Political Institutions in Foreign Direct Investment:
Case Study on the Philippines and Thailand

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I. Introduction

FDI in Southeast Asia

For the last two decades, foreign direct investment (FDI) has been offering an unprecedented opportunity for developing countries to achieve faster economic growth. Through FDI, foreign investors benefit from utilizing their firm-specific assets and resources efficiently, such as technology and managerial know-how. For capital-scarce developing economies, FDI implies access to not only capital but also the benefit of acquiring advanced technology, managerial expertise, employment productivity, human resource development, global marketing networks, and best-practice systems of corporate governance. In particular, Asian countries have been successful in attracting FDI. Consequently, FDI in Asian developing countries increased from $396 million in 1980 to $275 billion in 2010,[1] indicating Asia as a main destination of FDI. While dramatic shifts in the composition of recipient countries have changed over time, with China currently becoming an attractive destination for FDI, Southeast Asia continues to remain an attractive hub for foreign investors.

Although Southeast Asian countries have been successfully attracting FDI inflows, success in attracting FDI has varied widely between countries. Some countries fare much better than others in attracting and hosting foreign investment projects within Southeast Asia. Within this context, this study aims to understand the reasons behind why certain countries have high FDI inflows while other countries have low FDI inflows, with special reference to countries in Southeast Asia. In particular, the Philippines and Thailand will be examined. The two countries share many of the economic determinants of FDI in common, however, the level of FDI inflows differ substantially.

[1] United Nations Conference on Trade and Development. (2011). "Global and Regional FDI Trends in 2010." UNCTAD Global Investment Trends Monitor.

This study examines the importance of political institutions as determinants of FDI inflows by conducting a case study on the Philippines and Thailand between 1997 and 2009.

The purpose of this study is twofold; first, to examine the political and institutional determinants of the vulnerabilities of FDI inflows for the purpose of finding the reasons behind the ineffectiveness of low FDI inflows in the Philippines compared to that of Thailand; second, to propose institutional improvements in the Philippines to attract higher levels of FDI in the future. To demonstrate this argument, the study is divided into five sections. With the first section being the introduction, the second section reviews significant literature regarding determinants of FDI inflows. The next section will then proceed to explaining similarities and differences between the Philippines and Thailand in depth. The fourth section attempts to understand the reasons behind why Thailand has been able to provide an environment that attracts FDI, while the Philippines hasn't, examining the reality that the variables are representing. In this sense, the study will look behind the figures to determine what could and should be changed. Lastly, this study ends with the conclusion, mentioning the limitations of the research, and proposing recommendations to help improve the level of FDI inflows in the Philippines in the future.

Research Hypothesis

I hypothesize that the results will point out institutional variables as a major determinant of FDI inflows. Improvements in democratic institutions and governance should be associated with greater FDI inflows, as multinational corporations are more likely to undertake investment where there is an institutional set up that ensures stability.

Significance of Study

The results of this study are expected to give contributions to the political and institutional determinants of FDI inflows. The most significant contribution of this study is to provide further insight into the reasons behind Thailand's high FDI inflows, as well as better comprehend the institutional determinants and major obstacles of FDI inflows in the Philippines. From the mid 1990s, China has been boasting the largest amount of FDI inflows, with FDI being diverted from Southeast Asia to China.[2] Southeast Asian countries have been alarmed by China's rapid economic growth, expressing apprehensiveness of China harming the economic prospects of the region. Given the picture of China's overwhelming presence, Southeast Asian countries must remain competitive and relevant in the future to attract FDI inflows. Thus, an effective institutional system in attracting FDI inflows becomes a pivotal means for the Philippines and Thailand to stay competitive in attracting foreign investments.

Research Methodology

The planned methodology is secondary research. The study will make use of published materials such as books, working papers, and publications to collect information regarding the topic. It is based on data derived from a variety of sources, such as governmental agencies and international organizations. Namely, these institutions include the Asian Development Bank, World Bank, United Nations Conference on Trade and Development, World Trade Organization.

This study will conduct a case study between the Philippines and Thailand to analyze the impact of institutions on FDI inflows. The Philippines and Thailand were selected as they receive remarkably different volumes of FDI inflows, even though these two countries share fairly similar factors. In detail, this paper will use FDI inflows as the dependent variable. The control variables will focus on

[2] Wu, F., Tiong Siaw, P., Han Sia, Y., & Kok Keong, P. (2002). "Foreign Direct Investments to China and Southeast Asia: Has ASEAN been Losing Out?" Retrieved July 9, 2011, from http://unpan1.un.org/intradoc/groups/public/documents/apcity/unpan010347.pdf

factors, such as exchange rate, natural resource dependence, inflation, GDP growth, infrastructure, and human capital. The independent variable will be Worldwide Governance Indicator from the World Bank, which captures six key dimensions of governance (political stability and absence of violence, control of corruption, voice and accountability, government effectiveness, regulatory quality, rule of law). The dataset includes series from 1997 to 2009.

II. Literature Review: Determinants of FDI

The available literature examines a large number of variables that have been put forward to explain FDI inflows. A study by Ana Marr (1997) finds significant and positive effects for the size of the economy, low labor costs, and availability of natural resources.[3] In addition, Nonnemberg and Mendoca (2004), studying a sample of 38 developing countries during the 1975-2000 period, find that the determinants of FDI are level of education, economy's degree of openness, inflation, risk, and growth rate.[4] Similarly, Garibaldi, Mora, Sahay, and Zettelmeyer (2001) conducted a study on 26 transition economies in Europe and former Soviet Union from 1990 to 1999. The results indicated that macroeconomic variables, such as market size, fiscal deficit, inflation, economic reforms, trade openness, availability of natural resources have significant correlations with FDI inflows.[5]

While immense studies focus mainly on the economic determinants of FDI inflows to developing countries, the importance of political institutions in host countries have also received attention. Rodrik (1996) investigated the determinants of FDI from 1982 to 1989 by majority-owned United States affiliates abroad, examining whether the level of investment is influenced by a constructed

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[3] Marr, A. (1997). "Foreign Direct Investment Flows to Low-Income Countries: A Review of the Evidence." Overseas Development Institute: 1-11.

[4] Nonnemberg, M.B., & Mendoca, M.J.C. (2004). "The Determinants of Foreign Direct Investment in Developing Countries." The Pakistan Development Review 46(3): 285-299.

[5] Garibaldi, P., Mora, N., Sahay, R., & Zettelmeyer, J. (2001). "What Moves Capital to Transition Economies?" IMF Staff Paper, Vol. 48, Special Issue. International Monetary Fund.

indicator of democracy which combined an index of political rights with a civil liberties index.[6] The results showed that democracy is statistically significant, implying that countries with weaker democratic rights attract less FDI. In addition, a study by Singh (1995) focused on the influences of FDI, considering not only economic variables but also social and political determinants of FDI. Although the main emphasis is on economic factors, Singh takes a number of political influences into consideration, namely political risk and business conditions.[7] Sociopolitical stability and favorable business operating conditions turn out to be significant determinants of FDI.

More recently, empirical studies have reported contradicting results with respect to linkage between democracy and FDI. Jensen (2003) conducted a study on the relationship between fundamental democratic rights and FDI, ascertaining that foreign investors are more likely to be attracted to democratic countries.[8] In addition, Jensen concluded that trade openness, natural resource dependence, higher budget deficit, and growth rate are found to be statistically significant with positive effects in his study.[9] Examining a wider range of indicators for political risk and institutions, Busse and Hefeker (2005) show that government stability, absence of internal conflicts, and basic democratic rights are significant determinants of FDI inflows.[10] On the other hand, Li and Resnick (2003) report that democracy reduces FDI inflows, claiming that control of property rights protection results in democracy lowering FDI to developing countries.[11]

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6 Rodrik, D. (1996). Labor Standards in International Trade: Do They Matter and What Do We Do About Them? "Emerging Agenda for Global Trade: High Stakes for Developing Countries." 37-79. Baltimore, MA: John Hopkins University Press.

7 Singh, H. (1995). "Some New Evidence on Determinants of Foreign Direct Investment in Developing Countries." Policy Research Working Paper. International Finance Division, World Bank.

8 Jensen, Nathan. (2003). "Democratic Governance and Multinational Corporations: Political Regimes and Inflows of Foreign Direct Investment." International Organization 57(3): 587-616.

9 Jensen, 587-616.

10 Busse, M., & Hefeker, C. (2007). "Political Risk, Institutions and Foreign Direct Investment." European Journal of Political Economy. Vol. 23(2), 397-415.

11 Li, Q., & Resnick, A. (2003). "Reversal of Fortunes: Democracy, Property Rights and Foreign Direct Investment Inflows in Developing Countries." International Organization 57(1): 175-214.

As can be seen from above, the literature review reveals that there are contradicting perceptions and findings on the role of political institutions as a FDI determinant. Thus, it is necessary to look at the Southeast Asian region, specifically the Philippines and Thailand where they share similar economic characteristics to determine what role governance plays in relation to FDI inflows. This study contributes to the debate on political institutions and FDI by examining the institutional developments that attract FDI inflows. In the next section, the study will propose an analytical framework to evaluate the political and institutional determinants of FDI inflows in the Philippines and Thailand.

III. Case Study: The Philippines and Thailand

Analytical Framework

This section reviews the analytical framework of the political and institutional determinants of FDI inflows. The analytical framework discussed here is used as a groundwork for the empirical model in the next section. The study will examine the relationship between FDI and political institutions, using a time-series cross-sectional study with data set from the year 1997 to 2009. Specifically, the focus of the analysis is on the Philippines and Thailand, as the two countries share many variables in common yet the amount of FDI inflows differ substantially, which can be seen in Appendix A.

As was seen in the section of the literature review, a wide array of studies has signified the importance of macroeconomic conditions as factors affecting inflow of FDI to a country. In many of the literature, one of the most important factors in the determination of FDI inflows is GDP growth. It is said that higher GDP level of economic development attracts higher levels of FDI inflows. Economic growth of a host country reflects potential market expansion and business opportunities for foreign firms, thus inducing more foreign investors to invest. This study uses GDP Growth from World Bank's World Development Indicator to measure economic growth.

Another factor is the availability of natural resources. The effect of FDI inflow of abundance of natural resources is reported to be positive and significant. Jensen (2003) also supports the importance of natural resources as a determining factor for the inflow of FDI.[12] This study measures the availability of natural resources through Natural Resource Dependence, which is from the World Bank's World Development Indicator.

Inflation is also an important determinant of FDI inflows. Inflation rate reflects economic stability of the presence of internal economic tension and the ability of the government and central bank to balance the budge in a country. According to a study on Malaysia and FDI, Tsen (2005) find this variable to have a negative and statistically significant impact upon FDI inflows, concluding that inflation plays an important role for the determination of FDI into Malaysia.[13] In other words, if inflation rate has a negative effect on FDI inflows, this means an increase in inflation leads to a decrease in FDI. This study uses inflation as a variable, which is from the World Bank's World Development Indicator.

A variable that plays a similar role to inflation is the exchange rate. The strength of the host country's currency is an important factor in the FDI decision. When the domestic currency depreciates or appreciates, there can be negative or positive effects on FDI inflows. For example, a depreciation of the currency of the host country may reduce FDI inflows into the host country, as a

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12 Jensen.

13 Tsen, Wong Hock. (2005). "The Determinants of Foreign Direct Investment in the Manufacturing Industry of Malaysia," Journal of Economic Cooperation and Development 26(2), 91-110.

lower level of the exchange rate may be associated with lower expectations of future profitability in terms of the currency of the source country. On the other hand, depreciation of the currency of the host country can increase wealth of foreign firm, attracting the host country for FDI. Thus, exchange rate is used as a variable in this study, which is from the World Bank's World Development Indicator.

In recent years, a variable measuring human capital has been included in most studies of the determinants of FDI. Raising the level of local skills and building up human resource capabilities attract FDI inflows. A more educated labor force will understand better and new technology, and will be able to better participate in production. An indicator of the general level of secondary school enrollment from World Bank's World Development Indicator is included among the variables in this study.

Lastly, infrastructure also appears to be an important factor in the FDI decision. Infrastructure covers many dimensions, ranging from roads to railways to telecommunication system. The better the infrastructure of the host country, the more attractive is it to FDI. It is assumed that good infrastructure allows faster transport and communication and facilitates production activities, which increases the productivity of investment, and therefore stimulates FDI inflows. This study uses Quality of Trade and Transport-Related Infrastructure from World Bank's World Development Indicator as an indicator of infrastructure development. This indicator evaluates six core dimensions, such as the quality of ports, railroads, information technology, basing it on a scale of 1 to 5, with 1 being the worst condition and 5 being the best condition.

Empirical Model

To test whether political institutions can be considered as significant incentives or deterrents to FDI inflows in the Philippines and Thailand, this case study uses control variables indentified in previous empirical analyses as important determinants of FDI inflows. The control variables are GDP growth, natural resource dependence, inflation, exchange rate, human capital, and infrastructure. The significance of each control variable is discussed in the above analytical framework. The dependent variable is FDI inflows, measured as the level of net FDI inflows in current US dollars, which enter into a country each year. The data is collected from World Bank's World Development Indicator. The general form of model in this paper has the following form:

FDI inflow = Worldwide Governance Indicator + (GDP growth, natural resource dependence, inflation, exchange rate, human capital, infrastructure)

All of the variables in the above model have been selected on the basis of how significant they are to FDI inflows. The control variables are chosen based on the variables that the Philippines and Thailand share more or less in common. When looking at Appendix B, one can see the similarities of the variables between the Philippines and Thailand. The similar macroeconomic indicators of inflation rate and exchange rate suggest that the level of fiscal policy is about the same. This also indicates that both governments can control for inflation rate and a stable monetary policy. One important point to note is the level of inflation. When comparing just the Philippines and Thailand, the level of inflation seems rather different, however, when comparing the inflation rate with the other ASEAN countries, one can see that the Philippines and Thailand have similar inflation rates.

To measure whether political institutions matter, the study employs the Worldwide Governance Indicator from World Bank generated by Daniel Kaufmann, Aart Kraay, and Massimo Mastruzzi. From the year 1996, the Worldwide Governance Indicator measures six dimensions of governance, which includes voice and accountability, political stability and absence of violence, government effectiveness, regulatory quality, rule of law, and control of corruption.[14] The aggregate indicators combine the views of think tanks, non-governmental organizations, and international organizations.[15] In terms of rating, higher values indicate better governance ratings. The ratings for the Philippines and Thailand for the six dimensions of governance can be seen on Appendix C.

The six indexes in the Worldwide Governance Indicator measures distinct concepts of the quality of governance. For example, voice and accountability represents the degree of citizen's right to freedom of speech and government selection.[16] The second index, political stability and absence of violence, measures the possibility of overthrowing or de-establishing the current government or authority.[17] Furthermore, government effectiveness represents government's credibility and commitment, especially when it comes to formulating and implementing policies.[18] Regulatory quality shows government's ability to implement policies and regulations in accordance with permitting and promoting private sector development.[19] Another important index is rule of law which shows the degree in which actors follow the rules, particularly with contract enforcement property rights, and policies.[20] Finally, the last index, control of corruption, represents the extent to which people use public authority for their own gain and interest.[21]

Findings and Estimation Results

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14 Kaufmann, David, Aart Kraay, and Massimo Mastruzzi. (2010). "The Worldwide Governance Indicators." Washington, D.C.: World Bank.

15 Kaufmann

16 Kaufmann.

17 Kaufmann.

18 Kaufmann.

19 Kaufmann.

20 Kaufmann.

21 Kaufmann.

The results of the comparison of the independent variables between the Philippines and Thailand are shown in Appendix C, where the Philippines is represented in blue and Thailand in pink. As expected, Thailand has a higher rating for most of the governance indicators except for voice and accountability. These higher ratings can explain higher FDI inflows in Thailand compared to the Philippines.

An interesting point to note is the fall in voice and accountability, political stability and absence of violence, rule of law, and control of corruption from the year 2005 had a revere effect for both countries, increasing FDI inflows substantially. When examining the story behind the decrease in these indicators but a rise in FDI inflows, this is due to the fact that intra-ASEAN investments grew by 66 percent during the same year,[22] which shows that ASEAN member states are supporting each other to enhance FDI inflows. With the intention to enhance FDI inflows within ASEAN, ASEAN member states will support other member countries regardless of their investment climate. Thus, despite a fall in governance in Thailand and the Philippines, the boost in intra-ASEAN FDI explains the increase in FDI inflows.

When looking at the Worldwide Governance Indicator, the six indexes represent either the political system or the investment environment. The first two indicators, voice and accountability and political stability and absence of violence are related to the political system. Thus, these two indicators may only have a small impact on FDI inflows. The other four indicators, government effectiveness, regulatory quality, rule of law, and control of corruption are related to the investment environment. As Thailand and the Philippines have similar levels of human capital and infrastructure

[22] ASEAN. (2007). "ASEAN Investment Report 2007: Sustaining FDI Flows into the ASEAN Investment Area." Association of Southeast Asian Nations.

which can be seen in Appendix B, I argue that regulatory level should matter, making a significant difference in attracting FDI inflows.

With the focus on regulatory environment, this study will look into how the environment works in attracting FDI. More specifically, it will examine the reasons behind why Thailand has been able to provide an environment that attracts FDI. This study will also attempt to answer why Thailand is FDI worthy compared to the Philippines, pinpointing the source of the difficulty in increasing FDI in the Philippines. While most of the readings contend that a stable and trustworthy FDI environment bring about higher FDI inflows, this study will further examine in detail the reality that the variables are representing.

IV. FDI Performance in the Philippines and Thailand

Trade and Investment Policies

Trade and investment policies in the Philippines and Thailand play an important role in determining each government's efforts in external economic policies. Both Thailand and the Philippines show ambitious and intensive efforts to increase its world export market share through the establishment of both regional and bilateral trade agreements. According to the World Trade Organization, Thailand currently has 11 trade agreements in force, including trade agreements with Australia and New Zealand, as well as trade agreements with Japan.[23] In contrast, the Philippines has 9 trade agreements in force, showing a number lower than Thailand's trade agreements. Furthermore, according to United Nations Conference on Trade and Development, Thailand has 38 bilateral investment treaties, while the Philippines has 30 bilateral investment treaties.[24] With the above

23 World Trade Organization. "Participation in Regional Trade Agreements" World Trade Organization (WTO).

24 United Nations Conference on Trade and Development. "Bilateral Investment Treaties." United Nations Conference on Trade and Development (UNCTAD).

results, the Philippines and Thailand show differences in the number of trade agreements and investment treaties. Thus, it can be said that Thailand is making significant efforts externally than the Philippines, showing commitment towards trade and investment with foreign countries. This low numbers of investment and trade treaties in the Philippines suggest that enhancement in the domestic environment is necessary, as well as expanding high potential markets and increasing trade partners.

Regulatory Environment in the Philippines and Thailand

The Philippines and Thailand have in common a mining industry, extracting natural resources. The mining industry covers the extraction of non-renewable resources, which includes precious metals, iron, petroleum, natural gas, and other valuable geological minerals from the earth. In particular, mining has long been a major contributor of the economy in the Philippines with mineral deposits of gold, nickel, copper, silver, platinum, zinc, and cobalt in the remote mountainous regions and coastal areas.[25] Although the number of mineral deposits are relatively small compared to the Philippines, Thailand has considerable resources of limestone, potash, gold, quartz, lead, tin, zinc, copper, natural gas, and oil. This section will focus on the regulatory environment in the mining industry in the Philippines and Thailand, and examine how the regulatory level differs with reference to examples.

The Philippines

In the Philippines, the regulatory climate for mining aims to be committed to developing fair, transparent, and predictable administrative rules; nevertheless, there are still signs of difficulty in eliminating bureaucratic red tape and corruption. Under the Regalian Doctrine of property ownership, natural resources belong to the country.[26] This means that extraction and utilization of natural

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[25] U.S. Department of State. (2011). "Background Notes: Republic of the Philippines." Bureau of East Asian and Pacific Affairs. Retrieved July 20, 2011, from http://www.state.gov/r/pa/ei/bgn/2794.htm

[26] Cruz, Ismael. (1999). "Setting the Scene: An Overview of the Mining Industry and Regulatory Climate in the Philippines." Minding Mining! Lessons from the Philippines. Philippine International Forum.

resources must first be given permission by the country to which such natural resources belong. Although ownership belongs to the state, the constitution allows the state to enter into mining agreements with Filipinos or 60 percent Filipino-owned corporations, giving preference to Filipino nationals.[27] The constitution also permits large-scale mining activities to seek the help of foreign corporations for the purpose of either financial or technical assistance.[28] With structural adjustment programs of liberalization of industries by the World Bank, International Monetary Fund, and proposals by the Asian Development Bank, the Foreign Investment Act of 1991 removed the 60 percent Filipino ownership provision, allowing foreigners to invest 100 percent equity in domestic market enterprises.[29] Furthermore, the Mining Act was enacted in 1995, which called for the liberalization of the Philippine mining industry in order to entice foreign investors to bring in money and revive the industry. Under the Mining Act, public and private lands are open to mining operations with different conditions. For example, the Mineral Production Sharing Agreement is a contract between the government and contractor, giving the contractor exclusive rights for mining operations as long as the contractor provides the necessary finances, technology, and other inputs.[30] Thus, as can be seen from above, the government made reforms in the mining industry to create a more favorable investment climate for foreign investors.

Despite the government's efforts to attract more foreign investors and expand the coverage of foreign participation in the mining industry, the residents living in the remote rural areas where mining operations take place have opposed this government's policies. When government policies are formed, the government does not take into account the people inhabiting the remote areas. Most

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27 Cruz.

28 Cruz.

29 Structural Adjustment Participatory Review International Network. (2008). "The Impact of Investment Liberalization and the Mining Act of 1995 on Indigenous Peoples, Upland Communities and the Rural Poor, and on the Environment: A Summary Report." Washington D.C.: SAPRIN.

30 Structural Adjustment.

of the people inhabiting the rural areas are indigenous people, forest people, rural poor farmers, and fisherfolks, and they also struggle to receive minimum social services, such as education and health services.[31] These people are the ones who are profoundly affected by mining exploration, being forced to leave their homes. Although acquisition of Free and Prior Informed Consent (FPIC) is necessary by the communities affected by the mining projects, a global network legitimizing the role of civil society in economic policymaking contend that the mining corporations do not commit themselves to the FPIC process. For the mining project to go through, mining corporations have used tactics of barring anti-mining advocates from public dialogues, restricting attendance of public dialogues to only those who are in favor with the project, and resorting to bribery and deception in certain cases.[32] As an illustration, Climax Arimco Mining Corporation (CAMC) proposed a mining project in Didipio, and the company used bribery as a means to ensure the community's consent. The company hired people from Didipio Barangay Council to serve as community liaison officers, paying them high salaries in exchange for council members' signatures that the community has agreed to the mining project.[33] Hence, despite community opposition of mining projects, corporations are one of the sources of corruption taking place at the local level.

Another case worth mentioning is the Sagittarius Mines Tampakan Project, which is controlled by Xstrata Copper with Australian firm Indophil Resources NL as junior equity partner. This company was exploring for copper and gold in the mountains of Tampakan, spending $72 million on a feasibility study for the project.[34] They also signed a contract with the central government in 1995

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31 Structural Adjustment.

32 Structural Adjustment.

33 Mines and Communities. (2005). "Denouncing the Actions of the Nueva Vizcaya Province in Endorsing the CAMC Mining Project in Dipido." Retrieved July 20, 2011, from http://www.minesandcommunities.org/article.php?a=784

34 Mines and Communities. (2011). "Tampakan Project Diven On, while Brakes Applied Elsewhere in Philippines." Retrieved July 20, 2011, from http://www.minesandcommunities.org/article.php?a=11001

which allowed for 100 percent ownership of large mining projects.[35] However, the community has opposed the massive mining venture due to environmental and food security concerns, which may affect agricultural production. Taking these concerns into account, the former government official, Governor Daisy Fuentes, signed a provincial ordinance, which was called the South Cotabato Provincial Environmental Code, prohibiting open pit mining due to environmental reasons.[36] However, this provincial ordinance is contradictory to the Philippines Mining Act of 1995, which states that open pit mining is an acceptable means to extract minerals and pursue economic development. Thus, as can be seen from the example given above, rules and regulations can be changed at the local level in ways that don't consider the contracts corporations have entered with the central government. It can be said that the provincial government contributes to regulation uncertainties.

Therefore, it can be said that the regulatory environment in the Philippines needs to be more effective, particularly at the local level. Not only the community members but also foreign and local investors face regulatory uncertainty at the local level. The central government must enforce policies, specifically the FPIC process, for the community members as they have a right to voicing their opinion. Furthermore, the provincial government must work in close cooperation with the central government to avoid contradicting agreements.

Thailand

Compared to the Philippines, Thailand's regulatory environment in the mining industry takes a more proactive approach to attracting foreign investors, and also in ensuring regulations to be accountable

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35 Mines and Communities. (2011).

36 Esmaquel II, Paterno. (2011). "Mining Firm Starts Talks on Tampakan Project." GMA News Online. Retrieved July 20, 2011, from http://www.gmanews.tv/story/223387/business/mining-firm-starts-talks-on-tampakan-project

and transparent at the same time. While the Philippines mostly focused on mining gold, copper, nickel, and other minerals, Thailand mainly focuses on the oil and gas industry which takes place at the Gulf of Thailand. The search for oil and gas began in 1921, and the right to explore for and produce petroleum was restricted to state agencies and Thai citizens.[37] During this period, due to the lack of technology and expertise, exploration and production was discontinued. In the 1960s and 1970s, the government attempted to attract foreign investment in petroleum exploration by enacting the Petroleum Act and Petroleum Income Tax Act in 1971, establishing agreements with a number of international oil companies such as the Union Oil Company of California.[38] The Petroleum Act regulates the conduct of operations, which includes exploration, production, storage, sale, and disposal of petroleum. The Petroleum Income Tax Act indicates the amount private investors are expected to pay in terms of petroleum income tax and government royalties, which are remuneratory benefits to the government for granting the agreement for oil production. In the early 1980s, Thailand heavily relied on imported energy. Due to the oil crisis characterized with petroleum shortages and higher prices, the Thai government took steps toward reducing energy dependence by encouraging increased investment. With the aim of promoting privatization and liberalization programs, the Thai government amended the Act on Private Participation in State Undertaking in 1992. Under this act, the government increased the total amount of investment for private sectors participating in energy-related industries.[39] Furthermore, the Petroleum Act was amended in 1991 to exempt machinery and equipment for oil exploration and production from import taxes, and the Petroleum Income Tax Act has amended its terms and conditions to be more suitable and

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[37] Pongsiri, Nutavoot. (2005). "Foreign Direct Investment and Regulation: A Case Study of Thailand's Upstream Oil and Gas Industry." Centre on Regulation and Competition.

[38] Ruangsuvan, Charu-Udom. (1981). "Evolution of Petroleum Legislation of Thailand: A Case History. Department of Mineral Resources. Thailand: Bangkok.

[39] Asian Development Bank. (1999). "Country Assistance Plan: Thailand (2000-2002). Asian Development Bank (ADB). Philippines: Manila.

attractive.[40] Thus, the Thai government's improvement in regulations to attract foreign investment can be seen.

In Thailand, oil and gas exploration and production are currently taking place mainly at the Gulf of Thailand. In 1985, Thailand developed the Petroleum Institute of Thailand (PTIT) to manage petroleum and petrochemical related industries, providing information services, technical services, and public policy and regulatory support.[41] PTIT also manages multilateral dialogues among domestic and foreign investors and other concerned parties to deliver sound and practical regulations.[42] With the enhancement in regulations to attract foreign investment, there are currently a significant number of foreign companies taking part in oil and gas production, including Chevron, Shell, Mitsui Oil Exploration, among many other foreign oil companies.[43] As most of the oil operations are conducted offshore at the Gulf of Thailand, these activities have not given rise to such problems that the Philippines has encountered, such as the rights of the rural poor and indigenous people inhabiting the potential oil and gas exploration and production sites. According to Chandler and Thong-ek Law Office Limited in regards to regulation, there has been only one instance when a regulatory problem arose, which had to do with Union Oil Company of California in 1985, disputing over government royalty of gas.[44] However, the foreign corporation and government authorities were successfully able to settle this dispute before bringing the issue to the domestic court.[45]

Hence, the regulatory environment in Thailand is generally transparent, accountable, and business

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40 Pongsiri.

41 Petroleum Institute of Thailand. "About Petroleum Institute of Thailand." Retrieved July 20, 2011, from http://www.ptit.org/index.php/About/About-PTIT

42 Petroleum Institute of Thailand. "About Petroleum Institute of Thailand."

43 Petroleum Institute of Thailand. "Membership List." Retrieved July 20, 2011, from http://www.ptit.org./index.php/Membership.MemList/mode/1/type/1/page/1

44 Chandler, Albert, T., & Chapman, Stefan. (2011). "The International Comparative Legal Guide To: Gas Regulation 2011." London: Global Legal Group Ltd.

45 Chandler.

friendly. The effort of the Thai government to establish the PTIT for management of all petroleum and petrochemical related industries has contributed to streamlining regulations and procedures. It seems that the government and foreign investors have a common understanding of the regulations to achieve a mutually successful outcome to the project.

V. Discussion and Concluding Remarks

This has been a brief examination of a study into the political and institutional determinants of FDI flows into the Philippines and Thailand. In common with previous studies, the hypothesis that political and institutional determinants influence FDI inflows is supported. Focusing on trade and investment policies, this study found that Thailand has a more open economy in terms of trade and investment treaties compared to the Philippines, which may explain the substantial differences in FDI inflows. Trade liberalization is an essential engine for growth for developing countries, including the Philippines. Thus, Philippines should engage in more intensive cooperation with other developing countries. Furthermore, domestic policy reforms, especially eliminating corruption and regulatory uncertainties, should be taken into account to attract higher investments.

Focusing on the regulatory environment, this study also found that Thailand has proactively adopted liberal policies earlier than the Philippines when examining the mining industry. In 1991, the Philippines established the Foreign Investment Act, which allowed foreign corporations to have 100 percent ownership. However, Thailand had already established agreements with international oil corporations, and was amending the Petroleum Act and Petroleum Income Tax Act to attract more foreign investors during 1991. Furthermore, Thailand has developed an institution that manages all of the petroleum related activities in the country. On the other hand, corruption and policy uncertainty of the Philippines has created the ground level climate for foreign corporation and community members to be challenging. There have been attempts to repeal the Mining Act of 1995 and establish provincial level laws banning mining. Bribery still continues among foreign investors and local government officials. Thus, corruption and irregularities taking place at the local level in the Philippines is found to be a significant hindrance of FDI inflows, which explains for the low FDI inflows.

In addition, this analysis of the Philippines and Thailand with FDI inflows suggests implications for policy lessons for the Philippines that is experiencing corruption and uncertain regulations at the local level. First of all, strong governance needs to be established to avoid corruption by foreign investors and local governments. The central government needs to realize that establishing policies is not enough, and that enforcement is a key to eliminating corruption and uncertain regulations. Furthermore, the government must take into account that policy consistency matters to investors, thus policy should evolve systematically and not add to uncertainty. It is the certainty of policy that attracts FDI inflows, and a long term reputation as a secure and stable country is fundamental in attracting FDI.

This study faced various limitations. The main impediment to this effort is the inadequacy of data from related agencies. For example, data for infrastructure has been limited to certain years. There has also been a problem of sufficient homogenous data from different sources, such as World Bank and Asian Development Bank. Therefore, the trends and estimated analysis may deviate from true ones. Results from the analysis can be improved further through incorporating other FDI determinants into the model as well.

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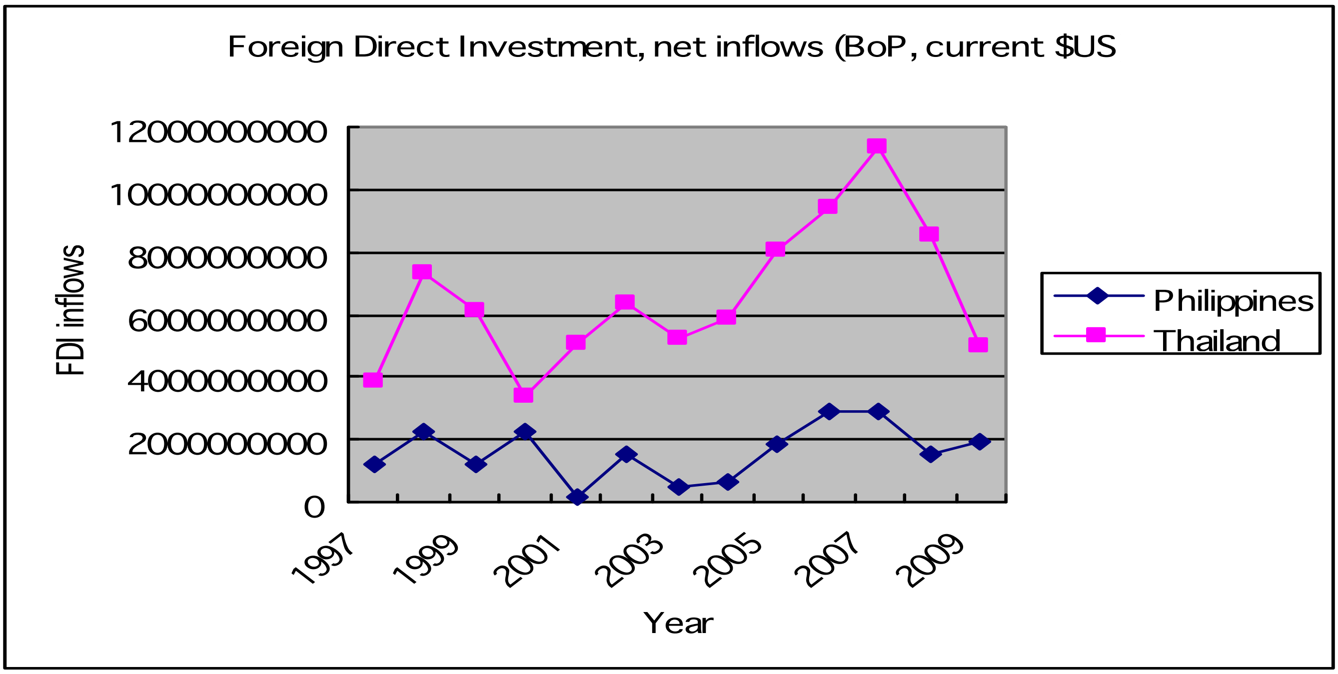
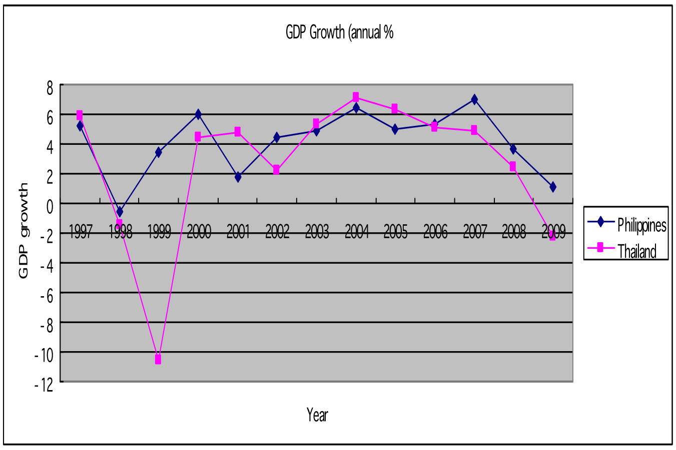
Appendix A

1. FDI Inflows

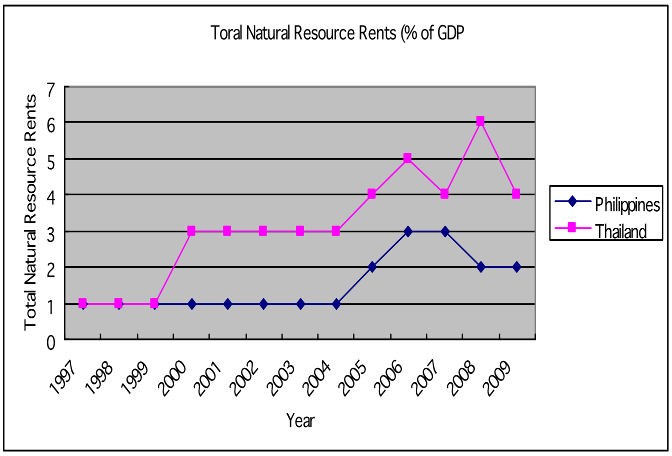


Appendix B

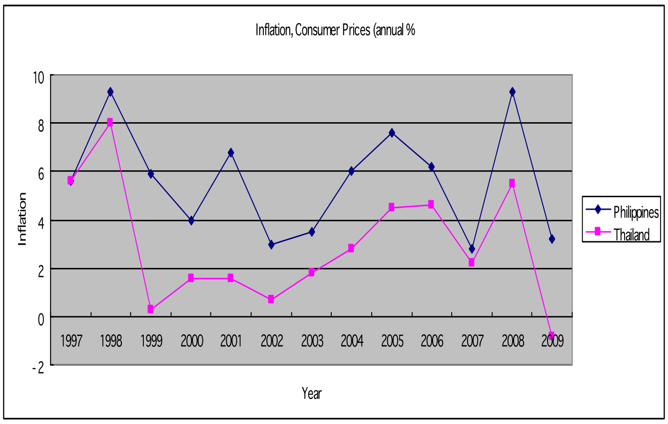
1. GDP Growth

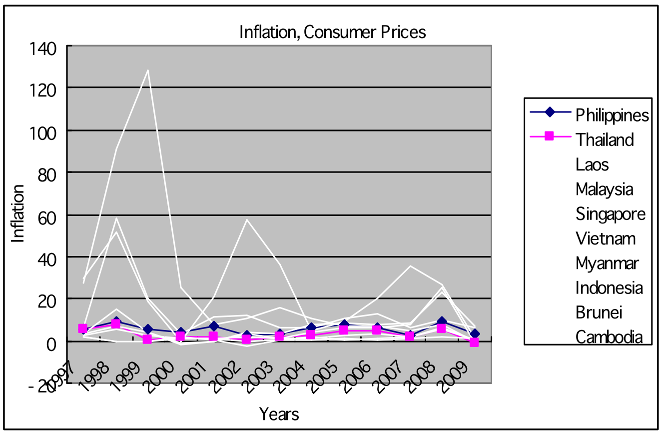


2. Natural Resource Dependence

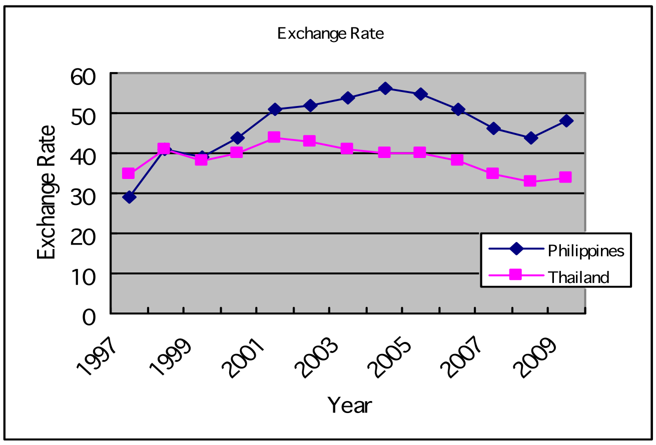


3. Inflation

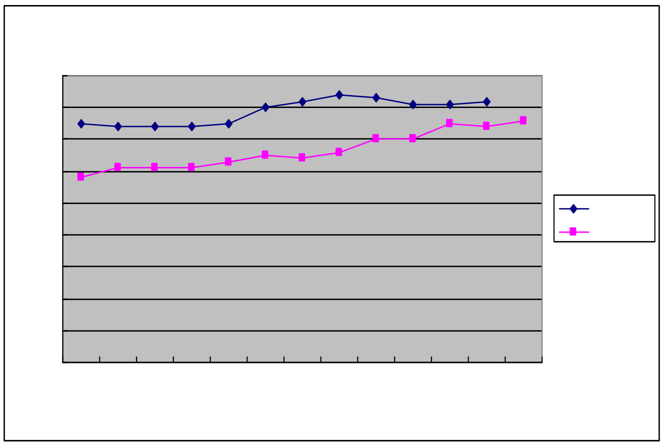




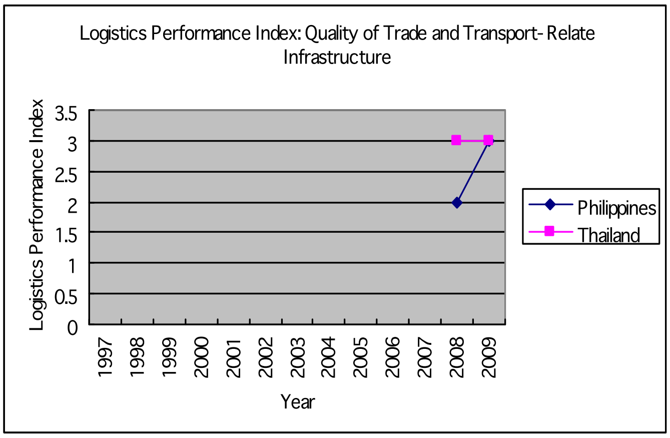
4. Exchange Rate



5. Human Capital (Education)

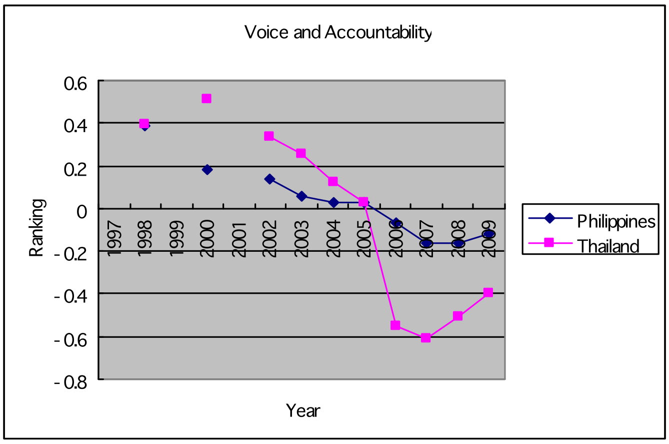


6. Infrastructure

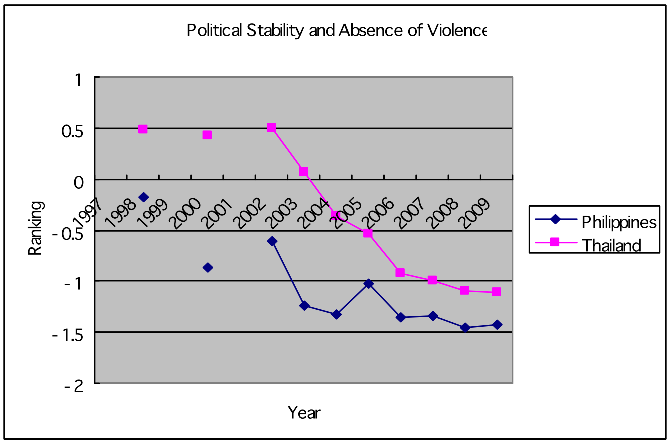


Appendix C

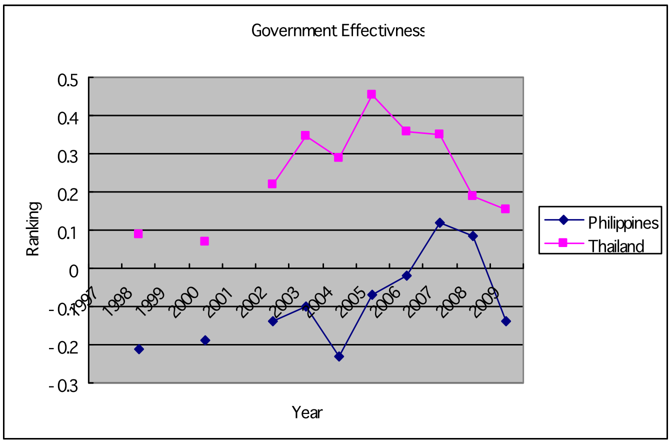
1. Voice and Accountability



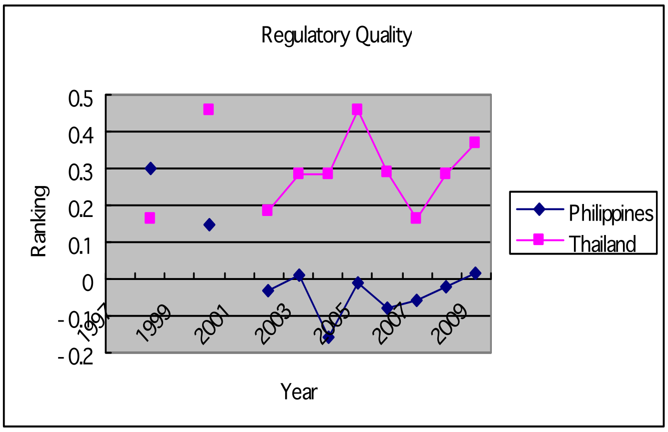
2. Political Stability and Absence of Violence



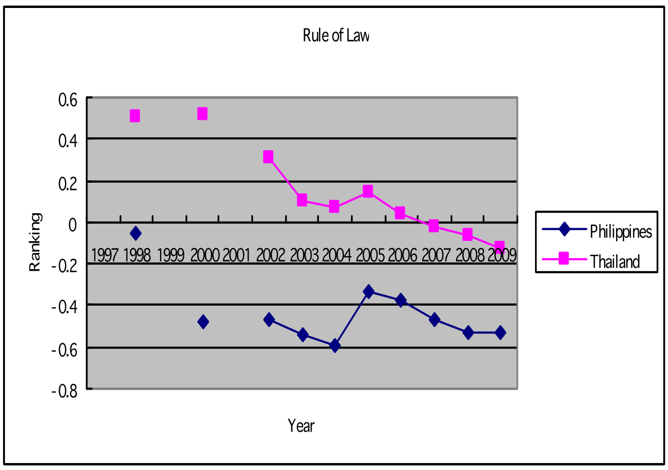
3. Government Effectiveness



4. Regulatory Quality



5. Rule of Law



6. Control of Corruption