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DETERMINANTS OF FOREIGN DIRECT INVESTMENT IN ASIAN COUNTRIES

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ABSTRACT

The foreign direct investment (FDI) is a key component in modern economic growth. FDI is a key driver of a country's capacity to trade and therefore, industrial structure of developing countries normally seeks to attract FDI inflows and the Asian countries have proven to be leading exponents in this regard. Asian countries have followed a process of reforms to open up their economies to create a core for foreign capital inflow. The manifold benefits of FDI, developing countries around the world have significantly eased limits on foreign capital convey. Recently, FDI in flow to developing economies reached their uppermost level and FDI inflows to Asia rose to dollar 41 billion in 2014. In this paper an attempt has been made to analyze the determinants of FDI in Asian countries with special reference to South Asian countries. The paper highlights the key components of FDI inflow to Asian countries.

KEY WORDS: *FDI, growth, Asia, Regional economics*

JEL: F39, O10, O53, R1

1. INTRODUCTION

Asian countries are performing vigorous economic performance since early 1970s which was mainly due to moderate inflation, strong savings & investment rates, strong trade, and growing FDI and low fiscal deficits. Asian countries have followed up a way of reforms to start their economies to create a center for foreign capital inflow. Recognizing the manifold profit of FDI, developing countries around the world have noticeably reduced restrictions on foreign capital movement. It is noted that FDI has not only provided the developing countries with much desirable funds for domestic investment, but also helps to transfer of managerial skill & technologies and creates employment prospects, all of which add to economic growth. International liberalization is one driver of FDI flows, as financial liberalization, permitting capital inflow more easily across the globe. This is proved by advances in global integration of manufacture, marketing and servicing system as unified systems etc. On average, South and East Asia attracted 7% of annual global FDI flows in the 1980s and just fewer than 15% in the 1990s which is in 2014 about 55%. According to 'World

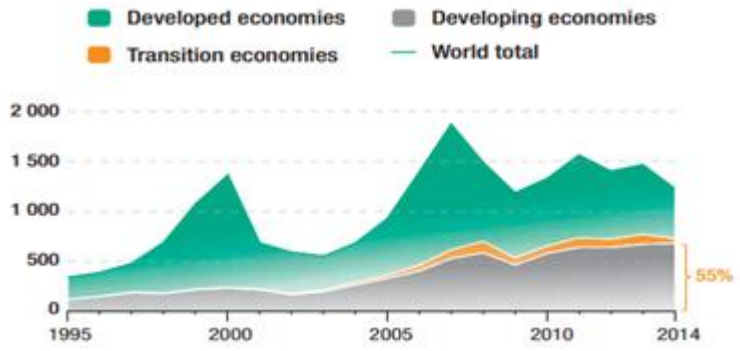
Investment Report-2015', global FDI inflows declined in 2014 and global FDI inflows fell by 16% to $1.23 trillion in 2014, mostly because of the weakness of the global economy, policy uncertainty for investors and elevated geopolitical risks (UNCTAD, 2015). Inward Foreign Direct Investment flows to developing economies arrived at their peak level at 681 billion dollar with a 2% rise and developing economies especially Asian countries are able to extend their fronts in global world. Among the top ten Foreign Direct Investment receivers in the world, five are from less developing economies. From Asian countries, China became the world's largest receivers of FDI. Investments by developing country multinational enterprises (MNEs) also reached a record level especially in developing Asia.

FDI has been recognized as a very important parameter in speeding up the process of growth and development in developing economies and therefore it is the main role of the govt. of these nations to smooth up the process of money inflow. Furthermore, the sizable reduction in foreign aid programs since the end of the cold war has forced countries until now to depend heavily on foreign public debt to look for alternative sources of foreigncapital. Accordingly, the annual inflow of foreign direct investment to the developing countries has increased multiple from 24% of total foreign investment in 1990 to 55% as per the information from (World Bank, 2015). A series of programs have been implemented by these countries over the last 30 years to increase the inflow of foreign direct investment. But, it is very crucial to understand the precise set of factors that can create maximum inflow of FDI and help these countries in achieving their goals. In this paper an attempt has been made to analyze the trend and determinant of foreign direct investment in Asian countries using GDP, trade openness, exchange rate, interest rate and labor quality etc.

According to World Investment Report 2015, foreign direct investment inflows to Asia rose to dollar 41 billion in 2014, primarily due to good performance by India and China. Foreign direct investment inflows to India improve by 22% to about dollar 34 billion and FDI inflows to Pakistan enlarged by 31% to dollar 1.7 billion as a result of rising Chinese Foreign Direct Investment flows in service sector. In Sri Lanka, FDI streams from China also rose and China has become the ruler source of foreign direct investment to the country in recent years. In the manufacturing sector, foreign direct investment successes have emerged with the automotive industry in India, showing how large-scale FDI inflows can revamp the route of industrial progress in low income countries. In recent years, the global FDI decline and there is a wide regional disparity of investment. While there is a significant decrease in inflows of FDI to developed and transitional economies, at the same time developing economies achieve high levels of capital inflow.

Figure: 2

FDI Inflows from 1995"2014 (Billions of dollars)



Source: UNCTAD database

FDI flows to developing economies increased by 2% to a historically high level in 2014, reaching dollar 681 billion. The FDI flows to Asia grew by 9 % to dollar 465 billion in 2014.

Figure: 3

FDI flow to Different Regions

Source: UNCTAD database

The paper has been divided into three parts: first part discuss the present trend and direction of FDI in Asian countries. In the second part, an endeavourer has been made to determine the determinants of FDI in Asian countries using simple regression model and in the last part some policy issues has been discussed such as whether growth stimulate FDI in these countries.

2. LITERATURE REVIEW

In Asian countries, there was a large augmentation of inward FDI flows since 1990s coupled with the swift globalization of production from developing countries (Chakraborty & Basu, 2002). Domestic investment is balanced by FDI and also have extra burden on current account balance in the short run. According to Romeo (1980), FDI does not speed up growth process. However, macro level analysis of FDI inflows for different countries, normally advocate an accommodating function of foreign direct investment on growth (Borensztein et al 1995). Economic growth is strengthening by foreign direct investment in the neoclassical outlook through addition in the level of savings or investment (Solow, 1956). FDI is comprises capital and technology and thus it improve the level of knowledge (DE Mello 1999). Foreign direct investment is more helpful for those economies where export endorsement instead of import substitution policies are adopted (Balasubramanyan et al, 1996). On the other hand, the growth theories use foreign direct investment as one of the regressors, relating to output growthfunction (Balasubramanyam et al 1996; Borensztein et al 1995). Technology transfers implied in foreign direct investment are broadcasted to local firms by multinationals firms. Foreign direct investment boosts the productivity of all the firms in the beneficiary economy. However, developing economies are benefited from these spillovers only if they have proper skilled workforce (Nelson and Phelps (1966), which pointed out towards the FDI-lead growth theory. At the same time, growth-driven foreign direct investment theory, move for superior rewards in the host nation are as a basis of attraction for FDI. According to this theory, there is capital inflow in the shape of FDI to plug the overload demand that exists in the home country as a result of economic growth (Markusen, 1995). FDI has optimistic impact upon growth too (Dunning, 1993; Ericsson and Irandoust, 2000; Trevino and Upadhyaya, 2003) and in some cases, it has off-putting effect on growth too (Moran, 1998). Positive effect of FDI on economic growth occurs when FDI comes into markets, while negative effects occurs when FDI comes into protected industries (Encarnation and Wells, 1986). Generally, the smaller rather the greater part of domestic investment is substituted by foreign direct investment. In order to attract FDI, education, tax law, wages, and socio-political and macroeconomic conditions of country in addition to market condition play an important role. Corporate taxes have negative, (Hsiao, 2001) while import tariffs, infrastructure, political and macroeconomic stability generally have positive impact upon FDI inflows (Biswas, 2002).

There is an extensive variety of literature on determinants of foreign direct investment in various countries and a sizable empirical literature has also focused on the determinants of FDI to the developing nations. These studies have identified a number of variables, such as trade, openness, infrastructure, labour cost, return on capital, domestic macro policies, political instability etc. that attract foreign direct investment. Domestic investment climate in the receiver countries is also measured as an important determinant of foreign direct investment which has been excluded in the empirical literature, as consistent and reliable set of quantitative data on investment climate is generally out of stock. Most empirical studies in the foreign direct investment literature have identified a number of variables. However, there is no general agreement in the literature as to the way of influence of a number of these variables.

2.1 Real GDP Per Capita:

Schneider & Frey (1985), Tsai (1994), and Lipsey (1999) found real Gross Domestic Product per capita to have a positive effect on foreign direct investment, while Jaspersen et al (2000) found it to have a negative effect.

2.2. Labour Cost:

Wheeler & Mody (1992) had found labor cost as a significant and positive factor on foreign direct investment, while Schneider & Frey (1985) found the opposite. Some studies had found results that suggest that even if all the factors that have influences on the foreign direct investment are accounted for, there still exits an inter-regional bias in the foreign investment inflow and outflow. Schneider & Frey (1985), Edwards (1990), Gastanaga et al (1998), Jaspersen et al (2000), Asiedu (2002), etc., have found that there exists a regional bias in the foreign capital inflow against Saharan Africa. These studies, however, could not concur on the factors that are accountable for attracting foreign direct investment.

2.3. Human Capital

Hanson (1996), Root & Ahmed (1979) and Schneider & Frey (1985) found that the level of human capital was a good indicator of the availability of a skilled work force which is considered as important determinant of the locational advantage of host countries. Noorbakhsh et al (2001) documented the significance of investment attractiveness as a factor in attracting foreign direct investment. In their model, they used the level of human capital as a proxy for investment attractiveness. However, uncertain economic environment create hurdles for long-term planning by reducing investment opportunities and Govt. Political turmoil also seriously set back the investors' assurance in the local investment climate.

2.4. Political Structure

Level of political structure, corruption, well-organized markets, contracts and property rights also affect in foreign direct investment. Asidieu (2002) challenged that South Asian countries are seemed to be as intrinsically risky, and that can be a factor which likely keeps away foreign direct investment from the region.

2.5. Economic Freedom

Quazi in his model (2004) applied economic freedom which was used as a proxy of domestic investment climate was included as one of the explanatory variable. These variables proved to be very noteworthy and remained vigorous under different model specifications. The amalgamation of economic freedom also showed that there was no inbuilt bias against Asian countries and North Africa, but there is indeed a regional bias in favor of countries located in Latin America and Caribbean vis-a-vis other regions, which is perhaps due to the physical propinquity of this region to the United States and. Some studies seeks to fill determinants of FDI using data on economic freedom from annual index published by published by the Heritage Foundation and The Wall Street Journal since 1995, as a proxy for domestic investment climate.

The Index of Economic Freedom calculated by Heritage Foundation takes a broad and comprehensive view of economic freedom, measuring country performance in 10 separate areas. Some of the measures of economic freedom that are evaluated are concerned with a country's interactions with the rest of the world; for example, the extent of an economy's openness to global

investment or trade. Most, however, focus on policies within a country, assessing the liberty of individuals to use their labor or finances without undue restraint and government interference. The 10 measured aspects of economic freedom may be grouped into four broad categories:

- Rule of law (property rights, freedom from corruption);
- Government size (fiscal freedom, government spending);
- Regulatory efficiency (business freedom, labor freedom, monetary freedom); and
- Market openness (trade freedom, investment freedom, financial freedom).

In assessing the conditions in these four categories, the Index measures 10 specific components of economic freedom, each of which is graded on a scale from 0 to 100. Scores on these 10 components of economic freedom, which are calculated from a number of sub-variables, are equally weighted and averaged to produce an overall economic freedom score for each economy. Economic freedom calculated by Heritage Foundation for the countries in the 2015 Index of Economic Freedom, the 21st annual edition included 186 countries included in the 2015 Index, 178 are fully scored and ranked. Because of insufficient data, Afghanistan, Iraq, Kosovo, Libya, Somalia, Sudan, Syria, and Liechtenstein are covered without numerical grading.

In the backdrop of this empirical literature, this study attempts two contributions to the empirical foreign direct investment literature. First, it adds Asia to the empirical regional studies of foreign direct investment. Second, and more importantly, it explicitly treats domestic investment climate, as captured by the index of economic freedom, as a determinant of foreign direct investment.

3. METHODOLOGY

This paper studies 30 Asian countries and quantifies the effects of factors that drive the flow of FDI into these countries. Employing 2013 to 2015 cross section data from UNCATED, this study focus on the impact of exchange rates, GDP per capita, Consumer Price Index, GDP growth rate, merchandise exports and imports, interest rate and economic freedom, public debt etc on FDI in Asian countries which is crucial for devising strategies to promote economic development that holds much up for grabs not only for Asia, but also for developing countries in general.

3.1. The Model

In the absence of a consistent theoretical framework in the FDI literature that incorporates economic freedom to guide our empirical, in the initial stage, it has been tried to incorporate a general model for all the countries, but fails to find any consistency of the values that determine the FDI and therefore, the regression analysis has been segregated in four different time periods using two sets of variables provided by United Nations Conference on Trade and Development (UNCTAD) for the year 2013 and three data set provided by The Heritage Foundation for 2013, 2014 and 2015

(i) The following model has been identified as the determinants of the FDI in Asian countries using data from UNCTAD for the year 2013.

$$FDI = \alpha + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \beta_4 X_4 + \beta_5 X_5 + \beta_6 X_6 + \varepsilon \quad (i)$$

Where, FDI = Foreign Direct Investment; X_1= GDP in US dollars (Millions US$); X_2 = Growth of Consumer Price Index; X_3 = GDP growth rate; X_4 = Merchandise exports (millions of US$); X_5 = Merchandise import (millions of US$); X_6 = Trade openness (sum of imports and exports as % of GDP); β_i = Co-Efficient; and ε = error term.

(ii) The following model has been identified specified tol find out the determinant of the FDI in Asian countries using data from Heritage Foundation for 2013, 2014 and 2015

$$FDI = \alpha + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \beta_4 X_4 + \beta_5 X_5 + \beta_6 X_6 + \beta_7 X_7 + \beta_8 X_8 + \beta_9 X_9 + \beta_{10} X_{10} + \varepsilon \quad (ii)$$

Where, X_1 = Economic Freedom Score; X_2 = Property Rights; X_3 = Business Freedom; X_4 = Labor Freedom; X_5 = Tariff Rate (%); X_6 = Corporate Tax Rate (%); X_7 = Tax Burden as % of GDP; X_8 = GDP (Billions, PPP); X_9 = Inflation (%) X_{10} = Public Debt (% of GDP);

β_i = Co-Efficient; and ε= error term. Several estimation of the same variable has been calculated to find out the general tendency of factors that affect FDI in Asian countries. On the other hand, two data sets: one from UNCTAD and Heritage Foundation. There are four situations when regression estimation has been used.

Situation-1:

In situation-1 model (i) has been used using data from UNCTAD for the year 2013.

Situation-2:

In situation-2 model (ii) has been used using data from Heritage Foundation for the year 2013.

Situation-3:

In situation-2 model (ii) has been used using data from Heritage Foundation for the year 2014.

Situation-4:

In situation-2 model (ii) has been used using data from Heritage Foundation for the year 2015.

It has been believe that the factors that determine FDI are vary from time to time. So, simple regression has been used several times to determine general factors of FDI in Asian countries.

Limitation of the Study:

Limited set of variables has been used for analysis due to lack of consistent data. Application of more sophisticated econometric methods such as panel data discussion and co-integration analysis using time series data will explore more hidden results.

4. RESULT AND DISCUSSION

In Asian countries, Foreign Direct Investment in China rose to dollar 129 billion, up 4 % from 2013, mainly because of an increase in FDI in the services sector. FDI inflows also rose in Hong Kong and Singapore. India experienced a significant increase in FDI of 22 % to $34 billion. However, FDI flows to West Asia continual their downhill trend in 2014 for the sixth consecutive year, decreasing by 4 % to 43 billion dollar, due to the defense situation in the region. Overall, China became the largest FDI receiver in the world in, while the United States dropped to the third largest host country.

Developing Asia became the world's largest depositor region in 2014 and MNEs from developing economies alone invested 468 billion dollar abroad which was a 23% increase from the previous year. Their share in global FDI reached a record 35%, up from 13% in 2007. Outward investments by MNEs based in developing Asia increased by 29% to 432 billion dollar in 2014. The growth was extensive, including all the major Asian economies and sub regions. In East Asia, investment by MNEs from Hong Kong (China) jumped to a historic high of 143 billion dollar, building the economy the second largest investor after the United States. The amazing growth was mostly due to blooming cross border activity. Investment by Chinese overseas grew faster than inflows into the country, attaining

Figure: 4
Top FDI in Flow countries, 2014

a new high of 116 billion dollar. In East Asia, the increase was mainly due to the result of mounting outflows from Singapore, to 41 billion dollar in 2014. In Asia, FDI outflows from India upturned the slide of 2013, increasing fivefold to 10 billion dollar in 2014, as large Indian MNEs resumed their international expansion. Among the South Asian countries, India is at the top with 34 million FDI inflows, followed by Pakistan, Bangladesh and Sri Lanka. FDI inflows in Developing Asian countries saw grow to historically high levels. Performance of South-East Asian economies differed significantly.

4.1. Situation 1: (Data from UNCATD -2013)

To explain the variation in FDI, a multiple regression analysis was carried out using UNCTAD data for the year 2013. Equation (i) for explaining variation in FDI across the countries is being estimated using the ordinary least square estimates.

Table: 1
The Results of OLS Estimation

Variables	Estimated Co-Efficients
(α) Constant term	-10895.797**
($??_1$) GDP	0.012**
($??_2$) CPI growth	414.081
($??_3$) GDP growth	1086.791
($??_4$) Merchandise exports	0.040**
($??_5$) Merchandise import	0.069**
($??_6$) Trade openness	0.448
R square	0.88
Adjusted R square	0.85
F	19.42**

** Significant at 5% level

The R square value is found to be 0.88 which is high even though extensive cross section data is used. Moreover the t-value of the three variables is statistically significant implying the relevance of the corresponding factors in explaining the variation in FDI. The F statistics for over all regression is also statistically significant. The co-efficient of the explanatory variables X_1, X_4 and X_5 variable is significant. The estimated results are noteworthy for several reasons. First, in addition to the usual determinants of FDI found in the literature, such as economic openness, consumer price index,etc., this study has found that GDP is also a significant determinant of FDI in Asian countries. Besides, GDP, export and import is also as usual found other two factors that determine the FDI in these countries.

4.2. Situation-2 (Data from Heritage Foundation -2013)

Second time, we use data from the Heritage Foundation using 10 variables as mention in model 2 (equation-2). The reason behind this was to explore some more variable that determine the FDI in Asian countries. It is found that only GDP is the sole significant variable in this model that determines the FDI in Asian countries.

Table: 2
The Results of OLS Estimation

Variables	Estimated Co-Efficients
(α) Constant	-99204.209
($??_1$) Freedom Score	1880.736
($??_2$) Property Rights	-111.722
($??_3$) Business Freedom	-32.062
($??_4$) Labor Freedom	-188.225
($??_5$) Tariff Rate	89.526
($??_6$) Corporate Tax Rate	116.730
($??_7$) Tax Burden % of GDP	NA
($??_8$) GDP	10.599**
($??_9$) Inflation	1552.841
($??_{10}$) Public Debt	-168.935
R square	0.75
Adjusted R square	0.61
F	5.46**

** *Significant at 5% level*

NA: Not estimated as sharp reduction in Adjusted R square

4.3. Situation-3 (Data from Heritage Foundation-2014)

Third time, the same data 10 variables are used mention in model 2 (equation-2). The reason behind this was to explore the general tendency and consistency of the variables of FDI in Asian countries. From the result four significant variables of FDI are found out. Along with significant constant term, Economic Freedom Index, Property Right, GDP and Public Debt are the significant variables in this model and R square and adjusted R square was high along with significant F statistic.

Table: 3
The Results of OLS Estimation

Variables	Estimated Co-Efficients
(α) Constant	-159927.121**
(β_1) Freedom Score	2942.982**
(β_2) Property Rights	-578.034**
(β_3) Business Freedom	-367.101
(β_4) Labor Freedom	192.493
(β_5) Tariff Rate	930.987
(β_6) Corporate Tax Rate	126.147
(β_7) Tax Burden % of GDP	862.991
(β_8) GDP	9.355**
(β_9) Inflation	1264.008
(β_{10}) Public Debt	-229.453**
R square	0.87
Adjusted R square	0.77
F	9.44**

** Significant at 5% level

The model imply that GDP is not the sole determinant but other fact such as economic environment, property rights public debt also determine the FDI flow in Asian countries.

4.4. Situation 4 (Heritage Foundation - 2015)

For confirmation of 2014 result, we again use same model using the 2015 data and found some similar results. The R square value is 0.84 which is high even though extensive cross section data is used. Moreover the t-value of the three variables is statistically significant showing the application of the corresponding factors in explaining the variation in FDI. The F statistics for over all regression is also statistically significant. The only difference is that variable 'Property Right' was not found significant.

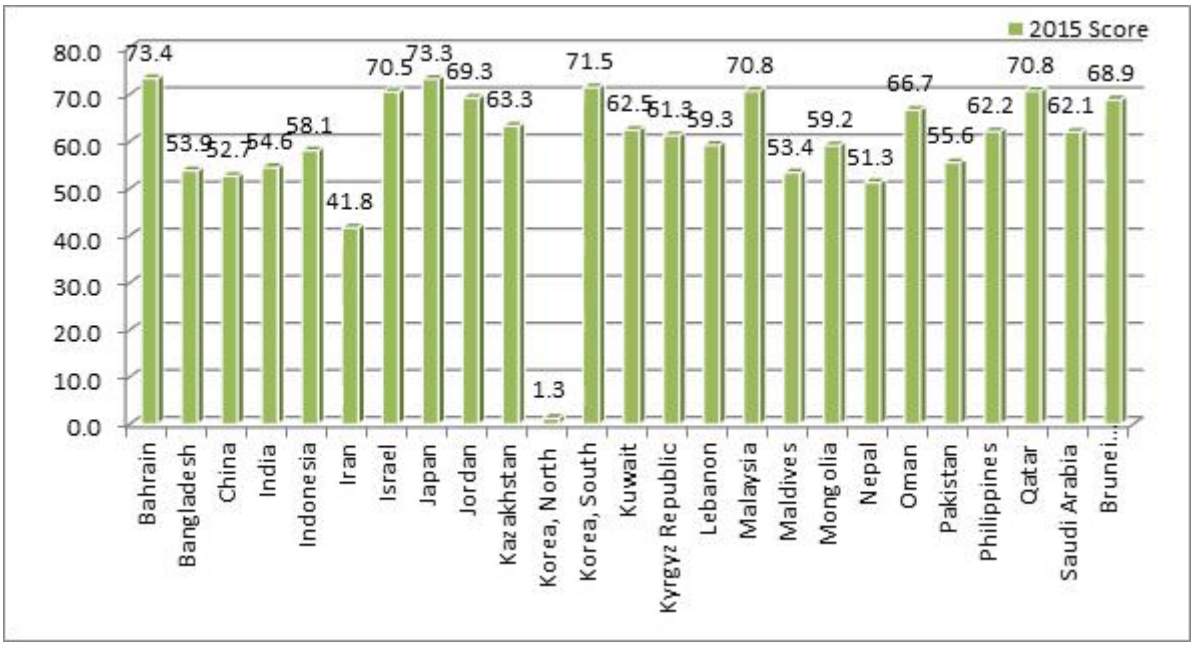
Table: 4
The Results of OLS Estimation

Variables	Estimated Co-Efficients
(α) Constant	-140346.108**
(β_1) Freedom Score	2591.545**
(β_2) Property Rights	-419.904
(β_3) Business Freedom	-21.916
(β_4) Labor Freedom	-120.372
(β_5) Tariff Rate	1214.056
(β_6) Corporate Tax Rate	185.656
(β_7) Tax Burden % of GDP	-38.075
(β_8) GDP	9.751**
(β_9) Inflation	488.721
(β_{10}) Public Debt	-155.662**
R square	0.84
Adjusted R square	0.73
F	8.08**

** *Significant at 5% level*

The estimated results are noteworthy for several reasons. First, in addition to the usual determinants of FDI found in the literature, such as economic openness, consumer price index, etc., this study finds that along with GDP, Economic Freedom, which is used as a proxy for economic environment is also a significant determinant of FDI in Asia. Besides, this, Public Debt is also found one determinants of FDI in these countries

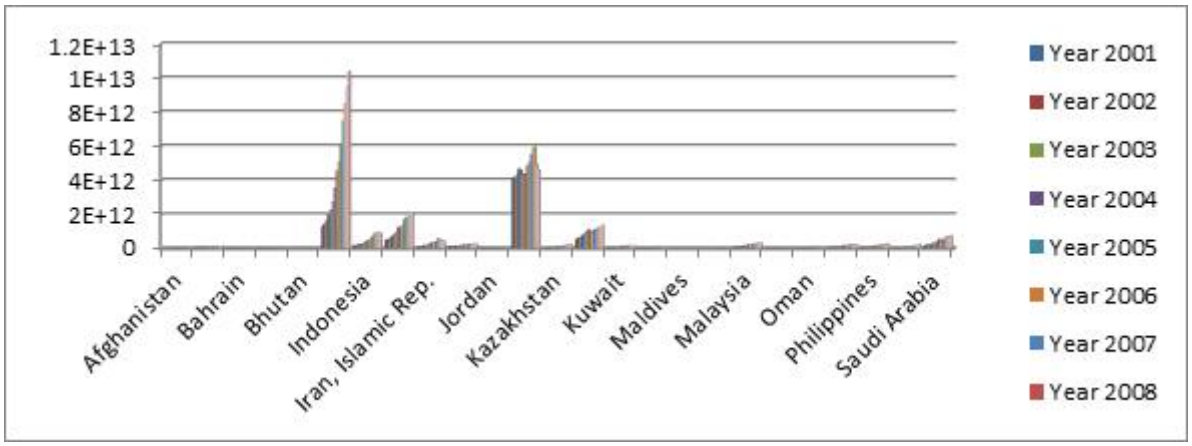
Figure: 5 Freedom Score-2015



Source Heritage Foundation, 2015

In Asian countries, the freedom score of China is at highest level followed by Bahrain, Japan, and Malaysia which is found lowest for North Korea and followed by Iran. On the other hand, looking at the GDP value for Asian countries from 2001 to 2010, the value of GDP in China is almost five times more as compared to other Asian Counties except Japan. In terms of GDP among Asian countries, Indian rank is 3rd and continues to grow faster.

Figure: 6 GDP Values of Asian Countries



Source: World Bank, 2015

The important finding is that GDP value is the sole determinant over the periods of FDI in these countries and economic environment is also another factor that determines the trade and FDI in these countries. Public debt situation is also determining the nature of FDI in these countries. These results generally suggest that in order to attract more FDI, Asian countries need to improve GDP value rather and short term growth rate which has no such impact on FDI in these countries. Improving GDP is however a difficult process, which cannot be realized overnight. A closer look at the trade arrangement suggests that governments can improve their domestic trade atmosphere by reducing by reducing tax rates, reducing government ownership of businesses and industries, average tariff rate and non-tariff barriers, and government expenditures, curbing the inflation rate, liberalizing the banking and financial sectors, thrilling restrictions on foreign ownership of resources,

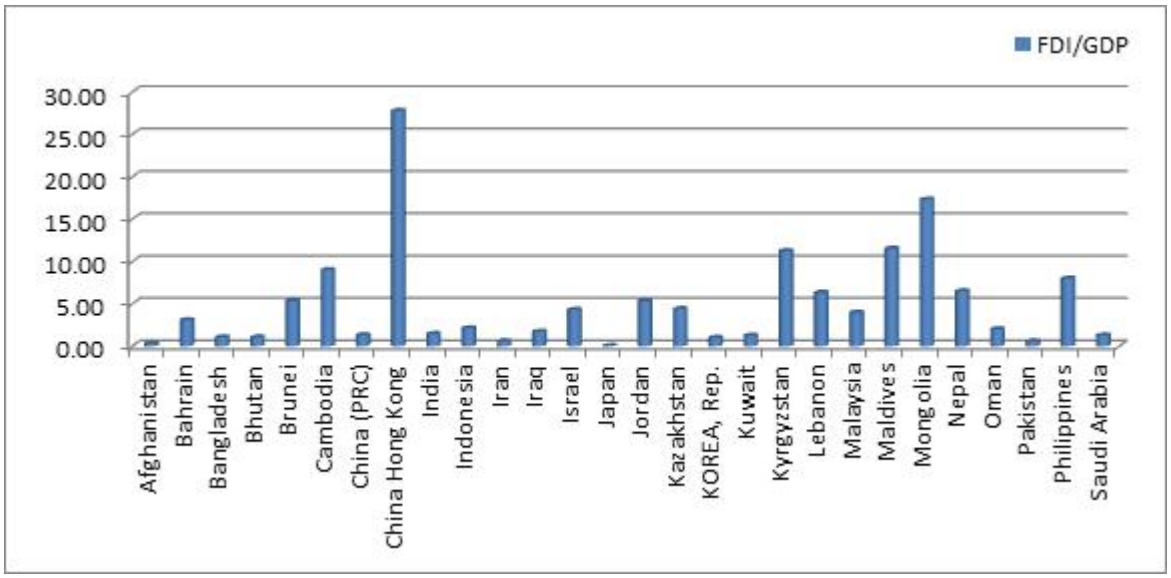
securing private property rights allowing market wages and prices and an independent judicial system, reducing excessive regulatory burden etc. Adoption of these policies may be politically tricky in the short run.

Low level of public debt, which is a proxy for financial structure, is found to attract more FDI inflow in South Asia. Since public debt is generally affected by economic growth and therefore, government strategies to promote higher FDI should comprise pro-growth economic policies. Policymakers should remain wary of the linkages between economic growth and a lower FDI inflow, which in turn reduces future economic growth potential and thus sets a vicious cycle in motion. However, growing public debt affects the FDI in Asian countries which is imply from negative sign in the model. Political instability is found to significantly depress FDI inflow in South Asia. Empirical results suggest that the occurrence of civil war is in fact the most damaging hurdle to attracting FDI inflow in Sri Lanka vis-a-vis other nations in the region. Although this study does not explicitly investigate the effects of politically destabilizing events, such as political eliminations, inveterate strikes and shutdowns, etc., it is quite conceivable that these events also severely erode the foreign investors' assurance in the Asian countries economy and consequently reduce FDI inflow. Developing nations should therefore try their utmost to prevent a politically undermine climate and instead promote a stable economic environment that is conducive to long-term planning and investment opportunities, which in turn will attract more FDI inflow.

The FDI as per cent to GDP is low except China (27.79. With the growing volume of FDI to Asian countries, it is essential to analyze the relationship between FDI and GDP in these countries with special reference to South Asian countries.

Figure: 7

Foreign Direct Investment as Per cent of GDP (2013)



Source: Composed from UNCTAD, 2015

Now the question is whether FDI also determine GDP in Asian Countries? The answer is positive FDI inflow and outflow also have a impact on the GDP in these countries. The reverse model also suggests the same with significant t vale and high r square value.

5. FOREIGN DIRECT INVESTMENT IN INDIA

FDI inflows to South Asia rose to $41 billion in 2014, primarily due to growth in Indian economy. In terms of sectoral composition, manufacturing is gaining strength, as policy efforts to refresh the sector. FDI outflows from South Asia originate

mainly from India. In 2014, Indian outflows saw a five-fold jump to $10 billion, recovering from a sharp decline in 2013. As the performance of the Indian economy has improved, large Indian MNEs have international expansion, including announcements of some intraregional investments in manufacturing (such as in the automotive and chemical products industries) in neighboring countries such as Bangladesh and Sri Lanka. In India, the automotive industry is played a key part of the Indian economy and has been identified as one of the key industries in which India has the potential of becoming a world leader. India accounted for the majority of Greenfield investment projects announced by global automakers and first-tier parts suppliers in Asia during 2013–2014, including 12 projects above 100 million dollar. Inward FDI has led to the emergence of a number of industrial clusters in India, including those in the National Capital Region (Delhi-Gurgaon-Faridabad) in the north, Maharashtra State (Mumbai-Nasik-Aurangabad) in the west, and Tamil Nadu State (Chennai-Bangalore-Hosur) in the.

Figure: 8
Major industrial clusters in the automotive industry

Though considerable differences exist in the patterns of the formation of these clusters, FDI can play an important catalytic role. On a smaller but significant scale, Bangladesh, Nepal, Pakistan and Sri Lanka recorded cases of Greenfield investment announced by foreign companies during 2013–2014. Investment from the growing automotive industry in India shows potentials of a positive 'spill-over effect' to productive capacity building in Asia as a whole. FDI helped the automotive industry in South Asia. Facing constraints such as weak productive capacities and poor infrastructure, South Asian countries have generally lagged behind East and South-East Asian countries in attracting FDI in manufacturing. However, some success stories have emerged at country, industry and local levels, partly because of higher growth rates in recent years and efforts to improve infrastructure and communication. The automotive industry shows how FDI inflows can reshape the trajectory of industrial progress.

6. CONCLUSION

It is a well noted in economics literature that foreign direct investment plays an important

role in the growth dynamics of developing countries. However, analysis suggests that there is wide divergence in FDI inflow among the Asian countries. This study makes significant contributions to the FDI literature, as it adds Asia to the regional studies of FDI, and more prominently, it unambiguously treats domestic investment. The estimated results, obtained from an OLS regression model based on 2013-2015 data, suggest that greater economic freedom, which is a proxy for better domestic investment climate, high economic openness, greater economic prosperity, higher GDP value significantly boost the FDI inflow, where high public debt reverse the FDI. While, these results are generally consistent with the current FDI literature, however the result that domestic investment climate, export and import is a statistically significant and robust determinant of FDI is a noteworthy improvement over the current literature, which by and large focuses on the other commonly used determinants. Domestic investment climate that is not conducive to economic freedom will likely negate the stimulating effects of other positive determinants of FDI, such as greater human capital, political stability, etc. Therefore, strategies should be formulated to promote long-term economic freedom in Asian countries, which will likely foster a healthy economic environment that is not only ready to attract more FDI inflow, but also prepared to nurture the economic ingredients necessary for economic development. Now, the question is whether FDI also determine GDP in Asian Countries? The answer is positive FDI inflow and outflow also determine the GDP in these countries. The reverse model also suggests the same with significant value. Connectivity between Asian countries is intensifying across communications, commerce connections and institution. Infrastructural connectivity intensifies, but more investment is needed**.** This trend is being driven by regional cooperation has helped improve infrastructural connectivity within the region and especially that between East Asia and South-East Asia. There is the scope to analyze the internal factors that determine the FDI in Asian countries and effect on regional inequality and poverty using panel data analysis.

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