

Determinants of Foreign Capital Inflows:

Evidence from Resource-Rich Countries

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【Abstract】

Many studies have shown that natural-resource abundant economies tend to grow at a slower pace despite the potentially beneficial impact of natural resource wealth on economic prosperity (the “natural resource curse”). The recent boom in commodity prices has brought about the increase in foreign capital inflows into resource-rich countries, which might amplify the business cycle fluctuations.

This study investigates the determinants of the foreign capital flows into resource-rich countries, focusing on the effect of institutional quality and soundness of macroeconomic policies. This paper shows that progress of democratization promotes the acceptance of FDI in resource-rich countries with a high income level but cause withdrawal of foreign companies in low-income resource-rich countries. This paper also shows that the prevalence of corruption facilitates FDI in low-income resource-rich countries while reduction of corruption brings about increased FDI in high-income resource-rich countries. The progress of democratization might result in reduced FDI if dictatorship administration allows more room for collusion with foreign-based companies, or if progress of democratization makes the checking system more complex to improve the transparency.

As for the effect of foreign exchange regime, it is verified that countries allowing foreign exchange rate flexibility and those with parallel foreign exchange practices decrease FDI and receive more capital inflow aiming at capital gain from the appreciated currency.