determine which independent variable is the most decisive for foreign investor's choice to invest in a country.

Based on the following three hypotheses, a conceptual model is visible on the next page:

Hypothesis 1:

H_0: There is no relationship or a positive relationship between human rights violations and FDI inflows.

H_1: There is a negative relationship between human rights and FDI inflows.

Hypothesis 2:

H_0: There is no relationship or a negative relationship between the rule of law and FDI inflows.

H_1: There is a positive relationship between the rule of law and FDI inflows.

Hypothesis 3:

H_0: There is no relationship or a negative relationship between democracy and FDI inflows.

H_1: There is a positive relationship between democracy and FDI inflows.

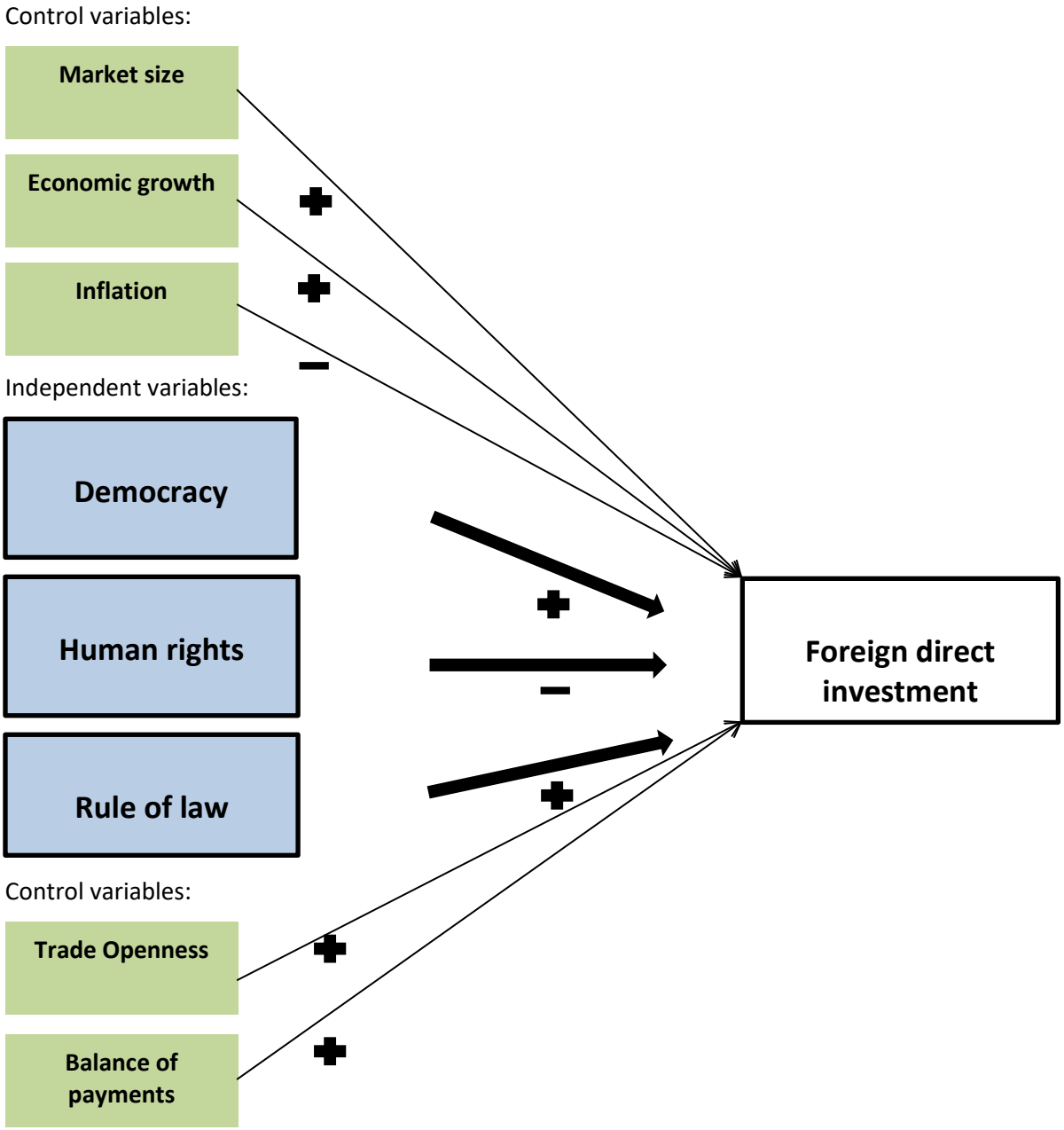

Figure 3: Conceptual model

Chapter 4. Research Design and Methodology

4.1 Methods and techniques

4.1.1 Quantitative research

In order to choose the right research design, the focus is on the causal relationship between the independent variables and the dependent variable. Different methods are possible in order to establish a relationship between human rights violations and FDI inflows.

The first necessary choice is to choose between quantitative and qualitative research. The benefit of a qualitative design is a high internal validity, which means that there exists high confidence in the causality between the independent and dependent variable. However, in this case, research has to be appropriate for a small-N analysis. In order to explain the relationship between human rights violations and FDI inflows in the all of Southeast Asia, qualitative research does not provide enough information for a generalized answer. Therefore, based on the availability of quantitative data, this research uses a quantitative research design.

4.1.2 Panel data

A lot of data is necessary to answer the research questions. Therefore, this research uses a panel data set. Panel data research is a combination of a time-series and a cross-sectional research design (Hsiao, 2005). This design is a combination of cross-sectional and longitudinal designs. The reason to choose a panel data research is not just because it is appropriate to answer the research question and hypotheses; it is also that the combination of a time-series and a cross-sectional design provides some advantages. First, the numbers of observations increase in a panel data design, which is necessary to be able to provide reliable and valid results (Hsiao, 2005). Second, panel data research can include other variables. Therefore, this research uses control variables to verify that the relationship between the independent and the dependent variables is not confounded by other factors (Hsiao, 2005).

4.2 Population and sample

The period for the time-series section is from 2003 to 2017, which is 15 years in total. Two reasons support the choice for this period. First, according to the theory discussed in chapter 3, Risk Mitigating model should be more applicable during a recent period (Spar, 1998; Dalsrud 2008). Second, this period is the most recent 15 years available to investigate the influence of political factors on the FDI inflows. Furthermore, during this period, more data is available for each of the variables than in earlier periods, which creates less bias.

This research focuses on the developing countries in Southeast Asia, which provide enough relevant data. The main advantage of focusing on Southeast Asian countries is the increase in internal validity. The definition of the internal validity, according to Heale & Twycross (2015) is, "the extent to which a concept is accurately measured in a quantitative study" (p.66). By focusing on the Southeast Asian countries, internal validity increases because this part of Asia is different from other parts of Asia, for example, Asian countries in the Middle East. The allocation of countries to Southeast Asia and developing countries follows the classifications by the World Bank. Besides the determinants mentioned in this research, FDI is also dependent on the contextual situation. Developing Southeast Asian countries that are similar and are in the same situation are therefore suitable to take as the research cases. By doing this, this research controls for factors, which may influence contextual situations in Southeast Asia. The choice to focus on developing countries was based on the importance of FDI inflows for developing countries (Barry et al., 2013). According to the World Bank, Malaysia is an upper middle-income country and thus, is excluded from this research.

The next 15 countries are the research cases: Afghanistan, Bangladesh, Bhutan, Cambodia, China, India, Indonesia, Laos, Myanmar, Nepal, Pakistan, Philippines, Thailand, Timor-Leste and Vietnam. This research does not include Sri Lanka; the main reason for its exclusion is the lack of data for a few variables in this research. To conclude, because of a mix between time-series and cross-sectional approaches, 225 observations will be incorporated in this research. This number of observations results from multiplying 15 countries by 15 years.

For this research, secondary data is necessary, which means that all public data that is available and appropriate will be used. Examples of this public data that were helpful are the World Bank, IMF and the Economist. The programs SPSS and STATA will perform the data analysis for this paper. With SPSS

Statistics 23.0, the statistic technics correlation will be used to examine the relationship between the independent variables and the dependent variable. STATA will test the final regression model.

4.3 Operationalisation

Foreign direct investment (FDI)

FDI inflows is the dependent variable in this research. For this research, it is about FDI inflows to Southeast Asian developing countries. This research uses data from the World Bank in order to measure the FDI inflows: Foreign direct investment, net inflows (percentage of GDP). The exact definition according to the World Bank is, "Foreign direct investment are the net inflows of investment to acquire a lasting management interest (10 per cent or more of voting stock) in an enterprise operating in an economy other than that of the investor. It is the sum of equity capital, reinvestment of earnings, other long-term capital and short-term capital, as shown in the balance of payments. This series shows net inflows (new investment inflows less disinvestment) in the reporting economy from foreign investors, and is divided by GDP" (World Bank, 2019A). The other measurement that the World Bank uses for FDI inflows is the total FDI inflows as a result of the BoP (Balance of Payments) in current US dollars. This measurement does not reflect the size of a country, which is vital for total FDI inflows.

Human rights violations

Human rights violations are the primary independent variable in this research. There are many methods to measure the presence or absence of human rights in countries. Similar research by Blanton & Blanton (2007), measured human rights from two indicators, data from Amnesty International and U.S. State Department *Country Reports.* They used the Political Terror Scale (PTS). Different researchers have developed this scale (Stohl & Carleton, 1985; Poe & Tate, 1994; Gibney & Dalton, 1997). PTS is a narrowed version of human rights, which focuses mainly on personal integrity rights but also political freedom, murder and torture (Blanton & Blanton, 2007). The main advantage of using PTS as a measurement of human rights is that it is not highly correlated with other (political) variables which may explain FDI inflows.

Repression is broader than the Political Terror Scale (PTS) since the use of violence and intimidation belongs to broader political aims (Tilly, 1978; Haschke, 2018). The PTS captures a part of repression (Political Terror Scale, 2019). This method of measurement compared to the measurement of the Freedom House civil liberties, like Gastil (2008) has done before, then the Freedom House includes more aspects of human rights such as freedom of assembly and speech (Blanton & Blanton, 2007). A

democracy also includes these freedoms; this research measures democracy as a separate independent variable of FDI. PTS will be used as the indicator to measure levels of human rights violations. The scale is from 1 (no violation) to 5 (abundant violation). The PTS measurement consists of three sources: 1. Amnesty International, 2. U.S. State Department, 3. Human Rights Watch. Because of the lack of data from the Human Rights Watch, the average of Amnesty International and the U.S. State Department determines the score of the PTS.

Democracy

Democracy is an independent variable, which tries to explain change in FDI inflows. For hypothesis 3, the relevant democracy indicator comes from the Economic Intelligence Unit (EIU, 2019A). The EIU uses a democracy index to rank the records of democracies in countries. There are five factors that determine the final score of this democracy index: 1. electoral process and pluralism, 2. civil liberties, 3. the functioning of government, 4. political participation, 5. political culture. Furthermore, the EIU features a complete dataset that contains more data than other democracy indexes. The overall score is on a scale from 0 (no democracy) to 100 (full democracy) (EIU, 2019A).

The rule of law

The rule of law is an independent variable in this research. The source for the rule of law is the same as democracy, namely the Economist Intelligence Unit (EIU, 2019B). This rule of law index determines an overall score for countries based on eight different factors: 1. violent crime, 2. organised crime, 3. fairness of judicial process, 4. enforceability of contracts, 5. speediness of judicial process, 6. confiscation/ expropriation, 7. intellectual property rights protection, 8. private property protection. The indicators range from 0 (bad) to 1 (excellent). The main advantage of the EIU is the availability of the data. In comparison to other rule of law indexes, such as International Country Risk Guide (ICRG) and World Justice Project (WJP) the EIU dataset is a more complete dataset (EIU, 2019B).

Market size

Market size is one of the control variables in this research. In order to measure the market size, the real GDP is a suitable indicator. Data from the World Bank is used to measure the real GDP. The main advantage of real GDP over nominal GDP is related to inflation, by controlling for inflation real GDP is more appropriate. Therefore, it should be measured by constant prices. This research uses data from the World Bank, and the data is in constant US dollars with 2010 as the base year (World Bank, 2019B).

Economic Growth

Economic growth is a control variable in this research. This research uses data from the World Bank in order to measure economic growth. The GDP annual growth rate is an indicator of economic growth. The definition of GDP is an, "Annual percentage growth rate of GDP at market prices based on constant local currency. Aggregates are based on constant 2010 U.S. dollars. GDP is the sum of gross value added by all resident producers in the economy plus any product taxes and minus any subsidies not included in the value of all the products. It is calculated without making deductions for depreciation of fabricated assets or depletion and degradation of natural resources" (World Bank, 2019C).

Inflation

For this research, inflation is a control variable. Data from the World Bank measures inflation. The World Bank defined inflation as, "measured by the consumer prices index reflects the annual percentage change in the cost to the average consumer of acquiring a basket of goods and services that may be fixed or changed at specified intervals, such as yearly" (World Bank, 2019D).

Balance of payments

Data from the World Bank is used to measure the BoP of Asian developing countries. The World Bank defined the BoP as the, "Current account balance is the sum of net exports of goods and services, net primary income, and net secondary income " (World Bank, 2019E). The current account as a percentage of GDP is the indicator for measuring the BoP. The current account gives an indication to what extent the BoP is out of balance.

Trade openness

Trade openness is the last control variable in this research. Different measurement methods are appropriate to measure trade openness. This research follows the reasoning of the World Bank to measure the openness of the Southeast Asian countries towards other countries. This openness is total trade as a percentage of the GDP, The World Bank defined this indicator as follows, "Trade is the sum of exports and imports of goods and services measured as a share of gross domestic product" (World Bank, 2019F).

4.4 Statistical model

4.4.1. Linear Panel Regression Model

This paper investigates figures, which change through time and amongst different countries. The best way to answer the research question is by using a multivariate regression model. Furthermore, a panel data design demands for a complex regression formula because it has to include cross-sectional and time-series elements. By making use of this method, this research can control for multiple confounding variables. The following general formula illustrates how this method works in practice:

$$Y_{i,t} = \beta_0 + \beta_k X_{i,t} + \beta_c X + \varepsilon_{i,t;} \quad i = 1,..; t = 1,\ldots$$

This general regression formula consists of several signs (Graddy & Wang, 2008). The sign Y represents the dependent variable; sign X is the explanatory variable for the independent and control variables. The little sign *i* stands for the cross-sectional part of this analysis. The little sign *t* stands the for the time-series part of this analysis. Sign β_0 represents the constant factor. β_0 provides the value of the dependent variable when the other independent and control variables are zero. β_k is the coefficient for the independent variable; β_c is the coefficient for the control variables. The last sign in this regression formula is ε. This sign stands for the error term in the dataset; this is a random effect on the dependent variable. $\varepsilon_{i,t}$ consists of the sum of two factors. First μ_i is an observable effect of the excluded individuals in the equation. Second, v_{it} stands for the error varying with the individuals and through time (Baltagi, 2008).

The translation of a general formula towards a specific formula leads to the following three regression formulas. For each of the independent variables, this paper uses one regression formula. With the help of these three regression formulas, it is possible to evaluate the relationship between the variables:

1. $FDI\ inflows_{i,t} = \beta_0 + \beta_2 * Human\ rights\ scale_{i,t} + \beta_c * Market\ size + \beta_c * Economic\ growth + \beta_c * Inflation + \beta_c * Balance\ of\ payments + \beta_c * Trade\ openness + \varepsilon_{i,t}$
   i=1,2……..225; t=2003,2004,……,2017; c= coefficient for control variable

2. $FDI\ inflows_{i,t} = \beta_0 + \beta_2 * Rule\ of\ law_{i,t} + \beta_c * Market\ size + \beta_c * Economic\ growth + \beta_c * Inflation + \beta_c * Balance\ of\ payments + \beta_c * Trade\ openness + \varepsilon_{i,t}$
   i=1,2……..225; t=2003,2004,……,2017; c= coefficient for control variable

3. $FDI\ inflows_{i,t} = \beta_0 + \beta_2 * Democracy_{i,t} + \beta_c * Market\ size + \beta_c * Economic\ growth + \beta_c * Inflation + \beta_c * Balance\ of\ payments + \beta_c * Trade\ openness + \varepsilon_{i,t}$
   i=1,2……..225; t=2003,2004,……,2017; c= coefficient for control variable

4.4.2 Assumptions (OLS panel data)

The first research method is the Ordinary Least Squares (OLS). The OLS is a proper manner to estimate the coefficients of the variables if this regression model meets the required five main assumptions (Kennedy, 2008). According to Graddy (1999), this paper adds two simple assumptions. The first of these is that all variables in this research have to be metric, so this includes dependent, independent and control variables. The answer to this assumption is quite easy. All the indicators of the variables are metric, so none of them are a nominal variable. So, this assumption is not violated. The second extra assumption, according to Graddy (1999), is related to the total number of observations. In practice, the total number of observations has to be higher than the total number of independent variables. This research consists of 225 observations for three independent variables. So, this assumption is not violated.

According to Kennedy (2008), there are five main assumptions that have to be met for OLS panel data research. These five assumptions are 1. Linearity 2. No autocorrelation 3.Homoscedasticity 4. No multicollinearity 5. Normality. These five assumptions require a broader explanation than the other two assumptions from Graddy (1999).

4.4.2.1 Linearity

This assumption means that the dependent variable is in a regression formula as a linear function of the independent variables and the error term (Kennedy, 2008). The most straightforward manner of testing the linearity is to use scatter plots for each independent and control variable (IDRE, 2017). In Appendix I, all the scatter plots are shown to illustrate whether the independent and control variables have a linear relationship with the dependent variable, FDI inflows. Practically all the scatter plots, which are visible in Appendix I, show a linear relationship between FDI inflows and the other measured variable. Therefore, based on these scatter plots, it is arguable that the assumption of linearity is not violated.

4.4.2.2 Normality

Normality is the assumption that the dependent variable of the dataset and all the error terms have to follow a normal distribution. There are different ways to measure whether there is a normal distribution. This paper tests the normality by looking at a histogram and a linear graph to check how the different variables and the error terms are distributed (IDRE, 2017). The histogram should illustrate a normal distribution. Appendix I shows the histogram and the line graph. This histogram displays a normal distribution of the dependent variable. Furthermore, the second line graph shows that all the residuals cluster approximately around the line. So these error terms do not deviate

much from the straight line. These two results together demonstrate that the dataset of this research is distributed normally, which indicates that the normality assumption is not violated.

4.4.2.3 No multicollinearity

The assumption of no multicollinearity means that multicollinearity may not exist amongst the different independent and control variables. So, these variables are not allowed to be highly correlated to each other, and therefore, there a linear relationship must not exist between any of the independent and control variables (Kennedy, 2008). Two different approaches are appropriate to test the assumption of multicollinearity, first by examining at the correlation coefficients and second by observing the VIF values.

Appendix III presents the results of the correlation method test in the table. In this table, the correlation between the different independent and control variables are visible. None of these correlations shows a very high correlation that may suggest multicollinearity. The strongest correlation in this table is the relationship between the human rights scale and trade openness with a negative correlation of .503. However, this value is still too low to argue that this correlation is a linear relationship that consists of perfect multicollinearity. The weakest correlation is between inflation and economic growth; this is a negative correlation of .005. So based on observations of correlations, the coefficients do not show high values of correlations between the independent and control variables. Therefore, this will not have a significant impact on the results of this research.

The second method that is appropriate for testing this assumption is to look at the values of the Variance Inflation Factor (VIF). The table below in Appendix III shows the VIF values for all the independent and control variables. If a VIF value is higher than 10, there may exist collinearity between these variables (IDRE, 2017). The variables of this research, according to the table, do not show high VIF values. All of the values are below 10 and closer to 1; this is similar to the result of the previous multicollinearity test, the correlation test. Based on similar results, the conclusion is that the assumption of no multicollinearity is met between the independent and control variables.

4.4.2.4 Homoscedasticity

The fourth assumption is the assumption of homoscedasticity. This assumption test whether the variance of the residuals is constant, or whether there is heteroscedasticity, which exists when the variance of the residuals varies, if heteroscedasticity comes forward in the dataset this assumption is violated (Kennedy, 2008). The easiest way to test homoscedasticity is to plot the residuals against the predicted values. At the end of Appendix I, this plot is shown. Unfortunately, it is possible to observe a pattern of the residuals and the predicted values. The distribution to the left side of the plot is

unequal to the right side of the plot. Therefore, for this research, the assumption of homoscedasticity is violated. In order to be able to execute a proper regression analysis, a robust command is necessary to tackle the presence of heteroscedasticity. This robust command will be explained further in section 5.3.

4.4.2.5 No autocorrelation

The fifth and last assumption is no autocorrelation; this assumption concerns the residuals not being correlated to each other (Kennedy, 2008). This phenomenon occurs a lot in research with time-series data. To check whether there is the presence of autocorrelation, the most common test in SPSS is the Durbin-Watson test. The Durbin-Watson test consists of a value between zero and four. A value around two means there is no autocorrelation, a value closer to zero means positive correlation and a value closer to four means negative correlation. In this case, the Durbin-Watson test scores a value of 0.456. This score is relatively low, which means a positive correlation between the residuals. This positive correlation often happens during a time-series analysis. The Wooldridge test is another method to test this assumption. This method is appropriate to test the autocorrelation in a panel data set because of its flexibleness (Drukker, 2003). The Wooldridge test presented a p-value of .2141. The null hypothesis of no autocorrelation has to be confirmed, because the P-value is higher than 0.05. Surprisingly, this result contradicts the result of the Durbin-Watson test. Since the Durbin-Watson test contradicts the results of the Wooldridge test, it is not without a doubt that the assumption of no autocorrelation can be met and, thus, the assumption of no autocorrelation is violated.

Unfortunately, violation of some assumptions occurred (homoscedasticity and no autocorrelation). Therefore, we can assume that Pooled OLS is not the best method for estimation in this case. Furthermore, the pooled OLS method measures all the 225 observations in this research together. The most serious issue concerning the pooled OLS method is that this method does not distinguish between the different Southeast Asian countries and the different years. This is known as ‘pooling’, all the observations end in the same ‘pool’, which means that spatial and temporal differences among and within countries are not visible and measured. This method does not take into account the heterogeneity or individuality, which may exist amongst these 15 different countries. This research will check for other methods of estimation to see if they are more applicable. Two other methods which are well-known in Panel Data analysis are fixed effects estimation (FE) and the estimation of the random effects (RE).

4.4.3 Fixed and Random effects estimation

The previous part concluded the shortcomings of the pooling OLS method. As a consequence, there are two other options to estimate the variable's coefficient that need to be considered:

1. Fixed effects estimation (FE)
2. Random effects estimation (RE)

1. Fixed effects estimation

In research where the focus is on a specific group of observations combined with a time series dimension, the fixed effects estimation (FE) method is a suitable way to estimate the variable's coefficient (Baltagi, 2008). This research did not choose the 15 Southeast Asian countries randomly, but they were chosen because of the 1) importance of FDI in this region and 2) the availability of data. FE is a popular method used in panel data analyses because it controls for country-level variation. The dataset can differ over time; for example, FDI inflows in 2003 can differ from FDI inflows in 2014. The FE estimation model aims to investigate unobserved factors that are not of main interest but still could influence the results. FE models control for unobserved country-level effects, which allows researchers to study temporal variation. Based on the dataset, the FE model would fit within this research because the countries are not chosen randomly. Furthermore, the FE model is used often because it solves problems concerning violations of the OLS assumptions, see section 4.4.2 (Best & Wolf, 2014).

2. Random effects estimation

The second appropriate method to use for panel data research is the RE method. This method uses a Generalized Least-Squares (GLS) estimation. Compared to the FE method, the RE is more applicable to datasets if the observations are chosen randomly from a large population. So, if a research question aims to reach conclusions from a large population and this sample is a representation of a larger population, then the RE method is an appropriate way to carry out this task. The main difference between FE and RE, RE also measures the individual effect of the data variables. This means that RE not only measures changes across time like FE, but RE also measures differences across the individual values of the dataset. For this particular study, the differences across individual values are the variations between countries. So, RE focuses more on individual changes compared to the FE method. For example, this means that the level of democracy in India, which is relatively high in 2003, will probably also be relatively high in 2012. This phenomenon exists because of the differences in individual values (countries).

The main advantage of the FE method for this research is that the FE method does not assume that the dataset is from a random sample. However, the RE method measures differences in time and

countries which is a better fit for this research. Both have their advantages. Because of the violations of the OLS assumptions, this research will make uses of FE and RE estimation methods. Still, according to the theories of the estimation models (Hoechle, 2007), a Hausman test has to decide which manner (FE or RE) is the most suitable approach concerning this case. Section 5.3 shows the result of the Hausman test.

4.5 Reliability and validity

According to Heale & Twycross (2015), reliability relates to the consistency of a measure. For reliability, it is crucial that this research executes the analysis without the presence of random measuring errors. Therefore, it is necessary that research is repeatable; the measuring instrument has the same results when there are more measurements. The fact that this paper measures a long period and many countries from the same region should mean high reliability. The only point that negatively influences the reliability is the fact that there are countries in south and East Asia that did not publish enough data. The democracy index is the indicator that has the most missing data, primarily from 2003 to 2005. Data from the democracy index is available from 2006 to 2017. Twelve years are measured which means the outcome will not be influenced significantly by the missing data.

This research focuses on Southeast Asia, which means the outcomes are less generalizable towards other parts of the world. The main reason for this is the context-dependent circumstances for FDI, which also is influenced by the region of a country in the world. The fact that this research is less able to be generalized influences external validity. The study region is quite large and the outcomes of this research may be similar to other developing countries around the world. The internal validity is already described in section 4.2 (population and sample).

There are three main types of validity. First, the content validity that tests whether the measurement of the variables covers the entire variable. This research uses well-known scales (PTS, the rule of law index and democracy index), which measures many factors to determine the final value of the variable. Evidently, this research is reliable concerning content validity. Second, construct validity is the extent to which the intended construct is measured. Because of the data that this research uses and the availability of this data for countries in east and south Asia, the construct validity is strong. Third, the criterion validity is about the extent the outcomes of this research are similar to other research outcomes. This criterion validity will become apparent in the analysis and the conclusion chapter.

Chapter 5. Research findings and analysis

5.1 Descriptive statistics

5.1.1 Descriptive analysis in general

This research uses data from 15 countries from east and south Asia for a period of 15 years, from 2003 to 2017. The programs IBM SPSS 23.0 and STATA execute different calculations to answer the research question and the sub-questions. Table 1 provides information about the descriptive statistics of the variables in this paper. This descriptive table gives a helpful insight into the values of the variables if we discuss the order of magnitude.

	N	Minimum	Maximum	Mean	Std. Deviation
Observations (15 countries x 15 years)	225	2003	2017	2010	4,33
FDI Inflows	225	-0,65	14,26	2,71	2,82
Human rights scale	225	1,0	5,0	3,4	0,98
Rule of law index	203	0,03	0,66	0,32	1,29
Democracy index	180	17,7	79,2	47,3	17,76
Inflation	223	-18,11	36,59	6,18	5,59
Trade openness	224	0,17	200,38	77,43	43,21
Economic growth	225	-26,05	64,07	6,79	6,49
Market size	225	888427847	10161000000000	653687747539,37	1671740751380,79
Balance of payments	214	-28,91	46,04	-0,56	11,20

Table 1: Descriptive statistics

Table 1 illustrates information about the number of observations (N), the minimum and maximum, the average and the standard deviation of the variables. Some numbers stand out in this table. The human rights scale, which is from 1 till 5, is relatively high because the mean is 3,4 where the average is typically expected to be around 2,5. In addition, the rule of law index scores are relatively low; the scale is from 0 till 1. The mean is 0,32, which is less than the middle of 0,50. Afghanistan has the lowest rule of law score. In 2003, Afghanistan scored 0,03 at the rule of law index, which is the lowest score measured. Not all the political variables scores are low because the democracy index has better results compared to the human right scale and the rule of law index. The mean for the democracy index is 47,3, which is relatively close to the expected average, which is around 50.

The dataset is almost complete. Only the democracy index has a fewer observations than the others, 180 out of 225. The main reason for these missing values is that the data of the democracy index is only available from 2006 instead of 2003. The control variables: inflation, trade openness, economic growth, market size and balance of payments do not show unexpected figures based on table 1. A few observations are missing from the balance of payments, which is why there are 214 observations instead of 225.

5.1.2 Illustration dependent and independent variables

The next phase of the descriptive analysis will show the most important variables (independent and dependent), and the tendencies of these variables will be shown here below separately. Because the main focus of this research lays on the dependent variable, FDI inflows, it is vital to investigate its characteristics.

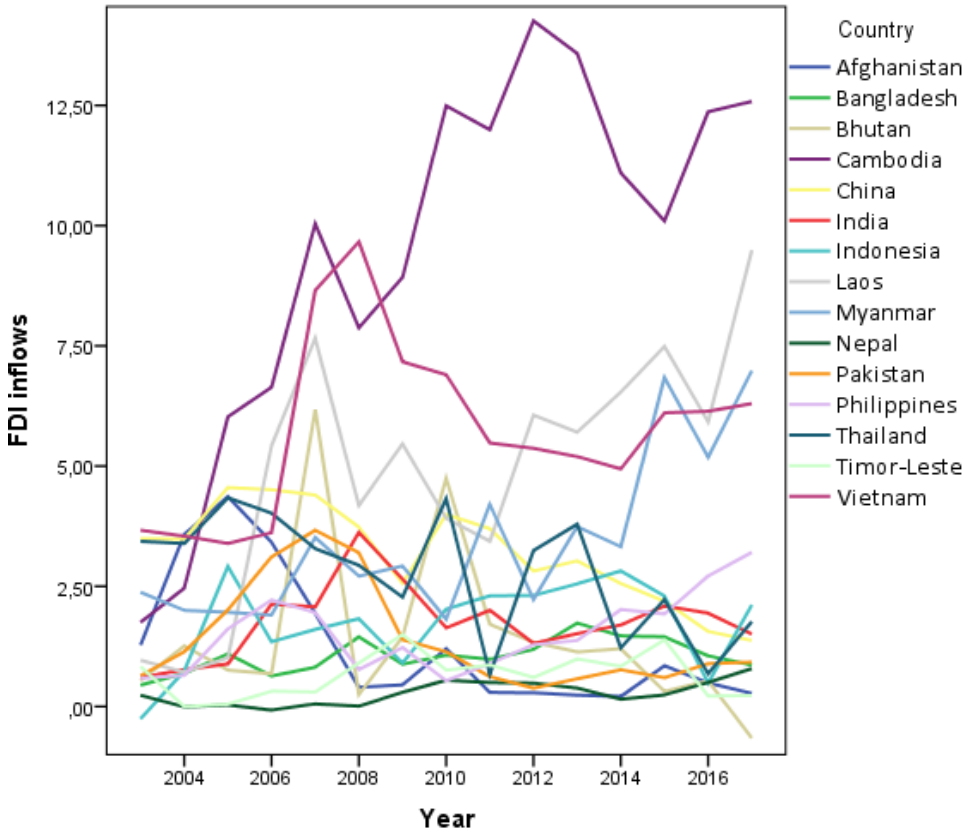

Figure 4: Development FDI inflows (percentage of GDP) 2003 to 2017

Figure 4 shows the development of Southeast Asian countries from 2003 to 2017. FDI inflows are measured as a percentage of GDP. This type of measurement is the same technique used for the regression analyses. Visible in this figure, there is no clear trend of the FDI inflows to the Asian countries. Some countries, such as Cambodia, Myanmar and the Philippines, have an increasing line,

which means the FDI inflows increased relative to their national GDP. Cambodia especially receives significant FDI inflows compared to other Southeast Asian countries. Furthermore, FDI inflows to Laos have increased a lot during the period of 2003 to 2017. Alternatively, many countries received relatively less FDI; countries such as Thailand, India, Pakistan and Afghanistan face a low percentage of FDI compared to GDP. However, the FDI inflows to Southeast Asian countries as a percentage of GDP are higher than the world average, which is around 2 per cent.

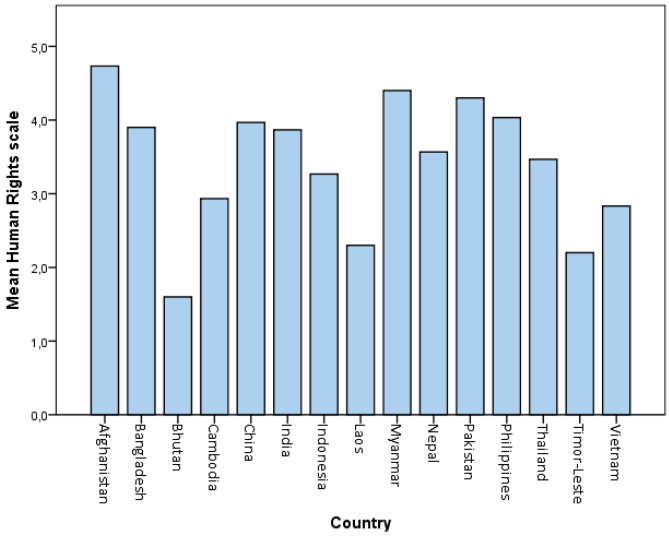

Figure 5: Average of human rights scale per country, 2003 to 2017

Figure 5 illustrates the scores per country concerning human rights violations on a scale from 1 to 5. This illustration is an average of the countries for the period 2003 to 2017. The result 1 means absolutely no violation of human rights, 5 means violence of all human rights in a country. Countries like Afghanistan, Nepal and Pakistan score relatively poorly on the PTS scale. It is striking that Bhutan scores way better than other countries. In addition, the countries that are positioned in the south of Asia, such as, Indonesia and Timor-Leste, have relatively better scores compared to other Asian countries.

Figure 6: Trend human rights scale in Southeast Asia 2003 to 2017

Figure 6 shows the development of the human rights scale of the whole region of Southeast Asia. During the whole period 2003 to 2017, the mean remained relatively high, namely between 3,2 and 3,6. Compared to other parts of the world, this score is relatively poor. However, since 2009, a slight decrease has started, and although this trend is slow, it appears to continue.

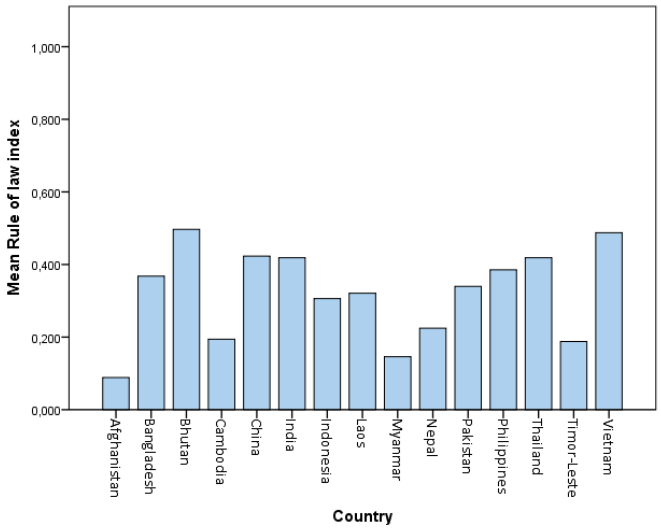

Figure 7: Average of the rule of law index per country, 2003 to 2017

Figure 7 illustrates the overall poor scores of the Asian countries for the rule of law index. The rule of law index is from 0 (poor rule of law) to 1 (good rule of law). Some of the 15 countries used for this research have relatively low scores on the index, including Afghanistan, Cambodia, Myanmar and Timor-Leste. The scores of Timor-Leste are contradictory to the results on the human rights scale and democracy index where Timor-Leste has relatively good scores. It is also valuable to mention that the development of the rule of law index for the different Southeast Asian countries remained stable. There were no significant changes in the presence or absence of the rule of law in diverse countries.

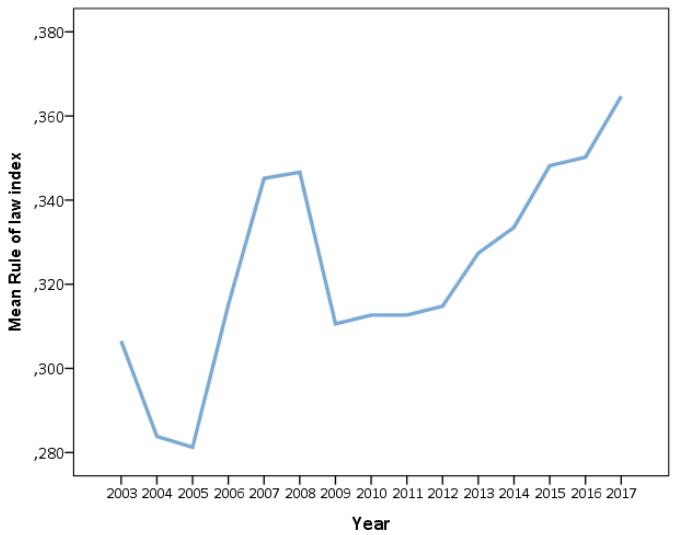

Figure 8: Trend the rule of law index in Southeast Asia 2003 to 2017

Figure 8 illustrates the development of the mean of the total rule of law index in Southeast Asia. A general increasing trend has started, which means a growth in presence of the rule of law. Although it is minor growth, just like the human rights scale, it is visible and evident that a trend is underway.

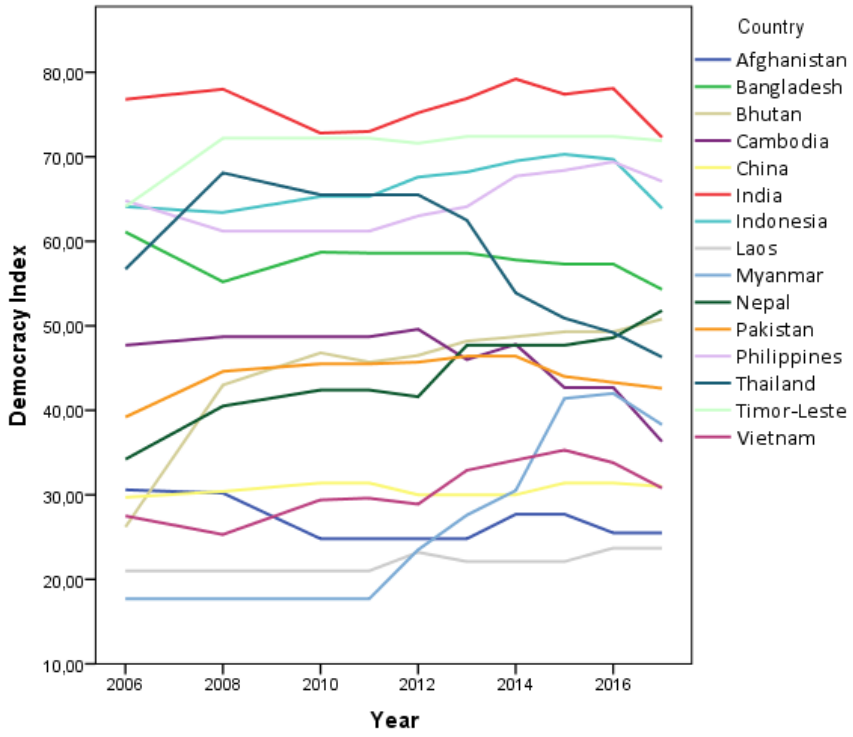

Figure 9: Development Democracy index 2006 to 2017

Figure 9 illustrates the scores of the Southeast Asian countries on the democracy index. The scale is from 0 (no democracy) to 100 (full democracy). It is interesting to note the main differences in the scores between some countries. For example, India, Indonesia and Timor-Leste show high scores on the democracy index where other countries such as Laos and Myanmar feature fewer factors, which contribute to a democratic society. However, it is valuable to mention the increasing trend of Myanmar. Myanmar was the least democratic country in Southeast Asia and democracy is still increasing. New elections in 2010, 2012 and 2015 were responsible for the growing line of Myanmar's democracy (David & Holliday, 2018). Compared to the human rights scale and the rule of law index, the democracy index results are more diverse, and the Asian countries represent more 'good' and 'bad' results. It is also notable that the scores of the countries remain relatively constant during the period 2006-2017. Countries stayed approximately in the same place regarding the extent of democracy within their borders.

5.1.3 Illustration control variables

This section shows the development of the control variables for the Southeast Asian countries. The first control variable here is economic growth. Economic growth is one of the determinants of FDI inflows. The country that stands out most is Timor-Leste, especially during the first period of 2003 to 2017, when the growth of GDP in Timor-Leste was enormous. In 2004, its economy grew as much as 64 per cent. The big fluctuating line represents the development of the economy of Timor-Leste because other years, for example, 2014, show an enormous decline in GDP growth, -26 per cent. These fluctuations occurred because of violence and civil insurgents, even security forces from the United Nations were necessary to restore order (Economist Intelligence Unit, 2011). Other countries that score relatively high are China and Vietnam that have a more stable development of their economy compared to Timor-Leste. Furthermore, the other countries show approximately a similar stable trend in their economy.

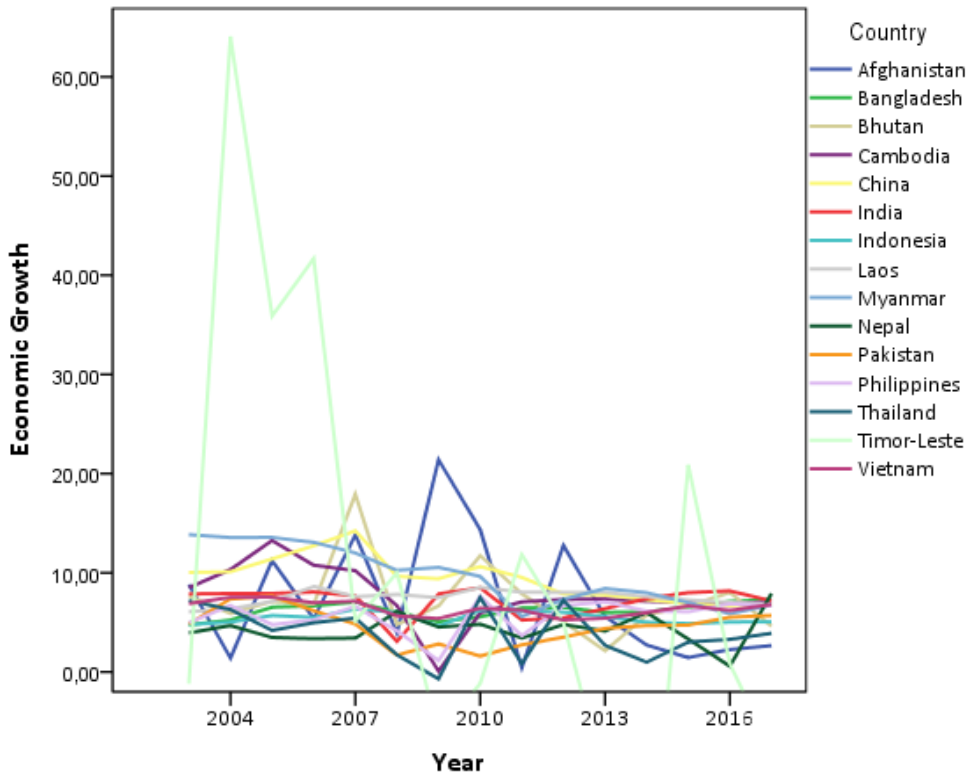

Figure 10: Development of economic growth 2003 to 2017

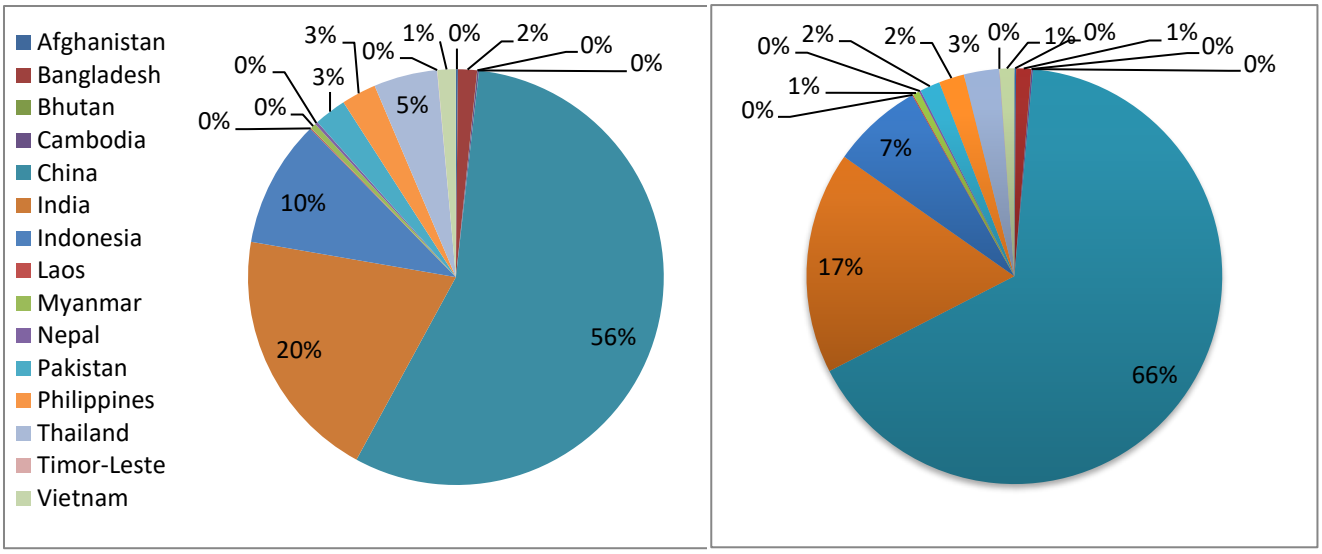

Figure 11: Market sizes in 2003 (left) and 2017 (right) in percentage of 15 Southeast Asian countries

Figure 11 shows the market size of the 15 Southeast Asian countries as a percentage of the total of these countries. Of course, the size of China is immense compared to other countries. China represents 56 per cent of the GDP in these countries. This percentage was even more prominent in 2017; here 66 per cent is represented by China. Furthermore, India has a large share of the total market size in Southeast Asia: 20 per cent in 2003, and 17 per cent in 2013. The decline of the share of almost all countries in 2017, as compared to 2003, is because of the substantial increase in the market size of China in this period. The other significant share of market size belongs to Indonesia, with 10 per cent in 2003 and 7 per cent in 2017. There are no evident changes in the share of total market sizes in the countries between 2003 and 2017. Therefore, this division remained relatively similar.

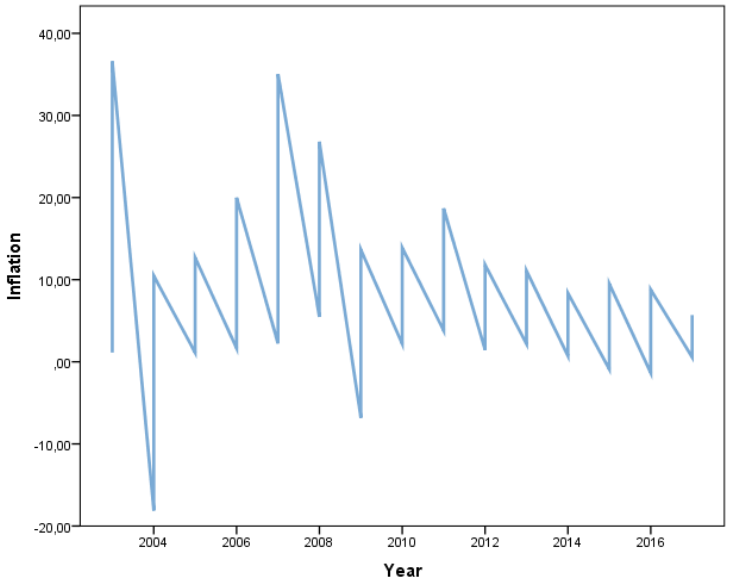

Figure 12: Development of Inflation (percentage) in Southeast Asia 2003 to 2017

Figure 12, previous page, illustrates the general development of inflation in Southeast Asia. The size of the fluctuations of inflation stands out because, at the beginning of the period 2003 to 2017, these fluctuations are much higher than in the last years of this period. Furthermore, the general trend is that inflation declines during this period. From 2010, the inflation in Southeast Asia has not fluctuated that much compared to the earlier years. This fact means that inflation in Southeast Asia is nowadays more predictable than before 2010.

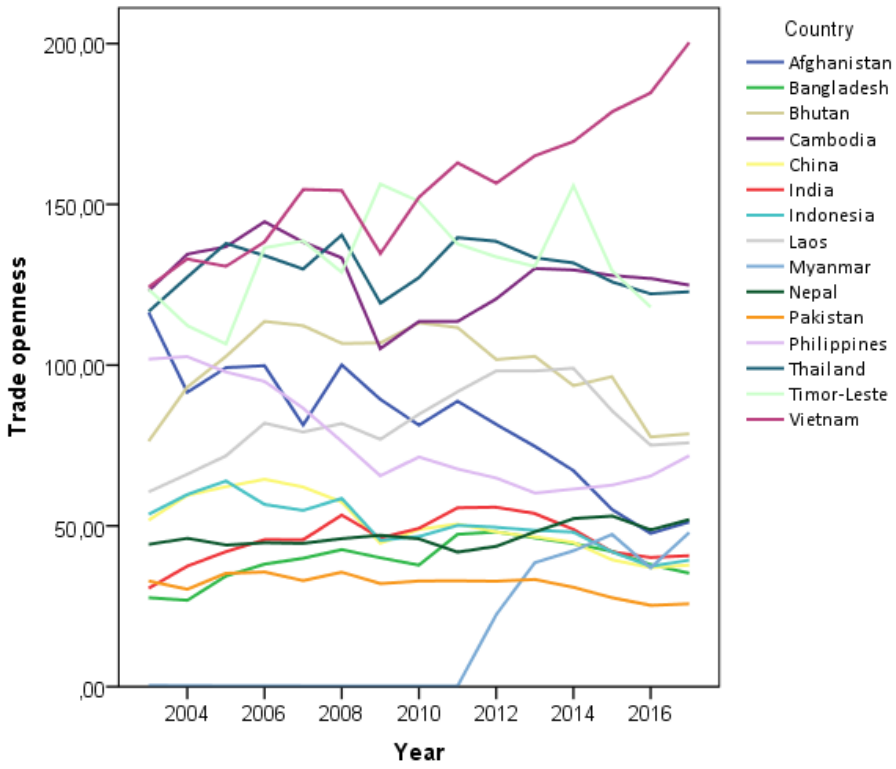

Figure 13: Development trade openness (trade as percentage of GDP) 2003 to 2017

Figure 13 shows the development of trade openness per country in the research period. What stands out are the significant differences between the countries. For example, Myanmar started relatively late in opening their economy towards other countries in the world. Now they are still increasing their openness to foreign trade. Cambodia has increased enormously and has a foreign trade culture, which is very open to the world. Most of the other countries show a stable development in economic openness, which means the percentage of trade abroad as a share of GDP remained approximately the same during this period.

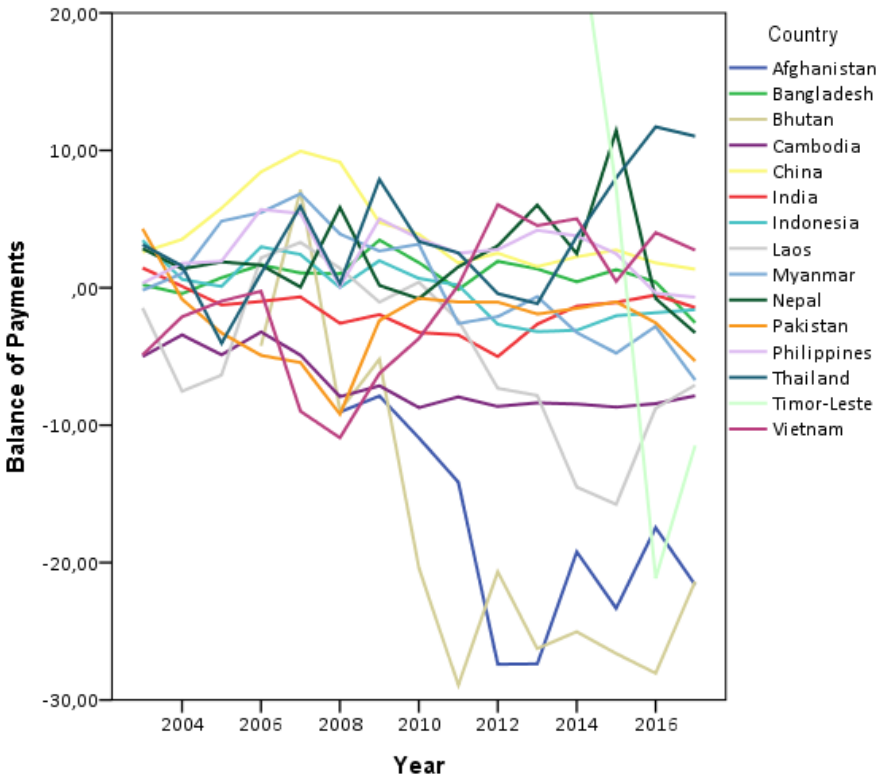

Figure 14 Development of BoP (current account as percentage of GDP) 2003 to 2017

Figure 14 shows the development of the last control variable, BoP. Just like the previous figure, this figure shows significant differences between countries in Southeast Asia. Afghanistan, which publishes data from 2008, has significant BoP problems that become apparent in this figure. Afghanistan is during the whole period far from even a positive BoP percentage. Another country which scores poorly is Bhutan, in 2011 Bhutan has the lowest percentage of all the countries in total, namely -28,9 per cent. On the other side, China, Thailand and Nepal have quite stable BoPs. They hardly have problems with their BoP.

5.2 Bivariate correlation analysis

Earlier in this paper, the conceptual model assumed the impact of human rights violations on FDI inflows. Furthermore, this model assumed an effect of the other two independent variables (the rule of law and democracy) and the other control variables (market size, economic growth, inflation, trade openness and balance of payments) on the dependent variable FDI inflows. With all these different variables, a bivariate correlation analysis is executed to observe the correlation between these variables. Table 2 shows the results of the bivariate correlation analysis. The section below this table discusses the interpretation of the numbers in this table.

Different approaches are possible to decide which relations are significant. This research follows Salkind (2017), who argues that relations between variables are significant if p<.05. Furthermore, Cohen (1988) determined which correlations are weak, moderate and strong. Correlations that are between .1 and .3 are weak, between .3 and .5 correlations are classified to be moderate, and correlations higher than .5 are called strong correlations. These guidelines will be used to analyse the bivariate correlation table.

Variables	FDI Inflows	Human rights Scale	The rule of law index	Democracy index	Market Size	Economic growth	Inflation	Trade openness	Balance of payments
FDI Inflows	x								
Human rights scale	-.195 (.003)**	x							
Rule of law index	-.066 (.348)	-.216 (.002)**	x						
Democracy index	-.290 (.000)**	-.066 (.377)	.162 (.035)*	x					
Market Size	-.019 (.782)	.180 (.007)**	.347 (.000)**	-.084 (.259)	x				
Economic growth	.048 (.473)	.010 (.884)	-.023 (.740)	-.217 (.003)**	.063 (.345)	x			
Inflation	-.029 (.667)	.187 (.005)**	-.165 (.019)*	-.095 (.205)	-.162 (.016)*	-.005 (.939)	x		
Trade openness	.398 (.000)**	-.503 (.000)**	.185 (.008)**	.042 (.576)	-.233 (.000)**	-.020 (.766)	-.175 (.009)**	x	
Balance of payments	-.162 (.017)*	-.020 (.771)	-.022 (.761)	.315 (.000)**	.093 (.174)	-.073 (.285)	.038 (.582)	.124 (.071)	x

Table 2: Bivariate correlation table (correlation is significant at the .01 level *correlation is significant at the .05 level)**

The correlation analysis between the variables FDI inflows and human rights resulted in a Pearson correlation of -.195 and a significance of p<.001. According to the guidance of Cohen (1988) en Salkind (2014), this means a significant relationship and a weak negative relationship.

The correlation analysis between the variables FDI inflows and the rule of law index gave an unexpected Pearson correlation of -.066 and no significance. This outcome means a negative, weak correlation. This research is unexpected because the relationship between these variables was expected to be positive according to the conceptual model.

The last independent variable, democracy, has a significant relationship with FDI inflows of p<.001. The correlation between these variables is -.290, which is a weak negative relationship, according to Cohen (1988). Just like the previous correlation, FDI inflows and the rule of law, this correlation is also contrary to the conceptual model. The relationship is negative instead of the assumed positive relationship.

Another interesting correlation coefficient is the coefficient between trade openness and FDI inflows. This number is the highest correlation between one of the independent/control variables and the dependent variable, FDI, a Pearson correlation of .398 and a significance of p<.001. This outcome means a moderate positive relationship between trade openness and FDI inflows.

5.3 Hausman test

Section 4.4.2 described the tests of the assumptions. Based on these assumptions, the conclusion was a violation of the assumptions of homoscedasticity and no autocorrelation. That is why other methods of estimation are more suitable than the OLS pooled data. Therefore, it is essential to choose between the FE or RE methods. This section will use the Hausman Test to determine which method is the most appropriate one for this research. If the result of the Hausman test is a P-value lower than .05, then the null hypothesis has to be rejected, this H_0 suggests that the differences in the coefficients are not systematic. If the H_0 is rejected, the consequence is that the FE estimation method is more applicable to the dataset. Contrarily, if there is no rejection of the null hypothesis, this means the RE estimation method is more applicable (Torres-Reyna, 2007).

The Hausman test in STATA resulted in a P-value of .608, which means no rejection of the null hypothesis because the p-value is higher than .05. Therefore, the RE method is more applicable to this dataset than the FE method. However, as discussed in section 4.4.3 earlier in this paper, the FE method is essential for this research because this research did not choose this dataset randomly from a larger population. Furthermore, the FE method can control for variation in the data because of time reasons. The research question in this research also aims to respond to time reason

differences. Therefore, this paper will execute a regression for two models; one model is the RE method, and the other is the FE method.

In section 4.4.2, it became clear that a robust estimation method is necessary to tackle problems of the violations of two assumptions, homoscedasticity and no autocorrelation. A robust estimation regression model is the solution, so as not to be sensitive to the violations of these assumptions (Fornalski, 2015). STATA is helpful to incorporate a robust method with higher robust standard errors and higher P-values (Torres-Reyna, 2007). Considering this, this research tries to answer the research question by using a robust estimator in both models, the random effects model and a fixed effects model.

5.4 Results multiple regression analysis

This paper mentioned different theories and concepts that led to the conceptual model. The conceptual model that is central in this paper assumes the dependent variable, FDI inflows, is dependent on three leading independent variables, namely human rights violations, democracy and the rule of law. Furthermore, the conceptual model assumes that other economic variables, which are inflation, the balance of payments, trade openness, market size and economic growth, also influence the dependent variable, FDI inflows.

Although the correlation matrix (5.2) provides helpful insights into correlations between variables and suggests whether these correlations are significant, it is still essential to execute a bivariate regression analysis to test the regression coefficients between all of these variables. This test is necessary because it will demonstrate whether a relationship is based on coincidence. The results of this regression analysis are in table 3 (next page). With the help of the (robust) FE and (robust) RE methods, STATA executed the regression analysis.

Variable	(robust) RE method			(Robust) FE method		
	Coefficient	Std. Error	P-value	Coefficient	Std. Error	P-value
Human rights scale	-.0110	.3135	.972	-.0103	3.4000	.976
Rule of law index	-2.4264	3.4583	.483	-2.6246	3.6348	.482
Democracy index	.0103	.0291	.723	.0421	.0387	.295
Market Size	-2.88e-13	9.81e-14	.003*	-4.28e-13	1.08e-13	.001*
Economic growth	.0133	.0159	.404	.0089	.0144	.548
Inflation	-.0101	.0370	.784	-.0078	.0370	.838
Trade openness	.0209	.0070	.003**	.0130	.0105	.235
Balance of payments	-.0427	.0311	.170	-.0391	.0348	.280
Constant	1.7857	3.0737	.561	1.2857	3.3028	.703
Sigma u (μ_i)		2.4756			3.0996	
Sigma e (V_{it})		1.1913			1.1913	
R^2		.1483			.1416	
Adjusted R^2		.1052			.0982	
F-Test		Not available			Not available	
N		167			167	
DF		7			7	

Table 3: Multiple linear regression model with (robust) RE and (robust) FE methods

(Significant at *P=.01, **p=.05, *** p=.10)

This table shows the outcomes of the bivariate regression models with (robust) FE and (robust) RE methods. This table shows several fundamental values. The first value that this table shows is the coefficient; this is the estimated coefficient. For the (robust) FE method this coefficient means that "…for a given country, as X varies across time by one unit, Y increases or decreases by β units" according to the definition of Torres-Reyna (2007, p.10). This definition is less applicable to the (robust) RE method because this estimation method does not make a distinction between country and time effects. In practice, this means that the estimated coefficients in a (robust) RE estimation model incorporate differences across time and countries. The second value in the table is the standard error. A very high standard error means the existence of high uncertainty about the

estimates. The third value is the P-value, which shows the level of significance, which determines whether this paper rejects the null hypotheses. The null hypothesis stands for zero correlation between the dependent and the independent/control variable. Therefore, if the P-value is lower than .01, .05, or .1, then the null hypothesis will be rejected, which means a correlation between the two variables exists (Salkind, 2017).

Other values that are visible in the table are sigma *u* and sigma *e*. These values were explained in the section of the regression models, 4.4.1. The R^2 is the value, which indicates whether the regression model can predict the variability of the dependent variable (Miles, 2014). This paper uses the 'within' value to measure the R squared for the FE estimation method; this value explains the mean-deviation in the regression analysis. The RE estimation method uses the 'overall' value to measure the R squared; this value explains the weighted average between the 'within' and 'between' values. Although the R^2 (R squared) provides helpful information about the outcomes of a regression model, in this case, R^2 seems to be less helpful for insights in the regression models because of the heterogeneity which is not possible to observe in different sections (Miles, 2014). A similar value is the adjusted $R^{2,}$ which estimates the model in the total population; this value is more helpful than the R squared. In this table, the adjusted R-squared is higher in the RE model with a value of .1052 against a value of .0982 from the FE model. These results mean that the RE estimation model predicts 10.52% of the variability of the FDI Inflows in Southeast Asia, while the FE estimation model predicts 9.82% of the variability of the FDI inflows in Southeast Asia. So, the RE model predicts the variations in the dependent variable in a more efficient way than the FE model, which connects to the Hausman test (section 5.3).

Other options instead of the R^2 are essential in order to be able to interpret the outcomes of the regression analysis correctly. Therefore, the F-Test is more critical in panel data research, (robust) RE and (robust) FE models, to check whether the regression model is significant. However, these multiple regression models do not show an F-test as a result. Unfortunately, that is why the result of the F-tests are not visible in the table. The last remaining values in the table are DF, which stands for degrees of freedom and N, which is the total number of observations in the models.

5.5 Interpretation of results multiple regression analysis

This section tries to understand the outcomes of the results of table 3. It discusses the effects of the different independent and control variables on the dependent variable FDI by comparing the different results of the (robust) RE and (robust) FE estimation models. It is crucial to notice that this section reflects on the analysis of the two multiple regression model. However, this section also discusses other specification models in order to control the results of the multiple regression model. These other specification models execute for each independent variable, and each independent variable, four extra regression models. Namely, two models without other independent and control variables for RE and FE and two models with the control variables but not the independent variables, again with a RE and FE estimation model. The results of these regression models are visible in the tables in Appendix IV. Because both models use a robust estimator, this paper will not mention the word 'robust' hereafter.

5.5.1 Human rights scale

According to the conceptual model, the expectation was a negative relationship between the human rights scale and FDI inflows. This negative direction is similar to both of the coefficients in the table, for the RE and FE models. In practice, this means when the human rights scale increases with one per cent, according to the RE and FE models, the FDI inflows decrease 1.0 and 1.1 per cent. This percentage is relatively low. Furthermore, the P-values obtained are .972 and .976. These P-values mean no significant relationship between the human rights scale and FDI inflows because the P-values are very high. So, based on this multiple regression model, the null hypothesis of zero correlation between these variables cannot be rejected.

As described in the introduction of 5.5, this part will also have a look at the other specification models. In Appendix IV, the other human rights models are visible in tables 6 & 7. Compared to the primary multiple regression model, the other models in this Appendix give higher coefficients. The regression model without the control variables shows coefficients of -39.4% and -37.1% (RE and FE). The regression model, which includes the control variables, also shows higher coefficients, namely -39.7% and -45.5% (RE and FE).

Furthermore, all the P-values are again too high to be significant except the FE model, including the control variables; this model shows a P-value of .092, which is significant at .1 level. Although based on this significance, it is arguable that this research should reject the null hypothesis; this is not the case since all the other models have a P-value that is even higher than .1. Therefore and based on all

regression models, this paper does not reject the null hypothesis of zero correlation/positive relationship between human rights and FDI inflows. On the contrary, this means that this paper rejects the first hypothesis (the negative relationship between human rights scale and FDI inflows).

5.5.2 Rule of law Index

Based on the theories and the conceptual model, the predicted relationship between the rule of law index and FDI inflows should be positive. However, both of the models (RE and FE) indicate a negative relationship between the rule of law index on the dependent variable. In practice, this means when the rule of law index increases with one value, the FDI inflows decreased by 242.6% and 262.5 per cent. Again, these coefficients are relatively close to each other. There was no significance proven with the almost similar P-values of .483 (RE) and .482 (FE). These high P-values are in line with a high P-value in the correlation table (5.2). So, none of the multiple estimation models can reject the null hypothesis of zero correlation between the rule of law index and FDI inflows. Therefore, based on the multiple regression model, this paper rejects the second hypothesis H2 (the relationship between the rule of law index and FDI inflows).

The second independent variable, rule of law, other specification models are visible in Appendix IV, tables 8 & 9 show the results of these other models. Compared to the primary multiple regression model, the results in this Appendix give lower coefficients. The regression model without the control variables shows coefficients of -178.7% and -197.9% (RE and FE). The regression model, which includes the control variables show even lower coefficients, namely -97.6% and 52.2% (RE and FE). Notable is the positive coefficient in the FE model (including control variables).
Furthermore, all the P-values are again excessively too high to be significant. Therefore, based on all the regression models together, there is no doubt that this paper does not reject the null hypothesis of zero correlation/negative relationship. On the contrary, this means that this research rejects the second hypothesis (the negative relationship between the rule of law index and FDI inflows).

5.5.3 Democracy index

The expected relationship between the democracy index and the FDI inflows was positive according to the conceptual model. The outcomes of the RE and FE estimation models are also positive; the coefficients are respectively .0103 (RE) and .0421. These coefficients mean that when the democracy index increases with one per cent, FDI inflows will increase with 1.0% (RE) or 3.9% (FE). It is not relevant to have a look at the differences between these percentages since the P-values are too high in both models. The RE estimation model has a P-value of .723, the FE estimation's P-value is .295. Although between these models, there is a massive difference visible, the conclusion based on the

multiple regression models is that there is no significance concerning the P-values. Therefore, the null hypothesis of zero correlation/negative between democracy index and FDI inflows could not be rejected.

For the last independent variable, democracy, other specification models are visible in Appendix IV, tables 10 and 11 show the results of these other models. Compared to the primary multiple regression model, the results in this Appendix show approximately the same. The regression model without the control variables shows coefficients of 2.5% and -4.7% (RE and FE). The regression model, which includes the control variables, shows lower coefficients, namely 0.8% and 2.75% (RE and FE). Notable is the negative coefficient in the FE model (excluding control variables). Furthermore, all the P-values are again excessively too high to be significant. Therefore, based on all the regression models combined, this paper does not reject the null hypothesis of zero correlation/negative relationship, which means that this research cannot reject the third hypothesis (the positive relationship between democracy index and FDI inflows).

5.5.4 Market size

Although the theories argue in favour of a positive relationship between market size and FDI inflows, the relationship is close to zero and negative according to the coefficients. The RE coefficient is -2.88e-13, the FE coefficient is -4.28e-13; these coefficients are relatively similar. The P-values of the RE method and the FE method are also relatively similar, RE has a P-value of .003, and the FE method has a P-value of .001. Based on these outcomes, the null hypothesis of zero correlation cannot be rejected. According to the multiple regression model, there is a little negative relationship between market size and FDI inflows. Therefore, there is no positive relationship measured between these variables. In contrast to the previous hypotheses, this does not mean any relationship but a significant negative relationship between market size and FDI inflows.

5.5.5 Economic growth

The conceptual model assumed a positive relationship between economic growth and FDI inflows. Indeed, the coefficients suggest a positive relationship. The RE and FE methods show relatively similar results. In practice, when the economic growth increases one per cent, the FDI inflows will increase by 1.3% and 0.9%. However, the P-values are too high, which means there is no significant relationship existing between economic growth and FDI inflows, namely P-values of .404 and .548. Therefore, according to the multiple regression models, the null hypothesis of zero correlation cannot be rejected. The consequence is that this paper rejects the H1.

5.5.6 Inflation

The development of inflation is supposed to be negatively related to the FDI inflows. Indeed, the coefficient obtained from the multiple regression model is negative. In practice, when inflation increases one per cent, the FDI inflows decrease by 1.0% and 0.8% based on the RE and FE methods. These coefficients are not only very low, but this relationship is also not significant since the P-values are .784 and .838, which is much higher than it should be to be significant. The results of the RE and FE methods are relatively similar, which means that this paper does not reject the null hypothesis. Conversely, the H1 cannot be accepted, meaning that inflation does not affect FDI inflows directly in these multiple regression models.

5.5.7 Trade openness

According to the conceptual model, the relationship between trade openness and FDI inflows should be positive. Indeed, the relationship is positive in both of the models (RE and FE). In practice, this confirmation means that, when trade openness increases one per cent, the FDI inflows increase 2,1% and 1,3%. Although these coefficients are relatively similar, the P-values differ between the RE and FE estimation models. On the one hand, the RE estimation model has a P-value of .003, which means a significant relationship between trade openness and FDI inflows. On the other hand, the FE estimation model has a P-value of .235, which is higher than the significance levels. It is crucial to take into account that the RE method is more appropriate in order to regress this variable since trade openness also varies across countries. Therefore, the P-value retrieved from the RE method will be considered as the correct P-value. According to this P-value, this paper rejects the null hypothesis of zero correlation between trade openness and FDI inflows. Conversely, based on the multiple regression model, this research confirms a positive relationship between trade openness and FDI inflows.

5.5.8 Balance of payments

The relationship between BoP and FDI inflows is assumed to be positive according to the conceptual model. However, both of the multiple regression models predict a negative relationship. In practice, this means when BoP increases one per cent, the FDI inflows decrease by 4.3% and 3.9% respectively. Furthermore, the P-values are also relatively similar in the RE and FE estimation models. The P-values are .170 (RE) and .280 (FE). Bases on these P-values, there is no significance. The results of the RE and FE methods are relatively similar, which means that this paper does not reject the null hypothesis. Conversely, this holds that this research does not confirm H1 (the positive relationship between BoP and FDI inflows), meaning that inflation does not affect FDI inflows directly in these multiple regression models.

Chapter 6. Conclusion and recommendations

6.1 conclusion

In section 1.3, the main research question and sub-question became clear. After discussing the findings in the previous chapter, it is finally possible to answer these questions. To start with the main research question:

What is the effect of human rights violations on the foreign direct investment inflows in Southeast Asian countries?

Based on section 5.5.1, the conclusion is that there is no significant relationship visible, which means both theories from section 3.1.1 and 3.1.2, the Profit Maximization model and the Risk Mitigating model, are not applicable for this research. There is no effect of human rights violations on the foreign direct investment inflows in Southeast Asian countries.

Different reasons can be responsible for this lack of effect; 1. a balance between the Risk Mitigating model and the Profit Maximization model 2. a reason related to the region of Southeast Asia. The first possible explanation is a balance between these two models. On one hand, investors aim to create maximum profit by focusing on countries where it is possible without taking care of the local citizen's circumstances (the Profit Maximization model). On the other hand, these investors aim to have respect for the local circumstances and perhaps do not prefer to take too many reputational risks (Risk Mitigating model). In the end, taking into account both sides of this dilemma, human rights violations do not have an evident influence on the choice of foreign investors to invest in a country.

The second explanation is a possibility that other regions in the world do show a relationship between human rights violations and FDI inflows in contrast to Southeast Asia. In this case, the conclusion is that foreign investors in Southeast Asian countries are not sensible concerning the human rights circumstances of Southeast Asia. One of the explanations why this is the case in Southeast Asia is because of China. China has a lot of influence in Southeast Asia; they also contribute a large percentage of FDI in the region (Haddad, 2007). Most of the trade in this region remains inside this region, with a significant role for China. China has become an important trading partner for other East Asian countries. All East Asian countries have increased their share of exports to China (Haddad, 2007). Furthermore, there is the possibility that China does not pay much

attention to human rights issues. Therefore, it can be argued that human rights circumstances do not matter for Chinese investors concerning their investments in Southeast Asia.

After answering the main research question, this conclusion chapter will answer the two sub-questions. The first sub-question was about the rule of law:

What is the effect of the rule of law on the foreign direct investment inflows in Southeast Asian countries?

The answer is that the rule of law does not have a significant impact on FDI inflows. There is no effect of the rule of law on FDI inflows in Southeast Asia. This outcome is in contrary to the theories discussed in section 2.2. Furthermore, the coefficients of the analyses were very high, which is unrealistic. It is possible that other ways of measuring this relationship can find a significant relationship.

The second sub-question was about democracy:

What is the effect of democracy on the foreign direct investment inflows in Southeast Asian countries?

The results of the analysis were that there is no significant relationship between the democracy level and FDI inflows. The conclusion is that the independent variable democracy does not affect FDI inflows in Southeast Asia. This result rejects the theories of Jensen (2008) and Shah (2017), who are in favour of a positive relationship between democracy and FDI inflows. Furthermore, this relationship rejects the theory of Li & Resnick (2003), who explained there is a negative relationship between these variables. However, this result does support the theories of Oneal (1994) and Busse (2003). They assume the existence of no influence of democracy on FDI inflows. The main reason why this result came forward is that the positive and negative effects of democracy on FDI inflows outweigh each other.

In contrast to the conceptual model and the assumed hypotheses, only hypothesis seven (H_1: There is a positive relationship between trade openness and FDI inflows) is accepted. In practice, this conclusion means that trade openness has a positive and significant effect on FDI inflows in Southeast Asia. This paper rejects the other hypotheses, which means the outcomes provide other results than what was previously expected. Market size is the only control variable that has a significant influence on FDI inflows, but this relationship is shallow, and it is negative instead of the expected positive relationship.

6.2 Limitations of this research

This research was not without limitations. This section describes the limitations of this study, which are the missing values of democracy, no measurement of Sri Lanka, the focus on FDI inflows in host countries instead of the origin of foreign investors, the focus on indicators only, the external validity and the measurement of FDI inflows. First, the data on democracy was available from 2006 instead of 2003. This lack of data may affect the analysis in STATA. Second, Sri Lanka did not publish enough data on the relevant variables to become one of the analysed countries. Therefore, Sri Lanka was not taken into account in this research, which may affect the analysis in STATA since this country can have contradictory results compared with the studied Southeast Asian countries. Third, the focus of this research was on FDI inflows in host countries. The focus was not on the origin of the foreign investors, which could influence the relationships between the independent variables of FDI inflows. For example, the values of Chinese investors are different from the values of European investors. Fourth, this research mainly focused on indicators of the independent variables and used scales as indicators for the variables. This research did not look at whether negative human rights records lead to a societal discussion to avoid 'negative' countries. For example, big events in public can increase public debate regarding choices to invest in a country with poor human rights scores. For example, if the media gives more attention to one country with poor human rights scores, then multinationals can affect their image by investing in this country. These events can intervene in the relationship between human rights violations and FDI inflows in Southeast Asia. Fifth, external validity is decreased by focusing on the Southeast Asia region. Therefore, this research is less applicable than research that focuses on countries across the world. Sixth, there is criticism regarding the measurement of FDI because locally financed FDI is often not reported in the BoP, which is the case in this research as well. Therefore, it is excluded from the host country's data. This affects the study since this exclusion may exceed more than 50 per cent of the total investment (Bellak, 1998). On the other hand, flows of capital which run through holding and daughter companies can enlarge FDI inflows with the only goal of entering and leaving the specific host country (Bellak, 1998).

6.3 Recommendations for future research

Future research should narrow the scope to FDI inflows of Southeast Asian countries differentiated by the country of origin of the investor. For example, how much do human rights violations affect the FDI inflows for Chinese investors? The second recommendation is that future research should intervene in the relationship between human rights violations and FDI inflows by using essential

events as an intervening variable. In that case, the time-dimension should be different, for example, quarterly instead of yearly. The third recommendation is that future research should move the scope from Southeast Asia to other parts of the world to investigate if other regions provide similar results. Other regions, which could be interesting for this kind of research, are regions in Africa or South-America. The fourth recommendation is that future research should focus more on the impact that the media has on the choices of international investors. The last recommendation for future research is time-related. Future research should compare the most recent period with earlier periods. An earlier period than 2003 to 2017 might give contradicting results.

Overall, this research used a broad perspective of the most recent period. In general, this research answers the expected relationship between human rights and FDI. There is a probability that narrows the scope to several factors (origin investors, media, essential events, different periods) may lead to a different outcome. However, this research showed no relationship between human rights and FDI.

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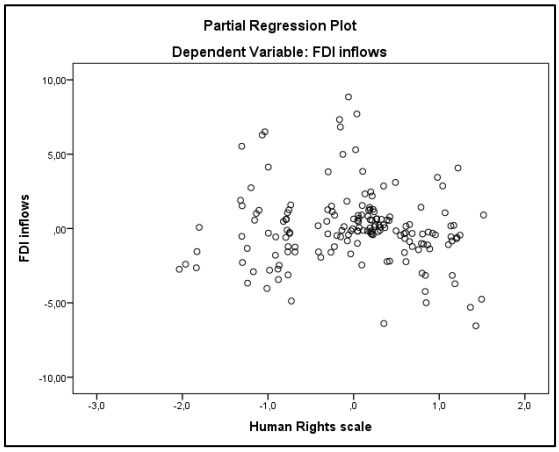
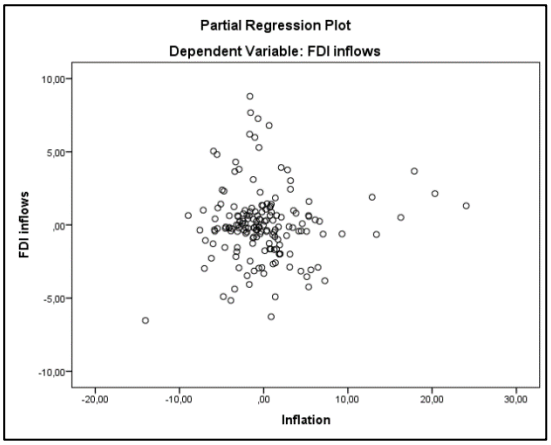
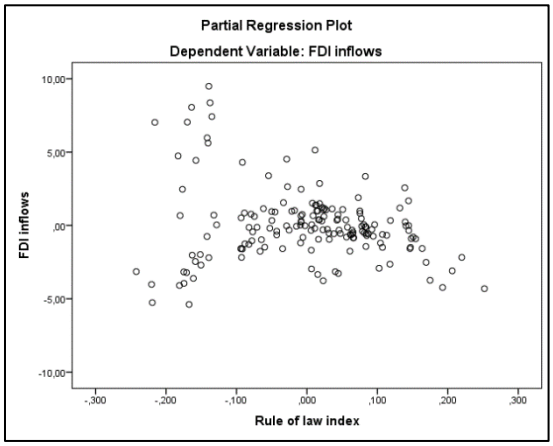
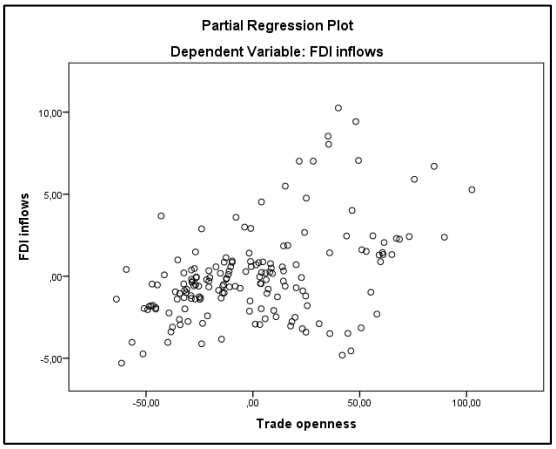
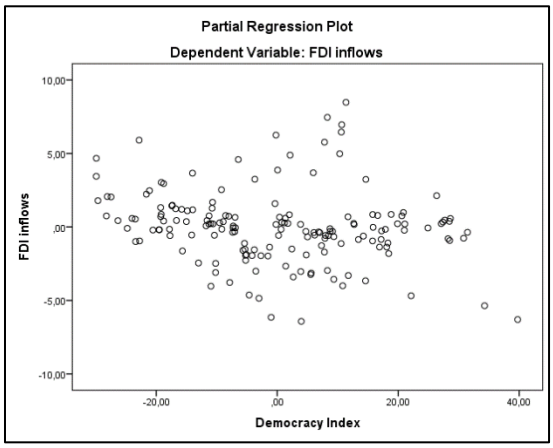
Appendix I – Linearity plots

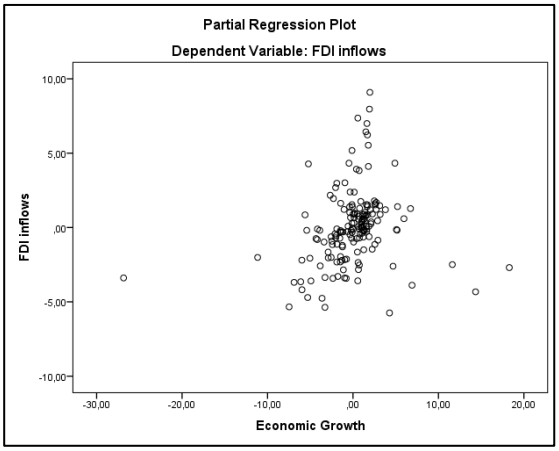


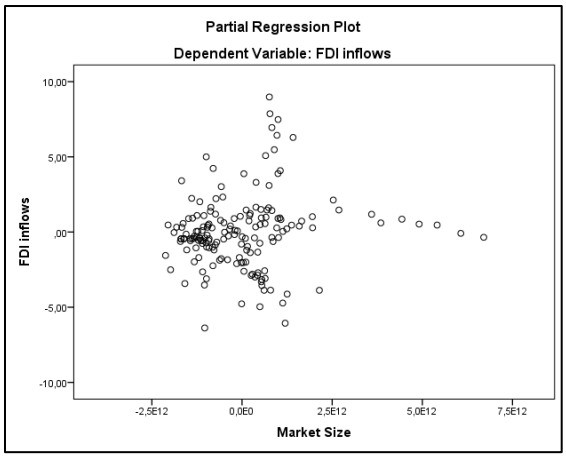


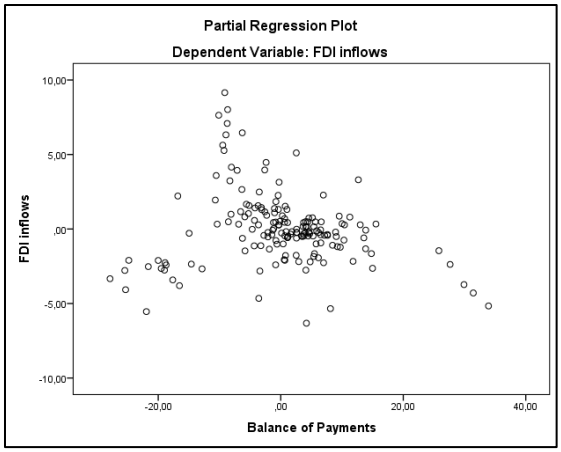




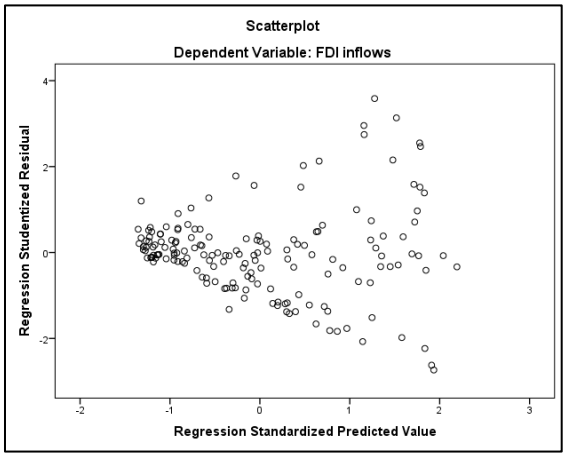








Graphical test for homoscedasticity



Appendix II - Normality tests

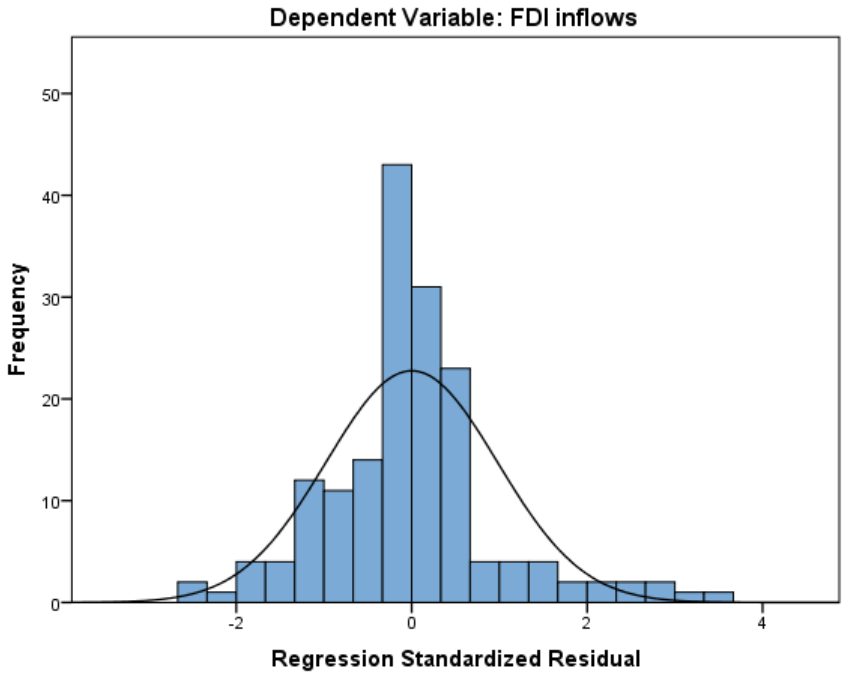


Figure 15: Histogram normal distribution

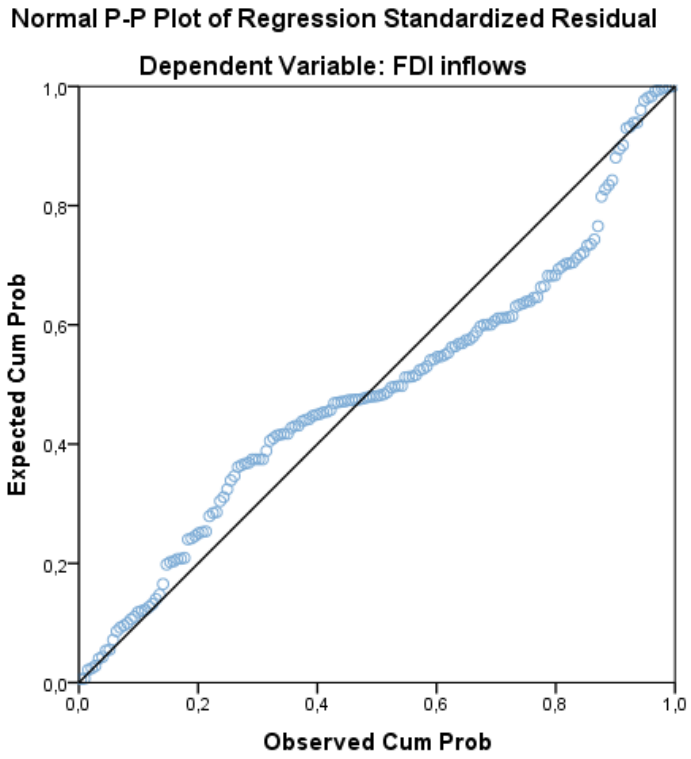


Figure 16: Linear Graph error terms

Appendix III - Multicollinearity test

Variables	Human Rights Scale	The rule of law index	Democracy index	Market Size	Economic growth	Inflation	Trade openness	Balance of payments
Human rights scale	x							
Rule of law index	-.216 (.002)**	x						
Democracy index	-.066 (.377)	.162 (.035)*	x					
Market Size	.180 (.007) **	.347 (.000)**	-.084 (.259)	x				
Economic growth	.010 (.884)	-.023 (.740)	-.217 (.003)**	.063 (.345)	x			
Inflation	.187 (.005)**	-.165 (.019)*	-.095 (.205)	-.162 (.016)*	-.005 (.939)	x		
Trade openness	-.503 (.000)**	.185 (.008)**	.042 (.576)	-.233 (.000)**	-.020 (.766)	-.175 (.009)**	x	
Balance of payments	-.020 (.771)	-.022 (.761)	.315 (.000)**	.093 (.174)	-.073 (.285)	.038 (.582)	.124 (.071)	x

Table 4: Correlation table of independent and control variables

(correlation is significant at the .01 level *correlation is significant at the .05 level)**

Variable	VIF
Human rights scale	**1.48**
The rule of law index	**1.46**
Democracy index	**1.30**
Market size	**1.13**
Economic growth	**1.61**
Inflation	**1.91**
Trade openness	**1.62**
Balance of payments	**1.26**

Table 5: VIF table of independent and control variables

Appendix IV - Other specification models

For each of the independent variables, this Appendix provides two other specification models. Namely, a model that includes just the control variables (without other independent variables) and a model that excludes these control variables. This research uses both FE and RE models for each regression analysis. This Appendix makes it possible to see the differences between the different models.

Human rights scale

Variable	(robust) RE method			(Robust) FE method		
	Coefficient	Std. Error	P-value	Coefficient	Std. Error	P-value
Human rights scale	-.3938	.2939	.180	-.3706	.2821	.211
Constant	4.0619	1.4762	.006*	3.9807	.9661	.001*
Sigma u (μ_i)		2.4141			2.3705	
Sigma e (V_{it})		1.6096			1.6096	
R^2		.0379			.0113	
Adjusted R^2		.0336			.0068	
F-Test / Wald Test		1.79 (P-Value=.1803)			1.72 (P-Value.2107)	
N		225			225	

Table 6 Regression model for Human rights scale, control variables are excluded
(Significant at *P=0.01; **P=0.05; ***P=0.1).

Human rights scale

Variable	(robust) RE method			(Robust) FE method		
	Coefficient	Std. Error	P-value	Coefficient	Std. Error	P-value
Human rights scale	-.3967	.2669	.137	-.4554	.2521	.092***
Market Size	-1.44e-13	6.36e-14	.024**	-2.23e-13	7.50e-14	.010*
Economic growth	.0103	.0267	.700	.0062	.0277	.826
Inflation	-.0045	.0267	.871	-.0048	.0280	.866
Trade openness	.0292	.0073	.000*	.0325	.0130	.025**
Balance of payments	-.0360	.0294	.221	-.0353	.0301	.261
Constant	1.8112	1.6066	.259	2.0026	1.5509	.218
Sigma u (μ_i)		2.2215			2.3234	
Sigma e (V_{it})		1.5586			1.5586	
R^2		.2003			.1007	
Adjusted R^2		.1770			.0745	
F-Test		not available			not available	
N		213			213	

Table 7: Regression model for Human rights scale, control variables are included
(Significant at *P=.01; **P=.05; ***P=.1).

Rule of law Index

Variable	(Robust) RE method			(Robust) FE method		
	Coefficient	Std. Error	P-value	Coefficient	Std. Error	P-value
Rule of law Index	-1.7873	2.3347	.444	-1.9790	2.7134	.478
Constant	3.3679	.9680	.001*	3.5580	.8803	.001*
Sigma u (μ_i)		2.5476			2.4963	
Sigma e (V_{it})		1.5612			1.5612	
R^2		.0044			.0044	
Adjusted R^2		.0006			-.0006	
F-Test / Wald Test		0.59 (P-Value=.4440)			1.72 (P-Value.2107)	
N		203			225	

Table 8: Regression model for Rule of law index, control variables are excluded
(Significant at *P=0.01; **P=0.05; ***P=0.1).

Rule of law Index

Variable	(Robust) RE method			(Robust) FE method		
	Coefficient	Std. Error	P-value	Coefficient	Std. Error	P-value
Rule of law Index	-.9756	2.6267	.710	.5224	2.9437	.862
Market Size	-1.06e-13	1.28e-13	.407	-3.09e-13	1.77e-13	.102
Economic growth	-.0049	.0347	.888	-.0213	.0370	.574
Inflation	.0092	.0236	.698	.0105	.0223	.644
Trade openness	.0264	.0061	.000*	.0242	.0139	.103
Balance of Payments	-.0539	.0317	.089***	-.0578	.0377	.147
Constant	1.0095	1.1922	.397	1.1609	1.4785	.445
Sigma u (μ_i)		1.6631			2.4072	
Sigma e (V_{it})		1.4808			1.4808	
R^2		.2271			.0970	
Adjusted R^2		.2029			.0688	
F-Test		Not available			Not available	
N		199			199	

Table 9: Regression model for Rule of law index, control variables are included
(Significant at *P=.01; **P0=.05; ***P=.1).

Democracy index

Variable	(Robust) RE method			(Robust) FE method		
	Coefficient	Std. Error	P-value	Coefficient	Std. Error	P-value
Democracy index	.0245	.0378	.517	-.0469	.0443	.308
Constant	1.7892	2.0213	.376	.7316	2.0931	.732
Sigma u (μ_i)		2.7422			3.2267	
Sigma e (V_{it})		1.2724			1.2734	
R^2		.0842			.0269	
Adjusted R^2		.0791			.0214	
F-Test / Wald Test		0.42 (P-Value=.5165)			1.72 (P-Value.2107)	
N		180			225	

Table 10 Regression model for Democracy index, control variables are excluded
(Significant at *P=0.01; **P=0.05; ***P=0.1).

Democracy index

Variable	(Robust) RE method			(Robust) FE method		
	Coefficient	Std. Error	P-value	Coefficient	Std. Error	P-value
Democracy index	.0076	.0287	.792	.0275	.0376	.477
Market Size	-3.27e-13	8.42e-14	.000*	-4.19e13	9.57e-14	.001*
Economic growth	.0167	.0257	.516	.01713	.0244	.494
Inflation	-.0129	.0315	.681	-.0123	.0314	.701
Trade openness	.0214	.0083	.010*	.0169	.0127	.204
Balance of Payments	-.0236	.0272	.386	-.0186	.0277	.513
Constant	1.0911	1.9445	.575	.6141	2.0010	.763
Sigma u (μ_i)		2.8362			2.9157	
Sigma e (V_{it})		1.226			1.2356	
R^2		.1253			.0958	
Adjusted R^2		.0944			.0638	
F-Test		Not available			Not available	
N		177			177	

Table 11: Regression model for Democracy index, control variables are included
(Significant at *P=.01; **P=.05; ***P=.1).