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**Political Governance, Civil Liberties and Human Capital: Evaluating their effect on  
Foreign Direct Investment in Emerging and Developing Economies**

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**Abstract**

We study the influence of a country's political governance on its attractiveness to foreign direct investors. We argue that democracy is not a unidimensional concept and that the effect of host country political governance on incoming Foreign Direct Investment (FDI) differs depending on whether FDI originates from a democratic or an autocratic country. We also hypothesize that the effect of civil liberties depends on the motivations of investing Multinational Enterprises (MNEs) and that human capital moderates this relationship. We test our hypotheses on a sample of 35,000 investments in emerging and developing countries between 2003 and 2013.

**Keywords:** Political governance; civil liberties; human capital; foreign direct investment; investment motivations

## INTRODUCTION

With the end of the Cold War in the 1980s, the number of countries pursuing democratic, pro-market reforms increased steadily (Levitsky & Way, 2010), but more recently, especially over the last decade, there has been a decline in democratic governance (Freedom House, 2017). Regimes, many of them autocratic, that held sway in strategic geopolitical locations had long enjoyed the support of the US or the USSR as the two main Cold War protagonists (Wright, 2009; Bermeo, 2011). Unsurprising, when the forty-five year stalemate finally came to an end there were economic implications for recipient countries, and their leaders undertook policies they hoped would ensure stability--and allow them to remain in power. One such policy was to proactively attract foreign direct investment (FDI). In this paper, we focus on democratic capital, capital that originates from firms based in democratic countries. As those firms engage with the governments of host countries, democratisation is promoted (Mosley, 2017).

A large stream of studies, predominantly taking an international political economy perspective, considers the relationship between democratic capital and the level of democracy in a host location. Olson (1993), McGuire and Olson (1996), and Ursprung and Harms (2001) provide evidence that MNEs invest more in countries where democratic rights are respected. Rodrik's (1996, p.57) seminal work investigating specifically the relationship between US FDI and host country democratic rights finds that countries with weaker democratic rights attract less US capital. The study of Ursprung and Harms (2001) also finds a significant positive relationship between democracy and FDI. On the other hand, Huntington and Dominguez (1975), Wintrobe (1998), and Greider (1998) all report a negative relationship. Later studies including Li and Resnick (2003), Adam and Filippaios (2007), and Asiedu and Lien (2011) find a non-linear relationship.

To explain these inconsistencies and provide a more multidimensional definition of democracy, another strand of literature focuses on the disaggregated measures that constitute democracy; namely political rights and civil liberties. Studies by Huntington and Dominguez (1975), Wintrobe (1998), and Greider (1998) provide evidence in support of the idea and show that multinational enterprises (MNEs) tend to invest in countries with a low level of civil liberties, that is, where repression is high. Three

factors can explain the mixed results. First, most studies tend to focus on the ‘rules of the game’ (North, 1990) rather than the ‘play of the game’ (Williamson, 1998). Whilst the overall level of democracy and quality of institutions (‘rules of the game’) does influence the decisions of MNEs, the interaction between an MNE and a host country government (‘play of the game’) is also important. To shed more light on the role of the play of the game, we build on the work of Levitsky and Way (2010), adopting their approach in order to capture democracy’s multi-dimensional nature, and the varying levels of influence individual components of democracy can have on the investment decisions of MNEs. Thus, our definition of democracy includes free and fair elections, adult suffrage, protection of civil liberties, and few non-elected tutelary authorities (e.g. militaries, monarchies, religious bodies).

Complimentary to this, we look to the work of Henisz and Mansfield (2006). They see political institutions within democracies bounded by the extent to which political decisions are subject to veto points, arguing that as the effects of societal forces depend on domestic institutions, so the effects of institutions are contingent on societal forces. Their findings suggest that democratisation to promote prosperity and free trade depends on institutional factors, on global and local macroeconomic conditions, and on competition between interest groups.

Building on the above, we use the term political governance to capture both the rules of the game that determine the institutional characteristics of the political regime status but also the play of the game that determines the interaction of political parties with other actors in the economy.

From an International Business (IB) perspective, what motivates MNEs to invest and the role civil liberties plays in this choice are crucial. We are interested, thus, in how civil liberties allow MNEs to extract additional rents and maximise profits. One would expect civil liberties to influence differently investments depending on whether they are market seeking, resource seeking, efficiency seeking or strategic asset seeking. Building on the international political economy perspective (Locke, 2013; Lim et al., 2015), we argue that civil liberties suppression will have a negative effect on incoming market-seeking and strategic asset-seeking FDI, but a positive one on resource-seeking and efficiency-seeking FDI. Finally, we postulate that the stock of human capital in a host country moderates the relationship

between investment motivation and civil liberties, primarily through changes in terms of labour force productivity. This is where we make our third conceptual contribution. We build on the work of Mosley and Uno (2007) and argue that human capital, especially when semi or highly skilled, can have a moderating effect on the relationship between civil liberties suppression and FDI.

We empirically test our hypotheses on a large sample of approximately 35,000 investment projects in 110 developing and emerging economies over the 2003-2013 period. We have collected data from thirteen investor home countries, some democratic and some not. This allows us to consider country of origin effects and home-host political governance differences. To the best of our knowledge, we are the first to use data at the individual investment level. We provide a holistic approach to analysing the effect of political governance and civil liberties suppression through the examination of a comprehensive number of home and host countries and industries over the ten-year period of the dataset. To demonstrate the impact of our interaction effects, we follow an approach suggested by Kingsley et al. (2017) and calculate and present the marginal effects, ensuring that we neither overstate nor understate our interaction results.

We structure the remainder of the paper as follows: In Section 2, we present our theoretical framework and key arguments and develop our hypotheses. In Section 3, we describe our methodology and the key characteristics of our sample, after which in Section 4 we present the results of our regressions and discuss them. Finally, in Section 5 we conclude by offering possible future research directions.

## **THEORETICAL FRAMEWORK**

In this section, we present our theoretical arguments regarding the role of political governance in attracting FDI, the interaction of civil liberties and motivations for FDI, and the moderating effect of human capital on that relationship.

### **FDI and Political Governance**

Most studies of the kind we undertake look at different dimensions of democracy. Ursprung and Harms (2001) explore the relationship between democracy and incoming FDI to determine if in fact, as some have espoused, political repression boosts FDI. They consider 62 developing and transitional economies over the 1989-1997 period and find that MNEs tend to be attracted to countries where political and civil liberties are respected. Indeed, the extant literature finds a positive relationship between democracy and FDI, with few exceptions. One of them is Yang's (2007) investigation of the relationship between political regimes and FDI inflows. He considers two regime types, democracy and autocracy, and three measures of FDI, absolute level of FDI inflows, FDI over GDP, and FDI per capita, using a sample of 134 developing countries over nearly twenty years, 1983 to 2002. He finds no evidence of a systematic relationship between democracy and FDI inflows.

Different approaches have been taken to study the democracy-FDI relationship. Among those that focus primarily on the effect the rules of the game have on FDI, Busse (2004) investigates the impact of the quality of institutions and the degree of political rights and civil liberties on FDI using aggregated and disaggregated measures of democracy, and finds a positive and statistically significant relationship between democracy and inward FDI. In a similar vein, Busse and Hefeker (2005), using a panel of 83 developing countries over the 1984-2003 period, explore links between institutions, political rights and civil liberties, and FDI inflows. They find that "government stability, internal and external conflict, corruption and ethnic tensions, law and order, democratic accountability of government, and quality of bureaucracy are highly significant determinants of foreign investment inflows" (2005: 5). In a recent study, Gossel (2017) finds that FDI is influenced by a country's past history of democracy, not simply its contemporaneous status. At the same time, he finds no relationship between FDI and civil liberties. In the same vein, Li et al. (2018) conducted a meta-analysis of the relationship between FDI and democracies. Their findings support the idea that democracies tend to attract more FDI.

Although few, there are studies that examine the play of the game and the way government-MNE interaction determines investment outcomes. Oneal (1994) argues that autocratic governments and MNEs can mutually benefit from collaboration. If a regime grants MNEs access to resources and guarantees their profitability in the local market, MNEs may in turn bring new technology and know-

how to the host country. If economic development results from the exchange, the government will be strengthened. Jensen (2003) empirically explores the effect of host country political conditions on FDI inflows. He uses both cross section and panel analysis for 114 countries, and finds that democratic governments attract higher levels of FDI. He holds that MNEs find democratic countries attractive as democratic systems include opposition parties and decisions may be subject to veto, both of which are likely to prevent sudden policy changes; thus such countries offer economically and politically stable environments. Henisz (2004) argues that economic policy is determined by political struggle within institutional frameworks. In democracies, policymaking does not hinge on a single political player, but is the result of a bargaining process between actors with diverse objectives. Autocracies are characterised instead by few checks and balances. As there is no consultation, there is less volatility in policymaking, and this impacts the speed with which policies can be adjusted in response to changes in the environment.

Huntington and Dominguez (1975) initiated a debate in the field by arguing that autocratic regimes provide a better economic environment for both domestic and foreign investment as they are better positioned to enact efficiency-enhancing policies. This is disputed by Olson (1993) and McGuire and Olson (1996), who point to the risk of policy reversals in dictatorships and to the lack of credibility of policy stability in countries with weak democratic rights. It is well-established in the literature (Ferejohn, 1986; Drazen, 2000) that elections are a disciplining device for policymakers. When elections are free and fair, voters will punish officeholders for bad economic outcomes, and knowing that, those in office will pursue what they consider to be sound economic policies. Olson (1993) and McGuire and Olson (1996), argue that an insecure autocrat has a shorter time horizon as circumstances change, thus in countries where political liberties are low, i.e. where electoral mechanisms do not exist or do not work efficiently, there will be worse economic outcomes than where citizens have political liberties. As less efficient policies have a negative effect on the returns to FDI, FDI falls. We conclude from the seemingly contradictory positions taken in these studies that it is not democracy or autocracy per se that influence FDI, but how effective the electoral mechanism is in a host country, or put more broadly, how effectively an incumbent government is held responsible for economic outcomes.



Political regimes range from autocracy to full democracy. Levitsky and Way (2010) hold that there are many kinds of autocratic governments and under them significant differences in the protection of political rights and civil liberties, while in a true democracy both are universally strongly protected. They identify an additional type, the Competitive Authoritarian regime which usually guarantees civil liberties, while in reality only partially protecting them. This is closely aligned to the argumentation of others. Henisz and Mansfield (2004) hold that there is conditionality attached to interest group demands and also to institutions in determining the commercial openness of an economy. The extent to which domestic institutions filter the effect of interest groups on policy is determined by the degree of concentration of governmental authority or by the existence of veto points. Building on this reasoning, Henisz and Zelner (2005) argue that there is a clear difference in the complexity of goals between foreign investors and governments. Whilst investors focus on the maximisation of returns, policy makers must balance the diverse interests of a variety of interest groups and stakeholders. This creates volatility in the final outcome of the negotiation process as interest group reactions might influence the process. It is arguable that if a spectrum of democratisation exists, with authoritarianism at one end and full democracy at the other, competitive authoritarianism would lay between the two (Levitsky & Way, 2010). As we wrote earlier, Henisz (2004) reasons that economic policy is determined by political struggle within an existing institutional framework. Small economies that depend significantly on external capital, be it FDI or developmental aid from Western donors, are subject to a higher degree of leverage from MNEs based in democracies (democratic capital). This is demonstrated by the fact that the regimes of such countries have the strongest links to Western democracies. Often a key reason for attempting to strengthen ties is to avoid isolation by Western governments (Levitsky & Way, 2010). The actions of opposition political parties or the existence of veto points may lead to a change in policy (Henisz, 2004). Based on the above, we argue that countries with democratic political environments will attract greater FDI inflows, whereas those which are overtly autocratic, will attract less. We further postulate that politically transparent and democratic countries are more likely to be attractive to MNEs themselves from democratic countries. Those MNEs understand not only the rules of the game but also the play of the game in democratic environments where there are more checks and balances. On this basis, we formulate our first hypothesis:

**Hypothesis 1a:** An autocratic regime in a country reduces the amount of FDI from democratic countries.

Conversely, autocratic countries such as China are more likely to direct FDI to other autocratic countries, either for ideological reasons or strategic motives (Buckley et al., 2007). This is especially true in the case of emerging and developing countries. We assume that this is related primarily to the heterogeneity of host countries and not to the limited political idiosyncrasies of home countries. However, Chinese FDI has a different pattern, with Chinese firms acquiring targets in developed economies. Clegg et al. (2018) investigate the relationship between home country autocracy and the internationalisation of state-owned MNEs and find that such MNEs can become an autocratic government's instrument to get access to resources and to advance a mercantilist agenda. Because many Chinese MNEs are state owned, this accounts for a significant share of Chinese outward FDI. Narula (2012) argues that location assets and their availability are affected by the way governments restrict or encourage particular activities. Commercial and strategic considerations, in addition to serving the interests of specific groups, are the key reasons for this type of government intervention. Consequently, we argue that the relationship between an autocratic regime and inward FDI from other autocratic countries will differ from the one postulated in Hypothesis 1a. We therefore hypothesise:

**Hypothesis 1b:** An autocratic regime in a country increases the amount of FDI from other autocratic countries.

### **FDI and Civil Liberties – The Role of FDI Motives**

The way MNEs interact with local governments is one factor that influences FDI. They interact as well with a variety of social actors--including trade unions. Such interaction determines the ability of an MNE to maximise profits and extract rents. A number of papers have considered the influence of non-government institutions on FDI with results supporting a range of outcomes. Pournarakis and Varsakelis (2004) investigate the factors leading to uneven allocation of FDI in economies in transition. They look at the 1997-2001 period, and find that higher levels of civil rights combined with better quality institutions have an indirect positive effect on FDI. Blanton and Blanton (2007) examine the impact of human rights on FDI inflows and empirically show that those rights have both direct and indirect effects,

with repression negatively related to FDI inflows. They also find human rights significantly positively related to human capital, and that human rights have a significant indirect effect upon FDI through their impact on human capital. Finally, they do not find a significant relationship between democracy and democratic institutions and FDI inflows. According to Mosley (2017), improvement in workers' rights is only possible if there is clear alignment between MNE intentions to improve procedural rights and working conditions, and governmental incentives. Mosley (2011) shows in previous work that the presence of MNEs usually strengthens the protection of labour rights, a key component of civil liberties. MNEs originate from both developed and developing economies, thus the labour standards and institutional environment of their home country may differ from those prevailing in host countries (Pandya, 2016). The crucial actor is a host government willing to enforce strict labour standards regardless of the risk that FDI may be lost to countries with lower labour standards (Mosley, 2017). It is arguable that greater alignment of interests between MNEs and governments exists in industries where the demand for workers or specific skills exceeds local supply. FDI can have a positive impact on workers' rights when it is contingent on a government improving them. Industry specifics can also influence labour rights as Locke (2013) shows in looking at the athletics footwear sector. He demonstrates how in a fast paced, efficiency-seeking industry, the incentive to relax working standards and in general suppress the rights of workers is quite high.

The body of work we have highlighted shows that civil liberties can influence FDI in different ways. When FDI is market seeking or strategic asset seeking it is not likely to flow to economies where civil liberties are suppressed, whereas FDI which is resource seeking or efficiency seeking will be attracted to such economies to capture cost reductions and efficiency gains. We expect differences in the impact on FDI inflows of civil liberties between market-seeking and strategic asset-seeking investment on one hand, and resource-seeking and efficiency-seeking investment on the other.

Cuervo-Cazurra and Narula (2015) argue that changes in the behaviour of MNEs that have taken place over the last 30 years have led to a rethink of the internationalisation motives proposed by Dunning (1993). There is now increased emphasis on strategic assets both by investing firms and by host governments. Whilst it is arguable that strategic asset-seeking investment can have significant

positive externalities and therefore welfare effects, this does not mean that countries should concentrate on attracting such investments to the exclusion of others. Giroud and Mirza (2015) underscore this in arguing that the economic structure of a country determines the investment motives of potential investing MNEs. The business activities of a firm determine whether it will have market-seeking, resource-seeking, efficiency-seeking or strategic asset-seeking motives. We identify what kinds of activities correspond to each of the four investment motives (see Table 6). Following Cuervo-Cazurra et al. (2015) we combine arguments on the choice between economics-driven exploitation of resources or exploration of new ones, and on the psychology-driven set of pull and push factors that impact the search for better country conditions.

Strategic asset-seeking firms internationalise in pursuit of foreign assets they need for the medium and long-term regeneration of their competitive scope. This type of investment is motivated by the increased geographical dispersion of the key inputs to an MNE's creative and learning processes. In developing and emerging markets, strategic asset seeking is motivated by the need to tap the host country's system of innovation in order to develop locally-adapted products. To achieve its strategic asset-seeking goal an MNE needs to have access to well-educated, highly-skilled and innovative workers and workers having such attributes are found, or can be developed, where civil liberties are strongly protected. Thus we hypothesise:

**Hypothesis 2a:** Civil liberties suppression will have a negative effect on strategic asset- seeking FDI.

An MNE having a market-seeking motivation intends to produce in a host country goods or services for consumption either in that country or in the region. Two distinct factors determine the suitability of a location for an MNE having a market-seeking motivation. First, there needs to be a fit between the firm's competitive environment and the target market, i.e. there must be reason to believe an investment will be profitable. Second, local production must be preferable to exports for serving the market. One important consideration here is the need for local responsiveness: the MNE needs a local presence to adapt its products and processes to local tastes and market conditions (e.g. regulations).

Market-serving MNEs are likely to be keen to have high labour standards because of reputational benefits. We thus hypothesize:

**Hypothesis 2b:** Civil liberties suppression will have a negative effect on market-seeking FDI.

In contrast to market-seeking investments, efficiency-seeking ones entail the relocation of production abroad to achieve cost competitiveness in the MNE's mature high-income home market. The main driver is cost reduction and that can be achieved by maximisation of rents extracted from local operations. Civil liberties suppression, including reducing or doing away with bargaining rights, saps the power of trade unions, to the advantage of MNEs (Cuervo-Cazurra et al. 2015). Hence:

**Hypothesis 2c:** Civil liberties suppression will have a positive effect on efficiency-seeking FDI.

Finally, firms with resource-seeking motives are usually interested in obtaining natural resources at lower cost than in their home country. In many instances, especially when the resources are scarce in their home country, they will be looking for a long-term guaranteed supply. Witte et al (2017) look at the effect of political conflict on FDI. They distinguish between resource and non-resource sectors and conclude that FDI in resource-based sectors is less sensitive to political conflict, irrespective of its nature, because of the high profitability of the investment. A second resource-seeking motivation is accessing an abundant labour force to remain cost competitive. In both cases, the MNE motivation is cost reduction and therefore we hypothesise:

**Hypothesis 2d:** Civil liberties suppression will have a positive effect on resource-seeking FDI.

### **The Moderating Effect of Human Capital**

Globalisation impacts labour rights in at least two ways. FDI may contribute to a climb to the top in which case governments are pressured to improve labour standards, alternatively MNE competition may have a negative effect, a labour-standard race to the bottom (Mosley & Uno, 2007). There are three avenues open to MNEs to improve workers' rights: (i) applying direct pressure on local governments, (ii) implementing best practices, and (iii) focusing on the quality of labour over its cost. Borensztein et

al. (1998) suggest that FDI has a stronger impact on host country growth when the country has a minimum level of human capital.

Productivity is a key consideration in making FDI decisions and a host country's level of human resources clearly correlates with FDI inflows. Dunning (1988) tested the influence of skills and educational level on FDI inflows and found that both have a significant impact. Noorbakhsh et al. (2001) go a step further seeing human capital as one of the most important determinants of FDI inflows. We assume, in this paper, that significant civil liberties suppression has a negative effect on worker productivity as in such an environment workers do not take the initiative, do not cooperate effectively, and have less incentive to be productive. These weaknesses mean lower returns to foreign investment. An increase in civil liberties, including economic rights, may stimulate the working of the market, and so lead to better productivity and growth (Friedman, 1962). As the level of civil liberties rise, the productivity of the workforce increases, but it must be acknowledged that at the same time there may be adverse consequences. Labour unions and special interest groups are likely to form and as they gain power their ability to extract rents from MNEs will increase. As a number of empirical studies have shown, the effect of a change in civil liberties on FDI is similar to the non-linear relationship between civil liberties and growth (see Przeworski & Limongi, 1993 and Barro, 1997). We argue that the effects are contingent on the investment motive of the MNE, but will be moderated by the quality of the labour force in the host country. For instance, Kuncera and Principi (2017) evaluate the impact on FDI of political rights and a country's governance and find that for market-seeking industries with highly-skilled labour force requirements the effect of rights on FDI is positive. Thus, a highly-skilled labour force will positively moderate the effect of civil liberties suppression on FDI inflows in the case of market-seeking and strategic asset-seeking investments. On the other hand, an unskilled or semi-skilled labour force will enable efficiency-seeking and resource-seeking MNEs to maximize their bargaining power, and this will reduce the positive impact of civil liberties suppression on FDI. On this basis, we formulate our third hypotheses:

**Hypothesis 3a:** A high level of human capital in the host country will positively moderate the relationship between civil liberties suppression and FDI inflows for market-seeking and strategic asset-seeking FDI.

**Hypothesis 3b:** A high level of human capital will negatively moderate the relationship between civil liberties suppression and FDI inflows for resource-seeking and efficiency-seeking FDI.

## METHODOLOGY AND SAMPLE DESCRIPTION

We adopt a quantitative approach to test our hypotheses. The database we use, FDI Markets, is unique in that it covers foreign direct investments across a wide array of developing and emerging countries. Despite its shortcomings, it is gaining traction among researchers. As far as we know, none of the published papers that have used this database have collected such an extensive sample. We collected data on greenfield investments globally from 2003 onwards. The database provides information on the number of jobs created by each investment. One limitation is that when information is not available from the firm, an algorithm is used to calculate an estimated value for the investment and jobs created.<sup>2</sup> To overcome this shortcoming, we have selected jobs created as a dependent variable as there are much fewer estimated values for jobs created than for investment value.<sup>3</sup> Apart from the obvious desirability of better data, we opt to measure jobs created for two reasons. First, jobs created are more sensitive than investment value to political rights and civil liberties (Mosley & Uno, 2007). Most of the arguments we have developed relate to the ability of an MNE to extract rents from the labour force, thus we would expect a stronger impact on jobs created than on capital invested. Second, a number of studies prior to this one have convincingly used jobs created to investigate the effect on FDI of political rights and civil liberties.<sup>4</sup> As sensitivity analysis, we have performed our regressions based on projects with actual values and the results are robust.<sup>5</sup>

To test our first set of hypotheses, we selected thirteen MNE home countries from which investments were made in developed, developing and emerging markets having different regime types (see Table 1). There are 110 host countries across four continents.<sup>6</sup>

### **Insert Table 1 here**

The projects included in our analysis were undertaken between January 2003 and December 2013 during which time more than 12 million jobs were created in the host countries. By far the investor country with the highest number of projects is the US, nearly a third of the total, followed by Germany, Japan, UK and France. The average number of jobs created per project is 228, and the average capital invested per project 69.4 million USD. South Korea and China undertook fewer projects than the top five countries listed above, but outstripped them all by a considerable amount in terms of the average number of jobs created per project. China tops the list in capital invested per project.

### **Independent Variables**

Our main independent variables capturing political governance and civil liberties suppression come from two separate databases: the first from Polity IV<sup>7</sup> and the second from Freedom House. The variable used in our analysis, political governance (as measured by Polity IV), is a composite variable that takes a value from -10 (full autocracy) to +10 (democracy). Polity IV does not measure the level of civil liberties. We therefore measure civil liberties suppression separately, using data from the 2017 annual Freedom in the World report of Freedom House. Freedom House is a US-based not for profit NGO which since 1972 has rated all countries according to their democratic institutions. Two indices are reported, one measuring political rights and the other civil liberties. Each index has a scale of 1 to 7, 1 for full political rights and civil liberties and 7 for their total absence.<sup>8</sup> To complement the two we also



measure institutional quality through a composite measure based on data from the International Country Risk Guide. The political risk components we included were government stability, socioeconomic conditions, investment profile, the frequency of internal and external conflict, corruption, the role of the military and religion in politics, law and order, ethnic tensions, democratic accountability and bureaucratic quality. Low values indicate lower institutional quality and thus higher risk to potential investors. A possible limitation of this approach is that we do not capture the effect of individual institutional factors on FDI. We combined these different measures because there is a high level of correlation between them and because we want to keep the focus on the effect of political regime status and civil liberties.

We averaged (over the 2003-2013 period) the political rights, civil liberties and institutional quality scores of the host countries in which MNEs invested. Those averages are shown by MNE home country in Table 2. The data reported in the political governance column shows that MNEs based in the UAE, India, Japan and South Korea tend to invest in countries with autocratic regimes. In the case of the UAE this is perhaps not surprising as it is itself an autocratic regime, but it is unexpected in the case of MNEs based in the other three countries. Levitsky and Way (2010) call them, ‘dark knights’. MNEs based in Germany (4.17) and Spain (4.55) invest in more democratic regimes. After those two countries, it is China (3.51) that invests most in countries with high political governance scores. This may be explained by strategic asset-seeking investments in democratic countries.

### **Insert Table 2 here**

To measure the level of human capital in host economies we have used gross enrolment in secondary and tertiary education.<sup>9</sup> The share of youth in secondary education captures the availability of a semi-skilled labour force, whilst that for tertiary education captures a highly-skilled one. We could have used a human development index or the proportion of those in the labour force who already have

secondary and tertiary educations. We did not select those indicators as they overlap with two of our other variables: labour cost, and the proportion of the labour force having different levels of education. We present some basic statistics for these key variables in Table 3.

**Insert Table 3 here**

Between 2003 and 2013, we see some progress in civil liberties, and even more in political governance, but in contrast to that positive picture, there was deterioration in the level of institutional quality. It is significant however that there was improvement in the skills of the population in host countries as reflected in gross enrolment in secondary education increasing roughly from 74% to 93%, and in tertiary education from 32% to 42%. These figures show that the most improvement took place in the semi-skilled segment of the workforce. During the same period, the average size of projects declined both in terms of jobs created and capital invested even though there was a significant increase in the number of projects.

### **Control Variables**

As control variables, we include country economic size (GDP), labour cost of production (GDP per person employed), FDI inflows, and trade openness (Trade). We also include ores and metals exports as well as fuel exports in order to capture a country's endowment of natural resources and therefore its attractiveness to resource-seeking FDI. We summarise in Table 4 key variables and data sources.

**Insert Table 4 here**

The summary statistics of our dependent and independent variables can be seen in Table 5 whilst we provide a correlation table in Appendix 2.

**Insert Table 5 here**

Despite the high number of observations for our dependent variables, data limitations, in particular for host country human capital, resulted in a significantly smaller usable sample.

### **Classification of Activities by Investment Motivation**

An important contribution of this study is that we are able to clearly distinguish between the motivations for FDI. FDI Markets provides information on industries, business activities and, for a number of investments, their key motives. We did not proxy these motives by the industry classification of the investment, since investment motives may differ within a single industry. For example, a number of oil and natural gas extraction investments are classified by the database as retail, i.e. their primary goal was servicing the local market. It would have been incorrect to have classified their motivation as resource seeking. We have used the additional information provided by FDI Markets about specific motives indicated by certain business activities, and cross-examined this with industry information to form a basis for linking investment information on business activities with MNEs' motivations<sup>10</sup>. We present those classifications in Table 6.<sup>11</sup>

**Insert Table 6 here**

### **Estimation Method**

Our sample consists of individual investments across multiple countries over a number of years. As such, it is not a panel dataset and therefore applying panel data estimation methods would be inappropriate. We decided to use a pooled OLS estimation with year and industry effects. The R-square and the Variance Inflation Factor (VIF) as well as the correlation table do not indicate any multicollinearity problems for our estimations. We also report the F-statistic associated with the time and industry effects. Finally, we have used White-corrected standard errors to control for heteroscedasticity. We log-transformed the number of jobs created (our dependent variable) and host

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country GDP. We did not standardise our interaction effects in order to allow for better interpretation of the marginal effects.<sup>12</sup> To look for interaction effects we follow the approach proposed by Kingsley et al. (2017). Most studies report only the size and significance of the interaction coefficient. This could lead, according to the authors, to an overstating or understating of the interaction effect. It is therefore important to investigate the marginal effect and its value across the range of the moderating variable. Examining the marginal effect, especially through a graphical representation, can show whether there are values of the moderating variable which have a statistically significant effect, in spite of the overall coefficient being insignificant, or inversely, whether there are values for the moderating variable where the effect is insignificant despite the fact that the interaction coefficient is statistically significant. We calculate the marginal effects of civil liberties when entering our two moderating variables, gross enrolment in secondary and in tertiary education. We compare the two levels of human capital for each of the FDI motivations. This enables us to have a very specific picture of the moderating effect and therefore avoid understating or overstating the interaction results.

## **RESULTS AND DISCUSSION**

### **FDI and Political Governance**

We use our first set of regressions to investigate the impact of democratic capital on FDI, and present in Table 7 the determinants of FDI from democratic and autocratic home countries. We also present robustness checks excluding Russia<sup>13</sup> from the sample of democratic countries (as an investor), including it instead as an autocratic host country (Models 5 and 6). We do something similar in the case of China, excluding it from the sample as an investment destination (host country) (Model 3). We also look at Chinese investments separately (Model 7). All model specifications in Table 7 show VIF values to be within an acceptable range, and include time and industry effects, when they are statistically significant. Our first models (1-3) in Table 7 present the individual effects of political governance, civil liberties suppression, institutional quality, and human capital on jobs created by each FDI project. In

Model 1, all investing countries (including Russia and China) are classified as democratic (using Polity IV data).

**Insert Table 7 here**

When running on all democratic countries, the size of the host economy (GDP) has, as expected, a positive and statistically significant impact on jobs created, whilst the cost of labour (GDP per person employed) has a negative and statistically significant one. This indicates the existence of a competition effect which acts as a deterrent to FDI. Both measures of human capital, gross enrolment in secondary and in tertiary education, have negative and significant coefficients, indicating that the cost of labour and the existence of semi-skilled or highly-skilled workers negatively influences the number of jobs created per project. Our results also indicate that the institutional quality of the host country has a positive and statistically significant impacts on inward FDI. Political governance has a strong positive effect in all specifications, indicating that FDI from democratic countries is positively and statistically significantly influenced by the existence of a democratic regime in the host country<sup>14</sup>. This result is in line with the extant literature and confirms H1a. It provides evidence of the existence of democratic capital. Similarly, civil liberties suppression has a negative and statistically significant impact, indicating that countries where they are suppressed attract less FDI, as measured by jobs created per project. These results allow us to make an important contribution to the debate on the impact of democracy on FDI be it through rules of the game or play of the game.

Results for autocratic countries (as investors) are presented in models 4-7. Market size, measured by GDP, and labour cost, measured by GDP per person employed, appear to be the most significant factors, with the exception of Chinese investments (Model 7) where GDP loses significance. These findings indicate strong market-seeking and efficiency-seeking motives by Chinese, Emirati, and Russian MNEs. The effect of political governance remains positive and statistically significant, with

the exception of the model for China (Model 7). We do not find overall support for our hypothesis H1b, according to which autocratic regimes tend to invest more in other autocratic regimes. On the other hand, institutional quality and civil liberties suppression lose significance. It appears that autocratic country MNEs tend to invest where the rules of the game are weak but the play of the game, through transparency in political governance, strong. This too is in line with the extant literature. In conclusion, we find support for H1a but not H1b, political governance appears to impact FDI, but the effect of democracy on FDI is stronger than that of autocracy.

### **FDI and Civil Liberties – The Role of FDI Motives**

Our finding of a strong negative effect of civil liberties suppression on FDI from democratic countries led us to explore the relationship further. We have argued that there is a positive relationship between civil liberties suppression and resource-seeking and efficiency-seeking investments (H2a and H2b), but that the relationship is negative in the case of market-seeking and strategic asset-seeking ones (H2c and H2d). To be able to compare results with those of the previous runs, we run separately for democratic and autocratic investing countries. We present our results for democratic countries in Table 8 (Models 8 -15) and for autocratic countries in Table 9 (Models 16-23). We see China as a special case so present those results in Appendix 4 (Models 24-27).

### **Insert Tables 8 and 9 here**

We found some support for the notion that in the case of democratic countries a large market size (GDP) attracts FDI if the motivation is market seeking, strategic asset seeking or efficiency seeking. High cost of labour (GDP per person employed) deters FDI if motivated by anything other than strategic asset seeking, the sole motivation for which there is a statistically significant positive effect. This is possibly due to a desire to access high skills. Institutional quality does not have a significant effect except when motivated by strategic asset seeking (models 8-10). We also observe a differential effect in the case of political governance, positive and significant only for resource-seeking and market-seeking FDI. Civil liberties suppression remains negative and statistically significant for resource-

seeking and strategic asset-seeking FDI. Thus we find in the case of democratic countries strong support for H2a and H2d but no support for H2b or H2c. It appears then that the effect of civil liberties is contingent on FDI motives--but not for all of them. The results differ in the case of autocratic countries (Models 16-19). Unsurprisingly, resource-seeking MNEs tend to be attracted by the availability of ores and metals. They are also attracted by autocratic regimes. This is in line with Oneal (1994) who holds that when an autocratic government can guarantee access to resources, both the investing MNE and the regime can benefit. Efficiency-seeking MNEs are attracted by large markets with low labour costs and a high level of natural resources, while market-seeking MNEs are attracted to large markets with low labour costs. Strategic asset-seeking MNEs do not demonstrate any particular preferences. The estimated effects of civil liberties suppression are all in line with our hypotheses, i.e. positive for resource-seeking and efficiency-seeking MNEs and negative for market-seeking and strategic asset-seeking MNEs, but fail to reach acceptable levels of significance. We cannot, therefore, find support for our H2a to H2d hypotheses for MNEs in autocratic home countries.

### **The Moderating Role of Human Capital**

In the final step of our empirical analysis we look at the moderating effect of human capital (gross enrolment in secondary and in tertiary education) on the impact of civil liberties suppression on FDI. Our results are presented in Tables 8 (models 12-15) and 9 (models 20-23)<sup>15</sup>. Following Kingsley et al. (2017), we graphically present the marginal effects of the interactions. We do not focus on the interaction coefficients, as the marginal effects offer a better interpretation. Figures 1 through 8 show the effect of secondary and of tertiary education on FDI contingent on the level of civil liberties suppression (low on the left of the figure and high on the right). A statistically significant effect is represented in each figure by a solid line. We present four democratic home country-autocratic home country pairs, each illustrating a different FDI motivation, thus Figures 1, 3, 5 and 7 show democratic country estimations and Figures 2, 4, 6 and 8 autocratic country ones. We have hypothesised that when FDI is resource seeking or efficiency seeking, high levels of human capital will decrease the positive

effect of civil liberties suppression on FDI, whilst when FDI is market seeking or strategic asset seeking high levels of human capital will boost the negative effect of civil liberties suppression on FDI. Figures 1 and 2 illustrate the marginal effect of secondary and of tertiary education and civil liberties suppression on FDI when it is strategic asset seeking. There is strong support for H3a for strategic asset-seeking FDI from democratic countries. The negative effect of high civil liberties suppression is especially clear in the case of tertiary education. The strong effect reflects the need for a highly-killed, productive and innovative labour force for strategic asset-seeking investments from democratic countries. The effect for autocratic countries is not statistically significant.

**Insert Figures 1 and 2 here**

Figures 3 and 4 illustrate the effect in the case of market-seeking FDI. There is a strong negative effect for both secondary and for tertiary education especially when there is a high level of civil liberties suppression, suggesting that not only are there productivity implications but also significant reputational effects for MNEs. This supports further H3a when FDI originates in democratic countries. This effect also exists for tertiary education in the case of market-seeking FDI from autocratic countries, but does not for secondary education.

**Insert Figures 3 and 4 here**

Figures 5 and 6 show the effect in the case of resource-seeking FDI. There are mixed results when the investment originates in democratic countries. Whilst the relationship for tertiary education remains overall negative, there is a diminishing effect the higher the level of civil liberties suppression, thus supporting H3b for democratic countries. There is no statistically significant effect for tertiary education in the case of FDI from autocratic countries.

**Insert Figures 5 and 6 here**



Finally, Figures 7 and 8 represent the relationship in the case of efficiency-seeking FDI. There is no statistically significant effect for FDI from democratic countries, but there is a strong positive effect for tertiary education as the level of civil liberties suppression increases when the investment comes from autocratic countries. There is no support for H3b, but this is not surprising as the effect suggests that MNEs from autocratic countries would prefer having the civil liberties of a highly-skilled labour force suppressed when they invest in other developing and emerging markets as it would give them the opportunity to extract additional rents from efficiency-seeking investment. Nonetheless, the fact remains that there is no support for H3b for investment originating in autocratic countries.

**Insert Figures 7 and 8 here**

## **CONCLUSIONS AND MANAGERIAL IMPLICATIONS**

An important contribution of our study lies in bringing closer the international business and the business and human rights literatures. We develop a holistic view of the impact of host country political governance and civil liberties on FDI inflows. We do so in response to the Wettstein et al. (2019) call. They suggest a research agenda that would enable IB scholars to address in a new way the impact of corporate social responsibility (CSR) practices on economic development and sustainability, a relationship with significant implications for the behaviour of MNEs. For instance, Tashman et al. (2018) find that institutional voids in the home countries of emerging market MNEs allow them to decouple CSR claims from their actual implementation.

We have been able to provide useful insights on the way institutions interact with MNEs in a number of contexts. Our approach also responds to Aguilera and Grøgaard (2018) who argue that in IB research there is a clear need to disentangle the role of institutions in order to understand their impact on firms. Different studies use the term ‘institutions’ in different ways resulting in too many constructs and ideas being captured. An approach, therefore, that takes into consideration the multi-faceted nature of institutions would advance the IB literature. Jackson and Deeg (2019) suggest that institutions have not only direct influence on firm behaviour but a moderating one as well on a number of relationships.

We argue that MNEs interacting with local governments and social actors such as trade unions, are influenced not only by the rules but also the play of the game (Williamson, 1998). This could have implications for investment decisions, but most of the extant literature focuses on just the rules. We argue that similarity in political governance helps MNEs negotiate with host governments. Thus we hypothesise a different effect when FDI originates from democratic countries than when it originates from autocratic ones. In the same vein, we theorise that there will be differences in the way civil liberties will impact FDI. Those differences arise from various investment motives. Finally, the relationship between human rights and FDI is moderated by the level of human capital, specifically the level of workforce skills. We focus on emerging and developing economies so as to provide evidence on the differential behaviour of MNEs originating from these countries. The results of our empirical analysis provide overall support for our theoretical argumentation. They are also in line with the findings of Asiedu and Lien (2011), Adam and Filippaios (2007), and Li and Resnick (2003).

We find in addition that autocratic regimes discourage FDI, which supports our first hypothesis and is in line with the findings of Jensen (2003), Addison and Heshmati (2003), Sethi et al. (2003), and Adam and Filippaios (2007). We conclude that it is important for MNEs based in democratic countries to invest in developing and emerging markets that are committed to the protection of political rights, as investing in those that do not can have a detrimental effect on their reputation.

Our study has also clear policy implications for host countries. Although we do not directly address the issue of economic development and sustainability, we are able to offer useful insights into the ways host countries can maximise the benefits of inward FDI. Narula and Dunning (2010) argue that the quantity and quality of FDI and its motivation matter for the economic development of a host country. Host country governments need to take a proactive approach to attract the type of FDI that will maximize benefits. We evaluate the role of human capital, which requires continuous investment in education. What we find is in line with Narula's (2018) argument that only host countries that maintain investment in their location advantages are able to secure benefits from MNEs. We provide insights on the ways host country governments can maximise benefits and minimize costs of FDI.

Narula and Pineli (2018) show that MNE operations can have both positive and adverse effects on the economic development of host countries. They argue that a full understanding of the impact of MNE activities on economic development requires taking a global value chain perspective. Similarly, Awad and Ragab (2017) investigate the nexus between democracy and FDI in Africa in a dynamic way. They find that FDI has a positive effect on economic growth that is reduced by past experience with democracy, not the current level of democracy. They conclude that as the impact of FDI on growth decreases as a country becomes more democratic, more sustainable activities must be found.

Our study has a number of limitations. Although we have controlled for industry-effects, further work on the differential effect of political rights and civil liberties suppression on specific industries is warranted. Our study, although it captures investment motives, does not address this dimension as we aim to provide a more general perspective. We also do not provide a detailed examination of host countries. It would be interesting to look at FDI in African countries and to explore further the impact of political governance and civil liberties within them, especially in the case of those that are resource-rich. We do not offer a detailed examination of all the institutional factors that influence FDI decisions, focusing instead on political governance and civil liberties.

Future research on the effect of civil liberties on FDI might use more detailed measures. Wong (2016) provides evidence that democracies fail to reduce inequality, but argues that those with well-established economic institutions and property protection laws in place are attractive to foreign investors. FDI tends to create a pool of well-paid workers, although they usually are a small proportion of the general population. Thus, while we would expect a reduction in inequality in developing and emerging countries experiencing high FDI inflows, actually FDI is likely to increase income inequality.

Finally, we have controlled for the effects of time and industry, but a closer examination of the manner in which firms from various countries invest abroad would, we believe, shed further light on a home country effect.

## NOTES

<sup>1</sup> Further information on the algorithm used can be obtained from the authors upon request.

<sup>2</sup> We run our regression on a sample excluding imputed values and the results were unchanged. They are available from the authors.

<sup>3</sup> Paniagua and Sapena (2014) use jobs created to investigate the influence of democratic rights on FDI. Wren and Jones (2010) investigate the impact of regional grants on jobs created. They see jobs created as having a stronger influence on policy than investment value.

<sup>4</sup> These results are available from the authors upon request.

<sup>5</sup> The list of recipient countries can be found in Appendix 1.

<sup>6</sup> Given the complementarity between Polity (2007) and Henisz (2000a, b) Political Constraint Index we have also used the latter as an alternative measure of polity. The two variables have a significant correlation close to 0.74 and results remain almost identical. These alternative estimations can be obtained from the authors upon request.

<sup>7</sup> Civil liberties index and Polity have high correlation coefficient. To avoid issues with multicollinearity we have orthogonalised the civil liberties index on Polity for the respective regressions. The estimations used to transform the variable can be found in Appendix 3.

<sup>8</sup> Secondary and Tertiary Education Gross Enrolments have high correlation coefficient. To avoid issues with multicollinearity and to only pick up the effect of highly-skilled labour force in our regressions we have orthogonalised the two variables. The estimations used to transform the variable can be found in Appendix 3.

<sup>9</sup> A significant number of activities are classified as manufacturing. We have classified the high-technology activities of manufacturing as strategic asset-seeking. An alternative classification was used with all manufacturing activities classified as efficiency seeking but this did not significantly change the results.

<sup>10</sup> A more detailed table containing the industry information can be obtained from the authors upon request.

<sup>11</sup> We also ran the models with standardized values as a robustness check. All variables were standardized with a mean of zero (0) and a standard deviation of one (1). These results can be obtained from the authors upon request.

<sup>12</sup> Russia has a mean of 4.77 (over the 2003-2013 period) for its Polity score and therefore is closer to a democracy than an autocracy.

<sup>13</sup> The results are identical when we use the Political Constraint Index of Henisz (2000a, b) and these are available from the authors upon request.

<sup>14</sup> The same set of results with China excluded as host market and with the interaction effects based on standardised variables have been estimated as robustness checks.

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Table 1. FDI projects included in the analysis

Home Country	Number of Projects	Total Jobs Created	Average Jobs per project	Total Capital Invested (Mil US\$)	Average Capital invested per project (Mil US\$)
<b>Canada</b>	1,565.00	403,573.00	257.87	203,314.05	129.91
<b>China</b>	1,057.00	411,229.00	389.05	148,865.26	140.84
<b>France</b>	4,393.00	980,429.00	223.18	300,924.13	68.50
<b>Germany</b>	7,273.00	1,567,548.00	215.53	393,281.01	54.07
<b>India</b>	1,674.00	321,881.00	192.28	125,453.74	74.94
<b>Italy</b>	2,091.00	460,448.00	220.20	145,737.95	69.70
<b>Japan</b>	6,345.00	1,710,261.00	269.54	421,610.11	66.45
<b>Russia</b>	964.00	195,570.00	202.87	97,364.21	101.00
<b>South Korea</b>	1,558.00	647,072.00	415.32	182,280.94	117.00
<b>Spain</b>	2,734.00	578,749.00	211.69	170,458.47	62.35
<b>UAE</b>	1,438.00	382,398.00	265.92	191,550.36	133.21
<b>UK</b>	5,975.00	1,1048,19.00	184.91	366,500.50	61.34
<b>United States</b>	16,694.00	3,527,618.00	211.31	983,760.59	58.93
<b>Grand Total</b>	<b>53,761.00</b>	<b>12,291,595.00</b>	<b>228.63</b>	<b>3,731,101.29</b>	<b>69.40</b>



Table 2. Average political governance, civil liberties and institutional quality of host locations (by investing country)

Home Country	Political governance (Average of host locations)	Civil Liberties Suppression (Average of host locations)	Institutional Quality (Average of host locations)
Canada	2.39	3.66	67.31
China	3.51	3.64	65.41
France	1.85	3.75	68.12
Germany	4.17	3.28	69.11
India	-0.69	4.28	68.59
Italy	3.03	3.55	68.22
Japan	0.71	4.28	66.83
Russia	2.16	3.62	66.77
South Korea	0.32	4.29	66.57
Spain	4.55	3.16	67.96
UAE	-3.21	4.60	64.43
UK	1.93	3.73	68.88
United States	2.37	3.79	68.31
<b>Grand Total</b>	<b>2.18</b>	<b>3.77</b>	<b>68.01</b>

Table 3. Average political governance, civil liberties, gross enrolment in education, jobs created, labour force and capital invested between 2003 and 2013

	2003	2013	Overall Average
Political governance	1.93	2.59	2.18
Civil Liberties Suppression	3.98	3.77	3.76
Institutional Quality	68.91	65.08	68.01
Secondary enrolment	74.45	93.60	80.84
Tertiary enrolment	31.50	41.95	36.48
Jobs created	266	183	228
Capital invested	85.59	55.79	69.40
Projects	4140	5900	

Table 4. Definitions and sources of variables

<b>Variable</b>	<b>Definition</b>	<b>Source</b>	<b>Transformation</b>
<b>Jobs created</b>	Jobs created by project	FDI Markets	Logarithmic
<b>GDP</b>	GDP, PPP (constant 2011 international \$)	World Development Indicators	Logarithmic
<b>GDP per person employed</b>	GDP per person employed (constant 1990 PPP \$)	World Development Indicators	None
<b>FDI Inflows</b>	Foreign direct investment, net inflows (% of GDP)	World Development Indicators	None
<b>Trade</b>	Trade (% of GDP)	World Development Indicators	None
<b>Ores and metals exports</b>	Ores and metals exports (% of merchandise exports)	World Development Indicators	None
<b>Fuel exports</b>	Fuel exports (% of merchandise exports)	World Development Indicators	None
<b>Gross enrolment ratio, secondary</b>	Gross enrolment ratio, secondary, both sexes (%)	World Development Indicators	None
<b>Gross enrolment ratio, tertiary</b>	Gross enrolment ratio, tertiary, both sexes (%)	World Development Indicators	Orthogonal on Gross enrolment ratio, secondary
<b>Institutional quality</b>	Composite measure of institutional quality that includes: Government Stability, Socioeconomic Conditions, Investment profile, Internal and External Conflict, Corruption, Military and Religion in Politics, law and Order, Ethnic Tensions, Democratic Accountability and Bureaucratic Quality Takes values 0-100 with lower values indicating lower institutional quality	International Country Risk Guide	None
<b>Political Governance</b>	Composite index capturing the position of a country along the spectrum of autocratic and democratic regimes. Takes values -10 (strongly autocratic) to 10 (strongly democratic).	Polity IV Project	None
<b>Civil liberties suppression</b>	Composite index capturing: Freedom of Expression and Belief, Associational and Organizational Rights, Rule of Law, and Personal Autonomy and Individual Rights. Takes values 1-7 with higher values indicating suppressed civil liberties	Freedom House	Orthogonal on Political governance

Table 5. Summary statistics

Variable	Obs	Mean	Std. Dev.	Min	Max
<b>Jobs created</b>	53761	228.63	463.65	0.00	19000.00
<b>Capital invested</b>	53761	69.40	275.76	0.00	20000.00
<b>GDP</b>	52879	3020.00	3930.00	1.72	16000.00
<b>GDP per person employed</b>	52552	16970.95	10595.55	663.00	51860.00
<b>FDI Inflows</b>	53605	4.47	5.93	-16.09	173.45
<b>Trade</b>	53408	89.16	72.36	0.31	439.66
<b>Ores and metals exports</b>	51195	5.43	8.70	0.00	85.97
<b>Fuel exports</b>	51221	17.23	23.55	0.00	99.79
<b>Gross enrolment ratio, secondary</b>	39529	80.84	16.13	7.57	124.61
<b>Gross enrolment ratio, tertiary</b>	42142	36.48	22.62	0.72	117.89
<b>Institutional quality</b>	53761	68.01	7.90	24.04	90.92
<b>Political Governance</b>	53630	2.18	8.74	-10	10
<b>Civil liberties suppression</b>	53709	3.77	1.69	1.00	7.00

Table 6. Classification of activities by investment motivation

Motivation	Business Activity
Market Seeking	<ul style="list-style-type: none"> <li>• Business Services</li> <li>• Construction</li> <li>• Customer Contact Centre</li> <li>• Maintenance &amp; Servicing</li> <li>• Retail</li> <li>• Sales, Marketing &amp; Support</li> </ul>
Resource Seeking	<ul style="list-style-type: none"> <li>• Electricity</li> <li>• Extraction</li> </ul>
Efficiency Seeking	<ul style="list-style-type: none"> <li>• Construction</li> <li>• Logistics, Distribution &amp; Transportation</li> <li>• Recycling</li> <li>• Manufacturing</li> </ul>
Strategic Assets Seeking	<ul style="list-style-type: none"> <li>• Design, Development &amp; Testing</li> <li>• Education &amp; Training</li> <li>• Headquarters</li> <li>• ICT &amp; Internet Infrastructure</li> <li>• Research &amp; Development</li> <li>• Technical Support Centre</li> <li>• Shared Services Centre</li> <li>• Manufacturing</li> </ul>

Table 7. Regression analysis of the effect of polity and civil liberties suppression on FDI from democratic and autocratic home countries (Dependent variable logarithm of jobs created)

	Democratic Countries			Autocratic Countries			
	All Countries	Excluding Russia	Excluding China (Destination)	China & UAE	China, Russia & UAE	Russia & UAE	China
	(1)	(2)	(3)	(4)	(5)	(6)	(7)
GDP	0.09883*** (0.00897)	0.10042*** (0.00919)	0.10275*** (0.00962)	0.09556*** (0.03454)	0.08991*** (0.02588)	0.11247*** (0.02880)	0.06055 (0.05949)
GDP per person employed	-0.00271* (0.00140)	-0.00290** (0.00144)	-0.00363** (0.00147)	-0.02456*** (0.00712)	-0.01288*** (0.00465)	-0.00481 (0.00511)	-0.03107** (0.01277)
FDI inflows	-0.00290** (0.00147)	-0.00302** (0.00149)	-0.00278* (0.00151)	0.01104 (0.00984)	0.00269 (0.00713)	0.00013 (0.00998)	0.00549 (0.01034)
Trade	-0.00076** (0.00032)	-0.00076** (0.00032)	-0.00072** (0.00032)	0.00202 (0.00199)	0.00130 (0.00152)	0.00350** (0.00175)	-0.00018 (0.00258)
Ores and metals exports	-0.00217** (0.00108)	-0.00206* (0.00109)	-0.00264** (0.00107)	0.00145 (0.00577)	-0.00005 (0.00432)	0.00541 (0.00595)	-0.00555 (0.00711)
Fuel exports	-0.00184 (0.00440)	-0.00204 (0.00405)	-0.00235 (0.00650)	0.00033 (0.00183)	0.00302** (0.00148)	0.00336* (0.00176)	-0.00167 (0.00363)
Gross enrolment ratio, secondary	-0.00706*** (0.00077)	-0.00705*** (0.00078)	-0.00667*** (0.00085)	0.00314 (0.00365)	-0.00388 (0.00256)	-0.00661** (0.00279)	0.00403 (0.00557)
Gross enrolment ratio, tertiary (ORTH)	-0.00313*** (0.00056)	-0.01574*** (0.00057)	-0.00256*** (0.00357)	-0.01817* (0.00270)	-0.02654*** (0.00769)	-0.02605*** (0.00283)	-0.02016 (0.00418)
Institutional quality	0.00605*** (0.00178)	0.00627*** (0.00181)	0.00772*** (0.00207)	-0.01217* (0.00695)	-0.00738 (0.00568)	-0.00618 (0.00696)	-0.00875 (0.01120)
Political governance	0.02220*** (0.00176)	0.02246*** (0.00180)	0.01845*** (0.00331)	0.01571* (0.00942)	0.02267*** (0.00710)	0.01830** (0.00821)	0.01797 (0.01655)
Civil liberties suppression (ORTH)	-0.01604*** (0.00280)	-0.00318*** (0.00286)	-0.01282*** (0.00058)	0.00488* (0.00999)	0.00237 (0.00210)	0.00258 (0.00880)	0.00466 (0.01911)
Constant	2.25606*** (0.27987)	2.17241*** (0.28683)	2.00389*** (0.31866)	1.96183 (1.20885)	3.19356*** (0.95021)	2.35732** (1.04369)	4.05383** (1.83191)
Observations	33676	33055	26008	1309	1930	1387	543
Adjusted R-squared	0.14234	0.14276	0.14212	0.26674	0.22972	0.23735	0.23471
VIF	3.45	3.48	3.41	3.86	4.34	3.98	3.71
Time effects	3.88***	3.82***	3.84***	0.55	0.55	0.58	0.56

Sector effects	118.62***	117.76***	87.62***	15.63	16.16***	16.88***	9.09***
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Robust standard errors in parentheses, \* significant at 10%; \*\* significant at 5%; \*\*\* significant at 1%

Table 8. Regression analysis of the effect of civil liberties suppression and moderating factors on FDI from democratic home countries by investment motive (Dependent variable logarithm of jobs created)

	Democratic Countries							
	Resource Seeking	Efficiency Seeking	Market Seeking	Strategic Asset Seeking	Resource Seeking	Efficiency Seeking	Market Seeking	Strategic Asset Seeking
	(8)	(9)	(10)	(11)	(12)	(13)	(14)	(15)
GDP	0.01166 (0.04725)	0.04002* (0.02109)	0.10180*** (0.00996)	0.06067*** (0.01749)	0.00586 (0.04968)	0.04311* (0.02224)	0.09096*** (0.01030)	0.05806*** (0.01783)
GDP per person employed	-0.01555* (0.00835)	-0.01077*** (0.00333)	-0.01013*** (0.00156)	0.00739*** (0.00264)	-0.01590* (0.00871)	-0.01057*** (0.00338)	-0.01172*** (0.00157)	0.00922*** (0.00270)
FDI inflows	-0.01270 (0.00942)	0.00071 (0.00321)	-0.00280 (0.00181)	-0.00203 (0.00245)	-0.01261 (0.00944)	0.00059 (0.00321)	-0.00324* (0.00181)	-0.00142 (0.00246)
Trade	-0.00376* (0.00202)	-0.00296*** (0.00065)	-0.00076** (0.00038)	-0.00131** (0.00056)	-0.00395* (0.00209)	-0.00287*** (0.00067)	-0.00091** (0.00038)	-0.00155*** (0.00056)
Ores and metals exports	-0.00161 (0.00350)	0.00063 (0.00270)	-0.00434*** (0.00125)	-0.00501*** (0.00187)	-0.00179 (0.00353)	0.00076 (0.00275)	-0.00356*** (0.00125)	-0.00585*** (0.00188)
Fuel exports	0.00727*** (0.00254)	0.00524*** (0.00121)	-0.00315*** (0.00046)	0.00103 (0.00087)	0.00680** (0.00268)	0.00567*** (0.00138)	-0.00225*** (0.00054)	-0.00060 (0.00108)
Gross enrolment ratio, secondary	-0.01099*** (0.00401)	-0.01041*** (0.00159)	-0.00133 (0.00089)	-0.00856*** (0.00141)	-0.01123*** (0.00431)	-0.01033*** (0.00164)	-0.00018 (0.00091)	-0.00950*** (0.00150)
Gross enrolment ratio, tertiary	-0.00305 (0.00343)	-0.00799 (0.00123)	-0.02150*** (0.00063)	0.00502 (0.00100)	-0.00339 (0.07094)	-0.00172 (0.03483)	0.00175** (0.00070)	-0.00322 (0.00109)
Institutional quality	0.00486 (0.00972)	0.00597 (0.00398)	0.00082 (0.00210)	0.01109*** (0.00316)	0.00545 (0.00986)	0.00583 (0.00399)	0.00100 (0.00212)	0.01143*** (0.00316)
Political governance	0.03850*** (0.01300)	-0.00175 (0.00427)	0.02889*** (0.00206)	0.00151 (0.00279)	0.03858*** (0.01467)	-0.00188 (0.00520)	0.02112*** (0.00244)	0.00463 (0.00348)
Civil liberties suppression (CL)	0.04169*** (0.01541)	-0.00195 (0.00886)	-0.00019 (0.00272)	-0.00620*** (0.00515)	0.01935 (0.00414)	-0.01538 (0.00135)	-0.05013*** (0.01566)	-0.00728*** (0.02557)
CL* Gross enrolment ratio, secondary					-0.00024 (0.00075)	0.00007 (0.00038)	-0.00082*** (0.00017)	0.00011 (0.00028)
CL* Gross enrolment ratio, tertiary (ORTH)					0.00047 (0.00083)	-0.00016 (0.00037)	-0.00067*** (0.00014)	-0.00081*** (0.00028)
Constant	5.63048*** (1.39145)	3.20267*** (0.61986)	1.65365*** (0.32894)	3.17943*** (0.53958)	4.78482*** (1.41510)	3.11877*** (0.64694)	1.90039*** (0.33294)	3.29175*** (0.53930)

Observations	1012	5498	16343	10823	1012	5498	16343	10823
Adjusted R-squared	0.14180	0.12440	0.39624	0.18658	0.14028	0.12414	0.39731	0.18727
VIF	3.20	1.37	4.09	2.53	4.72	5.08	4.13	4.64
Time effects	3.52***	3.67***	3.05	3.86***	3.53***	3.44***	2.72***	4.26***
Sector effects	33.07***	33.58***	328.19***	78.03***	32.92***	32.98***	329.75***	78.96***

Robust standard errors in parentheses

\* significant at 10%; \*\* significant at 5%; \*\*\* significant at 1%

Table 9. Regression analysis of the effect of civil liberties suppression and moderating factors on FDI from autocratic home countries by investment motive (Dependent variable logarithm of jobs created)

	Autocratic Countries							
	Resource Seeking	Efficiency Seeking	Market Seeking	Strategic Asset Seeking	Resource Seeking	Efficiency Seeking	Market Seeking	Strategic Asset Seeking
	(16)	(17)	(18)	(19)	(20)	(21)	(22)	(23)
GDP	0.02394 (0.23851)	0.17891** (0.07819)	0.11446** (0.04747)	0.08741 (0.07559)	0.04020 (0.04695)	0.16530* (0.08429)	0.11055** (0.04726)	0.08131 (0.08044)
GDP per person employed	0.02032 (0.05628)	-0.03540* (0.01801)	-0.02076** (0.00950)	0.01135 (0.01472)	0.01482* (0.00843)	-0.02705 (0.01803)	-0.02247** (0.01104)	0.01192 (0.01499)
FDI inflows	0.04793 (0.12771)	-0.00196 (0.01642)	0.03243 (0.02326)	-0.00459 (0.01161)	-0.01129 (0.00874)	0.00331 (0.01675)	0.03068 (0.02337)	-0.00499 (0.01179)
Trade	0.00536 (0.00949)	0.00088 (0.00447)	-0.00033 (0.00304)	-0.00049 (0.00372)	-0.00330* (0.00197)	0.00160 (0.00431)	0.00005 (0.00305)	-0.00020 (0.00380)
Ores and metals exports	0.13973** (0.06332)	0.03366*** (0.00951)	-0.00034 (0.00597)	-0.00449 (0.02084)	-0.00035 (0.00351)	0.02816*** (0.01045)	-0.00146 (0.00594)	-0.00580 (0.02120)
Fuel exports	-0.00867 (0.00794)	0.00412 (0.00413)	0.00287 (0.00247)	-0.00296 (0.00441)	0.00577** (0.00264)	0.00239 (0.00431)	0.00386 (0.00254)	-0.00225 (0.00463)
Gross enrolment ratio, secondary	0.00672 (0.01702)	0.00377 (0.00847)	-0.00532 (0.00505)	0.00148 (0.00699)	-0.00625 (0.00417)	-0.00277 (0.00930)	-0.00492 (0.00541)	-0.00225 (0.00668)
Gross enrolment ratio, tertiary (ORTH)	0.00574 (0.01748)	-0.01792 (0.00579)	0.00212 (0.01547)	-0.00035 (0.02277)	-0.00012 (0.00401)	-0.00239 (0.00671)	-0.10820* (0.06389)	-0.00373 (0.12670)
Institutional quality	-0.01940 (0.02873)	-0.00473 (0.01572)	0.01328 (0.01210)	-0.02067 (0.01558)	-0.00532 (0.00893)	-0.00633 (0.01555)	0.00755 (0.01246)	-0.01944 (0.01613)
Political governance	-0.10795* (0.05992)	0.01361 (0.01952)	0.01309 (0.01455)	0.00434 (0.02234)	-0.03708*** (0.01407)	0.02812 (0.01979)	0.01527 (0.01582)	0.01204 (0.02356)
Civil liberties suppression (CL)	0.10202 (0.09034)	0.00564 (0.02377)	-0.01686 (0.00368)	-0.00147 (0.00547)	-0.05571 (0.06878)	-0.11181 (0.11334)	0.00180 (0.00401)	-0.13837 (0.00525)
CL* Gross enrolment ratio, secondary					0.00005 (0.00079)	0.00128 (0.00129)	0.00099 (0.00073)	0.00175 (0.00141)
CL* Gross enrolment ratio, tertiary (ORTH)					-0.00028 (0.00079)	0.00256** (0.00128)	-0.00044 (0.00072)	0.00055 (0.00097)
Constant	-1.57028 (5.95451)	0.66142 (2.13796)	0.00735 (1.49988)	3.79783* (2.22665)	4.60786*** (1.37250)	0.10739 (2.31482)	0.51307 (1.49915)	4.21050* (2.42253)



Observations	1064	199	788	270	1064	199	788	270
Adjusted R-squared	0.29962	0.28676	0.39915	0.19002	0.12884	0.29695	0.40274	0.18772
VIF	2.63	4.76	4.00	4.79	4.90	3.68	3.20	3.06
Time effects	0.27	1.87*	2.86***	1.06	0.30	2.04**	2.16**	1.08
Sector effects	47.25***	12.47***	34.61***	15.45***	238.73***	14.77***	35.79***	15.61***

Robust standard errors in parentheses

\* significant at 10%; \*\* significant at 5%; \*\*\* significant at 1%

Figure 1. Marginal effects of secondary and tertiary education and civil liberties (CL) suppression on FDI for democratic countries and strategic asset-seeking investments (solid lines indicate a statistically-significant effect)

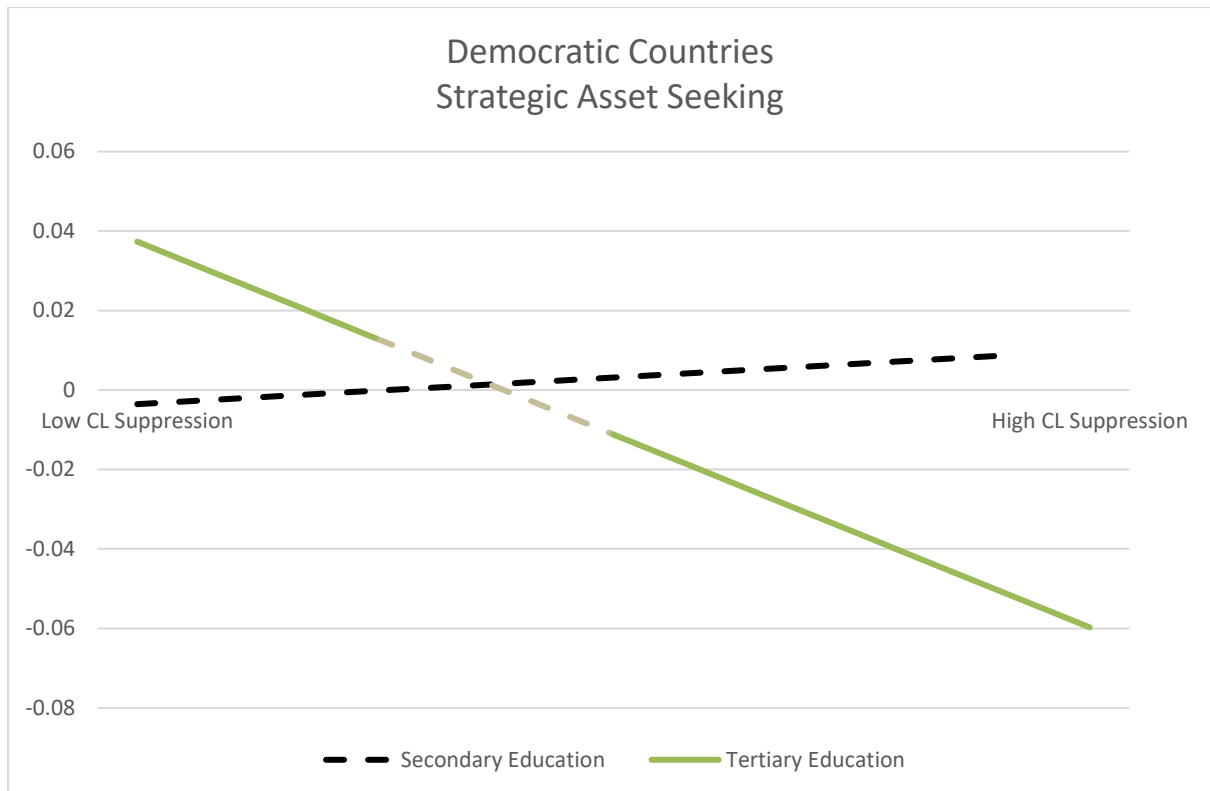


Figure 2. Marginal effects of secondary and tertiary education and civil liberties (CL) suppression on FDI for autocratic countries and strategic asset-seeking investments (solid lines indicate a statistically-significant effect)

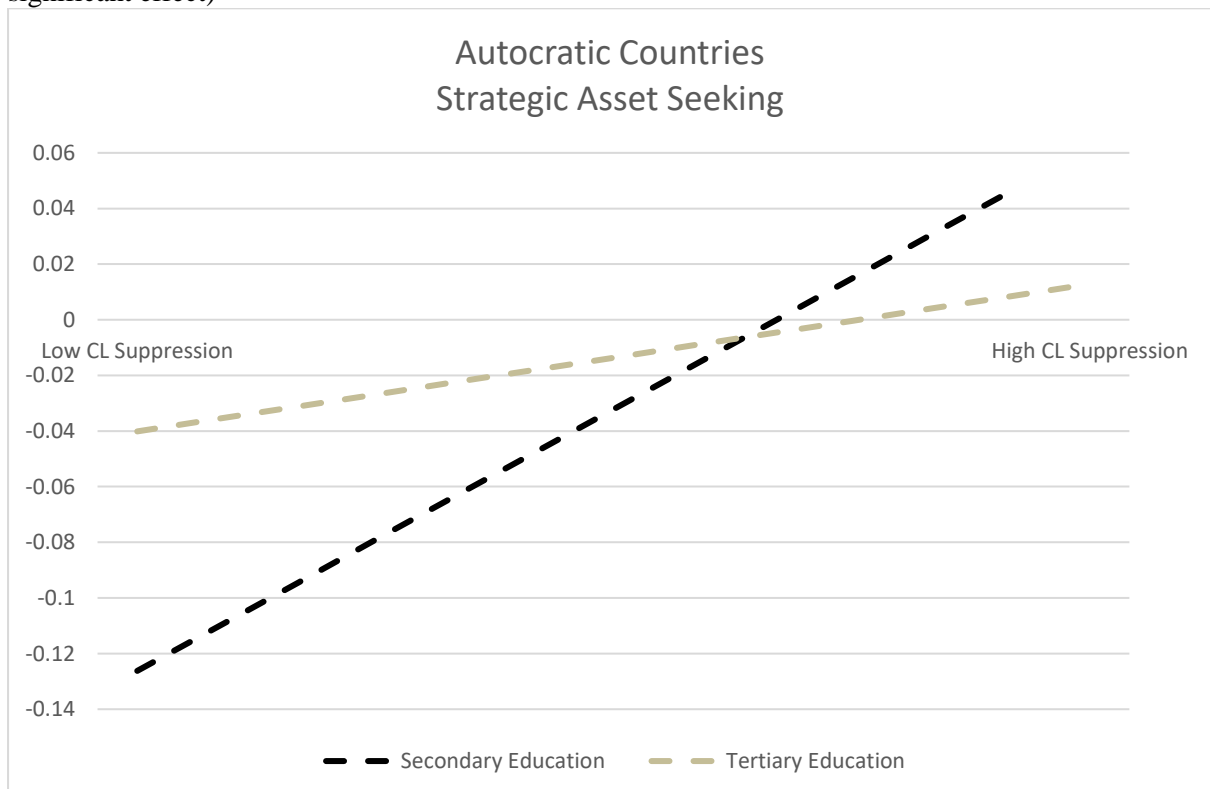


Figure 3. Marginal effects of secondary and tertiary education and civil liberties (CL) suppression on FDI for democratic countries and market-seeking investments (solid lines indicate a statistically-significant effect)

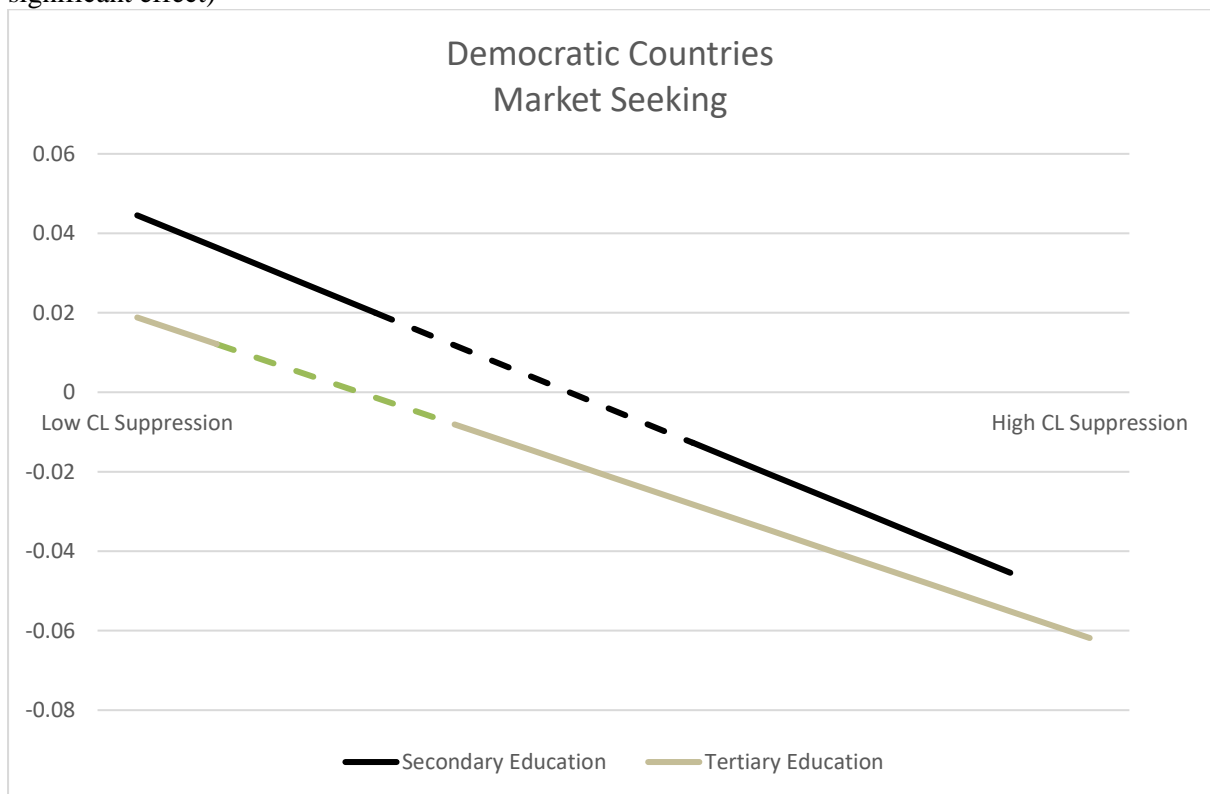


Figure 4. Marginal effects of secondary and tertiary education and civil liberties (CL) suppression on FDI for autocratic countries and market-seeking investments (solid lines indicate a statistically-significant effect)

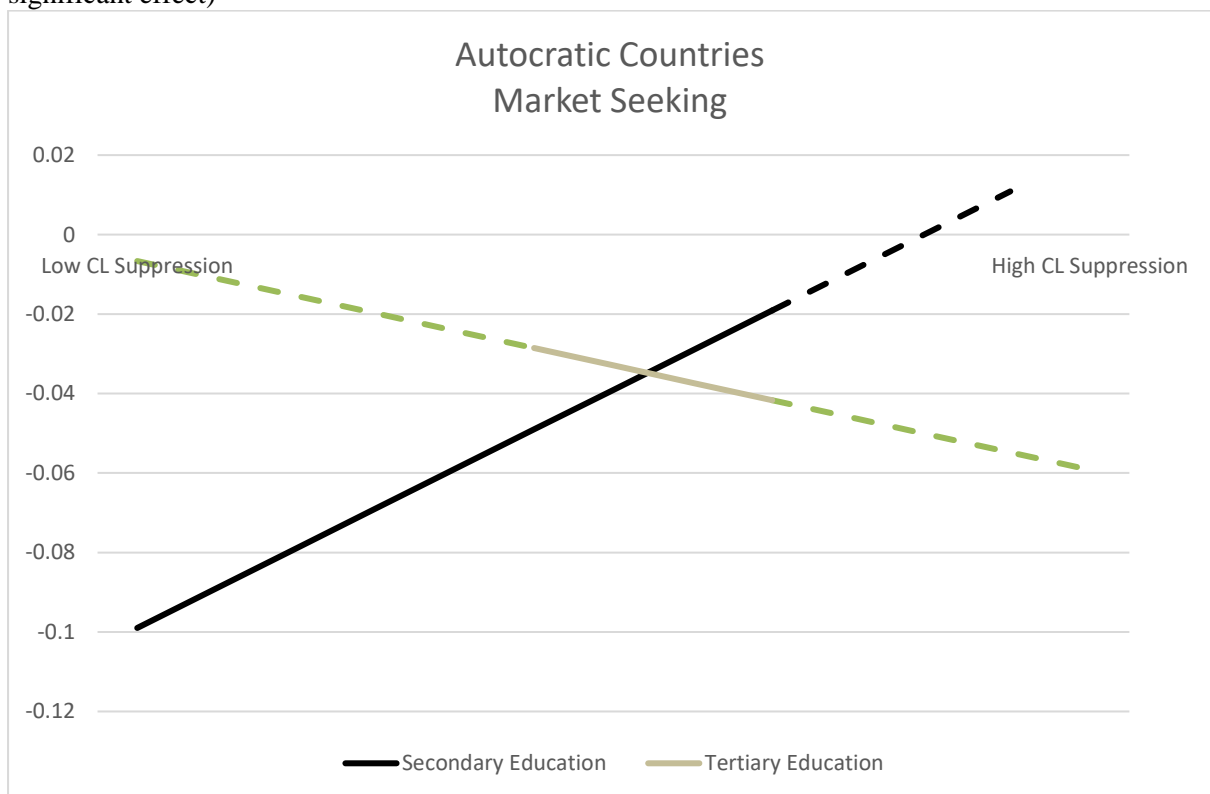


Figure 5. Marginal effects of secondary and tertiary education and civil liberties (CL) suppression on FDI for democratic countries and resource-seeking investments (solid lines indicate a statistically-significant effect)

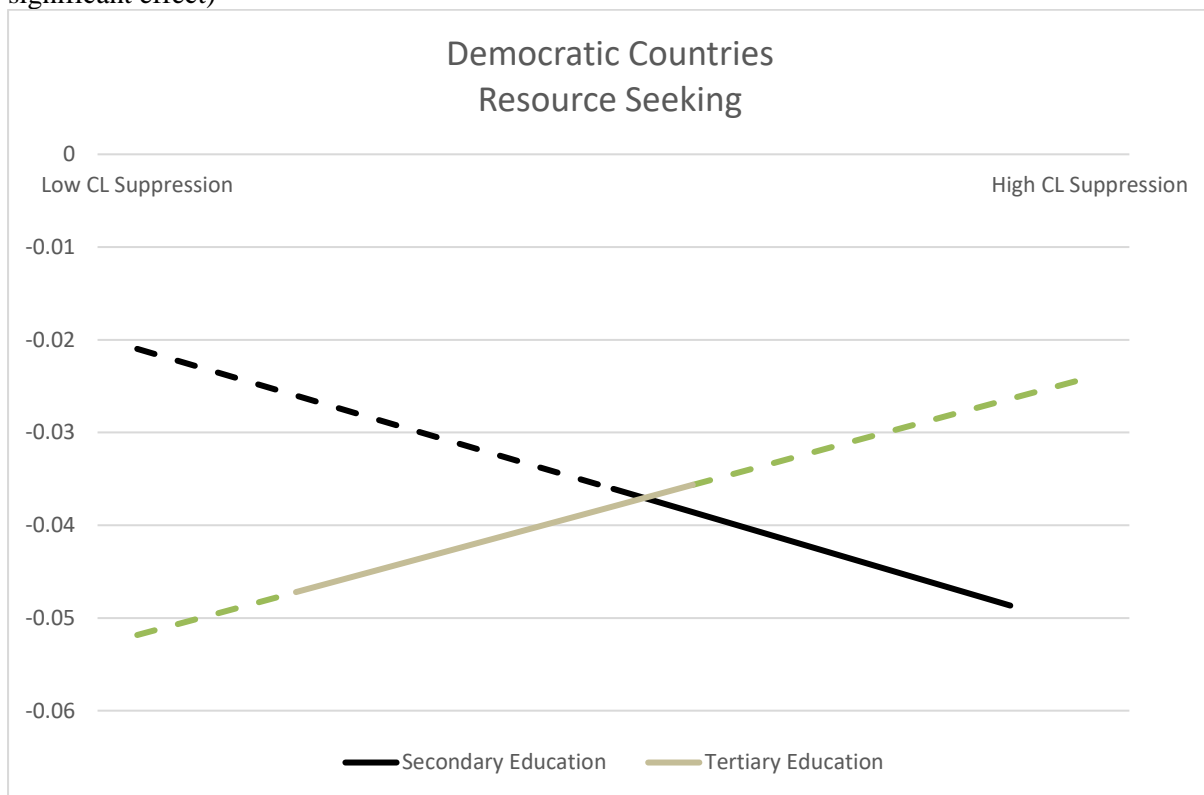


Figure 6. Marginal effects of secondary and tertiary education and civil liberties (CL) suppression on FDI for autocratic countries and resource-seeking investments (solid lines indicate a statistically-significant effect)

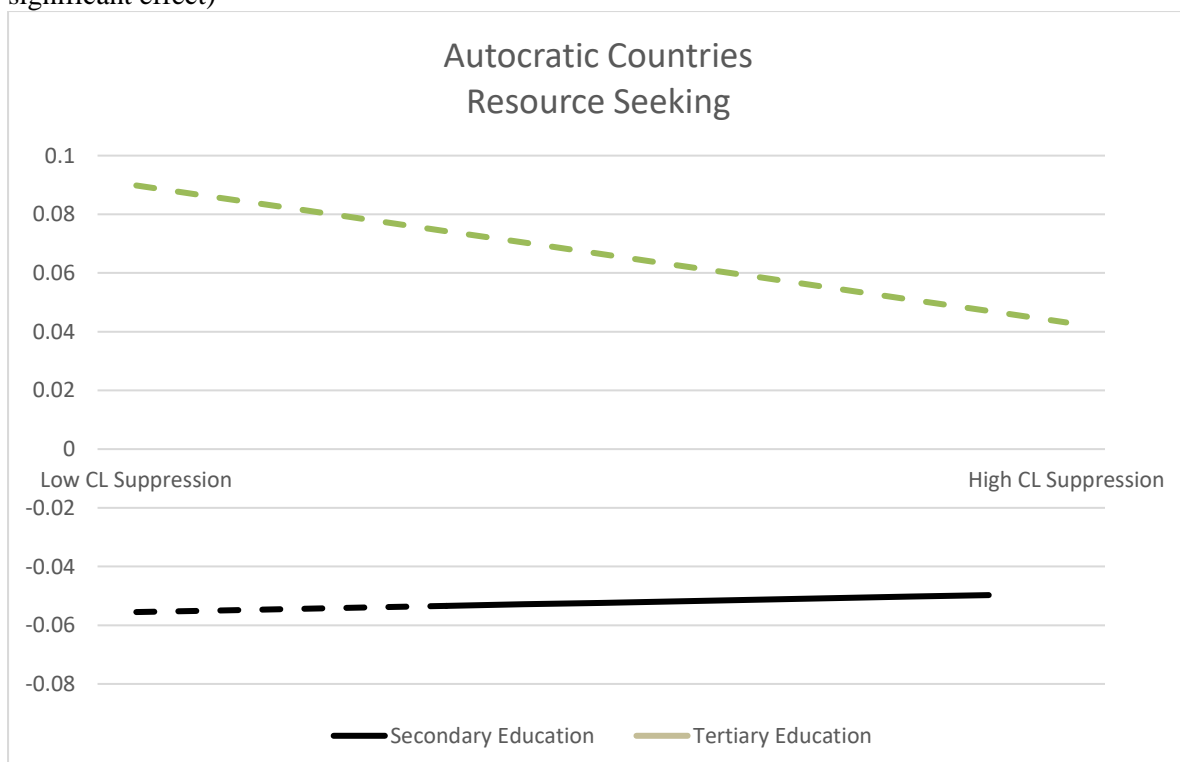


Figure 7. Marginal effects of secondary and tertiary education and civil liberties (CL) suppression on FDI for democratic countries and efficiency-seeking investments (solid lines indicate a statistically-significant effect)

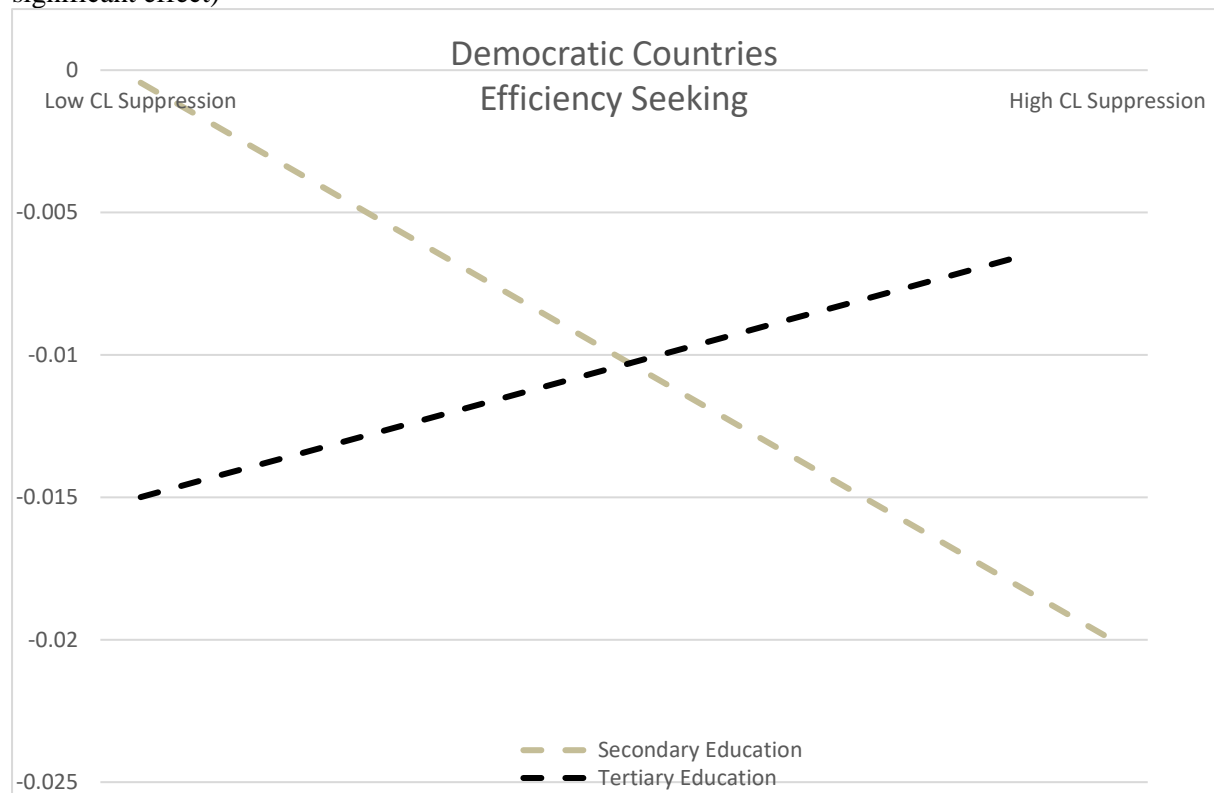
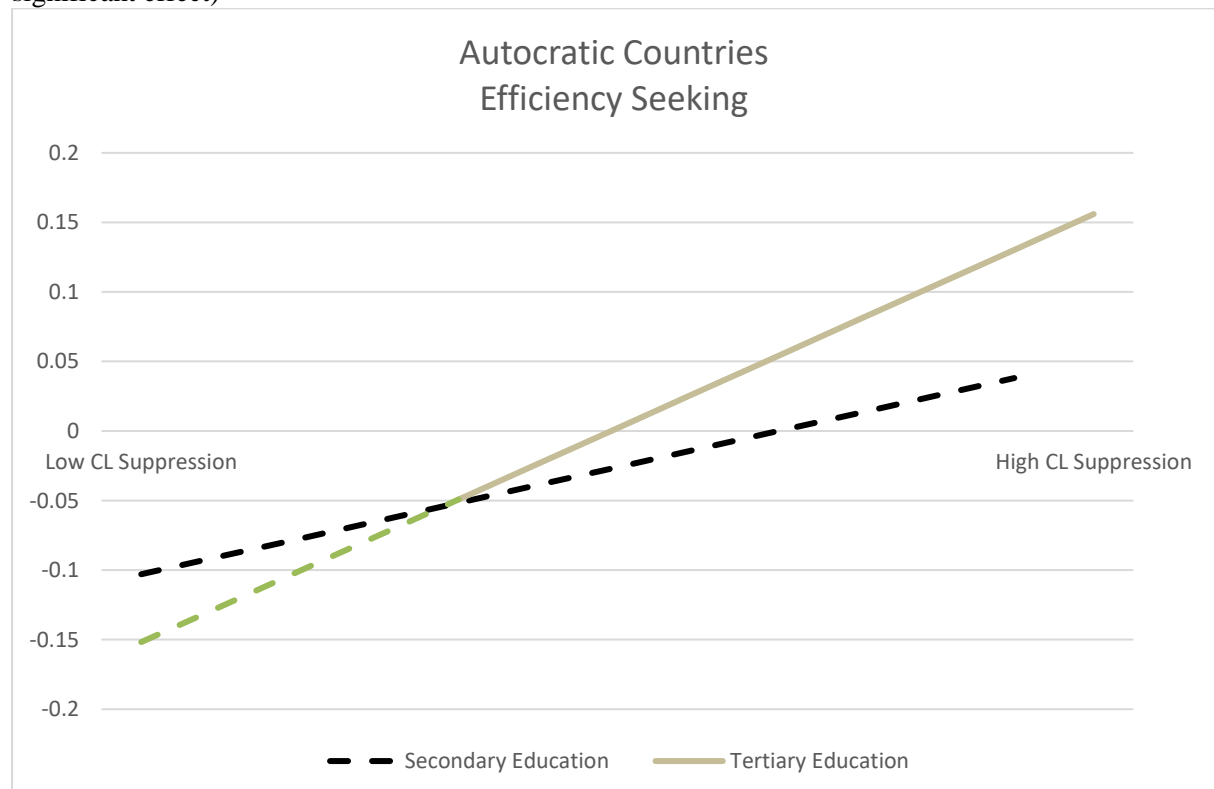


Figure 8. Marginal effects of secondary and tertiary education and civil liberties (CL) suppression on FDI for autocratic countries and efficiency-seeking investments (solid lines indicate a statistically-significant effect)



## Appendix 1. List of recipient countries

Albania Algeria Angola Argentina Armenia Azerbaijan Bahamas Bahrain Bangladesh Belarus Bolivia Botswana Brazil Bulgaria Burkina Faso Cameroon Chile China Colombia Congo(DRC) Costa Rica Cote d'Ivoire (Ivory Coast) Croatia Cuba Czech Republic Dominican Republic Ecuador Egypt El Salvador Estonia Ethiopia Gabon Gambia Ghana Guatemala Guinea Guinea-Bissau Guyana Haiti Honduras Hungary India Indonesia Iran Iraq Jamaica Jordan Kazakhstan Kenya Kuwait Latvia Lebanon Liberia Libya Lithuania Madagascar Malawi Malaysia Mali Malta Mexico Moldova Mongolia Morocco Mozambique Myanmar (Burma) Namibia Nicaragua Niger Nigeria North Korea Oman Pakistan Panama Papua New Guinea Paraguay Peru Philippines Poland Qatar Republic of the Congo Romania Russia Saudi Arabia Senegal Serbia Sierra Leone Slovakia Slovenia Somalia South Africa South Korea Sri Lanka Sudan Suriname Tanzania Thailand Togo Trinidad & Tobago Tunisia Turkey UAE Uganda Ukraine Uruguay Venezuela Vietnam Yemen Zambia Zimbabwe

# Appendix 2. Correlation Matrix

	Jobs created	GDP	GDP per person employed	FDI Inflows	Trade	Ores and metals exports	Fuel exports	Gross enrolment ratio, secondary	Gross enrolment ratio, tertiary (orth-secondary)	Institutional quality	Polity	Civil liberties suppression (orth - Polity)
Jobs created	1											
GDP	0.0805*	1										
GDP per person employed	-0.1319*	-0.3580*	1									
FDI Inflows	-0.0568*	-0.2803*	0.3595*	1								
Trade	-0.1259*	-0.4223*	0.6601*	0.5498*	1							
Ores and metals exports	-0.0235*	-0.2126*	-0.0215*	0.0356*	-0.1529*	1						
Fuel exports	-0.0828*	-0.1520*	0.0937*	-0.0085	0.0049	-0.0657*	1					
Gross enrolment ratio, secondary	-0.0807*	-0.3091*	0.6810*	0.1312*	0.2908*	0.0552*	0.1011*	1				
Gross enrolment ratio, tertiary (orth-secondary)	-0.0096	-0.2196*	0.2968*	0.0359*	0.1760*	0.1262*	0.0630*	0	1			
Institutional quality	-0.0825*	-0.2506*	0.6282*	0.3525*	0.5681*	-0.0169*	-0.1368*	0.4637*	0.0995*	1		
Political governance	0.0685*	-0.1697*	0.0757*	-0.0591*	-0.1326*	0.2501*	-0.1521*	0.1152*	0.3840*	0.0121*	1	
Civil liberties suppression (orth - Polity)	0.0630*	0.2347*	-0.1873*	-0.1557*	-0.2192*	0.0431*	0.0816*	-0.2121*	0.1642*	-0.2331*	0	1

\* significant at 5%;

### Appendix 3. Orthogonalisation regressions for Civil Liberties Suppression and Political governance

	Political governance
Civil Liberties Suppression	-3.8786*** (0.0121)
Constant	16.8115*** (0.0372)
Observations	53630
Adjusted R-squared	0.5599

	Secondary Education
Tertiary Education	1.05923*** (0.00522)
Constant	-46.8049*** (0.3845)
Observations	36600
Adjusted R-squared	0.5206

Robust standard errors in parentheses, \* significant at 10%; \*\* significant at 5%; \*\*\* significant at 1

### Appendix 4. Regression Analysis of the effect of civil liberties suppression and moderating factors on FDI from China (as home country) by investment motive (Dependent variable logarithm of Jobs created)

	Resource Seeking (24)	Efficiency Seeking (25)	Market Seeking (26)	Strategic Asset Seeking (27)
GDP	0.03082 (0.54999)	0.21132* (0.11884)	0.12353 (0.12034)	0.12620 (0.08998)
GDP per person employed	0.18779 (0.22899)	-0.04225*** (0.00271)	0.04567** (0.01907)	0.00573 (0.01581)
FDI inflows	0.19987 (0.30341)	-0.01797 (0.02137)	0.06272** (0.02733)	-0.00701 (0.01157)
Trade	0.02256 (0.01854)	0.00684*** (0.00056)	0.00143 (0.00365)	0.00043 (0.00410)
Ores and metals exports	0.31395*** (0.00978)	0.01372 (0.01540)	0.00256 (0.00758)	-0.00784 (0.02068)
Fuel exports	-0.04668 (0.05059)	0.01348 (0.00835)	-0.00151 (0.00488)	-0.00076 (0.00479)
Gross enrolment ratio, secondary	0.00453 (0.03280)	-0.00587 (0.00968)	0.00169 (0.01096)	-0.00253 (0.00741)
Gross enrolment ratio, tertiary (ORTH)	0.69139 (0.81419)	0.01152 (0.00990)	0.08004 (0.00617)	-0.17359 (0.16613)
Institutional quality	-0.08662 (0.08118)	0.01904 (0.02057)	0.02903 (0.02114)	0.02895* (0.01707)
Political governance	-0.38267 (0.45930)	0.04297 (0.03377)	0.03000 (0.03856)	0.03781 (0.02359)
Civil liberties suppression (ORTH)	-0.00473 (0.03707)	-0.01221 (0.15727)	0.00794 (0.25626)	-0.00249 (0.00627)
CL* Gross enrolment ratio, secondary	-0.00367 (0.00549)	-0.00058 (0.00201)	-0.00142 (0.00294)	0.00161 (0.00189)
CL* Gross enrolment ratio, tertiary (ORTH)	-0.00237 (0.01108)	0.00139 (0.00199)	-0.00091 (0.00140)	0.00066 (0.00112)
Constant	5.79207 (14.47008)	-2.05136 (3.78779)	-2.42765 (4.16252)	3.51553 (2.80614)



Observations	310	102	186	224
Adjusted R-squared	0.06636	0.25071	0.61080	0.18714
VIF	2.45	2.51	1.79	1.72
Time effects	0.51	0.51	0.71	1.28
Sector effects	5.86***	5.99***	46.47***	8.91***

Robust standard errors in parentheses

\* significant at 10%; \*\* significant at 5%; \*\*\* significant at 1%