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정치적 불안정과 외국인 직접 투자: 신흥국 정부부패의 관점

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Political Instability and Inward Foreign Direct Investment: The Perspective of Government Corruption from an Emerging Economy

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요 약 파키스탄은 남아시아의 상서로운 개발도상국이다. 국제투명성기구(Transparency International)의 2020년 부패인식지수 보고서에 따르면 파키스탄은 0(최저)에서 100(최고)까지의 정치적 안정성 측면에서 전 세계적으로 총 31점으로 124위, -2.25점으로 188위를 기록했다. 더 결정적으로, 파키스탄에 대한 외국인 직접 투자의 유입은 2008년과 2019년 사이에 감소했다. 정치적 불안정과 정부 부패는 외국인 직접 투자와 양의 선형 관계와 음의 선형 관계를 모두 가지고 있지만, 본 연구에서는 시간이 지남에 따라 정치적 불안정과 외국인 직접 투자 사이의 정부 부패의 완화된 영향을 테스트했다. 또한 같은 국가의 여러 정치 체제에서 정치적 불안정과 외국인 직접 투자 사이의 관계를 테스트했다. 따라서, 본 연구의 결과는 권위주의 정권이 민주적 정부 기간보다 더 많은 외국인 직접 투자를 유치했음을 시사하였다. 더욱이, 우리는 그 나라에서 정부의 부패가 심할 때 외국인 직접 투자가 적다는 것을 발견했다. 그러나 정부의 부패는 정치적 불안정과 외국인 직접 투자(FDI) 사이의 긍정적인 관계를 약화시켰다.

주제어 외국인 직접 투자, 정치적 불안정, 권위주의 체제, 정부 부패

Abstract Pakistan is a South Asian auspicious developing country. Based on the corruption perception index report 2020 by transparency international, Pakistan has ranked 124 with total scores of 31 globally and 188 ranks with a score of -2.25 in terms of political stability ranging from 0 (lowest) to 100 (highest). More crucially, the inflow of foreign direct investment toward Pakistan has declined between 2008 and 2019. Though political instability and government corruption have both positive and negative linear relationships with foreign direct investment, we tested the moderating impact of government corruption between political instability and inward foreign direct investment over time. We also tested the relationship between political instability and inward foreign direct investment in different phases of political regimes in the same country. Our results suggested that authoritarian regimes attracted more inward foreign direct investment than that during democratic periods of government. Furthermore, we found that there was low inward foreign direct investment when government corruption was high in the country. However, government corruption weakened the positive relationship between political instability and inward foreign direct investment (FDI).

Key Words Foreign Direct Investment (FDI), Political Instability, Authoritarian regime, Government Corruption

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1. Introduction

The study of the country's political instability, government corruption, and its aftereffects has attracted many scholars nowadays with the expansion of international business. One stream of researchers argues that there is a positive relationship between political instability and foreign direct investment [3,11,16,22,23]. Several other empirical studies supported the argument that corruption in the host country has a negative relationship with foreign direct investment [18,19,25,35,40,41]. These two perspectives are employed independently to understand the relationship with FDI activities. How do political instability and political stability directly affect FDI in the same country? How is government corruption associated with FDI in political stability and political instability? Does government corruption moderate the relationship between political instability and FDI over time? We will try to find out the empirical answers to these questions in this study.

Political instability as defined by [11], is when a country faces political disruption and there is a comparatively high probability of the existing government authorities involuntarily removal by force. At the early age of studies on FDI and political risk, [24] argues that empirical evidence is inconsistent and found mixed (positive/negative) effect of political instability on foreign direct investment (FDI) flows. Recently researchers are interested in and trying to search for the factors that affect FDI directly and indirectly. For instance, [8] argues that political instability has only a negative effect on FDI and keeps the capital inflows limited. Investment in a developing country like Pakistan, where half of its total age is politically unstable, is exposed to have huge political risk, so large FDI inflows are during the period of political instability. On the same token, a trend is found from highly politically stable countries of FDI outflows to the countries with high political risks [23].

The "Grabbing hand" theory of corruption as endorsed by the previous economists like [2,9,36,37] affirm that corruption is like a grabbing hand in an economy that increases the cost of economic activities being done in the market. According to the theory, the cost of doing business is increased by corruption, it deforms the resource allocation and reduces the output capacity generated by investment [43]. Furthermore, corruption increases transaction costs and reduces incentives for investors [29,36,40,41]. [40] found that cost of investment can be as much as 20% more in relatively high corrupted countries as compared with low corrupted/uncorrupted counterparts.

Several empirical studies supported the theme that FDI may be obstructed by corruption in the host country by raising economic uncertainty, thus investor's confidence in political institutions and the market system becomes weakened. On the other hand, some scholars argued about the positive relationship between corruption and FDI [23]. [3] concludes that inward FDI may be increased by 9.1% points if the level of corruption in a country is decreased by 1%.

This study distinguishes from existing research on the effect of different political environments and government corruption in the same country on FDI. Current studies only focus on the countries having only political stable environment or political unstable environment individually. This study first, focuses on the different phases of political regimes (stability and instability) in Pakistan and their effect on FDI and the rate of government corruption during those periods.

Then later, investigate how the relationship between FDI and political instability is moderated by host country government corruption over time. We test the primary question using data between 2001 and 2019 (19 years of data out of which 08 years of political instability and 11 years are supposed to be political stability as per the given definition).

This study is organized as follows:

Section 2 describes a literature review from previous studies about political instability, government corruption, and FDI. Section 3 consist of different political phases with government corruption and FDI and develop a hypothesis. Section 4 details the method of research, data used for estimation, research model, and equation. Section 5 presents and analyzes the statistical results for FDI, political instability, and government corruption. Section 6 consists of our conclusion, discussion, and suggestions for future research.

2. Literature review

2.1 Political Instability and FDI

Host countries get many major benefits from the inward flow of FDI like innovation, foreign exchange, managerial skills, transfer of technologies, foreign capital, research and development, increasing job opportunities for the local population, and intensifying the exports of the country [15; 35] and in turn, labor productivity and economic growth are enhanced [10,12,27]. Other researchers argue that local investment is also supported by foreign direct investment [4]. Usually, developed countries and developing countries offer plenty of remarkable packages and facilities to international investors to attract foreign direct investment so they can select their location for investment. They liberalize policies related to FDI [7,31], offer different financial incentives and tax rebates to foreign investors [6,42], and show their business commitment to foreign investors by joining global and domestic organizations and bilateral treaties. Foreign direct investment (FDI) is believed to be a major contribution to the growth of the economy for any developed or developing economy in the new global economic era [5]. The World Bank and International Monetary Fund (IMF) also encourage the global world to acquire benefits from FDI rather than Foreign Aid (FA). FDI may be an integral source of developmental process and planning by developing countries under the vigorous move of globalization in 21st century [45].

Several previous studies have explained the impact of political instability on foreign direct investment, both from theoretical and empirical perspectives. A survey by [17], provides a brilliant link between political instability and economic performance. [11] developed a theoretical political instability model of investment, and another model of investment was constructed by [39] that integrates indicators of political instability. Many other related studies describe the effect of political instability on investment and economic growth. [17] found a negative impact of political instability on FDI, hence, increased political instability hurts foreign direct investment and economic growth. [11] concluded how government policies and changes in the political process discourage foreign direct investment. They explained that the lack of commitment from the government for policymaking and uncertainty created from changing the groups in power affects foreign direct investment negatively. The volatility of stock markets has been linked with political instability by several previous scholars [1,8]. One stream of researchers explains how foreign exchange markets are affected by political instability and it clearly shows that political instability causes to decline in the currency exchange rate and makes it more volatile [14,24]. Further, it is demonstrated by [11], that political instability, whether originated by own country or from global tensions and conflicts, decreases foreign direct investment and economic growth. They conclude that reduction in FDI in Balkan economies as compared to Central European economies is in fact due to the regional political instability. The econometric conclusion by [38] shows that investor's home country market size provides the huge significance, displaced by memberships in global and domestic trade treaties. Political stability, e.g., the efficiency of government to carry on policymaking effectively, has also a positive effect on the decisions made by investors whether to invest abroad or not.

2.2 Government Corruption and FDI

The impact of government corruption on foreign direct investment is still controversial. One stream of researchers provides empirical evidence that government corruption in the host country is adversely related to FDI [2,18,20,21,25,40,41]. Nonetheless, many other scholars assert that government corruption has a positive linear association with foreign direct investment [26,36,37]. They argue that some countries such as China, India, Thailand, or Nigeria have a high level of corruption, but this corruption doesn't restrict FDI to come into these countries. These countries can attract a higher level of foreign direct investment with a higher prevalence of corruption. This factual evidence raises the question of how government corruption influence FDI. This study will carefully contribute to exploring the established complicated relationship between government corruption and foreign direct investment.

Institutions in any country set the regulations for economic activities to carry on [33]. Government corruption is defined as misuse or pervert of government official dominance to get personal objectives [33,36]. Foreign firms are inclined to pay bribes to government authorities to get a favorable environment for licensing, permits, bank loans and so other benefits [41]. [29] argued to connect government corruption with FDI activities that government corruption has solid impact on performance.

3. Hypothesis Development

3.1 Political Instability and Foreign Direct Investment

Political instability as defined earlier is a situation when an authoritarian person creates democratic political disruption and there is a high probability of the existing government authorities involuntarily removal by force. Political instability has become a critical issue for developing countries especially Pakistan [30]. Authoritarian rules in Pakistan for almost three decades didn't permit democratic politics to grow.

Nonetheless, many scholars in political science have argued that economic performance is positively affected by democracy, but several other researchers have different points of view about the relationship between democracy and economic performance. [28], have a different argument about the relationship between democracy and economic performance, it is more complicated beyond one's imaginations. [28], and [32], found in a spectacular empirical analysis that there is not an exceptional relationship between democracy and economic performance but the growth rate in democracy and authoritarian regimes are quite similar.

These mentioned theories on the effect of political regimes e.g., democracy and authoritarianism on economic performance are disparate from the studies on international investment and political regimes. In common sense, multinational enterprises prefer to invest more in the regimes of authoritarian. The answer to the question of why MNEs will prefer to invest in authoritarian regimes is, that the authoritarian leader has a monopoly on decision making and he is not liable to anyone in the country as he is the supreme leader. Authoritarian leaders can offer better facilities to multinational enterprises to attract foreign direct investment. These leaders may provide multinational firms with better entry deals, discounts in taxes, and access to markets because of no or less pressure from their government and the public [22]. As a result of these reasons, foreign direct investment inflow is increased in authoritarian regimes or authoritarian countries.

Another argument that foreign direct investment inflow is increased in authoritarian regimes by providing the lower labor cost to multinational enterprises also gets support from literature [3].

Authoritarian leaders can repress the labor unions and use their authority to retain the low wages. But the question is that lowering the labor cost is only the factor that can cause to increase in the foreign direct investment inflow in authoritarian regimes? The answer will be negative because most researchers in FDI argue that hiring low-wage labor can be one of the many decisions made by multinational enterprises [27]. Furthermore, the argument on the role of authoritarian regimes has been overemphasized in bargaining with multinational firms. It is assumed that authoritarian leaders have fewer constraints and pressure for policymaking so there is a munificent situation available for MNEs in authoritarian regimes. [8] argues that both constraints and dominance are part of a two-level game for political leaders. Democratic leaders face more constraints as compared to authoritarian leaders because they have more pressure on the public for policy making and to work on merit, they have less bargaining power. Authoritarian leaders having more discretionary authorities, bargaining power with MNEs, monopoly for policymaking and more control on labor wages can facilitate multinational firms by providing extra offers and deals. Authoritarian leaders can use their discretionary authorities to provide MNEs better entry deals, can bargain for a rebate in taxes, can provide low-cost labor, and have freedom of policymaking in favor of multinational enterprises. In return for all these, relationships between authoritarian leaders and MNEs increase which results in a higher amount of foreign direct investment inflow in authoritarian regimes. Following these theories, we assume that there are more chances to increase foreign direct investment inflow when there are authoritarian regimes.

Hypothesis 1: Higher the authoritarian regimes in the country, the higher the likelihood of foreign direct investment inflows.

3.2 Government Corruption and FDI

As mentioned earlier, corruption has become a serious economic, political, social, and moral issue especially in emerging economies which may hinder foreign direct investment inflows by accelerating uncertainty [3], hence decreasing the confidence of foreign investors in political institutions. Although some researchers [43,33] found a positive association between corruption and FDI, and they view corruption as an opportunity for MNEs since [19] found it as a serious obstacle for FDI. Theoretically, most foreign investors look at corruption in dual contexts: ethically and economically. They believe that corruption is a morally wrong activity, and they also avoid corruption because it may increase cost and risk. Corruption is found as a “neighbor” effect by [28]. That means corruption in developing countries also affects foreign direct investment in a particular host country. For example, a high level of corruption prevalence in South Asian countries will adversely affect foreign direct investment in Pakistan.

Government corruption in Ukraine is found very organized and established. According to [33], “There are many factors taking bribes and there is often no guarantee that goods or services that have been ‘paid for’ will be delivered. There are organized crime groups that expect payment for services and there are various payments that need to be made to multiple government officials, and these bribes and unnecessary payments lead to negatively affect the intention of foreign investors to invest in such corrupted countries. Following the previous theories, we assume that:

Hypothesis 2: Higher the prevalence of government corruption, lower the likelihood of foreign direct investment inflows

3.3 Moderating effect of Government Corruption

[23] argues that hosting countries with higher political stability have a higher level of FDI outflows, but higher political instability will negatively affect FDI inflows. On the other hand, [21] empirically found that more instability is better for economic growth. He argued that democratic political regimes are good for competition but once the democratic governments fail to deliver, more competent people take place which led to economic growth. As mentioned earlier that authoritarian leader has a monopoly of decision and policymaking and have more power to offer excessive facilities (e.g., tax rebates, better entry deals and access to local markets) to international investors [22]. These leaders can attract more FDI in politically unstable regimes.

Higher Corruption Perception Index (CPI) has a negative association with foreign direct investment. It is further disclosed by [35], that developing countries are generally recognized as more corrupted as compared to developed countries. However, [40] found empirically that host governments' restrictions on FDI become the causes of corruption. Nonetheless, political instability has a positive impact on FDI, the decision to invest in other countries can't be made in isolation from government corruption in each country. Hence, the endmost question is that how the positive impact of political instability on FDI in beginning progress over time when MNE continues operations in a given country. This paper investigates how the positive political instability-FDI relationship is moderated by government corruption effect, given that firms while operating in the politically unstable environment, they also learn about the prevailing corruption and the way to deal with it over time. Therefore, we hypothesize that the political instability-FDI relationship can be moderated by the diminishing effect of government corruption in a said country such that the positive effect of political instability on FDI discovered at the prior stage will decrease over time.

Hypothesis 3: The positive relationship between political instability and foreign direct investment will be moderated by the decreasing effect of government corruption.

4. Research Methodology

4.1 Data Collection

We tested our research hypothesis using firm-level data. A sample of 230 MNE subsidiaries operating in Pakistan is used from 2001 to 2019. The data is collected from the State Bank of Pakistan (SBP) and the Pakistan Board of Investment (PBI) database. Even though collecting firm-level data was very difficult due to privacy and confidentiality but we arranged to get just partial data required for our research. Political instability measures are found from The Worldwide Governance Indicators (WGI) from the World Bank website. Measures of scale for political instability are found from 2.5 to -2.5 where 2.5 represents the highly politically stable country and -2.5 is for the highly unstable country. Corruption Indices are downloaded from World Bank Corruption Index and Transparency International Index which uses 0 to 10 scales where 0 is the most corrupted country and 10 shows most clean country. For the years 2001 and 2019, the scale was used 0-100 but we change it with the same 1-10 for more convenience to understand. Moreover, data of other control variables like GDP%, Inflation Rate%, Unemployment, Education, and Money lending are also collected from World Bank indicators.

Our research is driven by longitudinal data on firm-level from 2001 to 2019. No doubt, the data of FDI inflows in Pakistan may be available since 1948 but there were very few observations. The reason to set 2001 as the beginning of the observation period is autocratic or dictators' regime started in 1999 and then a successful democratic regime started from 2008 and it continued till 2019 by the end of our observations. From 1999 till 2008, it was an authoritarian regime and again a democratic regime for 11 years from 2008 till 2019.

4.2 Dependent Variable

Our dependent variable in this research is the amount of foreign direct investment because we are interested to know the effect of political instability and government corruption on FDI. Foreign direct investment is the total amount invested by the foreign multinational firms in Pakistan during the period between 2001 and 2008, and then between 2008 and 2019 to investigate the results altogether as well in different regimes.

4.3 Independent Variable

4.3.1 Political Instability

The definition of political instability is derived from [17]. The key independent variable is political instability (PI), and the data is obtained from The Worldwide Governance Indicators (WGI) by World Bank. The researcher recalculated political instability by deducting the secured number of the country from 5 where 0 refers to higher political stability and 5 refers to higher political instability.

4.3.2 Government Corruption

Government corruption index is available on different resources e.g., World Bank Corruption Index, Transparency International Corruption Index. These organizations measure corruption by surveys and interviews by a third party in most countries. In 2019, data on the government corruption index for 194 countries were published. We used both indices to test whether they produce the same results or different indices show different results. The original government corruption scale in the Transparency International Index range between 0 (highly corrupted country) and 10 (highly clean). To understand easily, the researcher recalculated the scale where 0 represents the highly clean country and 10 refers to the highly corrupted country by deducting the original scale out of 10.

4.4 Control Variables

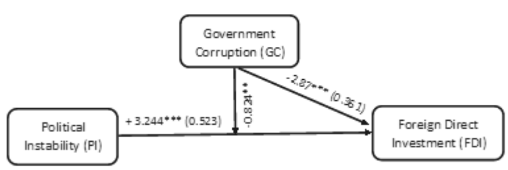
Money Lending % (ML)
GDP Rate %
Unemployment Rate % (UE)
Inflation rates %

The reason to control these variables is that money lending, GDP, unemployment, and inflation rate in the country can make a significant difference for the MNEs to decide whether to invest in authoritarian regime or democracy keeping in view the level of corruption.

4.5 Analytical Methodology

Our sample contains unbalanced data. That is, some firms are found for 20 years, and some are found more or less than 20 years in our sample. We used multi regression to test our hypothesis. To investigate the fitness of the model, we used the SPSS model fit test which shows that model is fit related to the data sample. We used exploratory factor analysis to check the reliability and validity of variables being used to test the hypothesis. We found that the model is fitted with the data sample. Moreover, reliability and validity are also confirmed. We found that this model is appropriate, so the final regression model is:

$$FDI = \beta 0 + \beta 1PI + \beta 2GC - \beta 3\ (GC) * (PI) + \beta 4Controls + \varepsilon i$$



[Figure 1] Research Model

Where, FDI = the amount of foreign direct investment by multinational firms on their subsidiaries operating in Pakistan, GC = host country government corruption indexes each year, PI = host country political instability scores each year, and Controls = money lending ratio by the host country, GDP growth ratio and unemployment ratio, inflation rates.

5. RESULTS

5.1 Reliability and Validity

The scales reliability of Political Instability and Government Corruption (GC), were based on internal consistency. The value of Cronbach's alpha coefficient was .961 for Political Instability and .821 for Government Corruption (for internal constancy of the scale, normal Cronbach's alpha was utilized because the items were analyzed in the same scale and the association between the items used), whereas for the Guttman test, it speckled between .860 and .892 with a lambda value 4.5 of .890 for Political Instability and varied between .679 and .896 with a lambda value 4.2 of .999 for Government Corruption.

The KMO's Measure of Sampling Suitability and Bartlett's assessment of sphericity of the factor assessment for the average of the questions of Political Instability and Government Corruption scales. The two dimensions help to control the fact ability of the statistics for factor analysis. Bartlett's test of sphericity essentially is substantial ($X2 = 786.156$, $df = 55$, $p \leq 0.05$) for the factor analysis to be considered suitable and the Kaiser-Meyer-Olkin's analysis of sampling adequacy can specify in advance if the sample size is huge enough to reliably abstract the factors. KMO value was found .887 for Political Instability and .885 for Government Corruption, values from 0.8 and 0.9 are prodigious however, values below .500 are deplorable. Hence, the KMO value specified that the factor analysis can be accomplished. Testing methods above have demonstrated that the data was correct and appropriate for the factor analysis.

5.2 Correlation and Regression

<Table 1> represents the correlation matrix, employs the data of 130 MNEs operating in Pakistan between 2001 and 2019 and shows that Political Instability, FDI, and Government Corruption are associated positively and someplace negatively but the positive connotation is dominant. <Table 1> explains standard deviation, means, and ranges as well. The relationship results illustrate that Political instability is positively correlated ($r = 0.39$, $p<0.01$) with Foreign Direct Investment at a significant level. Nevertheless, government corruption is adversely correlated ($r = -0.48$, $p<0.01$) with FDI but positively correlated ($r = 0.15$, $p<0.01$) with political instability.

〈Table 1〉
Correlation Matrix

Variables	Mean	SD	FDI	PI	GC	ML	GDP	UE	Inflation
FDI	13.68	6.72	1.00						
PI	5.18	0.69	0.39***	1.00					
GC	0.86	0.81	−0.48***	0.15*	1.00				
ML	3.75	0.95	0.32***	0.16**	−0.19**	1.00			
GDP	2.44	0.76	0.23***	0.21**	−0.12*	0.24*	1.00		
UE	4.71	0.68	0.16*	0.06*	−0.06*	0.09**	−0.15**	1.00	
Inflation	8.40	0.69	−0.45***	−0.12**	0.15*	0.21**	−0.45***	0.48***	1.00

Note: Sig *p < 0.1, **p < 0.05, and ***p < 0.01
FDI = Foreign Direct Investment; PI = Political Instability; GC = Government Corruption; ML = Money Lending; GDP = Gross Domestic Product; UE = Unemployment

The results from regression analysis are depicted in <Table 2> that examines the impacts of political instability on foreign direct investment, the effects of government corruption on foreign direct investment, as well as moderating effect of government corruption between political instability and foreign direct investment. After adding control variables in Model 1, the results show that money lending 1.304***(0.546) has a steady positive impact on foreign direct investment at a substantial level within all Models. It indicates that sizable firms can accomplish better and can have greater foreign direct investment as compared to small-size organizations [13]. GDP 1.780***(0.423) and unemployment rate -2.32***(0.671) have no or less significant impact on foreign direct investment through all models. The previous researchers identified diverse results from experimental research about the impact of a firm's time of life on its foreign direct investment such as the positive impact of age on FDI [13] and the adverse influence of age on foreign direct investment [32], but firms with a young age have greater chance to grow quicker and have a better operation in foreign direct investment than middle and larger size firms [38]. The gross domestic product growth of Pakistan is found amid 5 and 6 percent for the year 2001-2019 [5]. Outcomes from previous studies enlightened that local capital subsidization has an impartial or negative impact on foreign direct investment [39]. Thus we discovered in <Table 2> that unemployment rate has negative impact on foreign direct investment.

〈Table 2〉 Hierarchical regression, political instability, government corruption and their interaction on FDI

Variables	Dependent Variable: Foreign Direct Investment			
	Model No. 1	Model No. 2	Model No. 3	Model No. 4
	Independent variable with controls			
CONSTANT	16.120*** (4.201)	6.420 (5.155)	5.620 (4.145)	3.179 (3.668)
ML	1.304*** (0.546)	1.078** (0.520)	1.023** (0.441)	0.910** (0.437)
GDP	1.780*** (0.423)	2.110*** (0683)	0.725* (0.501)	0.389 (0.563)
UE	-2.32*** (0.671)	-1.451*** (0.785)	-0.919* (0.392)	-0.618 (0.517)
PI		3.244*** (0.523)	2.250*** (0.421)	3.458*** (0.534)
GC			-2.87*** (0.361)	-3.546*** (0.387)
Interaction effects PI x GC				-0.824** (0.461)
Obs.	230	230	230	230
R2	0.192	0.285	0.492	0.568
F Models	14.54***	19.14***	28.41***	36.23***

Note: *p < 0.1, **p < 0.05, ***p < 0.01

Discrete regressions are used to analyze in Model 2 whether the substantial connotation between political instability and foreign direct investment exists or not. Model 2 explains empirical indication that political instability 3.244***(0.523) has a reliable constructive relationship with foreign direct investment among all models at a strongly substantial level 2.250***(0.421) in Model 3 and 3.458***(0.387) in Model 4, which supports our Hypothesis 1. Afterward, we tested moderating effect in model 3. The outcomes of model 3 describe that government corruption has a negative association with foreign direct investment at a significant level -2.87***(0.361), in turn supporting hypothesis 2. Finally, moderating or interaction variables were included in model 4, which examines whether moderating effects are present, and results indicated -0.824***(0.461) that it does.

The results in <Table 2> illustrate that all hypotheses are strongly significant across all models. This study ran numerous regressions to evaluate how foreign direct investment is influenced by political instability and different kinds of government corruption. Political instability was included in model 2 of <Table 2>, which shows an anticipated strong positive relationship between political instability and foreign direct investment across all models, strongly supporting hypothesis 1. When government corruption was added in model 3, the results demonstrate that the association between government corruption and foreign direct investment is negative that strongly supports hypothesis 2. Subsequently, the moderating term between political instability and government corruption was added in model 4, which expects a negative moderating impact on the association between political instability and foreign direct investment. Here, to evade a problematical multicollinearity problem with the interface term, the moderating terms were mean-centered.

The results in model 4 describe that the adverse and significant moderating effect of government corruption on the relationship between political instability and foreign direct investment could be identified. Specifically, the results indicate that there is a significant relationship between political instability and foreign direct investment, this association can be weakened under government corruption context. Nonetheless, the results deliver empirical evidence that strongly supports hypothesis 3.

Similarly, the moderation interaction term between political instability and government corruption was included in model 4. The model 4 results demonstrate that the connection between political instability and foreign direct investment gets weaker, as expected from Hypothesis 3. That is, the results indicate that there is a considerable positive relationship between political instability and foreign direct investment and this relationship could be weaker under the government corruption context.

6. Conclusion, Discussion, and Future Research

Institutional theory is implemented in this study to understand the effects of government corruption and political instability on FDI of multinational firms' subsidiaries operating in Pakistan between 1990 and 2014. The purpose of this study is to fill the gap of existing International Business research by investigating the moderating effect of government corruption between political instability and foreign direct investment. This paper explicitly investigated that the effect of political instability on foreign direct investment diminishes as a multinational firm learns about the government corruption in each country.

First, the results from all models have strongly supported the positive effect of political instability on foreign direct investment as anticipated in hypothesis 1, especially developing countries like Pakistan with higher political instability attract more foreign direct investment from developed countries with higher political stability. This result is consistent with the argument of [23]. This study suggested that multinational firms face the negative effect of government corruption on FDI. FDI will be negatively affected when government corruption will moderate political instability and foreign direct investment, as anticipated in hypothesis 3.

Previous studies paid more concentration to the simple binary relationship between political instability and FDI, and government corruption and FDI, positive versus negative. After incorporating a dynamic framework of managerial theory into the model, the existed bifurcated effect of political instability on FDI is no more supported, suggesting that political instability doesn't influence FDI independently. The contribution of this study in existing research is that it interprets the indirect relationship between political instability and FDI. That is, a positive relationship between political instability and FDI is found empirically but this relationship became negative when government corruption moderated between political instability and FDI. These findings also provide some practical implications. Considering that the non-linear political instability-FDI relationship deviates from the level of government corruption in each country, managers can enact different FDI strategies overtime before they enter a country with a different level of government corruption.

We also investigated the relationship between political stability and FDI, we found that there is an adverse relationship between these variables. Furthermore, the relationship between government corruption and FDI is also found negative during the period of political stability/democracy same as we investigated in political instability regimes. That is, authoritarian leaders are more able to attract foreign direct investment by proposing extraordinary offers e.g., tax rebates by using their monopolistic decision-making power. On the other hand, democratic governments face huge constraints from the public and opposition when they need to make policies for multinational firms to enter and operate in their country so the foreign direct investment is adversely affected in politically stable regimes.

This study has some limitations like other studies. First, the sample data included in this study is for 19 years only between 2001 and 2019. The data before 2001 may also be available but some data was found missing before that time. Moreover, one object of this study is to investigate political instability-FDI relationship political stability-FDI relationship. Also, to investigate government corruption-FDI relationship in political instability and political stability regimes. So, we selected 19 years of data which include 8 years of political instability and 11 years of political stability that means democracy. The second limitation of this study is, that we selected Pakistan where there is high political instability and a high level of corruption so future research can apply a country with high political instability and low level of government corruption or vice versa. Finally, political instability and government corruption indices are available from the World Bank and Transparency International website which may be slightly different according to their way of measurement so results can be slightly different if use other indices.

Our data sample is of the current period so we believe that this study will contribute to International Business literature by describing the FDI activities of multinational firms in Pakistan during both regimes.

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