

FOREIGN ECONOMIC POLICY OF THE UNITED STATES

Political Instability, Interstate
Conflict, Adverse Changes
in Host Government Policies
and Foreign Direct Investment
A Sensitivity Analysis

BRAIMOH D. OSEGHAE

GARLAND PUBLISHING, INC.
NEW YORK & LONDON • 1993

Contents

List of figures	vii
List of tables	ix
Acknowledgements	xiii
1 Introduction	
Statement of the Problem	1
Purpose of the Study	6
Potential Contribution of the Study	7
Scope of the Study	8
Plan of the Study	8
2 Literature Review	
The Concept of Political Risk	11
Level of Analysis	14
Theoretical Models	15
Smith's Model of Political Risk	15
Root's Model of Political Risk	17
Schollhammer's Model of Political Risk	20
Simon's Model of Political Risk	20
Empirical Studies	24
Attitudinal Studies	24
Behavioral Studies	28
Limitations of Previous Studies	36
Conclusion	39
3 Theoretical Framework	
The Conceptual Framework	43
Host Government Policies	46
MNCs' FDI Decisions	52
The Conceptual Model	62
Hypotheses	65

4	Methodology	
	Research Design	67
	Sample	69
	Econometric Model	70
	Variables and Data Sources	74
	Analytical Procedures	93
	Conclusion	96
5	Analysis of the Findings	
	Statistical Procedures	99
	Statistical Results	99
	Multiple Regression Results	114
	MNCs' Manufacturing Foreign Direct Investment Decisions: New Inflows	118
	MNCs' Manufacturing Foreign Direct Investment: Reinvestment	123
	Regression Analysis: Controlling for Some Independent Variables	128
	Relative Importance of the Independent Variables	131
	Host Government Decisions	132
	MNCs' FDI Decisions: New Inflows	133
	MNCs' FDI Decisions: Reinvestment	135
	Interpretation of Findings	137
6	Conclusions and Implications	
	Summary	145
	Implications of Findings	147
	Multinational Companies	148
	Host Government Policy Implications	150
	Limitations of the Study	151
	Suggestions for Future Research	152
	Bibliography	156
	Index.	169

List of Figures

2.1	Smith's Model of Political Risk	16
2.2	Root's Model of Political Risk	18
2.3	The Political-Social Process Model	19
2.4	Schollhammer's Model of Political Risk	21
2.5	Simon's Model of Political Risk	23
3.1	Components of Business Environment	44
3.2	Political Risk and FDI: A Conceptual Scheme	45
5.1	Political Risk and MFDI	141
5.2	Political Risk and Reinvestment	143

List of Tables

1.1	U.S. Foreign Direct Investment Position in Some Selected Countries	2
2.1	A Typology of Macro Risk	22
2.2	Relationship Between Research Method and Findings in the Extant Literature	35
2.3	Measurement of FDI and the Level of Aggregation . . .	39
2.4	Shortcomings of the Extant Literature	41
3.1	Net U.S. Capital Flows 1950-1965 and 1960-1968	47
4.1	U.S. FDI in Sampled Countries as Percentage of U.S. Total FDI in Latin American Countries	69
4.2	Rank-Ordering of Indicators of CGP	77
4.3	Relative Importance of Political Environmental Factors	77
4.4	The Weighting of CGP Indicators	79
4.5	Reliability Test Results for the Indicators of CGP	80
4.6	Conflict and Peace Data Bank (COPDAB)	82
4.7	Reliability Test Results for the Indicators of Political Instability	84
4.8	Reliability Test Results for the Indicators of Inter-State Conflict	87

4.9	Sources of Data	92
5.1	Specification Test Results	101
5.2	Inter-correlation Results for Argentina	103
5.3	Inter-correlation Results for Brazil	104
5.4	Inter-correlation Results for Chile	107
5.5	Inter-correlation Results for Colombia	108
5.6	Inter-correlation Results for Mexico	109
5.7	Inter-correlation Results for Panama	111
5.8	Inter-correlation Results for Peru	112
5.9	Inter-correlation Results for Venezuela	113
5.10	Multiple Regression Results (Dep. Variable = CGP) .	116
5.11	Regression Results (Dep. Variable = MFDI)	120
5.12	Regression Results (Dep. Variable = Reinv)	125
5.13	Multiple Regression Results (Dep. Variable = RESID)	129
5.14	Multiple Regression Results (Dep. Variable = RESID)	130
5.15	The Relative Importance of Independent Variables (Dep. Variable = CGP)	133
5.16	The Relative Importance of Independent Variables (Dep. Variable = MFDI)	134
5.17	The Relative Importance of Independent Variables (Dep. Variable = REINV)	136
5.18	Hypotheses Test Results (Dep. Variable = CGP) ...	138

5.19	Hypotheses Test Results (Dep. Variable = MFDI) . .	139
5.20	Hypotheses Test Results (Dep. Variable = REINV) .	142