ABSTRACT

Koo Won Kyu (00000009417)

THE DETERMINANTS OF FOREIGN DIRECT INVESTMENT INFLOW IN SOUTH KOREA

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Over the years, South Korea has been experiencing rapid economic development by opening itself more for foreign investment through various trade liberalizations and tax policies that benefited foreign investments. However, for the past few years, direct investment from abroad has been declining, mainly due to the end of tax break in 2018. This research was done in order to explore important determinants of foreign direct investment (FDI) besides tax that would bring more investments into the country. Four determinants are proposed based on various existing researches: (1) trade openness, (2) labor cost, (3) exchange rate, and (4) macroeconomic uncertainty. Using AutoRegressive Distributed Lag (ARDL) with cointegration on publicly available data from the year 1975 to 2017, both short run and long run effects were estimated. The author found that trade openness might not necessarily result in increased FDI inflows in the long-run. In the short-run, trade openness is an important determinant for FDI inflows, however this effect is corrected within two years, giving the advantages from increasing openness short-term in nature. It is also found that there is a positive relationship between labor cost and FDI inflows in the long run, however the relationship is nonexistent in the short run. Exchange rate was found to have a lasting effect in the long-run, while not having any effect in the short-run. And finally, the researcher found no reason to support that macroeconomic uncertainty, as defined by the world uncertainty index (WUI) affects FDI inflows in Korea.

Keywords*: FDI, trade openness, labor cost, exchange rate, macroeconomic uncertainty*

References: 110 (1975-2021)