

# Threat of Corruption to Foreign Direct Investment and Economic Growth in Southeast Asia

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## Abstract

This research aims to look into the dangers caused by corruption against foreign direct investment in Southeast Asia by using the supporting variables: the investment of foreign direct in the shape like the economy expansion, data technology, also Trade Openness. The scope used in this study includes 2010 to 2020 using panel data, using annual data. The data used are data from Foreign Direct Investment that enters ASEAN countries, percentage data of internet users as an indicator of ICT, corruption perception index (CPI) as an indicator of perceptions of corruption, GDP (gross domestic product) data for indicator to the economic growth, and ratio data. International trade is an indicator of Trade Openness. The PLS technique testing procedure is initiated using construction by reconstruction incorporated into the PLS calculation. We found that the Increased of foreign direct investment (FDI) are indication by the international trust level in a country, including a reflection of financial transparency supported by information and communication technology. Financial transparency is reflected in the corruption perception index. Economic prospects as reflected in economic growth or GDP growth and trade openness. The better technology of information and communication, the higher the growth of economic and trade openness at the Southeast Asia region, and the more the growth of FDI in the Southeast Asia region. And conversely, the higher the level of corruption as reflected in the corruption perception index (CPI), the more depressed the growth of foreign direct investment at Southeast Asian region.

**Keywords :** Corruption, Economic Growth, Foreign Direct Investment, Southeast Asia

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## Background

Corruption is a phenomenon that has not been thoroughly studied until a concrete solution is found in eliminating corruption in this world, so that the relevance of studying this problem cannot be doubted (Topchii, Zadereiko, Didkivska, Bodunova & Shevchenko, 2021). Corruption's Impact on a Growth of Economy is an interesting study problem, some solution may be useful in the future (Castro, Phillips, & Ansari, 2020).

Corruption can be describe the of public office use by personal advantage. It comes in a variety of ways such as nepotism, bribery, Officials seizing state property, the abuse of financial resources and lobbying, (Chilunjika, 2018). Sources of corruption are excessive state intervention in the economy, bureaucratic traditions, and social history. Until now there is no consensus on the positive impact of corruption, but of course the negative impact is dominant (Mungiu-Pippidi & Hartmann, 2019). In countries with inefficient and complex regulatory

systems, providing bribes through inefficient state control plays a deregulating role and can therefore be assessed positively (Khan & Krishnan, 2019). However, at the same time, corruption is a source of declining quality of human resources, inefficient functioning of political institutions, undermining macroeconomic stability, etc (Muzurura, 2019).

A low level of corruption is an important factor for attracting foreign direct investment. GDP growth depends on the level of containment of corruption, FDI inflows, labor resources and export growth (Mohamed, Liu, & Nie, 2021). The fight against corruption must be fought at all levels. There is an inverse relationship between the income level of the population of the country and the amount of corruption in these countries (Liu & Dong, 2020). Corruption-ridden countries are less appealing to international investors so, among the economic growth sources is lost (Qureshi, Qureshi, & Junejo, 2021).

Disclosure of information and providing citizens access to it also reduces the level of corruption, therefore, the duty of the state is to make sure that citizens are informed of their rights and responsibilities (Tejedo-Romero & Araujo, 2020). The growth of corruption negatively affects economic growth, strengthening controls on the eradicating corruption is a necessary condition for the prosperity of the country (Igiebor, 2019). Corruption is a global problem, but it can only be tackled within national boundaries with the will and participation of every individual (Nurudeen & Waldemar Staniewski, 2019).

The Harrod-Domar theory explains that investment is a fund that is invested to increase economic capacity and have an impact on increasing income, where the investment forms capital or capital formation that increases production capacity (Liu & Jiang, 2018). Investments are of two types. First, investments made by the government, both central and local governments. Second, investments made by the private sector, both domestic and foreign (Yi-chong, 2018). There are two sorts of foreign investment that enter a country, namely Direct Foreign Investment (FDI) and Portfolio Investment (Voica, Panait, Hysa, Cela, & Manta, 2021). However, empirical facts show if FDI does have a greater influence. Because on the addition to providing investment in the form of capital, FDI also provides transfer of technology and skills (Widarni & Bawono, 2022).

ASEAN (Association of Southeast Asia Nation) is an organization of countries in the Southeast Asia Regional region. Where the countries that are members of the majority are classified as developing countries (Yahuda, 2013). These countries continue to strive to increase their economic openness, in addition, ASEAN is also showing an increase in its industrial sector which can attract foreign investors to invest in FDI (Lestari, Lesmana, Yudaruddin, & Yudaruddin, 2022). In general, it can be said that the investment climate in the ASEAN region is increasingly mature and lucrative for foreign investors. ASEAN Free Trade Area (AFTA) is realized through a tariff reduction policy of up to 0 to 5 percent (Aba, 2021). Removal of quantitative restrictions and other non-tariff barriers. In addition, there is also an agreement formed to eliminate all import duties (Sasongko, Bawono, & Prabowo, 2021; Viphindartin & Bawono, 2021).

The formation of ASEAN Free Trade Area (AFTA) provides opportunities for more smooth mobility of goods and capital along with the alignment of steps or harmonization in providing intensive investment, exchange of information, publishing various information, investment opportunities, and promotion with ASEAN. The investor country will choose the most attractive country as a place for investors to enter all ASEAN. ASEAN Free Trade Area (AFTA) has been fully implemented in ten ASEAN countries (Hofmann, Osnago, & Ruta, 2019). The structure of FDI particularly industrialized countries and some structure by FDI when emerging nations is

different. In developed countries such as Singapore, it is carried out with the aim of conducting sales activities, while in developing countries it is carried out with the aim of carrying out production activities (Armstrong and Westland,2018).

The ASEAN region is a new world economic power with members of the Southeast Asian region consisting of ten countries, namely Indonesia, Singapore, Malaysia, Thailand, Vietnam, the Philippines, Singapore, Myanmar, Laos, and Brunei Darussalam (Rohman & Napang, 2022). ASEAN is also a region known for being rich in terms of the natural and human resources. This area are listed as among the world's economies that has had rapid expansion. The rapid flow of FDI is inextricably linked to the high rate of economic growth into ASEAN nations (Mukhlis & Viphindartin, 2021). In the era of the Industrial Revolution 4.0, the internet has entered almost every aspect of human life (Murniati & Bawono, 2020 ; Murniati, 2021). Reducing the gap in internet users among nations both developed and emerging are agenda for policymakers, both at the national and international levels(Schwab,2017).

Some socio-economic condition by a country is also special consideration for investors before deciding to invest. Corruption is a socio-economic phenomenon that has caught the attention of investors and governments from various countries in the last 20 years. Costs caused by criminal acts of corruption can result in high costs (high-cost economy) and undermine investment competitiveness (Rapanyane, 2021). Governments in ASEAN countries must pay great care for dealing with some problem caused by corruption so that foreign investors are interested in investing (Koechlin,2013).

Theoretically, corruption causes an increase in transaction costs that have the potential to inhibit foreign investment. Corruption affects FDI inflows. Apart from corruption, FDI inflows are also heavily influenced by economic growth (George, et al., 2019). Another factor that is no less important in determining the entry of FDI into a country does Trade Openness. The definition of The ratio of trade openness by the value on the exports plus imports per GDP (Gross Domestic Product) are the metric to the economic prosperity relations by one nation to another (Banday, Murugan, & Maryam, 2021). Trade Openness can also be interpreted as a measure of economic openness policy that aims to control international instruments as an effort preventing an increase in the attitude of economic dependence which would later damage the dynamics of the national economy (Gómez-Mera,et al.,2014).

Trade Openness can provide benefits for every country involved. These advantages can be in the form of opening up wider market access and absorption of a wider workforce (Nantharath & Kang, 2019). In addition, Trade Openness allows for capital to flow from abroad in the form of FDI. The value of trade openness is high, causing the trade barrier to decrease (Thies,2018).

This research aims might look into the dangers caused by corruption against foreign direct investment in Southeast Asia by using the supporting variables in terms investment at the foreign directon on the shape of economy expansion, data technology, also Trade Openness.

## **Research Method**

The scope used in this study includes 2010 to 2020 using panel data, using annual data. The data used are data from Foreign Direct Investment that enters ASEAN countries, percentage data of internet users as an indicator of ICT, corruption perception index (CPI) as an indicator of perceptions of corruption, GDP (gross domestic product) data for indicator to the growth of economic, and ratio data. International trade is an indicator of Trade Openness.

This research uses descriptive quantitative research methods. The quantitative descriptive research method is used when the research aims to describe an event or a phenomenon that

occurs in the form of numbers that contain certain meanings. This method was chosen because it aims to explain how the influence of ICT, perceptions of corruption, economic growth, and Foreign Direct Investment Trade Openness by describing some results by data processing.

The PLS method provides an explanation related to some issue formulation at this research. The PLS method testing procedure begins with the development of the reconstruction utilized in the PLS estimate model. Economic factors and actual data shape the reconstruction, where the aim is to provide a limit on connection among some variables that we utilized on this research. And then reconstruction are created, The Generalized Least Panel Method will then be used to carry it out. The formula model that will calculated in this study are following:

$$FDInv_{it} = \beta_0 + \beta_1 ICT_{it} + \beta_2 Co_{it} + \beta_3 EG_{it} + \beta_4 TOpen_{it} + \epsilon_{it}$$

Information:

$ICT_{it}$  = ICT development

$Co_{it}$  = corruption perception index (CPI) score in country

$EG_{it}$  = the value of GDP

$TOpen_{it}$  = Trade Openness Ratio

$i$  = country to  $i$

$t$  = time period

$\beta_0$  = Intercept / Consistent

$\beta_1, \beta_2, \beta_3, \beta_4$  = Coefficient of Regression

$\epsilon_{it}$  = erroneous term in the country  $i$  in year  $t$

### Results And Discussion

Panel data analysis was carried out to see how much influence Information and Communication Technology (ICT), Perceptions on the Corruption, The Growth of the Economic and Trade Openness on FDI on the ASEAN in the 2010-2020 period.

**Table 1.** Comparison of Estimates with Panel Data

Dependent Variabel: FDI						
Variabel	PLS	Prob	FEM	Prob	REM	Prob
C	-4.012312	0.0000	-7.911211	0.0002	-4.998771	0.0000
ICT	0.001892	0.2911	-0.000311	0.0312	0.001992	0.4011
Co	0.020112	0.0002	0.007311	0.4011	0.009011	0.0401
EG	1.311217	0.0000	2.201112	0.0059	1.593112	0.0000
TOpen	0.492112	0.0201	1.724772	0.0301	0.776641	0.0081
R-squared	0.811312		0.851812		0.742721	

In the estimation results, the largest R-Square is found in FEM (Model with a Fixed Effect) so that are use in terms of the Constant Regression Analysis can be selected in the measurement. This selection is triangulated with the Chow test. Table 2 are showing the result of Chow Test.

**Table 2.** The Result of Chow Test

Effect Test	Statistic	d.f	Prob.
Cross-section F	3.011269	(4.93)	0.0192
Cross-section Chi-square	14.991123	4.98	0.0096

According upon that Chow test results the Chi-square possibility is lower than the alpha value ( $\alpha = 5\%$ ) so that final outcome of both the Chow test strengthen the results at the table 1, namely a utilized by most appropriate fixed effects model in panel testing in this study. To confirm the choice, a test of Hausman that we can see on the table 3 is carried out, to select a concept of fixed effect with the Theory of regression design.

**Table 3.** The test of Hausman

Test Summary	Chi-Sq. Statistic	Chi-Sq. d.f.	Prob.
Cross-section random	6.011241	5	0,1918

We can see at the table 3 there is probability is higher than the alpha value ( $\alpha = 5\%$ ). So the best data from a panel model of random effect. Table 4 are showing the result of the model’s estimate random effect.

**Table 4.** The Test of Random Effects Model

<i>Variable</i>	<i>Coefficient</i>	<i>Std. Error</i>	<i>t-Statistic</i>	<i>Prob.</i>
C	-4.919241	1.091114	-5.012324	0.0001
ICT	0.001926	0.001981	0.902143	0.4011
Co	-0.009011	0.003934	-2.202341	0.0401
EG	1.594112	0.301121	6.011235	0.0001
TOpen	0.906621	0.298672	2.801172	0.0081
<i>R-squared</i>	0.712211			
<i>Adjusted R-squared</i>	0.716623			
<i>F-statistic</i>	22.093665			
<i>Prob(F-statistic)</i>	0.000001			

Based on the estimation results of FDI growth in ASEAN, it has a significant positive effect on Information and Communication (ICT), economic growth, and constant Trade Openness. However, FDI has a significant negative relationship with perceptions of corruption. We know that investment in Direct Foreign are suffers and resulting the corruption.

**Conclusion**

Increased the foreign direct investment (FDI) are indication by the international trust level in a country, including a reflection of financial transparency supported by information and communication technology. Financial transparency is reflected in the corruption perception index. Economic prospects as reflected in economic growth or GDP growth and trade openness. The better technology of information and communication, the higher the growth of economic and trade openness at the Southeast Asia region, and the more the growth of FDI in the Southeast Asia region. And conversely, the higher the level of corruption as reflected in the corruption perception index (CPI), the more depressed the expansion of foreign direct investment at Southeast Asian region.

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