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Attracting Foreign Direct Investment: The Case of Malaysia

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Abstract: Foreign Direct Investment (FDI) has contributed significantly to the transformation of the Malaysian economy as reflected by the changing composition of its exports and the rising share of FDI inflows. From previous studies, it has been identified that financial market development, market size of the economy, government infrastructure expenditure, economy openness, real exchange rate, corporate tax and inflation rate do contribute to the FDI inflows into a country. However, the significant contribution of each of the factors vary by countries. Thus, this study attempted to find out determinants of FDI inflows in Malaysia. The study used data concerning the FDI inflows into Malaysia from the year 1991-2010. Analysis was then carried out to identify the relevance of these determinants towards FDI inflows into Malaysia. Based on the results obtained, it shows that FDI inflows have significant positive relationship with financial market development and market size of the economy. However, FDI inflows are negatively related to corporate tax. Therefore the Malaysian government has to take certain measures to increase financial market developments and the market size of the economy but reduce or stabilize their corporate tax to encourage more FDI inflows into Malaysia.

Key words: FDI, financial market development, market size of the economy, economy openness, government infrastructure expenditure

INTRODUCTION

The establishment of the Federal Industrial Development Authority (FIDA) in 1965 which was renamed the Malaysia Industrial Development Authority (MIDA) in 1967 marks the first foray into the formulation of policies to attract FDI to Malaysia. The government introduced the Investment Incentive Act in 1968 to promote export-oriented FDI by offering several financial incentives. These included exemptions from company tax and duty on imported inputs, investment tax credits and accelerated depreciation allowance on investment (Athukorala and Menon, 1996). Since then, Malaysia has been encouraging Foreign Direct Investment (FDI) inflows not only for its role in technology transfer but also for its economic contribution. Identifying the factors affecting FDI is important in explaining the Malaysian economy performance. Therefore the aim of this research is to investigate the impact of the financial market development, market size of the economy, government infrastructure expenditure, real exchange rate, economic openness, corporate tax and inflation rate towards FDI inflows.

There have been many attempts by many previous studies and researches to identify and to explain the key determinants of FDI in Malaysia. The FDI inflows model explains about the potential importance of FDI activities in a Developing Country (DC) like Malaysia's development process which is gaining appreciation. Malaysia has been encouraging FDI inflows because of the potentials that FDI possesses to heighten economic growth. Therefore, the aim of this study is to investigate the impact of financial market development towards FDI inflow performance in Malaysia for a period of 20 years which is from the year 1991 up to the year 2010. This study denotes financial market development as the Malaysian stocks. On the other hand, there are a lot of arguments in explaining the magnitude of the relationship between FDI inflows and Malaysian stocks (Asan *et al*., 2011). Therefore, the influence of exports and stock markets on the stability of FDI inflows in Malaysia in the short and long run is being sought through this study.

This study tried to identify the widely researched upon relationship between FDI and economic growth. This study also attempted to devote attention again on this causality between GDP and FDI however with different sample period. Research on FDI has been on the most intensive areas of international economics in the last decade (Pan, 2002). Theory, however, provides conflicting predictions concerning the growth effects of FDI. The economic rationale for offering special incentives to attract FDI frequently derives from the belief that foreign

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investment produces externalities in the form of technology transfers and spillovers. According to Rodrik (1995) FDI may boost the productivity of all firms not just those receiving foreign capital. Thus, transfer of technology through FDI may have substantial spillover effects for the entire economy.

In contrast, some theories predict that FDI in the presence of preexisting trade, price, financial and other resource allocation and slow growth. Thus, theory produces ambiguous predictions about the growth effects of FDI and some model suggests that FDI will promote growth only under certain policy conditions. Firm-level studies of particular countries often find that FDI does not boost economic growth and these studies frequently do not find positive spillovers running between foreign owned and domestically owned firms. This study uses datacollected from the World Bank dataset to reassess the relationship between economic growth and FDI. This is carried out by utilizing available information to identify the causal relationship between FDI and economic growth. The findings from this study then can further help the Malaysian government to focus on key areas to make the necessary improvements that way they can boost FDI inflows into Malaysia.

Foreign Direct Investment (FDI) and its causal relationship with economic growth generated interest from many countries. As investors search the globe for the highest returns they are often drawn to places endowed with bountiful natural resources but are handicapped by weak or ineffective environmental law. The recently released UNCTAD (2009), World Investment Report has ignited a heated but nonetheless welcome policy debate about Malaysia's Foreign Direct Investment (FDI) performance and economic policies. Two issues are involved in this debate. The first is the much steeper-than-expected fall in FDI inflow in 2009 while the second is the sizeable outflow of FDI from Malaysia.

Given the near global economic collapse in late 2008, the fall in FDI was not entirely unexpected. But while global FDI dipped by 37%, Malaysia's FDI fell by a whopping 81% from the previous year from US$ 7.3 billion in 2008-2009. The second issue is a related but different one, namely there was a FDI outflow from Malaysia to tune of US$ 8.04 billion, resulting in the country experiencing a negative FDI flow on a net basis. Should we be concerned about these two issues? If so, how should we react? One thing is certain: we cannot understand, let alone resolve, anything solely in macro and abstract terms. We need to examine the facts in detail but also holistically if we are to come to grips with the problem and propose solutions. The foreign direct investment flows can fluctuate wildly from year to year. In 2001 for example, Malaysia only managed to get US$ 0.5 billion but in 2002, FDI shot up by astounding 540% to US $3.2 billion. Other countries have had similar experiences. Singapore's FDI inflow declined by 70% in 2008 but rebounded back by 54% in 2009. Given the sharp year to year volatility, it is recommended to look at FDI over a longer period. When we do so, we see that FDI inflows to Malaysia have increased, although not as robustly as other countries. From 2000-2009, the country's FDI inflows grew by 4.2% annually while other countries in the region increased by double digits. Many measures and funds have been given to promote innovation, R&D and technology development and acquisition. Education reforms, improving teachers' skills, expanding vocational and technical training, easier importation of skilled foreign workers and brain gain programs are among the measures to address the issue of skilled manpower. The Government Transformation Programme (GTP) aims to improve public sector delivery. A long overdue decision has been taken to corporatize and empower the Malaysian industrial (now investment) development authority because Malaysia needs to move faster in the highly competitive world of FDI.

Literature review: This study has a purpose to understand the determinants of FDI activities to understand the changing role of FDI in a country's economy and the causal relationship of FDI and growth towards Malaysia. Past literatures on related scholarly models were reviewed to understand the research findings of Foreign Direct Investment, its impact towards the Malaysian economy growth and to construct a theoretical model concerning the findings. The following study concerning, the market size of the economy is being represented by Gross Domestic Product (GDP) to show that the Malaysian economy relied on the foreign funds as a major source of capital, modern technology and technical skills (Marial and Teng, 2009). Globalization, international financial integration and expansion of global production have intensified FDI. This study examines the determinants of foreign direct investment in Malaysia from 1991-2010. The causality and dynamic relationship between Foreign Direct Investment (FDI) and its key determinants is identified using an Autoregressive Distributed Lag (ARDL) framework (Shahrudin *et al*., 2010).

A causal relationship between FDI and growth: Chowdhury and Mavrotas (2005) did a study on the relationship between Foreign Direct Investment (FDI) and economic growth has motivated a big empirical literature focusing on both industrial and developing countries. Neoclassical models of growth as well as endogenous growth models provide the foundation for most of the

empirical work on the FDI-growth relationship. The relationship has been studied by explaining four main channels determinants of growth, determinants of FDI, role of multinational firms in host countries and direction of causality between the two variables (Chowdhury and Mavrotas, 2005). A large number of empirical studies on the role of FDI in host countries suggest that FDI is a significant source of capital, complements domestic private investment is usually related with new job opportunities and enhancement of technology transfer and boost overall economic growth in host countries. A number of firm-level studies, on the other hand, do not lend support for the view that FDI encourage economic growth (Addison and Heshmati, 2003). Regarding developing countries in particular, macro-empirical work on the FDI-growth relationship has shown that-subject to a number of critical factors such as human capital base in the host country, the trade regime and the degree of openness in the economy, FDI has a positive impact on overall economic growth. The use of Toda-Yamamoto test involves the addition of one extra lag of each of the variables to each equation and the use of a standard Wald test to see if the coefficients of the lagged 'other' variables excluding the additional one are jointly zero in the equation (Chowdhury and Mavrotas, 2005). The results of The Wald test are given in Table 1. In the case of Chile, the assumption of non-causality from GDP and FDI is rejected at least at the 5% level, however, we cannot reject the non-causality assumption from FDI to GDP. Hence GDP causes FDI in Chile, In case of both Malaysia and Thailand there is a strong evidence of a bi-directional causality between GDP and FDI (Anwar and Nguyen, 2010).

Table 1: Optimum lag structure using Akaike's FPE criterion

	Own lags				
Variables	0	1	2	3	4
Dependent variable					
GDP	0.0677	0.0674	0.0663	0.0711	0.0705
FDI	0.0083	0.0081	0.0079	0.0076	0.0084
Other variable lags					
GDP (FDI)	0.0817	0.0856	0.0910	0.0872	0.0838
FDI (GDP)	0.0083	0.0080	0.0074	0.0089	0.0095
Malaysia (dependent variable)					
GDP	0.0241	0.0236	0.0229	0.0256	0.0298
FDI (GDP)	0.0566	0.0542	0.0610	0.0607	0.0594
Other variable lags					
GDP (FDI)	0.0242	0.0228	0.0230	0.0293	0.0277
FDI (GDP)	0.0585	0.0569	0.0532	0.0577	0.0564
Thailand (dependent variable)					
GDP	0.0044	0.0037	0.0048	0.0051	0.0046
FDI	0.1366	0.1320	0.1319	0.1377	0.1368
Other variable lags					
GDP (FDI)	0.0039	0.0036	0.0040	0.0043	0.0041
FDI (GDP)	0.1377	0.1310	0.1420	0.1364	0.1390

Chowdhury and Mavrotas (2005)

Table 2: Test results and misspecification diagnostics

Equation	Wald	JB	LM1	LM2	LM3	RR
Chile						
GDP	0.714	0.673	0.866	1.041	1.289	0.009
	(0.530)	(0.874)	(0.773)	(0.649)	(0.552)	
FDI	11.383	0.833	0.677	0.719	0.736	0.034
	(0.013)	(0.820)	(0.244)	(0.230)	(0.197)	
Malaysia						
GDP	19.041	1.049	2.044	2.709	2.933	0.163
	(0.003)	(0.340)	(0.378)	(0.314)	(0.362)	
FDI	16.383	0.875	1.985	2.066	2.843	0.199
	(0.011)	(0.477)	(0.442)	(0.343)	(0.267)	
Thailand						
GDP	9.838	0.704	3.020	3.085	3.128	0.075
	(0.008)	(0.552)	(0.744)	(0.689)	(0.640)	
FDI	11.120	0.533	1.642	1.744	2.104	0.144
	(0.007)	(0.694)	(0.381)	(0.363)	(0.224)	

The figures in parentheses are the p-values (Toda and Yamamoto, 1995)

It is notable that given the small size employed in this research, the Toda-Yamamoto test may suffer from size misrepresentation and low power. In view of this, this research checks for the sturdiness of the causality test results by recalculating the p-values obtained in the initial Wald test using a bootstrap test with 1000 replications. The idea behind a bootstrap test is to use the estimation residuals to artificially generate additional observations which have the same distribution as the original observations. Using the additional observations, a more robust estimation can be undertaken. The results are given below. The p-values in Table 2 show the probability that the independent variables in regression is equal to zero. The results confirm the findings reported in Table 1 (Chowdhury and Mavrotas, 2005). This research has employed an innovative methodology to test the direction of causality between FDI and growth for three major FDI recipients in the developing world that is Chile, Malaysia and Thailand, each with different macroeconomic episodes, policy regimes and growth patterns over the period 1969-2000. The empirical analysis based on Toda-Yamamoto causality test seem to suggest that it is GDP that causes FDI in Chile and not vice versa. In the case of both Malaysia and Thailand there is a strong evidence of a bi-directional causality between GDP and FDI (Akinboade *et al*., 2006).

At the same time, the results clearly suggest the need for more individual country studies on the above relationship, since causality between the two variables is also country specific. This is aligned with recent empirical work in this area which based on causality testing within a panel of 24 developing countries over a period of 25 years, proposes that the causal relationship between FDI and growth is characterized by a considerable degree of heterogeneity.

The financial market development and FDI Inflows Model: FDI was a major source of growth for manufacturing

development in Malaysia that mainly targeted the export market. Reviewing the literature, some past studies found mixed evidences of FDI and its key determinants relationship. A plausible explanation for this is different countries characteristics offers different results. The determinants may affect differently in different countries. In Malaysia, study by Ang and Van Dyne (2008) detects the significant effect of the variables in five models that that takes turn excluding some of the variables via 2SLS estimation. Although, the analysis was based on Error Correction Model, the issue of co-integration and error correction representation of the model was not addressed. The aim of this paper is to investigate the determinants of FDI in Malaysia during the period 1970-2010 using an Autoregressive Distributed Lag (ARDL) technique. Specifically, it seeks to identify the most important variables that affect the FDI in Malaysia via the co-integration analysis.

Data spanning from 1970-2010 are obtained from various sources of publications. Data on FDI, rate of growth, openness and government development expenditure are taken from various issues of Bank NegaraMalaysia Reports. International Financial Statisticsprovides data on exchange rate, money supply and inflation rate. Statutory corporate tax data is taken from the Department of Inland Revenue Annual Reports. Many macroeconomics variables are non-stationary in their level form and a liner combination ofnon-stationary variables does not imply that all the variables are co-integrated. An autoregressive distributedlag model allows co-integration at different orders of integration and is a robust estimation in a small sampledata. Failure to model appropriately the relationship may not give accurate results of the relationship and thisis crucial especially when it involves with policy recommendations.

The market size of the economy towards FDI: Market size of the host country which also represents the host country's economic conditions and the potential demand for their output as well is an important element in FDI decision-makings. Market size has proved to be the most important determinants of FDI, particularly for those FDI flows that are market seeking. Those countries which have large markets, the stock of FDI are expected to be large. The importance of the market size has been confirmed in many previous empirical studies (Asiedu, 2002). Foreign Direct Investment (FDI) is considered responsible for numerous areas being studied. A major growth-enhancing characteristic of FDI is the advanced technology that often go with foreign capital investment which the domestic investors can also adopt (Asari *et al*., 2011).

Malaysia is also one developing country that encourages FDI's in order to hasten growth and development. However according to Ishak, N.F in the early 90's the FDI inflows contributed to almost a quarter of the country's Gross Fixed Capital Formation and equivalent to over 8% of the country's GDP. Malaysia has been one of the most successful ASEAN countries to attract FDI. The positive relationship between FDI inflows and exports in relation to economic performance has been largely expected. Most of the existing research highlighted the substitutability of relationships between inflows of FDI and exports. The existing literature on the Malaysian position in relation to this subject matter proves to be insufficient (Asari *et al*., 2011).

Government infrastructure expenditure and exchange rate towards FDI: A considerable volume of literature has highlighted the importance of physical infrastructure as a determinant of economic growth by Marial and Teng (2009) and World Bank (2010). The estimated coefficient of infrastructure is positively signed as expected and statistically significant at a 1% level. In simpler terms, a 1% point improvement in infrastructure would induce FDI inflows to rise by approximately 2.6% annually. Multinational Enterprises (MNEs) may consider the quality of infrastructure available to be especially important while deciding to relocate export-platform production undertaken for efficiency considerations. In other words, quality of physical infrastructure could be an important consideration for MNEs in their location choices for FDI in general and for efficiency-seeking production in particular.

On the other hand, the evidence on the effect of real exchange rate in the short or long run has been consistently mixed. Based on the currency area hypothesis, the assumption is that firms would not invest in countries with weaker currencies. Capital market bias is said to arise because income streams from countries with weaker currencies and are associated with an exchange rate risk and therefore, an income stream is capitalized at a higher rate by the market when it is owned by a weaker currency firm. Similar evidence was reported by Kiyota and Urata (2004) who claimed a depreciation of the currency of the host country attracted FDI while high volatility of the exchange rate discouraged FDI. As exchange rate correlation converges towards one, exchange rate risk diversification becomes a weaker determinant of location at the same time as other factors like rate of return become more relevant (Marial and Teng, 2009). Previous study, therefore, concluded that exchange rate volatility generally has stronger negative effects on FDI inflows. The estimated coefficient of real exchange

rate is positively signed and statistically significant at the 1% level, suggesting that real appreciation of exchange rate causes FDI flows to surge into Malaysia. Hasan (2008) suggests that a weak currency is likely to increase the FDI flows into a country over time.

FDI in malaysia and its economic openness: The economic openness is another determinant widely claimed to be critical in influencing the FDI inflows into a country. Nonnemberg and de Mendonca (2004) and Sahoo (2006) found that openness variable is parallel with the inflows of FDI and exerted positive influence on the FDI. With exception of economic openness the estimated coefficients of all the specified determinants of FDI are statistically significant at least at the 10% export levels. FDI flows into Malaysia fell sharply in 2009 as exports contracted sharply. FDI faced its worst contraction, 81%, in 2009 when Malaysia fell out of the top ten FDI destinations in Asia. Apart from the global crisis, the overall decline in FDI inflows is attributed to two main factors. FDI in recent years has increasingly flowed into higher value added services sectors like financial and shared services which tend not to be located in Malaysia. The scale of investment in services is less than in manufacturing, Malaysia's main recipient sector of FDI which is more capital intensive. Secondly, competition among Asian countries, namely India, China, Singapore, Vietnam and Hong Kong, China has intensified. Manufacturing, services and oil and gas still dominated inward FDI in Malaysia during the period 2006-2010.

The Malaysian policy environment for FDI in the primary and secondary sectors has generally been liberal. MITI is the main government organization undertaking the evaluation and approval of FDI inflows as well as investment incentives, since the enactment of the Promotion of Investment Act of 1986. MITI's sub organization, the Malaysian Industrial Development Authority (MIDA) is the main promotional body that has been instrumental in attracting FDI to Malaysia. Despite the liberalization efforts under both the Association of South East Asian Nations (ASEAN) Free Trade Area (AFTA) and World Trade Organization initiatives, recent trends show a decline in FDI flows into Malaysia. Apart from the global recession, reasons for the decline in FDI include rising competition for FDI, especially from other emerging markets. Malaysia's transformation from capital-intensive to knowledge-based industry while still facing relatively weak human capital development and technological capabilities, adds to the challenge of competing for FDI inflows. Slower growth in manufacturing value added projected to grow only at average of 2.2% per annum over the period 2006-2010 and a severe contraction in FDI inflows in 2009 have again driven the government to rethink its FDI policy (Malaysia, 2010).

The role of corporate tax towards FDI inflows: In general, corporate taxes or taxes imposed on corporate income is an important determinant of MNCs' location decisions, just as individual income tax rates is an important determinant of where a person decides to work and live. However, concerns over fiscal competition between countries leading to ever lower tax rateshave given rise to notions such as fiscal dumping and race-to-the-bottom. While suchconcerns tend to be exaggerated, it is undoubtedly true that a government's ability to raise corporate tax rates is more restricted in a world of mobile capital than in a world of immobile capital. Although, the actual impact of corporate taxation on FDI inflowsis uncertain, there is widespread perception among governments that an internationally competitive corporate tax rate regime is vital for attracting FDI inflows. While corporate taxes will almost certainly affect firms' FDI decision-making, it is worth remembering that there is a wide range of factors other than corporate taxes that enter into the calculation as well.

The intensifying international competition for FDI inflows is likely to have had a substantial impact on both reduction of corporate tax rates and provision of more tax rebates. To date, few studies have systematically analyzed the impact of lowering levels of corporate taxation on changes in FDI inflows. Utilizing dynamic tests for up to 19 OECD countries from 1980-2000 and isolating the impact of time-varying factors on FDI inflows, some studies find no empirical relationship between corporate taxation and FDI inflows. Using a number of different tax rate variables, control variables and estimation techniques, the study finds no relationship between corporate tax rate changes and FDI flows. This null results remains even after using delayed tax rate changes as an identification strategy to moderate concerns. This result has the potential to drive the tax policy literature and the broader literature on globalization and the states in a slightly different direction.

The role of inflation rate towards FDI inflows: Previous studies by Lahreche-Revil and Benassy-Quere (2002) and Akinboade *et al.* (2006) identified that "low inflation is taken to be a sign of internal economic stability atthe host country. High inflation indicates the inability of the government to balance its budget and the failure of the central bank to conduct appropriate monetary policy". A history of low inflation and sensible fiscal activity signals to investors about the commitment and credibility of the

government. So, low inflation rate is taken to be a sign of internal economic stability in the host country and low or manageable level of inflation in country encourages FDI. (Borensztein *et al*., 1998) proved inflation statistically insignificant while (Benassy-Quere *et al*., 2001) have found that inflation has a negative effect of FDI. The level of threshold varies from various results obtained from various investigations however, depending on a sample of countries, time periods and estimation methods. Some previous study offers distinctions on the level of inflation. Rogoff and Reinhart (2002) found that high inflation does not happened in the absence of other macroeconomic problems. The cost of inflation can have prominent effect on the economy's growth. Wint and Williams (2002) show that a stable economy attracts more FDI, thus, a low inflation environment is desired in countries that promote FDI as a source of capital flow.

In conclusion it can be summarized that Malaysia has had an open FDI climate. Inward FDI has been seen as a major element in fostering economic growth and development and has remained a major component of gross fixed capital formation, though it contracted sharply in 2009. The government's planned efforts in the 10th Malaysian Plan, the NEM, the ETP and GTP in attracting FDI flows easing the regulatory burden, reducing corporate income tax, upgrading physical infrastructure, providing incentives have led to better economic growth prospects and the healthy resumption of capital inflows in the first quarter of 2010. Given IFDI's impact on the economy, it will remain an important part of the Malaysian economy. The government's restructuring efforts need to include the transformation of the country's knowledge stimulating organizations such as universities, polytechnics, R&D labs to enable the upgrading of firms so that they can engage in high value added activities.

MATERIALS AND METHODS

The collection method, interpretation of the data towards the FDI inflows into Malaysia and result of the study undertaken while including the causal relationship between FDI and economic growth show that there are key determinants that influences the inflows of FDI into a country. The theoretical framework of this study was drawn through literature review. The dependent variable is FDI inflows into Malaysia that leads to economic growth in which the variable is attempted to be explained by the seven independent variables of:

- Financial market development
- Market size of the economy
- Governmental infrastructure expenditure
- Real exchange rate
- Economic openness
- Corporate tax
- Inflation rate

Based on the these independent variables, the following hypothesis were generated for this study, a total of 7 hypotheses statements were established to test whether the relationships that have been theorized do in fact, hold true. The formulated hypotheses for this study are.

Hypothesis 1: There is a significant relationship between financial market development and FDI inflows into Malaysia.

The results from this study suggest that among the variables, financial development and economic growth contribute positively to the inflow of foreign direct investment in Malaysia. The evidence provides strong policy recommendation on sustaining high growth and financial deepening in Malaysia. Also a study by Ang and Van Dyne (2008) identified that financial development such as wage rates, income, economic growth and government spending on infrastructure has a significant impact towards FDI inflows into Malaysia.

Hypothesis 2: There is a significant relationship between the market sizes of the economy and FDI inflows into Malaysia.

The positive relationship between FDI inflows and exports in relation to economic performance has been largely expected. Most of the existing research highlighted the substitutability of relationships between inflows of FDI and exports. The existing literature on the Malaysian position in relation to this subject matter proves to be insufficient (Asari *et al*., 2011). A large number of empirical studies on the role of FDI in host countries suggest that FDI is an important source of capital, complements domestic private investment is usually associated with new job opportunities and enhancement of technology transfer and boosts overall economic growth in host countries (Chowdhury and Mavrotas, 2005).

Hypothesis 3: There is a significant relationship between government infrastructure expenditureand the FDI inflows into Malaysia.

The positive relationship between FDI inflows and exports in relation to economic performance has been largely expected. Most of the existing research highlighted the substitutability of relationships between inflows of FDI and exports. The existing literature on the Malaysian position in relation to this subject matter proves to be insufficient (Asari *et al*., 2011).

Hypothesis 4: There is significant relationship between real currency exchange rate in Malaysia and its FDI inflows.

As exchange rate correlation converges towards one, exchange rate risk diversification becomes a weaker determinant of location at the same time as other factors like rate of return become more relevant (Kumar, 2002). A weaker domestic currency will attract more inward FDI because it reduces the funding costs in source country, the conjecture that sharp depreciation can bring benefits from FDI if it also leads to higher exchange rate volatility is not accepted (Lipsey and Chrystal, 2006).

Hypothesis 5: There is a significant relationship between the Malaysian economic openness and FDI inflows into the country.

The economic openness is another determinant widely claimed to be critical in influencing the FDI inflows into a country. Nonnemberg and de Mendonca (2004) and Botric and Shuflic (2006) found that openness variable is parallel with the inflows of FDI and exerted positive influence on the FDI.

Hypothesis 6: There is a significant relationship between the corporate tax rate and FDI inflows into Malaysia.

Although, the actual impact of corporate taxation on FDI inflowsis uncertain there is widespread perception among governments that an internationally competitive corporate tax rate regime is vital for attracting FDI inflows. While corporate taxes will almost certainly affect firms' FDI decision-making, it is worth remembering that there is a wide range of factors other than corporate taxes that enter into the calculation as well (Dunning, 1993).

Hypothesis 7: There is a significant relationship between the inflation rate of Malaysia towards the FDI inflows into the country.

Lahreche-Revil and Benassy-Quere (2002) and Akinboade *et al.* (2006) stated that "low inflation is taken to be a sign of internal economic stability in the host country. High inflation indicates the inability of the government to balance its budget and the failure of the central bank to conduct appropriate monetary policy". In other words, inflation can be used as an indicator of the economics of the host country but the differences between "high" inflation and "low" inflation is not distinct (Ahn *et al*., 1998).

Data were collected from The National Bank via the internet. Raw data from previous statistics concerning the FDI inflows into the country was retrieved for further research and study. The reason for the choice of using the data directly from the National Bank would be because the data are more accurate easily collected and it is an effective and inexpensive way to gather data concerning all FDI activities in the country.

RESULTS AND DISCUSSION

One-tailed pearson correlation tests were employed to assess discriminant validity of the variables. All independent variables were found not to be too highly correlated among themselves which is the prerequisite condition for removing concerns about multi-collinearity problems prior to conducting multiple regression analysis in the subsequent section. In terms of predictive validity, the matrix in Table 3 shows that there are a number of significant variables which can warrant further multiple regression analyses. Visual inspection of their values suggests that only three out of the seven independent variables, i.e., openness to experience, conscientiousness, extroversion and agreeableness have significant correlations with job involvement.

Based on the obtained results from the correlation, we can see that in relation to financial market development there are three elements that have a significant relationship which is market size of the economy, corporate tax and FDI rate. However, the other elements like real exchange rate, economic openness, corporate tax and inflation has an insignificant relationship towards FDI inflows into Malaysia. Followed by identifying the significant relationships of other elements towards the market size of the economy. Only real exchange rate and FDI rate proved to have significant relationship.

All the other elements had an insignificant relationship. Looking, at the significance of other elements towards real exchange rate we identified only

Table 3: Pearson Correlation table

Parameters	1	2	3	4	5	6	7	8
Financial market development	-							
Market size of the economy	0.755**	-						
Government infrastructure expenditure	0.694	0.922*	-					
Real exchange rate	-0.282	0.255	0.286	-				
Economic openness	-0.208	-0.343	-0.075	0.374*	-			
Corporate tax	-0.569**	-0.791**	-0.777	-0.101	0.555**	-		
Inflation rate	-0.213	-0.321	0.084	-0.379*	-0.136	0.377*	-	
FDI rate	0.758**	0.507**	0.399	-0.341	-0.287	-0.375*	0.137	-

**Correlation is significant at the 0.01 level (1-tailed). *Correlation is significant at the 0.05 level (1-tailed)

economic openness had significant relationship. Followed by, the significance of other elements towards economic openness where we see that only corporate tax has a significant relationship. Also, based on the corporate tax, we can see that only one element which is inflation rate that is significant. Lastly, we see that for inflation rate, only FDI rate has significant relationship. Looking at the results of the correlation analysis, we see that financial market development has the highest level of significance towards FDI rate at 0.758 and followed by a 0.507 significance level for FDI rate in relation to the market size of the economy. And lastly, it is identified that there is a negatively significant level of -0.375 for corporate tax rate that is in relation towards FDI inflows rate into Malaysia.

The purpose of this study is to investigate and identify the key determinants for FDI inflows into Malaysia. Reviewing the literature, some past studies found mixed evidence of FDI and its key determinants relationship (Lean, 2008). A plausible explanation for this is different countries characteristics offers different results. The determinants may affect differently in different countries. Financial market development, market size of the economy, government infrastructure expenditure, real exchange rate, economic openness, corporate tax and inflation rate are among the variables commonly analyze in the FDI dynamic to identify the factors attracting FDI inflows.

CONCLUSION

This study has identified that the factors affecting FDI inflows most are financial market development and market size of the economy which are positively significant. However, the corporate tax rate is a negatively significant independent variable. The study contributes to the better understanding of factors influencing FDI inflows into Malaysia. This research also contributes to the understanding of factors that the Malaysian government has to intensify and reduce to attract more FDI inflows into the country for further economic development. This study sheds some attention again on this causality between economic growth and FDI inflows; however with different periods which is from the year 1991 until the year 2010. Research on FDI has been on the most intensive areas of international economics in the last few decades (Pan, 2002). This study on the FDI inflows into Malaysia would contribute to many possible corrective actions by the Malaysian government and other parties involved in FDI activities at Malaysia. The Malaysian government should however be sensitive to the importance of FDI inflows in the country and take measures through research to intensify the FDI inflows into the country through the accepted independent variables like financial market development, market size of the economy and corporate tax rate. The global FDI environment will remain challenging as advanced countries wrestle with their growth, deficit and debt problems. It is imperative that we do not resist change and merely insist on the status quo. But it is equally imperative that we do not initiate counter-productive change. The present economic and government transformation reforms must be taken seriously if we want to be an attractive investment centre and to return to being an economic dynamo.

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