

---

**Electronic Theses and Dissertations**

---

2023

# Effect of institutional quality on Foreign Direct Investment: a case of selected Eastern African countries.

Musili, Daniel Mwanzau  
*Strathmore Business School*  
*Strathmore University*

## **Recommended Citation**

Musili, D. M. (2023). *Effect of institutional quality on Foreign Direct Investment: A case of selected Eastern African countries* [Strathmore University]. <http://hdl.handle.net/11071/13384>

Follow this and additional works at: <http://hdl.handle.net/11071/13384>

**EFFECT OF INSTITUTIONAL QUALITY ON FOREIGN DIRECT INVESTMENT: A  
CASE OF SELECTED EASTERN AFRICAN COUNTRIES**

**DANIEL MWANZAU MUSILI**

**REG NO. MDF/52380/2017**



**A RESEARCH THESIS SUBMITTED IN PARTIAL FULFILMENT OF THE  
REQUIREMENTS FOR THE AWARD OF THE DEGREE OF MASTER OF  
SCIENCE IN DEVELOPMENT FINANCE OF STRATHMORE UNIVERSITY**

**MAY 2023**

## Declaration

I declare that this work has not been previously submitted and approved for the award of a degree by this or any other University. To the best of my knowledge and belief, the dissertation contains no material previously published or written by another person except where due reference is made in the dissertation itself.

© No part of this dissertation may be reproduced without the permission of the author and Strathmore University

Name of Candidate: Daniel Mwanzau Musili

## Approval

The dissertation of Daniel Mwanzau Musili was approved by the following:

Name of Supervisor: Dr. Bernadette Wanjala

School/Institute/Faculty: Strathmore University Business School

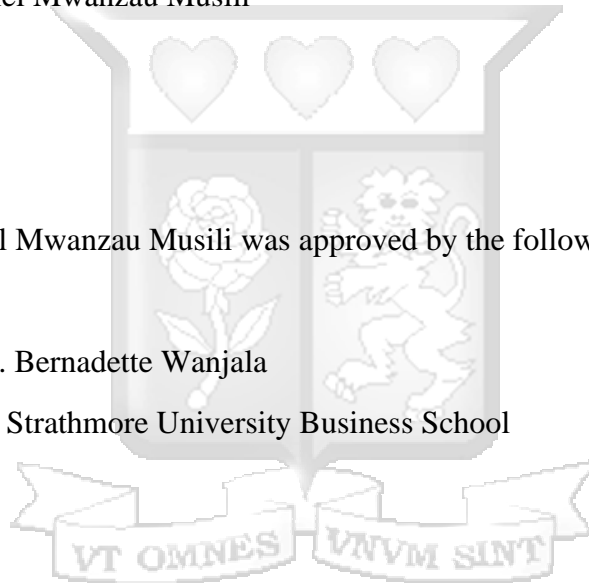
Dr. Ceaser Mwangi

Executive Dean

Strathmore University Business School.

Dr. Bernard Shibwabo

Director, Office of Graduate Studies



## ABSTRACT

Empirical evidence points to a positive relationship between Foreign Direct Investment (FDI) and economic growth, especially in developing economies. However, research shows that multiple country-specific factors influence FDI inflows to respective countries, for example, the policy environment. Data show that while investment inflows have increased in Asian countries, and in Northern and Southern Africa, FDI inflows to Eastern Africa have decreased in recent years, with the Covid-19 pandemic that restricted international capital flows exacerbating the issue. Given the reduced FDI inflows in the Eastern Africa region in recent years and the fact that it is important to increase the attractiveness of Eastern African states to foreign investors to ensure sustainable development in the region, this study examined the effect of institutional quality factors (political stability, government effectiveness, regulatory quality, control of corruption, rule of law and voice and accountability) on FDI in East Africa. The research was grounded on the Eclectic Paradigm (Ownership-Location-Internationalization- OLI theory) and the institutional FDI fitness theory. A positivist philosophy focused on quantitative analysis of the relationship between the selected research variables was adopted. The interaction between institutional quality factors and FDI was analysed using panel data analysis covering Kenya, Tanzania, Rwanda, Burundi, Ethiopia, and Uganda over the period from 2005 to 2021. A panel regression model was used to determine the interaction between the research variables. Cointegration tests revealed there existed a long-run relationship between institutional quality factors and foreign direct investment in the Eastern Africa region. Panel regression results showed that 58.95% of foreign direct investment in the Eastern Africa region can be predicted by institutional quality factors. The study established that overall, institutional quality factors have a positive and significant effect on the volume of foreign direct investment in the Eastern African region and calls on Eastern African countries to embrace the role of institutions and good governance in enhancing FDI inflows. To enhance foreign direct investment (FDI) inflows, it is recommended that East African states develop and enforce policies that promote investment in the private sector. This can be achieved by leveraging institutional quality metrics as a foundation for attracting investment into the different countries.

*Keywords: Institutional Quality, Foreign Direct Investment*

## TABLE OF CONTENTS

<b>DECLARATION</b> .....	<b>ii</b>
<b>ABSTRACT</b> .....	<b>iii</b>
<b>TABLE OF CONTENTS</b> .....	<b>iv</b>
<b>LIST OF TABLES</b> .....	<b>viii</b>
<b>LIST OF FIGURES</b> .....	<b>ix</b>
<b>DEFINITION OF TERMS</b> .....	<b>x</b>
<b>ABBREVIATIONS AND ACRONYMS</b> .....	<b>xii</b>
<b>CHAPTER ONE</b> .....	<b>1</b>
<b>INTRODUCTION</b> .....	<b>1</b>
1.1 Background to the Study.....	1
1.1.1 Institutional Quality Factors .....	4
1.1.2 Foreign Direct Investment (FDI) .....	7
1.1.3 FDI Trends in Eastern Africa.....	8
1.2 Statement of the Problem.....	10
1.3 General Objective .....	11
1.3.1 Specific Objectives .....	11
1.4 Research Hypotheses .....	12
1.5 Scope of the Study .....	13
1.6 Significance of the Study .....	13
1.6.1 To Policy Makers.....	13
1.6.2 To Industry Players .....	13
1.6.3 To Scholars .....	14
1.7 Organization of the study.....	15

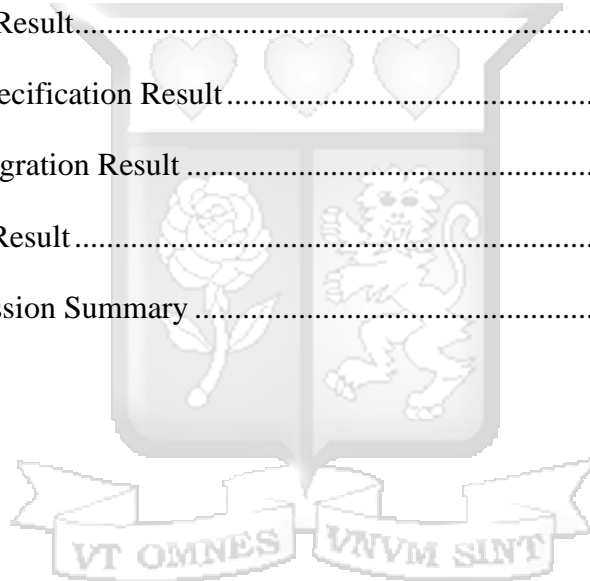
<b>CHAPTER TWO .....</b>	<b>16</b>
<b>LITERATURE REVIEW .....</b>	<b>16</b>
2.1 Introduction.....	16
2.2 Theoretical Literature Review .....	16
2.2.1 The Ownership – Location – Internalization (OLI) Theory (Eclectic Paradigm) .....	16
2.2.2 Institutional FDI Fitness Theory .....	17
2.3 Empirical Literature Review.....	19
2.3.1 Voice and Accountability and Foreign Direct Investment .....	19
2.3.2 Political Stability and Absence of Violence/Terrorism and Foreign Direct Investment .....	21
2.3.3 Regulatory Quality and Foreign Direct Investment.....	22
2.3.4 Control of Corruption and Foreign Direct Investment .....	24
2.3.5 Rule of Law and Trade Openness and Foreign Direct Investment.....	25
2.3.6 Government Effectiveness and Foreign Direct Investment.....	27
2.4 Summary of Research Gaps.....	28
2.5 Conceptual Framework.....	31
<b>CHAPTER THREE .....</b>	<b>34</b>
<b>RESEARCH METHODOLOGY .....</b>	<b>34</b>
3.1 Introduction.....	34
3.2 Research Philosophy .....	34
3.3 Research Design.....	34
3.4 Target Population.....	35
3.5 Data Collection Instruments .....	35
3.6 Data Collection Procedure .....	35

3.7 Diagnostic Tests.....	36
3.7.1 Autocorrelation Test .....	36
3.7.2 Multicollinearity Test.....	36
3.7.3 Normality Test .....	36
3.7.4 Stationarity Test.....	36
3.7.5 Hausman Specification Test .....	37
3.7.6 Panel Cointegration Test.....	37
3.8 Data Analysis and Presentation .....	37
<b>CHAPTER FOUR.....</b>	<b>39</b>
<b>PRESENTATION OF RESEARCH FINDINGS.....</b>	<b>39</b>
4.1 Introduction.....	39
4.2 Summary of Extracted Research Data .....	39
4.3 Diagnostic Tests.....	41
4.3.1 Autocorrelation Test .....	41
4.3.2 Multicollinearity Test.....	41
4.3.3 Normality Test .....	42
4.3.4 Stationarity Test.....	42
4.3.5 Hausman Specification Test .....	44
4.3.6 Panel Cointegration Test.....	45
4.4 Correlation Analysis .....	45
4.5 Panel Regression Analysis.....	47
<b>CHAPTER FIVE .....</b>	<b>51</b>
<b>DISCUSSION, CONCLUSION AND RECOMMENDATIONS .....</b>	<b>51</b>
5.1 Introduction.....	51

5.2 Summary .....	51
5.3 Discussion .....	51
5.3.1 Voice and Accountability on the Level of foreign direct investment in Selected Eastern African Countries .....	51
5.3.2 Political Stability and Absence of Violence/terrorism on the Level of foreign direct investment in Selected Eastern African Countries.....	52
5.3.3 Government Effectiveness on the Level of foreign direct investment in East African Countries.....	53
5.3.4 Regulatory quality on the level of foreign direct investment in selected Eastern African countries.....	54
5.3.5 Rule of law on the level of foreign direct investment in selected Eastern African countries.....	55
5.3.6 Control of Corruption on the Level of foreign direct investment in Selected Eastern African Countries.....	56
5.4 Conclusions.....	56
5.5 Recommendations.....	58
5.6 Areas for Further Research.....	59
5.7 Limitations of the Study.....	59
<b>REFERENCES.....</b>	<b>60</b>
<b>APPENDICES.....</b>	<b>69</b>
Appendix I: Data Extraction Tool (for each country: Kenya, Tanzania, Uganda, Burundi, Rwanda, Ethiopia and South Sudan) .....	69
Appendix II: Ethical Review Committee Approval.....	70
Appendix III: NACOSTI Research Approval.....	71

## LIST OF TABLES

Table 1.1: Worldwide Governance Indicators Percentile Rank (2021).....	5
Table 2.1 Literature Gaps .....	29
Table 2.2 Operationalization of Variables .....	32
Table 4.1 Summary of Descriptive Analysis .....	40
Table 4.2 Autocorrelation Result.....	41
Table 4.3 Multicollinearity Result .....	41
Table 4.4 Normality Result.....	42
Table 4.5 Stationarity Result.....	43
Table 4.6 Hausman Specification Result.....	44
Table 4.7 Panel Cointegration Result .....	45
Table 4.8 Correlation Result.....	46
Table 4.9 Panel Regression Summary .....	48



**LIST OF FIGURES**

Figure 2.1 Conceptual Framework ..... 32



## DEFINITION OF TERMS

<b>Foreign Direct Investment</b>	Investments made to acquire lasting interest in or effective control over an enterprise operating outside of the economy of the investor.
<b>Institutional Quality</b>	The legal, economic, political, and regulatory frameworks that measure the power, consistency, and robustness of a country's institutions.
<b>Rule of law</b>	The degree to which a government holds people, institutions and entities accountable to existing laws.
<b>Voice and accountability</b>	An indicator of the perceptions of the extent to which a country's citizens can participate in selecting their government, as well as freedom of expression, freedom of association, and a free media.
<b>Control of corruption</b>	An indicator capturing the perceptions of the extent to which public power is exercised for private gain, including both petty and grand forms of corruption, as well as "capture" of the state by elites and private interests.
<b>Political stability and absence of violence/terrorism</b>	An indicator capturing the perceptions of the government's ability to resist violent or unconstitutional coups and includes the frequency of politically-instigated violence and terrorism.
<b>Government effectiveness</b>	An indicator that captures the perceptions of the quality of public services, the quality of the civil service and the degree of its independence from political pressures, the quality of policy formulation and implementation, and the commitment of the government to instituted policies.
<b>Regulatory quality</b>	A variable that captures perceptions regarding the government's ability to formulate and implement sound

policies and regulations necessary for private sector development.

**Sustainable Development**

Growth, progress and positive change in physical, economic, environmental, social and demographic aspects that meet the needs of the present without compromising the ability of future generations to meet their own needs.



## ABBREVIATIONS AND ACRONYMS

ASEAN	Association of Southeast Asian Nations
AU	African Union
CPIA	Country Policy and Institutional Assessment
EAC	East African Community
EDB	Ease of Doing Business
FDI	Foreign Direct Investment
GMM	Generalized Method of Moments
GDP	Gross Domestic Product
IDA	International Development Association
IQ	Institutional Quality
MNC	Multinational Companies
MNE	Multinational Enterprises
MTP	Medium-Term Plan
OECD	Organization for Economic Cooperation and Development
OLI	Ownership Location Internalization
SAARC	South Asian Association for Regional Cooperation
VIF	Variance Inflation Factor
WBG	World Bank Group



## CHAPTER ONE

### INTRODUCTION

#### 1.1 Background to the Study

Foreign Direct Investment (FDI) is one of the main drivers of economic growth, contributing through the transfer of modern technology, promotion of learning and labour development, and provision of capital used to stimulate development (Sokang, 2018). FDI can play a big role in filling the savings-investment gaps that exist in developing economies and stimulate their economic growth (Nguyen, 2020). However, country-specific factors can either enhance or dampen FDI inflows. Since the 1990s, many developed and developing countries have adopted policies to create attractive environments for foreign investors, including the reduction of taxes, provision of subsidies, financial sector reforms, structural adjustment programs, and economic partnership agreements, among others (Musabeh, 2018).

More recently, the focus has shifted towards socio-political factors and how these may determine the level of FDI. Researchers have examined and understood the relationship between socio-political factors and FDI inflows for a long time as evidenced by Basi (1963) who investigated the association between political instability and FDI. The findings of this study are still valid as demonstrated by Chen and Jiang (2021) whose research affirmed that a country's attractiveness is highly dependent on the quality of its financial, regulatory and security institutions. Currently, researchers are intrigued by the impact of the quality of institutions on an investment destination's attractiveness. These researchers follow the framework developed by North (1990) on institutions and their impact on business performance showing the role of institutions in shaping incentives for investment, the influence of institutional reform on investor attraction and the specific components of institutional quality that influence investor decisions.

According to Aziz (2018), policy reforms are motivated by the assumption that good institutions attract more investment. Researchers such as Dobrowolska, Dorożyński and Kuna Marszałek (2021), for instance, provided evidence that country-specific factors such as governance and property rights have significant influences on investor decisions. Acquah and Ibrahim (2020) assert that a country's level of financial sector development has a significant influence on the volume and effects of FDI inflows. However, Bailey (2018) revealed inconsistency in the evidence. While political stability, democracy, and rule of law factors attract FDI inflows, a high degree of

corruption, high tax rates and cultural distance deter foreign investors. Paul and Jadhav's (2019) panel data analysis revealed the positive impact of regulations, infrastructure, tariff and trade incentives, and political stability on FDI inflows. Bureaucratic red tape and judicial transparency were shown to be less encouraging for investors. Chen and Jiang (2021) highlight how the rule of law and control of corruption attract FDI into Australia but their absence discouraged investment in Zimbabwe which has lower-quality institutions.

Liu, Tang, Chen and Poznanska (2017) made similar observations when exploring investment in China's Belt and Road Initiative and affirmed that investors will consider risks relating to the cost of investment and the macroeconomic conditions before making investment decisions. Some scholars argue that investor rights are usually not protected in territories with poorly developed property rights laws and regulations (Shah, 2018; Sabir, Rafique, & Abbas, 2019). According to Shah (2018), the adoption of trade-related intellectual property rights (TRIPS) regulations augmented investor confidence and stimulated investment in all 24 Latin American and Caribbean states. Challe, Lopez and Mengus (2019) made similar observations in their research which concluded that countries with institutions that protect investor assets, promote the rule of law and reduce the cost of doing business are generally more attractive to investors. These researchers associate high-quality institutions with greater freedom, and a high degree of openness and inclusion which creates conducive and competitive business environments.

The East African Community region considers Foreign Direct Investment (FDI) an important instrument that can support the modernization of the agricultural sector and industrialisation. The region through reforms has increased industrialization and service delivery, buoyed by investment in manufacturing, construction and financial services (Appiah-Kubi, et al., 2020). The region has also sought to ramp up its mineral exploitation and tourism industries and has implemented reforms to increase the attractiveness of its sectors. Recently, Chinese investment accounted for almost 60% of the FDI inflows in Eastern Africa, mainly for infrastructure projects. These investments had seen Eastern Africa emerge as Africa's fastest-growing region, growing at an average of 5% before the emergence of the COVID-19 pandemic (UNCTAD, 2022). In 2019, the region had seen FDI inflows increase from \$5.7 billion to \$11.5 billion, with the technology, manufacturing and services sectors benefitting the most. However, according to Mwesigye (2021), uncertainties from the pandemic saw FDI in Eastern Africa decrease by 43.39 per cent, reaching just US\$4.91 billion in 2020.

Despite the region rebounding in 2021, some countries have struggled to recover as evidenced in the UN Conference on Trade and Development's (UNCTAD's) World Investment Report 2022 which affirms that Kenya's FDI inflows fell by US\$ 269 million (Sh 31.47 billion) despite countries in the region recording a 35 per cent improvement in FDI. According to the report, while Kenya attracted FDI through infrastructure investment deals, Ethiopia prioritized investment in the renewables sector, while Uganda, Burundi and Tanzania prioritized the minerals extraction sectors. When comparing the region to the rest of the African continent, the report affirms that while Central Africa registered an increase in FDI in 2020, inflows to North Africa contracted by 25 per cent, by 12 per cent in Sub-Saharan Africa, and by 16 per cent in East and Southern Africa. However, while inflows to Sub-Saharan Africa stood at \$30 billion, \$10 billion in North Africa and \$9.2 billion in Central Africa, East Africa was only able to attract \$6.5 billion, an indicator that the region may not be as attractive as the western, northern and southern parts of Africa.

The persistent low FDI inflows into the East African Community have spurred numerous empirical studies with Marandu, Mburu and Amanze (2019) affirming that restrictions limiting the free movement of capital, services, and goods inhibit FDI in the region. Mosikari, Nthebe, and Eita (2018) asserted that corruption has been a major deterrent to foreign investment within the East African region, an observation supported by Nyakobo (2021) whose study investigated the reasons for reduced investment in Kenya's manufacturing sector. Shisya (2021) argues that lack of transparency has led to increased frequency of corruption and bribery, bureaucratic inefficiency, absence of property rights protection and unpredictable policy implementation which has negatively impacted FDI inflows. According to Schlesinger and Tomashevskiy (2022), Kenya's volatile political institutions and terror risk discourage foreign investment, especially during election years such as the 2022 general election period.

Researchers have developed theoretical frameworks in their bid to explain investment decisions and Musabeh (2018) affirms that no one theory can fully explain why companies decide to invest in some countries and not in others; and why some countries can attract more foreign investors than others. However, the researcher used the Eclectic Paradigm (internationalization theory) and the capital markets theory (Aliber, 1970; 1971). These theories assert that foreign investment is a result of capital market imperfections and local advantages. The Eclectic Paradigm (Dunning, 1980) posits that countries engage in FDI for ownership, internalization, and location advantages. This theory was used by Aswata, Nnyanzi and Bbale (2018) who showed a positive influence on

formulating and implementing business-friendly policies with increased investment. However, Sabir et al. (2019) aver that the magnitude of institutional quality may be more valuable in developed than in developing countries, while Bahati and Mbithi (2022) argue that governments hosting foreign firms in the SSA region need to consider the degree to which institutional quality will encourage further FDI inflows. This study employed the Eclectic Paradigm to explain the extent of the influence of institutional quality on FDI inflows into the East African region.

### **1.1.1 Institutional Quality Factors**

Institutional quality (IQ) refers to the legal, economic, political, and regulatory frameworks that measure the power, consistency, and robustness of a country's institutions (Adegboye, et al., 2020). Institutional quality factors show a country's ability to enforce contracts and safeguard property rights and guarantee shareholder expectations at a given time. According to Shisya (2021), institutional quality measures indicate the quality of governance and institutions in a country. Investors pursue personal goals and will assess an environment before making an investment decision, especially if the investment is in another country (Challe, et al., 2019). As a result, host countries need to consider the composition of the institutions that control investor behaviour since this has a direct influence on their ability to realize their objectives (Alonso, et al., 2020). For businesses, guarantees of government services such as enforcing contracts and protecting property rights tend to attract investors, and Bailey (2018) affirms that such activities ease the operating environment, lower the cost of production, reduce business uncertainty, and generate order.

The World Bank releases an annual Global Investment Competitiveness Report which asserts that while institutional quality is one of the key determinants of FDI, the degree of political stability, independence of legal institutions and regulatory quality are the top three investment decision factors, while predictability and transparency increase investor confidence and FDI flows (World Bank, 2020). The World Bank also publishes an index that focusses on six facets of governance that form the Institutional Quality Index, namely voice and accountability, political stability and absence of violence/terrorism, government effectiveness, regulatory quality, rule of law and control of corruption (World Bank, 2022). The Institutional Quality Index is represented by the Worldwide Governance Indicators (WGI) project by the World Bank (Kaufmann and Kraay, 2022). For Eastern Africa, the most recent scores across the indicators are as indicated in Table 1.1. The governance indicator ranges from -2.5 (indicating weak) to 2.5 (indicating strong)

governance performance while the percentile rank among all the countries ranges from 0 (lowest) to 100 (highest) (Kaufmann and Kraay, 2022).

**Table 1.1: Worldwide Governance Indicators Percentile Rank (2021)**

Country	Kenya	Ethiopia	Uganda	Rwanda	Tanzania	Burundi	South Sudan
Score	Rank	Rank	Rank	Rank	Rank	Rank	Rank
Voice and accountability	35.75	20.29	25.60	22.22	29.47	12.08	2.42
Political Stability and absence of violence/terrorism	13.21	4.25	18.40	52.36	30.66	10.38	3.30
Government Effectiveness	38.94	31.25	30.29	61.54	28.37	9.62	0.00
Regulatory quality	36.54	16.83	35.58	54.33	28.75	13.94	2.40
Rule of law	38.94	29.33	40.38	57.21	32.69	8.17	1.44
Control of corruption	26.44	39.42	17.31	71.63	42.79	2.88	0.00

Source: Kaufmann and Kraay, 2022.

From the recent data, Kenya and Rwanda led the East African countries across most of the indicators in the governance scores, followed by Tanzania and then Uganda. South Sudan had the weakest scores across indicators.

According to Akin (2019), WGI measures the process by which governments are selected, monitored, and replaced through voice and accountability, political stability and absence of violence/terrorism indicators, the government's capacity to effectively formulate and implement sound policies through the government effectiveness and regulatory quality, and to measure the respect of citizens and the state through the rule of law and control of corruption indicators.

The voice and accountability indicator captures perceptions of the extent to which a country's citizens can participate in selecting their government, as well as freedom of expression, freedom

of association, and free media (Hayat, 2019). The political stability and absence of violence/terrorism indicator captures perceptions of the government's ability to resist violent or unconstitutional coups and includes the frequency of politically-instigated violence and terrorism. Foreign investors will look to invest in regions with political stability and a proven record of rule of law where contracts are enforced, property rights protected and the police, as well as the judiciary, attend to reports of criminal activity and acts of violence (Aswata, Nnyanzi, & Bbale, 2018). Jurisdictions with violence and no regards for laws are highly deterrent to investors as reported in West Africa where coups have destabilized the region's geopolitical environment (Musavengane & Zhou, 2021).

The government effectiveness variable captures perceptions of the quality of public services, the quality of the civil service and the degree of its independence from political pressures, the quality of policy formulation and implementation, and the commitment of the government to instituted policies (Hayat, 2019). In highly bureaucratic governments, state officials hold significant power over business institutions and can expedite or elongate the processes of registering and running businesses (Dar, Muhammad, & Siddiqi, 2020). Moustafa (2021) associates increased bureaucracy with lower transparency and increased opportunities for corruption, hence lower investment attractiveness. According to Bahati and Mbithi (2022), corruption and bureaucratic delays are among the main factors hindering foreign investment in Bangladesh. Similar sentiments are echoed by Siddica and Angkur (2017) whose study shows a significant negative relationship between bureaucratic quality and FDI inflows. However, not all bureaucratic processes are detrimental and in fact, some serve to assure investors that a country follows its procedures to the letter (Siddica & Angkur, 2017). Godinez and Liu (2015) opine that only bloated bureaucratic processes can discourage investment.

The regulatory quality variable on the other hand captures perceptions regarding the government's ability to formulate and implement sound policies and regulations necessary for private sector development. Judicial transparency, for instance, shows the degree to which jurisdictions make policies and procedures, data, information, and decision-making open to members of the public (Siddica & Angkur, 2017). Independent justice systems are characterized by fairness, impartiality and justice and such environments discourage favouritism and are attractive to foreign multinationals (Mugauri, 2019). Siddica and Angkur (2017) aver that judicial impartiality signifies adherence to the rule of law and communicates confidence in the justice system and due process.

Judicial transparency expresses the citizen's voice and promotes accountability within the public and private sectors, and freedom of expression and association (Othman, 2022). A high degree of judicial transparency influences an agent's trust and acceptance of the rules in society and reinforces contract enforcement and property rights, thus deterring criminal behaviour. Kirovska, Gjozinska and Tanevska Jadrovska (2022) study concluded that reforms guaranteeing judicial independence reduce business risks and motivates companies to invest.

The rule of law component indicates the perceptions of a country's ability to enforce the rules governing societal behaviour and encompass the quality of contract enforcement, property rights, the police, and the courts, as well as the likelihood of crime and violence. The rule of law which is the restriction of arbitrary exercise of power through well-established laws has a significant positive impact on both domestic and foreign investment. Nguyen's (2020) study established that while multinationals are not necessarily put off by weak property rights, countries with trademark and intellectual property laws may discourage investment by companies that patent their products. Haydaroglu (2015) shares these sentiments with his study affirming a positive relationship between the level of property rights protection and FDI inflows to the EU and other OECD countries. Satoglu (2020) used panel data revealing a significant effect of institutions such as corruption, civil liberties, property rights, and good governance on FDI.

The control of corruption variable indicates perceptions of agents on the way a country's officials exercise power for private gain. Corruption refers to the dishonest or fraudulent conduct by individuals to gain some sort of preferential treatment and erodes trust, undermines democratic institutions and has been associated with organized crime and acts of terrorism which results in anarchy, chaos and lower FDI (Lestari, Lesmana, Yudaruddin, & Yudaruddin, 2022). Investors generally shy away from highly corrupt environments but according to Moustafa (2021), investors are attracted to Egypt despite its low capacity to convict corruption cases potentially given other aspects of the market that make it attractive for example, the strategic geographic location. Kasasbeh, Mdanat and Khasawneh (2018) argue that a country's ability to control corruption matters when the investor seeks efficiency rather than rapid market expansion.

### **1.1.2 Foreign Direct Investment (FDI)**

The United Nations defines foreign direct investment (FDI) as the "investments made to acquire lasting interest in or effective control over an enterprise operating outside of the economy of the

investor”. Njuguna and Nnadozie (2022) simplify it and define it as investments made in foreign countries. FDI is one of the main sources of foreign capital in many developing economies and is considered key to economic growth. In the recent past, FDI has gained renewed interest for its influence on transferring resources and technology across national borders and developing countries have been ramping up efforts to attract foreign investors. While some have succeeded, others have failed. Aizenman and Shushko (2011) opine that recent research into FDI has shifted from traditional investments and growth rates to institutions as indicators of income, growth and volatility, with a growing body of evidence linking FDI inflows to the implementation of economic institutional reforms (Tulu, 2021).

The World Investment Report 2022 reports that after an all-time low of \$859 billion reported in 2020, FDI inflows bounced back in 2021, standing at \$1.58 trillion, 64 per cent more than in 2020 (UNCTAD, 2022). The report affirms that this trend is unlikely to continue with the war in Ukraine and the lingering effects of the pandemic contributing to global uncertainty, food, fuel, and financial crisis. This business environment discourages investment and according to the World Bank (2022), FDI inflows to developing countries grew more slowly than in developed economies due to higher promises of returns and stability. African states showed a moderate rise in FDI, with continental GDP reaching \$83 billion, from \$39 billion in 2020 (World Bank, 2020). However, this steep rise was a result of a single corporate transaction as Greenfield investments remained depressed and most investments remained confined to the extractive industries. FDI flows to North Africa fell by 5 per cent to \$9.3 billion, while they increased by 48 per cent to \$14 Billion in West Africa, by 35 per cent to \$8.2 billion in East Africa and \$42 billion in Southern Africa (Xu, Han, Dossou, & Bekun, 2021). Central African FDI remained stagnant at \$9.4 billion. FDI is considered key to East Africa’s development and according to the International Monetary Fund (IMF), the region is one of the fastest growing in the world.

### **1.1.3 FDI Trends in Eastern Africa**

The East African Community comprises South Sudan, Ethiopia, Kenya, Uganda, Tanzania, Rwanda and Burundi and is home to Africa’s most prominent mountains such as Mt. Kilimanjaro and Mt. Kenya, the great lakes region and some of the most competitive business environments in Africa (Aswata, Nnyanzi, & Bbale, 2018). Being one of the sub-Saharan Africa (SSA) countries, the region is also endowed with mineral deposits, gold and oil reserves as well as tourist destinations which create a centre of attention for investors. While most SSA countries leverage

their extractive industries to attract investment, technologies, infrastructure, health and service sectors have emerged as viable sectors for investors. Indeed, while developing countries saw a 60 per cent increase in Greenfield foreign investment ventures in the extraction, quarry, and petroleum sectors in 2014, Bolwijn et al. (2015) report that Greenfield investment into African countries increased by 450 per cent, from US\$4 billion to US\$22 billion.

Kenya is the economic powerhouse of the region, and it is considered a standard setter for development in the region. FDI has been a major driver of economic growth in East Africa with major projects such as Kenya's Standard Gauge Railway, Uganda's oil refineries and Tanzania's Bagamoyo port being funded by foreign investors. However, East African states are struggling to attract FDI inflows, accounting for only 11 per cent of the inflows into the African continent, compared to Southern Africa which accounts for 35 per cent of foreign inflows (Xu, Han, Dossou, & Bekun, 2021). Data on FDI inflows shows a significant jump in FDI in South Africa between 2015 and 2021. In 2015, South Africa received inflows totalling \$1.7 billion. By 2021, South Africa's FDI inflows were \$40 billion while in the same period, Uganda's FDI increased from \$738 million in 2015 to \$1.1b in 2021, Tanzania's and Kenya's fell from \$1.5b and \$1.4b in 2015 to \$922 million and \$448 million in 2021 respectively (UNCTAD, 2022).

The region reported a 16 per cent decline in FDI into East Africa in 2020, dropping from \$8 billion to \$6.5 billion. Ethiopia was the most attractive country, with the country's inflows of \$2.4 billion accounting for more than a third of the region's FDI. Tanzania experienced minimal changes to its FDI inflows while Uganda reported a 35 per cent fall to just \$830 million from \$1.3 billion in 2019. In Burundi, inflows increased from US\$127.2 million to US\$348.10 million while the inflows to Rwanda and South Sudan decreased by 52.10 per cent and 64.9 per cent respectively, from US\$1.9 billion 83.32 million to US\$950.00 million in 2020 and from US\$3.3 billion to US\$1.1 billion in 2020.

While these drops in FDI can be attributed to the COVID-19 pandemic, it is clear that the effects were not spread out evenly. Tanzania's inflows were not majorly affected and remained consistent, while Burundi reported an increase in FDI inflows. Kenya, Uganda and Ethiopia all reported fewer FDI inflows. The EAC is in the process of reviewing relevant laws in a bid to progressively transform the region into a single market where goods, persons, services, labour and capital was allowed to move freely as rights to residence and establishment become integrated. The Intra-EAC

collaboration in investment promotion and development of global value chains is expected to support improved economic activity and a global rule-based trading system which would create attractive environments for foreign investment (Kalii, 2021).

Pamba (2022) asserts that policies aimed at improving the quality of institutions have had a significant impact on FDI inflows into South African states. Sabir et al. (2019) used data from developed and developing economies and concluded that in developing economies, trade openness, property rights and infrastructure are the key determinants of FDI inflows. Rwigema (2022) shows how Rwanda's reduction of the requirements for starting businesses, improvement of contract enforcement through integrated case management systems and credit access increased both domestic and foreign investment. Developing countries are often characterized by poor institutions which often fail to attract FDI. Effective policies, quality institutions, as well as infrastructure will enhance production effectiveness and flexibility in institutions. This study sought to examine the effect of institutional quality on FDI inflows into the East African region.

## **1.2 Statement of the Problem**

Empirical evidence points to a positive relationship between quality institutions and the volume of FDI in both developed and developing economies (Murageh & Wepukhulu, 2019). However, research shows that a host of country-specific factors influence FDI inflows into respective countries. Asongu, Akpan and Isihak (2018) show how policies instituted in MINT (Mexico, Indonesia, Nigeria and Turkey) and BRICS (Brazil, Russia, India, China, and South Africa) regions have seen the countries attract up to 30% of global FDI inflows (Yuldoshboy, et al., 2022). However, while Asian and European countries have been attractive destinations for investors, FDI inflows to East Africa have been decreasing for five straight years, and the Covid-19 pandemic exacerbated the issue (UNCTAD, 2021). Evidence points to a 6% drop in 2018, 14% in 2019, and between 35% and 40% in 2020 (UNCTAD, 2021; Bahati & Mbithi, 2022). This fall in the region's attractiveness motivates this research which sought to examine the extent to which the quality of governance institutions influences foreign investment.

Institutions impact a host country's economic profitability and present locational advantages sought by multinational enterprises. In Poland, for instance, Nazarczuk and Krajewska (2018) reported that infrastructural quality, proximity to urban centres and favourable government policies surrounding Special Economic Zones (SEZ) influence the country's attractiveness. Hayat

(2019) reports that investors are attracted to countries with free trade institutions and good human capital while according to Akin (2019), while economic freedom had statistically insignificant impacts on FDI inflows, trade freedom had moderate influences and political stability was the most important determinant of FDI entry into fragile countries. Regionally, Bosire (2020) presented evidence that the ability to ensure intellectual property rights are protected has a significant impact on ICT companies' investment in the East African region.

However, while establishing tax policies is associated with more secure borders, Tulu's (2021) exploration revealed that reducing entry requirements and providing financial incentives increased Ethiopia's attractiveness to local and foreign investors. Mutisya, Muturi and Kemboi (2019) also determined that export promotion incentives and industrial building allowances will attract FDI investments into Kenya. Findings from Nketiah, et al., (2019) demonstrated the positive effects of trade openness on FDI in West Africa, with inflation being reported to have significant negative impacts. While these studies provide important insight into how different factors influence FDI inflows, most of the studies focused on selected factors and paid little attention to the effect of multiple determinants of FDI (Nazarczuk & Krajewska, 2018; Akin, 2019).

Data-based monitoring has become common as empirical measures of governance become more widely utilized by policy-makers, analysts, journalists, risk rating agencies and investors. The East African region appears to have lost its attractiveness to foreign investors as evidenced by the low volumes received in comparison to other regions in Africa. Bosire (2020) argued that preventing all forms of corruption and promoting political stability would increase FDI inflows into the Eastern Africa region. This study sought to ascertain this in the immediate aftermath of the COVID-19 pandemic and examine the extent to which governance indicators influence FDI inflows.

### **1.3 General Objective**

The main objective of the research was to establish the effect of institutional quality factors on the level of foreign direct investments in selected Eastern African countries.

#### **1.3.1 Specific Objectives**

- i. To assess the effect of voice and accountability on the level of foreign direct investment in selected Eastern African countries.

- ii. To assess the effect of political stability and absence of violence/terrorism on the level of foreign direct investment in selected Eastern African countries.
- iii. To assess the effect of government effectiveness on the level of foreign direct investment in selected Eastern African countries.
- iv. To assess the effect of regulatory quality on the level of foreign direct investment in selected Eastern African countries.
- v. To assess the effect of the rule of law on the level of foreign direct investment in selected Eastern African countries.
- vi. To assess the effect of control of corruption on the level of foreign direct investment in selected Eastern African countries.

#### **1.4 Research Hypotheses**

- H<sub>01</sub>** There is no statistically significant effect of voice and accountability on the level of foreign direct investments in selected Eastern African countries.
- H<sub>a1</sub>** There is a statistically significant effect of voice and accountability on the level of foreign direct investments in selected Eastern African countries.
- H<sub>02</sub>** There is no statistically significant effect of political stability on the level of foreign direct investments in selected Eastern African countries.
- H<sub>a2</sub>** There is a statistically significant effect of political stability on the level of foreign direct investments in selected Eastern African countries.
- H<sub>03</sub>** There is no statistically significant effect of government effectiveness on the level of foreign direct investments in selected Eastern African countries.
- H<sub>a3</sub>** There is a statistically significant effect of government effectiveness on the level of foreign direct investments in selected Eastern African countries.
- H<sub>04</sub>** There is no statistically significant effect of regulatory quality on the level of foreign direct investments in selected Eastern African countries.
- H<sub>a4</sub>** There is a statistically significant effect of regulatory quality on the level of foreign direct investments in selected Eastern African countries.
- H<sub>05</sub>** There is no statistically significant effect of rule of law on the level of foreign direct investments in selected Eastern African countries.

**H<sub>a5</sub>** There is a statistically significant effect of rule of law on the level of foreign direct investments in selected Eastern African countries.

**H<sub>06</sub>** There is no statistically significant effect of control of corruption on the level of foreign direct investments in selected Eastern African countries.

**H<sub>a6</sub>** There is a statistically significant effect of control of corruption on the level of foreign direct investments in selected Eastern African countries.

### **1.5 Scope of the Study**

The study sought to examine the effect of institutional factors on the FDI inflows into selected Eastern African countries. The study used a quantitative approach and collect panel data on FDI inflows reported in Eastern Africa between 2005 and 2021. The study employed voice and accountability, political stability and absence of violence/terrorism, government effectiveness, regulatory quality, rule of law and control of corruption as the independent study variables and FDI inflows as the dependent variable. To explain the behaviour of investors in international markets, this study relied on the Ownership – Location – Internalization (OLI) Theory (Eclectic Paradigm) and the Institutional FDI Fitness theory.

### **1.6 Significance of the Study**

This study focused on the factors that influence FDI inflows. Its findings are key to directing various stakeholders seeking to increase the attractiveness of Eastern African countries as investment destinations.

#### **1.6.1 To Policy Makers**

East Africa has experienced a trend of decreasing investment in recent years and the region stands to benefit from policies that would increase its attractiveness to foreign investors. This study provides an extension of the understanding between foreign investment and institutional quality factors. Its findings are key to policy development, helping in the assessment of the policies that may have contributed to the negative FDI inflows trends and in suggesting policies that can restore confidence in East African economies. The findings will also be helpful in fiscal policy development which is key to determining a country's competitiveness.

#### **1.6.2 To Industry Players**

This study's findings are important to business groups by advocating for policies that promote growth, stability, and democratic participation, strengthening democracy, law & order. The study

shows the importance of institutional quality factors in attracting FDI. The study will help in guiding the regulation of capital market transactions and investments through policies that facilitate free capital movement. This study will also prove helpful to investors by identifying the suitable conditions for investment and the institutional factors that have a significant influence on returns from their investments.

### **1.6.3 To Scholars**

This study contributes to the research on foreign investment factors. The study identifies gaps that need to be addressed by future research and serves as reference material to future scholars investigating determinants of FDI inflows in developing economies.



## **1.7 Organization of the study**

An introduction to the study components was first presented, followed by a discussion of the institutional quality factors and FDI inflows into the Eastern Africa region, introducing the underlying relationships between the study variables. The statement of the problem was then introduced, as were the study objectives and the research hypothesis. The first chapter then concluded with the scope of the study and the significance of the study. The second chapter focused on the literature review which comprised of theoretical review, empirical review, research gaps and the conceptualization of the variables. The third chapter presented the methodology used in the study and the fourth chapter presented the findings of the study. The last chapter focused on the discussion, conclusions and recommendations drawn.



## CHAPTER TWO

### LITERATURE REVIEW

#### 2.1 Introduction

This chapter presented theoretical literature on FDI, a critical review of various empirical studies on FDI as well as a summary of the gaps. The chapter also presented the conceptual framework and the operationalization of the variables selected for the study.

#### 2.2 Theoretical Literature Review

The study was grounded on the work of Dunning (1980) and Rugman (1981) who proposed the Eclectic Paradigm or the Ownership – Location – Internalization (OLI) theory which determines the behaviour of businesses and organizations in pursuing FDI opportunities, and the work of Wilhelms (1998) who introduced the Institutional FDI Fitness theory.

##### 2.2.1 The Ownership – Location – Internalization (OLI) Theory (Eclectic Paradigm)

Rugman's (1981) internalization theory is considered the overarching theory explaining the existence and behaviour of multinational enterprises (MNEs). The theory provides an analytical framework through which International Business (IB) research utilizes in explaining the rationale behind international investments. This theory explains why firms would be willing to incur operational costs and face uncertain economic and political risks as well as expropriation in foreign jurisdictions (Muli & Aduda, 2017). The theory was first advanced by Buckley and Casson (1976) who explained that MNEs will enter new markets through the hierarchy rather than the market. It is an economic view whereby MNEs employed their superior efficiencies to address structural inefficiencies in the host country. Later, Hennart (1977, 1982) contributed to the theory by adding costs on transactions and enforcement that arose out of bounded rationality and opportunistic behaviour in markets. Hennart (1988, 2009) argues that MNEs will deploy their resources and exercise their strategic power over territories in a complementary way to bundle strategic assets. Hennart, Majocchi and Forlani (2017) have linked this viewpoint to the international expansion of small family firms which use economies of scale and enjoy asset bundling benefits.

Rugman (1981) presents a more firm-specific view in parallel to research leading to Wernerfelt (1984) and Barney's (1991) resource-based view (RBV) of the firm. Referring to the Ownership – Location – Internalization (OLI) framework (Dunning, 1980), Verbeke (2009) avers that the internationalization theory is based on the efficiency of firm-specific advantages (FSAs) such as

knowledge advantages, brand advantage, skills in management, and organizational capabilities. The OLI framework is an evaluation framework used when deciding whether to pursue foreign direct investment (FDI) goals. Rugman (1981) opines that these advantages can either encourage or discourage investment and that countries can refine certain aspects of their advantages to ease and attract investment. According to Rugman (1981), when the advantages of OLI exceed expected costs, foreigners will increase investment into a host nation.

In the OLI framework, ownership advantages are those firm-specific operational models, services, or products that other organizations cannot access (Rugman, 1981). These are reinforced by intellectual property rights. The locational advantages emerge from factors such as production cost, competition, market access and regional trade linkages. In making these considerations, MNEs consider whether it is more viable to set up a base of operations or export particular products (Kalii, 2021). Country policies, infrastructure and political factors take a significant consideration on land advantages and flexibility and stability are considered optimum. The internalization advantage emerges from the calculations on whether it would be more efficient to produce a particular product in-house against contracting with a 3rd party. This advantage speaks to the increasing number of joint ventures and start-ups that are some of the internationalization strategies that a company could pursue (Muli & Aduda, 2017).

This theory has been challenged for failing to adequately explain knowledge-based advantages considering intellectual property laws and the quality of institutions vary (Erminio & Rugman, 1996). However, according to Buckley and Casson (2011), the advantage of this model lies in its effectiveness in shifting in line with business behaviour. The scholars argue that the model is comprehensive and addresses emerging issues such as the strengthening of intellectual property laws over time and the decline in internalization. Therefore, it is adaptive and can address dynamic issues. The theory contributes to our understanding of how multinationals see boundaries and react based on internal competencies.

### **2.2.2 Institutional FDI Fitness Theory**

The Institutional FDI Fitness Theory theory was introduced by Wilhelms (1998) after inspiration from the Darwinian concept of the survival of the fittest. According to Wilhelms (1998), competitive advantage is a function of a country's institutions, policies and implementation, as opposed to generic variables such as natural resources. The term FDI Fitness refers to a country's

ability to attract, absorb and retain FDI and according to Wilhelms (1998), a country's fit to the internal and external expectations of its investors determines whether it has an upper-hand in harnessing FDI inflows. The theory has emerged as an important instrument in research seeking to explain the uneven distribution of FDI flows between countries. As per this study's stipulations, countries with high institutional fitness are more attractive to investors than countries with low institutional fitness. High institutional fitness shows the degree to which a country's institutions are transparent, well-functioning, reliable and predictable.

Wilhem's institutional FDI fitness theory is based on four fundamental pillars which include socio-cultural fitness, education, government and market. Wilhelms (1998) opined that socio-cultural factors are the oldest and the most basic of considerations followed by education which encompasses the quality of human capital. However, while education matters, it becomes a source of competitiveness if they match the skills and competencies needed for the undertaking of significant investment projects. Nevertheless, Popovici and Călin (2014) argue that basic education has significant impacts on a workforce's productivity and a more productive workforce is more attractive to investors. The market pillar accounts for financial markets as well as infrastructure and physical capital. The final pillar accounts for government fitness and it indicates the degree of control exerted by the government over its people and institutions. Government factors include factors such as freedom of speech, control of corruption, economic openness and exchange rate intervention. It also encompasses the policies enacted by the government and their impact on businesses and Wilhelms (1998) asserts that investors will shy away from countries with political instability and low rule of law.

The institutional FDI fitness theory has been empirically tested in previous research. Awadhi, James and Byaro (2022) used the theory when examining the influence of Institutional Development on FDI in sub-Saharan Africa and affirmed that out of six governance indicators, only the rule of law and government effectiveness have positive impacts on FDI inflows in sub-Saharan Africa. Ghana's Osei-Attakora (2022) argues that the rule of law moderates the relationship between politics and FDI inflows to Ghana while according to Matima (2021), political risk and weak institutional quality have had negative impacts on FDI in Sub-Saharan Africa. FDI Fitness Institutions interact in varying forms to influence one another with the overall outcome being the volume of FDI inflows. This theory explained the country-specific factors that influence FDI inflows.

## **2.3 Empirical Literature Review**

### **2.3.1 Voice and Accountability and Foreign Direct Investment**

As an institutional quality factor, voice and accountability are concerned with the degree to which a government allows its citizens to hold it accountable for its policies. Accountable governments are more responsive to the concerns raised by their citizens while less-responsive governments pay little attention to the needs and preferences of their citizens and are more susceptible to resource misallocation, favouritism in resource allocation and cronyism.

These observations are made in the study by Semenas (2020) who researched the relationship between governance and FDI in emerging markets. The study used six governance factors and a set of control variables comprising Gross Domestic Product (GDP), inflation, labour force participation rate and trade openness. The study used a dynamic panel data model with a systems Generalized Method of Moments (GMM) in analysis revealing that governance indicators as well as the macroeconomic factors all influence FDI inflows into emerging countries. Voice and accountability, political stability, regulatory quality and control of corruption were determined to improve FDI inflows while factors such as poor protection of property rights may create opportunities for corruption. The study called on governments to allow their citizens to express themselves through text and speech, as well as participate in selecting the government. This study examined only governance; the current study included multiple indicators and add control variables.

In Pakistan, Nadeem, Jiao, Nawaz and Younis (2020) observed that voice and accountability have significant impacts on foreign investment in terms of innovation. The research which applied the Autoregressive Distributed Lag (ARDL) approach to cointegration also assessed whether terrorism, infrastructure, and savings influence innovation in the country. The study asserts that investors do not always consider voice and accountability when planning to invest as they also consider the frequency of terrorism, infrastructure, and savings capabilities of the population. This study used only two indicators of governance while the current research expanded the scope to six indicators.

Munjil, Varma and Bhatnagar (2022) also confirmed that host country factors play a key role in the decisions of foreign investors in their comparative analysis of the impact of a host country's voice and accountability, as well as governance standards on investment from India and China.

The study collected data on FDI flows into Africa from China and India from 2008 to 2018 and applied a probit regression model revealing that the quality of governance has significant impacts on the investment decisions of Indian investors but insignificant impacts on investment among Chinese investors. These findings suggest that countries in alliances with the Indian government should strive to improve governance by guaranteeing free speech, media independence and high standards of accountability as well as control of corruption which complements voice and accountability factors. This study specified investment drivers for Chinese and Indian firms in a quest to gain economic supremacy in Africa.

Elsewhere, Saha, Sadekin and Saha (2022) sourced panel data reported between 2002 and 2018 from 28 lower-middle-income countries in an examination of the effect of IQ factors on FDI inflows. The analysis involved dynamic panel estimations using the two-step system GMM. From the analysis, while quality regulations and degree of control of corruption attract FDI inflows, having a high degree of accountability and rule of law in lower-middle income countries has mitigating effects. This study differs from the current having researched a wider dataset while the current study focussed on one region.

Furthermore, Bouchoucha and Benammou (2020) sampled 41 African countries in an analysis of the effect of governance factors on destination attractiveness. The study used the static panel data approach and the dynamic panel approach GMM. From the analysis, the researcher affirms that democratic African countries that can demonstrate the ability to guarantee freedom of speech, control corruption, design and implement effective policies and promote accountability are attractive investment destinations. The implication is that freedom and accountability are factors that indicate a country's ability to establish good governance practices.

Bosire (2019) casts doubt on the effectiveness of governance factors on FDI inflows into Eastern Africa. The study used generalized least squares on panel data reported between 2002 and 2016 from 12 countries and conceptualized governance into the rule of law, voice and accountability, control of corruption, political stability, and absence of violence. The analysis asserted that on their own, governance indicators do not necessarily predict the flow of FDI into the Eastern African region. However, with natural resources, open markets and labour forces, the relationship becomes significant. The study thus called on countries to institute policies guaranteeing trade freedom, a stable political environment and security for both life and property.

### **2.3.2 Political Stability and Absence of Violence/Terrorism and Foreign Direct Investment**

Noting an increase in the number of terrorist attacks, Ari and Ibrahim (2021) researched the effect of terrorism incidences on FDI inflows into Turkey. The study used data on FDI inflows from 1990 to 2019 and employed the Autoregressive Distributed Lag (ARDL) bounds co-integration testing approach. From the analysis, in the short run, terrorism does not have a significant effect on FDI, but in the long run, has a negative impact. Regarding other supportive variables, the degree of trade openness has negative and significant impacts on FDI while military expenditure had positive effects on FDI flows but only in the long run. This study implies that military spending does not necessarily attract foreign investors to the host country but was based on the ARDL approach while the current assesses the relationship using the panel regression methodology.

Kambou and Khariss (2020) carried out a similar exploration but focused on Burkina Faso where extremism has been reported in recent years. The study sought the effect of terrorism on FDI and relied on data reported over three years between 2015 and 2018. Using ordinary least squares (OLS) in analysis, the study asserts that the prevalence of terrorist activities has a significant negative impact on FDI and the country's economic growth. This study did not consider the role of the media in shaping investor decisions.

On the other hand, Shen (2020) chose to focus on China in the assessment of the factors impacting FDI investment in the country. The research specified economic, political and immigration factors and collected panel data reported between 2000 and 2019 on Gross Domestic Product (GDP), producer price index (PPI) and economic policy uncertainty (EPU), with data on immigration numbers from 1986 being utilized. Using regressions in analysis, the study's findings were that the studied factors all positively impacted FDI in China. Economic uncertainty created by the Chinese government's artificial devaluation increased the volume of investments in the country, suggesting the large Chinese market mediates the relationship between economic uncertainty risks and FDI. This data emerged from China where the government plays a significant role in controlling the firms.

A study on Pakistan by Azam, Nawaz and Riaz (2019) sought after the influence of specific IQ factors on FDI inflows, with a specific focus on the impacts of terrorism occurrence, incidences of violence and corruption. The study utilised data reported between 1973 and 2017 and relied on autoregressive distributed lag (ARDL) bound testing in analysis. The findings were that quality

factors such as control of corruption and terrorism have significant negative impacts on FDI inflows but that the large market size of Pakistan forms the main source of attraction. These findings show that the country can increase its attractiveness by addressing corruption and security challenges. This study's data was from Pakistan and only addressed the impact of the political environment in the country.

Meah, Onono and Ocharo (2016) affirm that the evidence on the role of IQ factors on FDI in Kenya is scant in a study that focused on the effect of IQ and structural breaks on FDI inflows and economic growth in Kenya. The study also relied on the OLS method in data analysis and the findings revealed significant positive effects of institutional quality and private investment on FDI while political risk, terrorism and personal consumption levels were determined to discourage investors. The recommendations are for the government to ensure the institutions are functioning properly, laws are enacted and enforced to guide business transactions and the power transition remains stable to ensure sustainable FDI-led development. The study specified Kenya only while the current study collected data from different countries to draw more robust conclusions.

### **2.3.3 Regulatory Quality and Foreign Direct Investment**

Bhasin and Garg (2020) focused on developing economies in their analysis of the impact of the institutional environment on inward FDI. The study collected data reported between 2006 and 2015 and employed panel data regressions (fixed effects) in the analysis. The study proxied institutional pillars using regulatory efficiency, the rule of law and the normative institutional environment. Principal component analysis was applied to the data revealing a negative impact of the rule of law and the local normative environment. However, FDI volume increases when a country has effective regulatory power. The findings from this study imply that foreign investors sought to take advantage of weak laws, norms and values but will also invest when the enabling environment is favourable and has minimal tax burdens. This study selected developing economies with similar levels of development.

In seeking to address the link between institutional quality and FDI in Africa, Appiah-Kubi et al., (2020) collected panel data reported from 17 West African countries. The study collected ten-year data ending 2018 on corporate governance structures and obligations and used the system GMM in analysis. From the analysis, exhibiting a high degree of ethical values and the ability to protect the interests of non-controlling parties progressively increases FDI. Interestingly, regulations in

securities and the stock exchange had insignificant impacts on FDI. Recommendations were for countries striving to increase FDI to focus on strengthening the independence of their institutions and empowering them through policy-backed concessions. This study did not consider the impact of institutional factors such as corruption and freedom of the press which can impact the effect of governance on investor trust in an investment destination.

Uddin, Chowdhury, Zafar, Shafique and Liu (2019) explored institutional determinants of inward FDI in Pakistan. The study used data reported since 2003 and applied correlation methods using regression analysis. The analysis asserts that the country, being the sixth most populous in the world has a large receptive market but weak governance scores, especially at the basic level. The researchers observe that the government's size, legal structure and property rights protection, and adherence to free trade practices and representation all influence FDI inflows as they are directly associated with regulations of labour markets and credit markets, which was identified as the most significant determinant of FDI inflows. These findings are from Pakistan while the current study collected data from Eastern African states.

Aziz (2018) carried out an empirical examination into the impact of IQ factors on FDI attraction in the Middle East, noting the importance of operating environment factors on FDI. The study relied on system GMM estimation in analysing data reported by 16 countries from 1984–2012. Findings were that economic freedom, ease of doing business and international country risk all positively impact FDI inflows in the Arabian region. The study also reveals that the presence of supportive policies and successful foreign multinationals also encourage FDI inflows. These findings are from Middle Eastern countries with potentially limited applicability to Eastern Africa.

Peres et al. (2018) conducted a study to analyse the impact of the quality of institutions on FDI inflows in developed and developing countries. Institutional quality is measured using the sum of control of corruption and the rule of law. The study used panel data and the generalized method of moments was used in the analysis. The findings were that while institutional quality attracts FDI in developing countries, the impact is not significant since the countries have weaker institutional frameworks. The study recommends developing countries take steps to ensure their institutions are competent and supported by quality policies and a high degree of independence. This study aggregated data from developed countries.

#### **2.3.4 Control of Corruption and Foreign Direct Investment**

Control over corruption reflects a government's formal mechanisms for the efficient functioning of bureaucratic structures in a country. Control of corruption variables present a greater view of transparency in the governance of a country. In this vein, Raza, Shah and Arif (2021) focused on the factors affecting investment attraction in the Organisation for Economic Co-operation and Development (OECD) countries with a specific focus on the presence of good governance systems. The study specified the period between 1996 and 2013 and used the fixed model GMM in analysis and reveals that all the governance indicators improve economic growth. The study also affirmed that while regulatory quality has a bidirectional causal relationship with FDI and economic growth, corruption control, government effectiveness, political stability as well as voice and accountability all have a unidirectional relationship. The researchers called on poorer countries to strengthen policies related to corruption control such as reporting and penalties for those prosecuted for corruption.

Adeel-Farooq, Khan, Nawaz and Akram (2020) investigated the IQ-FDI relationship using data on governance quality among South Asian Association for Regional Cooperation (SAARC) countries. The study collected time series data reported between 2002 and 2017 and relied on the random effects and fixed effects model. The analysis involved the robust least square (RLS) method, and the findings were that while governance, control of corruption, financial development and contractual obligations enforcement are positively related to FDI inflow, poor governance results in the inability to control corruption and facilitate financial development, highlighting the need for better governance policies. This study used two measures of IQ while the current will include the role of political stability and absence of violence, as well as voice and accountability factors on the institutions' quality.

While control of corruption may increase investment attractiveness according to much of the reviewed literature, in Nigeria, Omodero (2019) makes the opposite observation. The research specified the effect of corruption on FDI inflows and relied on data reported between 1996 and 2017. Ordinary Least Squares were used to carry out the multiple regression analysis with the findings indicating that in the country, higher scores in the corruption perception index attract foreign investors. The researcher attributes this to the potential benefits of natural resources and argues that the benefits may not last into the future and without improving oversight and regulatory

oversight, Nigeria ceased to be an attractive destination for foreigners. This study researched corruption control as the only institutional quality.

In Zimbabwe, the government's inability to control corruption was identified as one of the most significant hindrances to FDI inflows. In the study, Muzurura (2016) applied mixed methods in the analysis of cross-sectional time series data reported over thirty years ending in 2011. The study asserts that in addition to control of corruption scores, lack of trade openness, inconsistent government policies, political instability and poor governance contribute to the unattractiveness of the country as an investment destination. Shisya (2021) sought to establish the link between the scope of transparency factors and FDI investment. The study specified the role of information access and regional integration. The study reports that corruption and bribery, absence of property rights protection, bureaucratic inefficiency, disregard for the rule of law and unpredictable policy variations contribute to the lack of information transparency which discourages foreign investment as it illustrates a lack of openness. This study only assessed transparency factors while the current study added more measures of institutional quality.

### **2.3.5 Rule of Law and Trade Openness and Foreign Direct Investment**

Rule of law captures perceptions of the extent to which agents have confidence in and abide by the rules of society, and in particular the quality of contract enforcement, property rights, the police, and the courts, as well as the likelihood of crime and violence. Chen and Jiang (2022) used a sample comprising 42 countries in an analysis of the impact of institutional quality (IQ) on FDI inflows and utilized a fixed-effect model in the analysis of panel data reported between 2000 and 2020. The analysis revealed a significant impact of institutional quality on FDI inflows, with a higher quality of institutions increasing FDI through trade openness, quality industrial structures and facilitation of technology competency transfer. Investment increased with improved financial sectors as well as with the availability of natural resources. This research collected data from multiple countries while the current will utilize data from fewer countries which share certain infrastructures.

Contractor, et al. (2020) used the institutional theory and the theory of economic regulations in their analysis of the effect of country regulations and business environment on FDI inflows. The analysis which investigated specific aspects of a firm's life cycle revealed that multinationals are attracted to countries with stronger contract enforcement and more efficient international trade

regulations. Tag (2021) specified the role of judicial contract enforcement, judicial independence, and judicial impartiality on FDI inflows by sampling data reported from 150 countries. The study applied the system-GMM estimation approach, and the results revealed that while judicial independence and impartiality increase FDI net inflows, contract enforcement had insignificant impacts in developed economies. The study underscored the importance of unbundling institutions to better understand how they impact investment decisions. This study collected data from a mix of multiple countries at different levels of development.

In another study on the relationship between local institutions and FDI, Comi, Grasseni and Resmini (2021) investigated the effect of the efficiency of the judicial system on FDI attraction across administrative regions in Italy. The study reveals that poor contract enforcement discourages multinational investment. Further, the study asserts that this effect varies depending on the investor's industry as firms in the information and knowledge-intensive sectors were more responsive to efficient jurisdictions. This study was specific to the Italian judicial system and its efficiency.

In attempting to establish a more country-specific link between IQ and FDI, Yakubu (2020) collected data from Ghana. The study relied on the ARDL approach in examining the relationship between IQ and FDI as it used long-term data reported from 1985 to 2016. The bounds-testing cointegration and ARDL framework findings suggest a long-term link between IQ factors and FDI attraction. This study failed to assess how other IQ factors such as political stability, legal transparency, regulatory reforms and control of corruption affect the strength of institutions and; hence investor attraction.

Affirming increased efforts by the Egyptian government to attract high-technology foreign investment, Karamali (2020) carried out an empirical analysis of the conditions necessary for FDI attraction, retention, and optimization. The study reports that institutional inefficiencies have had significant impacts on the country's inability to meet its investment objectives including lack of transparency, delays in judicial complaints and intellectual property rights enforcement, and high instances of breach of contract. Further, legal restrictions placed on foreign firms and entry requirements have had negative impacts on multinationals' confidence in the country's operating environment (operational sustainability and growth). This study did not specify how institutional quality factors affect FDI in the country.

### **2.3.6 Government Effectiveness and Foreign Direct Investment**

Effective governments improve the efficiency of operations and can improve the success rate of businesses. The government effectiveness variable captures perceptions that investors have regarding the quality of public services, civil service and the degree of independence of institutions from political pressures (Paul & Jadhav, 2019). In research on the impact of effective governance on China's outward FDI, Li, Luo and De Vita (2020) provide evidence that the higher the institutional differences in the level of government effectiveness and control of corruption between China and a host country, the lower the volume of China's outward FDI. The study asserts that countries seeking China's FDI should align themselves with the country's effectiveness measures and policies. Huang, Meng, Chen and Liu (2022) also examined China's attraction factors in an examination which used the difference-in-difference method in assessing whether administrative simplification has a positive impact on outward FDI. The analysis revealed that the relationship is significant and that factors such as the presence of approval authorities can increase FDI.

Shah, Kamal, Hasnat and Jiang (2019) used a different unique approach in their investigation, focusing on whether institutional differences affect Chinese outward FDI by seeking evidence from non-resource-rich and resource-rich host nations. The analysis reveals that while the institutional differences between China and host countries have insignificant effects on outward FDI, Chinese firms are most likely to respond to institutional difference factors in countries without fuel resources. This provides insight into the priority factors for investing countries and enables host countries to evaluate the value of their resources. This study used natural resources as control variables.

Muhammad and Khan (2022) studied the link between IQ, natural resources and outward FDI from G7 countries to OECD countries. The analysis which investigated data reported from 37 countries on investments made between 2009 and 2017 reveals that while IQ factors of OECD do have an impact on FDI inflows, G7 investors were more receptive to OECD countries with quality institutions as well as resources. These studies specified investment from China, Japan and OECD countries. The current study did not discriminate based on individual investors to negate the effect of country relationships.

In Japan, Chiappini and Viaud (2021) provide evidence that while industry characteristics such as technological capability and labour costs contribute to FDI, differences in perception of

institutional power, control of corruption, and financial systems strength are also key considerations. The study used a gravity model in the analysis of data from 30 countries hosting Japanese firms. This study specified investment into manufacturing firms while the current expanded the scope to all foreign direct investments. Duanmu (2014) also sought after the role of strong institutions and policies on FDI outflows but focused on BRIC countries (Brazil, Russia, India and China). The study specified the role of labour law enforcement and its impact on location choice. The study asserts that while lower labour standards may attract FDI, the effect is insignificant and other factors such as previous trading relations and capital mobility were more influential. The study called on recipient countries to formulate more policies encouraging capital mobility, both human and physical.

Buitrago and Barbosa (2020) investigated the relationship between emerging host country institutions and outward FDI in an exploratory study. The study collected data from 48 countries and applied factor analysis with the findings finding a strong link between the study variables. Indications were that the extent of institutional transparency and commitment to research and development and innovation encourages outward FDI, while inequality and the level of development of financial markets have the opposite effect. Conclusions were that inability to guarantee stability, tackle corruption, and follow through on contracts, as well as poor economic liberalization, regulatory environment and societal culture all discourage FDI inflows. Kayani and Ganic (2021) researched the factors that influence inward FDI in China and relied on the GMM method in the analysis. Findings were that while governance components such as control of corruption, rule of law, and regulatory quality increase FDI inflows, government effectiveness, political stability, and voice & accountability had insignificant effects. The study based its findings on a country with a one-party state and findings may not be widely applicable to countries with different political systems.

## **2.4 Summary of Research Gaps**

The review points to varying effects of different institutional quality factors on FDI inflows in different regions around the world. The overall takeaway is that foreign investors mostly adhere to the internalization theory and leverage organizational resources and consider cost-benefit implications when expanding into foreign territory. The gaps that emerged are identified in Table 2.1.

**Table 2.1 Literature Gaps**

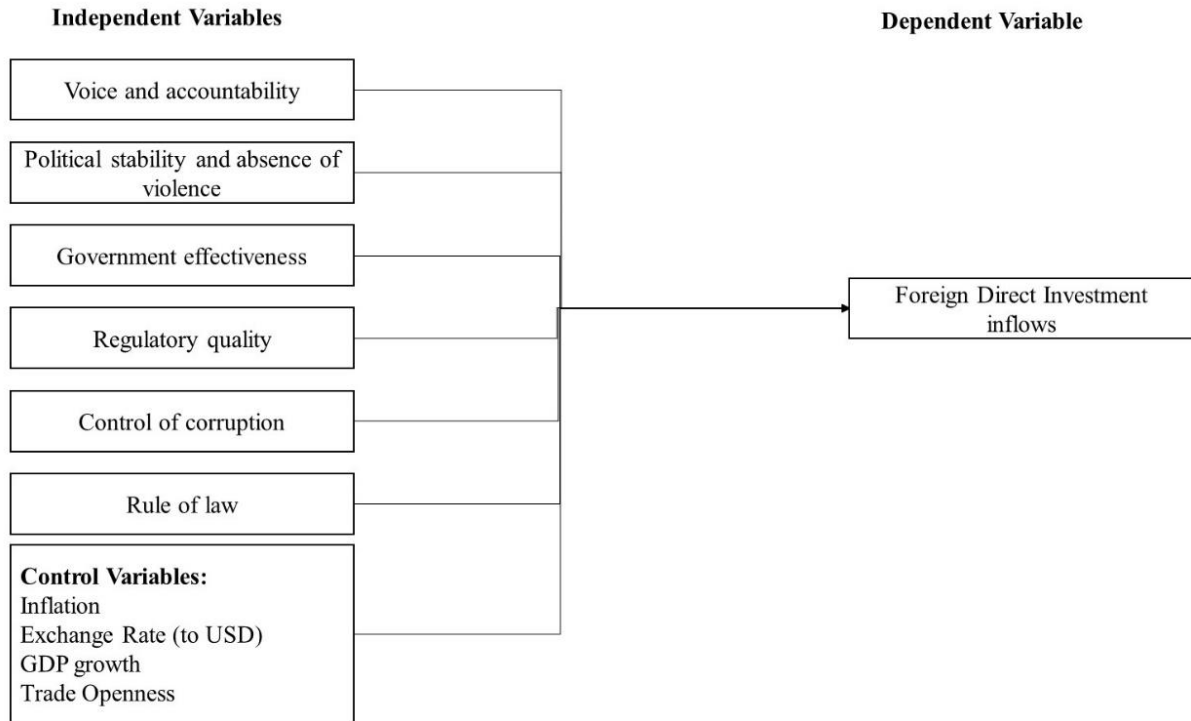
<b>Author</b>	<b>Title</b>	<b>Findings</b>	<b>Research Gap</b>
Huynh (2020)	Foreign direct investment and income inequality: Does institutional quality matter?	There exists a bidirectional relationship between IQ and FDI	This study relied on the two-step System GMM that compared data from middle- and upper-income countries while the current study focuses on lower-middle-income countries.
Chen and Jiang (2022)	The impact of institutional quality on foreign direct investment: an empirical analysis based on mediating and moderating effects	Higher quality of institutions increases FDI through trade openness, industrial structures and facilitation of technology competency transfer.	This study is from China, a large economy that uses market power to attract investors while the current specifies developing economies.
Uddin, Chowdhury, Zafar, Shafique and Liu (2019)	Institutional determinants of inward FDI: Evidence from Pakistan.	The government's size, legal structure and property rights protection, and adherence to free trade practices and representation all influence FDI inflows	Pakistan has been highly unstable and findings from the country may not be representative of other countries.
Omodero (2019)	Effect of corruption on foreign direct investment inflows in Nigeria	Higher scores in the corruption perception index attract foreign investors.	This study utilised one measure of IQ, control of corruption. The current study was enhanced through an analysis of multiple IQ factors.
Peres et al. (2018)	The impact of institutional quality	In developed countries, stronger control of	This study collected data from countries at

<b>Author</b>	<b>Title</b>	<b>Findings</b>	<b>Research Gap</b>
	on foreign direct investment inflows: evidence for developed and developing countries.	corruption and a stable rule of law increase FDI inflows while in developing countries, governance discourages FDI.	different levels of development while the current study examined data from a group of developing countries with similar development goals.
Bhasin and Garg (2020)	Impact of institutional environment on inward FDI: A case of select emerging market economies	There exists a negative impact of the rule of law and the local normative environment while FDI inflows increase when a country has effective regulatory power.	The study operationalized IQ using only regulatory efficiency, the rule of law and the normative institutional environment while the current study included additional indicators of institutional quality.
Hayat (2019)	Foreign direct investments, institutional quality, and economic growth	IQ factors and FDI all have positive impacts on economic growth. However, FDI-driven economic growth was only observed in low and middle-income countries where increasing regulation scores attract investors.	The study used a large panel dataset covering 104 countries which can skew the findings when investigating IQ factors specific to smaller regions.
Meah, Onono and Ocharo (2016)	Foreign direct investment, institutional quality and economic growth in Kenya.	There are significant positive effects of institutional quality and private investment on FDI while political risk, terrorism and personal consumption levels discourage investors.	The study specified Kenya only while the current study collected and data from different countries to draw more robust conclusions.

Author	Title	Findings	Research Gap
Appiah-Kubi et al., (2020)	The impact of corporate governance structures on foreign direct investment: A case study of West African countries.	A high degree of ethical values and the ability to protect the interests of non-controlling parties progressively increases FDI	This study did not consider the impact of institutional factors such as corruption and the freedom of the press which can impact the effect of governance on investor trust.
Bosire (2019)	Foreign Direct Investments into Eastern Africa region: The governance paradox	On their own, governance indicators do not necessarily predict the flow of FDI into the Eastern Africa region, however, controlling for the availability of natural resources, exports, imports and labour force, there is a significant relationship	The study focused on 12 countries in the greater Eastern Africa region over the period 2002 to 2016. The current study uses more current data.

## 2.5 Conceptual Framework

According to Green (2014), conceptual frameworks are structured from a set of broad ideas and theories that help a researcher to properly identify the problem they are looking at, frame their questions and find suitable literature. The conceptual framework in Figure 2.1 shows the interaction between the selected institutional quality index selected and the flow of foreign direct investment.



**Figure 2.1 Conceptual Framework**

Source: Researcher (2023)

The conceptual framework above shows how the selected institutional quality factors are hypothesized to influence the level of foreign direct investment within selected countries in Eastern Africa. The variables were operationalized as shown in Table 2.2.

**Table 2.2 Operationalization of Variables**

Variable	Indicator	Measurement	Source of Data
Voice and accountability	Voice and accountability score in the institutional quality index by the World Bank	Percentile rank (0-100) Time series data (2005-2021)	World Bank Governance Indicators Report for each Country
Political Stability	Political stability score in the institutional quality index by the World Bank	Percentile rank (0-100) Time series data (2005-2021)	World Bank Governance Indicators Report for each Country

<b>Variable</b>	<b>Indicator</b>	<b>Measurement</b>	<b>Source of Data</b>
Government effectiveness	Government effectiveness score in the institutional quality index by the World Bank	Percentile rank (0-100) Time series data (2005-2021)	World Bank Governance Indicators Report for each Country
Regulatory quality	Regulatory score in the institutional quality index by the World Bank	Percentile rank (0-100) Time series data (2005-2021)	World Bank Governance Indicators Report for each Country
Control of corruption	Control of corruption score in the institutional quality index by the World Bank	Percentile rank (0-100) Time series data (2005-2021)	World Bank Governance Indicators Report for each Country
Rule of law	Rule of law index score in the institutional quality index by the World Bank	Percentile rank (0-100) Time series data (2005-2021)	World Bank Governance Indicators Report for each Country
Controls	Assessing other factors impacting FDI (Inflation, GDP, Exchange rate, trade openness)	Time series (2005-2021) Scale value based on Central Bank Data and World Bank Development Indicators	Central Bank Data from Individual Countries
Foreign direct investment	Net FDI inflows into East Africa (by country)	Time series data (2005-2021) Scale value (log of Net FDI inflow)	World Bank Indicators Database for each Country

World Bank Governance Indicators scale ranges from: (0 = low to 100 = high)

Source: Researcher (2023)

## CHAPTER THREE

### RESEARCH METHODOLOGY

#### 3.1 Introduction

This chapter examined the various methodological techniques that were employed in attempting to solve the research problem. Areas covered included the research philosophy, the design, the population of interest, and data collection instruments. Research procedures, diagnostic tests as well as data analysis and presentation of the findings were also captured. Lastly, the various ethical guidelines observed during the study were presented.

#### 3.2 Research Philosophy

Research philosophy relates to the development of knowledge and the nature of that knowledge and contains important assumptions about how researchers view the world (Bryman & Bell, 2007). research approach or methodology used in the study was grounded in positivism. Positivism is a philosophical perspective that emphasizes objective knowledge, observable phenomena, and the use of empirical data for analysis. In this context, the research focused on quantitative analysis, which involves the measurement and numerical representation of variables and the examination of their relationships. (Ghuri, Grønhaug, & Strange, 2020). Thus, this philosophy was deemed adequate in meeting the requirements for the current research. Furthermore, the philosophy supports using scientific research methods to generate accurate, verifiable, systematic, and theoretical responses to the study's hypothesis.

#### 3.3 Research Design

Walliman (2010) defines a research design as a blueprint for conducting a study with maximum control over factors that may interfere with the validity of the findings. Pickard (2013) defined research design as an overall framework or a plan for investigation and a logical model of proof that guides the investigator in the various stages of research. This study was quantitative hence adopting an appropriate design that supported the aims of this study is key to establishing the relationship between the various objectives adopted in this study (Newby, 2014). A correlational research design was used in this study as it supports the utilization of quantitative techniques for the examination of how the selected research variables interact.

### **3.4 Target Population**

A population is defined as the entire collection of components from which inferences may be made, and it refers to all potentially interesting instances for a research study (Ghauri, Grønhaug, & Strange, 2020). A population, according to Walliman (2010) is a big group of all persons from whom a sample is taken. The population for this study was drawn from Eastern African countries namely; Kenya, Tanzania, Uganda, Burundi, Rwanda and Ethiopia. South Sudan was excluded from the analysis owing to a lack of data over the study period. The countries were selected for this study as they represent the specific bloc that is of interest to this research in establishing how the selected institutional quality dimensions have impacted the inflow of foreign direct investment in the bloc. This ensured that collected information was relevant to meeting the research objectives as well as developing relevant inferences that can be critical to policy guidance in the bloc.

### **3.5 Data Collection Instruments**

Data collection refers to the gathering of data to conduct analysis and make inferences from the data (Pickard, 2013). This study used secondary research data that was extracted from the selected countries' institutional quality indicators, foreign direct investment inflows and the countries' macroeconomic data. The selected research data was extracted using the form presented in Appendix I. The sources for the research data were the published World Bank Governance Index reports for the period 2005-2021, the World Bank Development Indicators Database as well as Central Bank data on the control variables for each of the targeted countries. The utilization of secondary data was supported by the nature of the information required for the current study as well as the measurements of the selected variables.

### **3.6 Data Collection Procedure**

The study ensured that necessary guidelines were observed. One, the research supervisor's approval was required before the submission of the proposal to the institution for authorization to proceed to the data collection phase. Secondly, a permit from the Institutional Ethical Review Board was acquired before proceeding to conduct the data extraction. Necessary approval was sought from the National Commission for Science Technology and Innovation. The study ensured that all the extracted research data was only applied to meet the stated academic objectives. Before the extraction of the research data, the extraction tool was reviewed with the assistance of the research supervisor to ensure that it met the operationalization adopted in the study and covered all the objectives of the research.

### **3.7 Diagnostic Tests**

The study data collected was a panel in nature hence it was necessary to conduct various diagnostic tests to ensure the data used met the requirements for panel regression analysis. The tests described in the subsequent sections were adopted in this study.

#### **3.7.1 Autocorrelation Test**

The term autocorrelation may be defined as a correlation between members of a series of observations ordered in time as in time series data or space as in cross-sectional data. The presence of serial correlation would be a clear indication that the variables in the model violate the assumptions of the regression (Honner et al., 2004). The study adopted the Durbin-Watson test to determine the correlation. The test standard is that the Durbin-Watson statistics should be between 1.5-2.5 to ensure there is no violation of the autocorrelation problem.

#### **3.7.2 Multicollinearity Test**

Multicollinearity was conducted to see the inter-correlations among all pairs of predictors and determine whether multicollinearity is likely to be a problem (Ullah, Aslam, Altaf, & Ahmed, 2019). In case of any presence of multicollinearity, Field (2009) recommends combining the variables into a composite variable or deleting one or more of the highly correlated ones. In this study, the collinearity tests were conducted using the Variance Inflation Factor and the Tolerance values. As a rule, the VIF value should not be above 10 and the Tolerance Value needs to be above 0.1.

#### **3.7.3 Normality Test**

The normality assumption is necessary for the conduction of single or joint hypothesis testing on the model parameters (Ghasemi & Zahediasl, 2012). The research relied on the skewness and kurtosis tests for normality checks. Burdinski (2000) opined that skewness fall between  $-3$  and  $+3$ , and kurtosis is appropriate from a range of  $-10$  to  $+10$  to result in an asymmetrical normal curve.

#### **3.7.4 Stationarity Test**

The nature of the time series data prompted the stationarity test. Unit root tests were carried out on all the study variables (Hadri & Kurozumi, 2012). The Augmented Dickey-Fuller (ADF) test was executed to test the time-series properties of the data series (Ghasemi & Zahediasl, 2012). The ADF tests the null hypothesis of non-stationarity against the alternative hypothesis of stationarity.

The rejection criterion is that if the ADF statistic is less than the  $p$ -value at a 5% level of significance, then the null hypothesis is rejected.

*H<sub>0</sub>*: The variable is non-stationary (i.e., it has a unit root)

*H<sub>a</sub>*: The variable is stationary (i.e., it has no unit root)

### **3.7.5 Hausman Specification Test**

Hausman specification test estimates the steadiness of an estimator compared to an alternate estimator (Hausman & Taylor, 1981). The Hausman test was used to test the random effect and fixed effect. The difference between random effect and fixed effects is whether the unnoticed individual effect represented fundamentals that are correlated with the independent variables within the regression model (Pace & LeSage, 2008). The test uses a null hypothesis that the preferred model is the random effect model. A Chi-square statistic  $p$ -value of the Hausman test less than 0.05 would imply that the preferred model is the random effect model (Torres-Reyna, 2007); a value above 0.05 leads to the adoption of the fixed model in the analysis.

### **3.7.6 Panel Cointegration Test**

Cointegration tests are performed where time series data are nonstationary to determine the extent to which the variables have a stable, long-run relationship (Pedroni, 1999). The Pedroni test uses seven-panel cointegration statistics allowing for analysis of fixed effects and deterministic trends, estimates of residual effects and deviations from the long-run relationship between variables (Bildirici, 2004). The cointegration test tests the null hypothesis of non-cointegration against the alternative hypothesis of cointegration. The rejection criterion is that if the calculated test statistic is smaller than the tabulated critical value, reject the null hypothesis (Bildirici, 2004).

## **3.8 Data Analysis and Presentation**

The study applied the generalized method of moments (GMM) to the dynamic panel in the estimation of the interaction between the selected research variables. The research data was extracted using a Microsoft Excel file and edited before exporting the data to Stata 16 for quantitative analysis. The study used descriptive tests; means, maximum, minimum, standard deviation, sum and the number of observations in presenting the summary of the research data. Secondly, correlation analysis was applied to establish the relationship between the selected variables using the Pearson correlation technique. Panel regression analysis was applied to determine the relationship between the predictor variables and the dependent variable foreign

direct investment. The findings were presented using tables. The following panel regression model was used in the research;

$$FDI = \beta_0 + \beta_1 VA_{it} + \beta_2 PSAV_{it} + \beta_3 RQ_{it} + \beta_4 CC_{it} + \beta_5 RLW_{it} + \beta_6 GE_{it} + \beta_7 IF_{it} + \beta_8 ER_{it} + \beta_9 GDP_{it} + \beta_{10} TO_{it} + \varepsilon \dots\dots\dots$$

Where;

FDI is the level of foreign direct investment inflows in Eastern African countries.

VA is the level of voice and accountability in Eastern African countries.

PSAV represents the level of political stability and absence of violence in Eastern African countries.

RQ is the level of regulatory quality in Eastern African countries.

CC is the determinant level of control and corruption in Eastern African countries.

RLW is the level of rule of law in Eastern African countries.

GE is the level of government effectiveness in Eastern African countries.

IF is the inflation level in each country (Kenya, Tanzania, Uganda, Burundi, Rwanda and Ethiopia).

ER represents the exchange rate against the USD in each country (Kenya, Tanzania, Uganda, Burundi, Rwanda and Ethiopia).

GDP represents the gross domestic product level in each country (Kenya, Tanzania, Uganda, Burundi, Rwanda and Ethiopia)

TO represents the level of trade openness in each country (Kenya, Tanzania, Uganda, Burundi, Rwanda and Ethiopia).

$\beta_0$  is the constant associated with regression models.

$\varepsilon$  is the error term of the model applied.

The index  $i$  denotes the cross section (the various countries in the panel) and  $t$  the time periods in the panel.

## CHAPTER FOUR

### PRESENTATION OF RESEARCH FINDINGS

#### 4.1 Introduction

Study findings from the analysis of the collected quantitative panel data are presented. The chapter comprises a summary of research observations, diagnostic tests, correlation tests and the panel regression analysis.

#### 4.2 Summary of Extracted Research Data

The study focused on extracting research data for selected Eastern African countries between 2005-2021. The period was selected due to currency and availability of data. The research excluded South Sudan in the extracted observations of the study owing to a lack of data (a large part of the period covered in the study coincided with the period when South Sudan had not yet attained independence). Thus, to ensure a balanced panel, observations for the country were not taken into consideration in this research. The summary of the analysis is presented using means showing the arithmetic averages, maximum, minimum and standard deviation as shown in Table 4.1.

The variables were assessed based on the percentile rank provided by World Bank as follows; Government Effectiveness captures perceptions of the quality of public services, the quality of the civil service and the degree of its independence from political pressures; Control of Corruption captures perceptions of the extent to which public power is exercised for private gain, including both petty and grand forms of corruption, as well as "capture" of the state by elites and private interests; Political Stability and Absence of Violence/Terrorism measures perceptions of the likelihood of political instability and/or politically-motivated violence, including terrorism; Regulatory Quality captures perceptions of the ability of the government to formulate and implement sound policies and regulations that permit and promote private sector development; Rule of Law captures perceptions of the extent to which agents have confidence in and abide by the rules of society, and in particular the quality of contract enforcement, property rights, the police, and the courts, as well as the likelihood of crime and violence; Voice and Accountability captures perceptions of the extent to which a country's citizens are able to participate in selecting their government, as well as freedom of expression, freedom of association, and a free media. The controls variables were assessed based on the percentage ranks of individual factors across the selected countries. The percentile ranks for each indicator range from 0 (lowest) to 100 (highest).

For FDI inflows, the natural log was used transforming the original variable into a new scale to avoid skewing the data given the vast difference in scale between FDI and all the other variables.

**Table 4.1 Summary of Descriptive Analysis**

Variable	Obs	Mean	Std. dev	Min	Max
FDI Net flow	102	8.316	1.120	4.499	9.629
Voice and accountability	102	25.778	11.749	4.8309	44.230
Political stability	102	20.113	13.886	4.245	52.830
Government effectiveness	102	32.112	13.480	6.635	63.461
Regulatory quality	102	33.015	14.420	8.333	60.096
Rule of law	102	33.095	13.715	5.769	61.538
Control of corruption	102	29.830	19.815	.947	75.480
Inflation rate	102	8.986	7.027	-2.814	44.356
Exchange rate	102	1125.894	1041.151	8.666	3727.069
GDP growth rate	102	5.991	3.181	-3.9	12.550
Trade openness	102	40.679	9.244	22.240	64.478

**Source:** Survey Data (2023)

The above analysis presents the summary of the six key governance indicators, the foreign direct investment inflow and the control variables (inflation rate, exchange rate, GDP growth rate and trade openness). Voice and accountability averaged 25.778 with a maximum of 44.230. The results also revealed a low level of political stability within the region with an average of 20.113 and a maximum of 52.830 with a deviation of 13.886. The study showed the regulatory quality within the countries averaged 33.015 and the control of corruption was on average 29.830. Further analysis demonstrated the average inflation rate within the countries averaged 8.986 with a GDP growth rate average of 5.591. The average level of trade openness among selected countries was 40.469 with a maximum of 64.478 within the region.

### 4.3 Diagnostic Tests

Panel data was utilized in this survey and thus was deemed necessary to conduct various diagnostic checks to ensure the extracted data can be utilized in the panel regression. The results of the diagnostic checks are presented.

#### 4.3.1 Autocorrelation Test

The presence of serial correlation would be a clear indication that the variables in the model violate the assumptions of the regression. The research applied the Durbin-Watson tests on the model with the result as follows.

**Table 4.2 Autocorrelation Result**

Model	Test
1	Durbin–Watson statistic (transformed) = 2.085332

**Source:** Survey Data (2023)

The test standard is that the Durbin-Watson statistics should be between 1.5-2.5 to ensure there is no violation of the autocorrelation problem. The results above showed a D-W value of 2.085 which is within the stated range thus confirming there was no issue of autocorrelation in the research.

#### 4.3.2 Multicollinearity Test

Multicollinearity was conducted to check for inter-correlations among all pairs of predictors and determine whether multicollinearity was likely to be a problem (Ullah, Aslam, Altaf, & Ahmed, 2019). The VIF and Tolerance values were estimated in the research.

**Table 4.3 Multicollinearity Result**

Variable	VIF	1/VIF
Voice and accountability	2.18	0.46
Political stability	6.45	0.16
Government effectiveness	10.	0.11
Regulatory quality	4.82	0.21
Rule of law	7.07	0.14
Control of corruption	10	0.11
Inflation rate	1.41	0.71

Exchange rate	3.44	0.29
GDP growth rate	1.73	0.58
Trade openness	2.41	0.42
Mean VIF	5.01	

**Source:** Survey Data (2023)

As a rule, the VIF value should not be above 10 and the Tolerance Value needs to be above 0.1. The analysis showed that all the variables had variance inflation factors below 10 with corresponding tolerance values (1/VIF) that were above 0.1 thus demonstrating there was no collinearity issue in the data.

### 4.3.3 Normality Test

The normality assumption is necessary for the conduction of single or joint hypothesis testing on the model parameters (Ghasemi & Zahediasl, 2012). The research adopted the Jarque-Bera test and the results were as follows.

**Table 4.4 Normality Result**

	Control of Exchange corruptions	Exchange rate	FDI	Gdp growth	Government effectiveness	Inflation rate	Political stability	Regulatory quality	Rule of laws	Trade openness	Voice and accountability
Jarque-Bera	12.592	10.117	59.988	4.455	0.132	253.438	13.8050	6.585	2.281	1.282	7.792
Probability	0.001	0.006	0.000	0.107	0.936	0.000	0.001	0.037	0.319	0.526	0.020
Observations	102	102	102	102	102	102	102	102	102	96	102

**Source:** Survey Data (2023)

The Jarque-Bera test is a goodness of fit test that focuses on assessing the sample data to ensure if there is normal distribution within the variables. The findings showed the Jarque-Bera statistic was not close to 1 in multiple variables suggesting the data was not normally distributed. The research solved for this by conducting nonparametric tests which do not require a distribution to meet the required assumption (distribution-free tests) in estimating interaction between variables.

### 4.3.4 Stationarity Test

The Augmented Dickey-Fuller (ADF) test was executed to test the time-series properties of the data series (Ghasemi & Zahediasl, 2012). The findings are presented in Table 4.5.

**Table 4.5 Stationarity Result**

Null Hypothesis: Unit root (individual unit root process)

Exogenous variables: Individual effects

User-specified lags: 1

Total (balanced) observations: 90

Cross-sections included: 6

Variable	Method	Statistic	Prob.**
FDI Net Inflow	ADF - Fisher Chi-square	30.7674	0.0021
	ADF - Choi Z-stat	-2.75109	0.0030
Regulatory quality	ADF - Fisher Chi-square	8.69294	0.7289
	ADF - Choi Z-stat	0.67264	0.7494
Control of corruption	ADF - Fisher Chi-square	16.9299	0.1523
	ADF - Choi Z-stat	-1.10420	0.1348
Political stability	ADF - Fisher Chi-square	24.0416	0.0201
	ADF - Choi Z-stat	-2.36002	0.0091
Government effectiveness	ADF - Fisher Chi-square	14.6664	0.2602
	ADF - Choi Z-stat	-1.30959	0.0952
Rule of law	ADF - Fisher Chi-square	12.6356	0.3961
	ADF - Choi Z-stat	-0.38050	0.3518
Voice and accountability	ADF - Fisher Chi-square	4.21682	0.9792
	ADF - Choi Z-stat	2.01296	0.9779
Trade openness	ADF - Fisher Chi-square	5.80816	0.9254
	ADF - Choi Z-stat	1.00369	0.8422
Inflation rate	ADF - Fisher Chi-square	11.6199	0.4767
	ADF - Choi Z-stat	0.13551	0.5539
GDP Growth rate	ADF - Fisher Chi-square	11.6611	0.4733
	ADF - Choi Z-stat	0.66921	0.7483
Exchange rate	ADF - Fisher Chi-square	1.27846	0.9999
	ADF - Choi Z-stat	3.92488	1.0000

\*\* Probabilities for Fisher tests are computed using an asymptotic Chi-square distribution. All other tests assume asymptotic normality. McKinnon critical values\*

**Source:** Survey Data (2023)

The null hypothesis of the ADF test is that the time series contains a unit root and is non-stationary. The natural log of FDI net inflow was 0.0021 and political stability (0.0201) indicating there was no presence of unit root at first difference. Further analysis of the other variables showed non-stationarity in its level form by accepting the null hypothesis of the results that there is a unit root. This is because the ADF- Test statistics of all the variables were greater than the McKinnon critical values at 5 per cent levels of significance.

### 4.3.5 Hausman Specification Test

The Hausman test was used to test the random effect and fixed effect. The difference between random effect and fixed effects is whether the unnoticed individual effect represented fundamentals that are correlated with the independent variables within the regression model.

**Table 4.6 Hausman Specification Result**

Variable	Coefficients			sqrt(diag(V_b-V_B)) Std. err.
	(b) fe	(B) re	(b-B) Difference	
Voice and accountability	-.0045	.0351	-.0397	.0223
Political stability	.0137	-.0117	.0254	.0142
Government effectiveness	.0109	.0209	-.0100	.0111
Regulatory quality	.0175	-.0088	.02627	.0121
Rule of law	.0169	.0540	-.0371	.0150
Control of corruption	-.0174	-.0068	-.0105	.0104
Inflation rate	-.0040	.0222	-.0262	.0095
Exchange rate	.0001	.00003	.0001	.0002
GDP growth rate	.0010	.0625	-.0615	.0204
Trade openness	-.0089	-.0221	.01321	.0073

**Source:** Survey Data (2023)

b = Consistent under H0 and Ha; obtained from xtreg.

B = Inconsistent under Ha, efficient under H0; obtained from xtreg.

Test of H0: Difference in coefficients not systematic

$$\text{chi2}(5) = (b-B)'[(V_b-V_B)^{-1}](b-B) = 51.55$$

$$\text{Prob} > \text{chi2} = 0.0624$$

The null hypothesis is that the preferred model is random effects; The alternate hypothesis is that the model is fixed effects. The Hausman test indicated a Prob>chi2 = 0.0624 that was greater than the significance value of .05 which signified that the most preferred model for selection in this research will be a random effects model.

### 4.3.6 Panel Cointegration Test

Cointegration tests are performed where time series data are nonstationary to determine the extent to which the variables have a stable, long-run relationship (Pedroni, 1999). The Pedroni test was adopted in this research.

**Table 4.7 Panel Cointegration Result**

<b>Pedroni test for cointegration</b>			
H0: No cointegration	Number of	panels	= 6
Ha: All panels are cointegrated	Number of	periods	= 16
Cointegrating vector: Panel specific			
Panel means: Included	Kernel:	Bartlett	
Time trend: Not included	Lags:	2.00 (Newey–West)	
AR parameter: Panel specific	Augmented	lags:	1
	Statistic	p-value	
Modified Phillips–Perron t	2.4865	0.0064	
Phillips–Perron t	-11.1510	0.0000	
Augmented Dickey–Fuller t	-6.4928	0.0000	

**Source:** Survey Data (2023)

The cointegration test tests the null hypothesis of non-cointegration against the alternative hypothesis of cointegration. The findings above showed a modified Phillips–Perron  $t = 2.4865$ ,  $P\text{-value} = .0064 < .05$  thus confirming there was a long-run relationship between institutional quality factors and the foreign direct investment in Eastern Africa region.

### 4.4 Correlation Analysis

The study adopted correlation analysis to estimate the direction of the relation between the selected research variables. The matrix of the correlation tests is presented in Table 4.8.

**Table 4.8 Correlation Result**

	FDI	VAA	PS	GE	RQ	ROL	COC	IR	ER	GDP	TO
<b>FDI</b>	1.000										
<b>Voice and accountability</b>	0.3298* 0.0007	1.000									
<b>Political stability</b>	0.2740* 0.0053	0.1658 0.0959	1.000								
<b>Government effectiveness</b>	0.5123* 0.0000	0.0360 0.7197	0.5968* 0.0000	1.000							
<b>Regulatory quality</b>	0.3977* 0.0000	0.4205* 0.0000	0.5964* 0.0000	0.6876* 0.0000	1.000						
<b>Rule of law</b>	0.6380* 0.0000	0.1571 0.1148	0.6952* 0.0000	0.8123* 0.0000	0.6832* 0.0000	1.000					
<b>Control of corruption</b>	0.2998* 0.0022	-0.2582* 0.0088	0.7143* 0.0000	0.7658* 0.0000	0.3623* 0.0000	0.6891* 0.0000	1.0000				
<b>Inflation rate</b>	-0.0014 0.9890	-0.0923 0.3560	-0.2978* 0.0024	-0.0487 0.6267	-0.3004* 0.0022	-0.2122* 0.0322	-0.0853 0.3938	1.0000			
<b>Exchange rate</b>	-0.0118 0.9064	0.1634 0.1009	0.2111* 0.0332	-0.2852* 0.0037	0.1564 0.1165	0.1125 0.2601	-0.2756* 0.0051	-0.3511* 0.0003	1.0000		
<b>GDP growth rate</b>	0.3687* 0.0001	-0.1540 0.1222	0.0798 0.4255	0.3687* 0.0001	-0.0104 0.9173	0.3415* 0.0004	0.3724* 0.0001	0.1738 0.0807	-0.3247* 0.0009	1.0000	
<b>Trade openness</b>	0.1715 0.0948	0.3911* 0.0001	0.3904* 0.0001	0.4148* 0.0000	0.5221* 0.0000	0.2844* 0.0050	0.1792 0.0807	0.1352 0.1890	-0.1779 0.0830	0.2628* 0.0097	1.0000

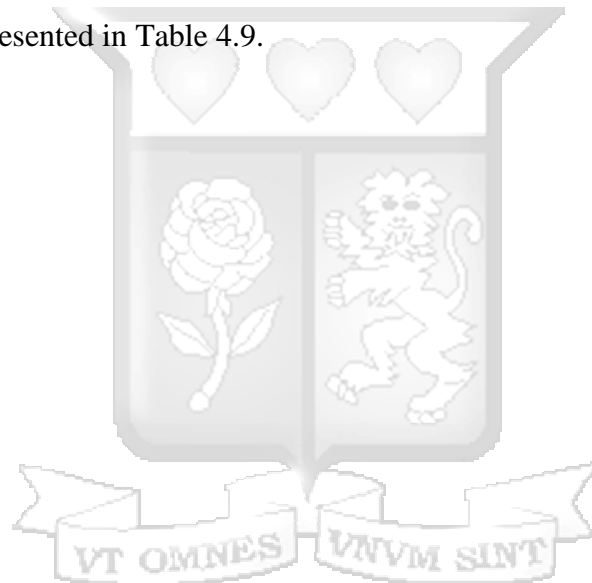
**Source:** Survey Data (2023)

The research revealed there existed a weak positive and significant relationship between voice and accountability ( $r = 0.3298^*$ ,  $\text{sig} = .0007 < .05$ ) political stability ( $r = 0.2740^*$ ,  $\text{sig} = .0053 < .05$ ) and the level of foreign direct investment in Eastern African Region. The correlation tests showed a moderate positive effect of government effectiveness on foreign direct investment in the Eastern

African Region ( $r = 0.5123^*$ ,  $\text{sig} = .0000 < .05$ ). The analysis revealed a strong positive effect of the rule of law on the level of foreign direct investment in Eastern African Region ( $r = 6380^*$ ,  $\text{sig} = .0000 < .05$ ). Findings revealed that inflation rate had a weak negative and insignificant effect ( $r = -0.0014$ ), and the exchange rate had a weak negative relationship ( $r = -0.0118$ ) with foreign direct investment in Eastern African Region. The study showed that GDP growth rate was positive and significantly related with foreign direct investment in the Eastern African Region ( $r = 0.3687^*$ ,  $\text{sig} = .0001 < .05$ ).

#### **4.5 Panel Regression Analysis**

The research estimated a panel regression analysis and based on the results of the Hausman specification tests, a random effects model was considered suitable for the data. The panel regression summary is presented in Table 4.9.



**Table 4.9 Panel Regression Summary**

Variable	Coefficient	Std. Error	t	P> z
Voice and accountability	.0351	.0102	3.45	0.001
Political stability	-.0117	.0146	-0.80	0.424
Government effectiveness	.0209	.0186	1.12	0.263
Regulatory quality	-.0088	.0123	-0.72	0.473
Rule of law	.0540	.0152	3.55	0.000
Control of corruption	-.0068	.0126	-0.54	0.588
Inflation rate	.0223	.0154	1.45	0.148
Exchange rate	.00002	.0001	0.18	0.856
GDP growth rate	.0626	.0353	1.78	0.076
Trade openness	-.0222	.0135	-1.65	0.100
_cons	5.9680	.5537	10.78	0.000
<b>Weighted Statistics</b>				
R-sq:		Number of obs	=	96
within = 0.0284		Number of groups	=	6
between = 0.9004		Wald chi2(10)	=	122.06
overall = 0.5895		Prob > chi2	=	0.0000

**Source:** Survey Data (2023)

The constant of the model was 5.9680,  $t = 10.78$ ,  $P > |z| = 0.000 < .05$  indicating there was a positive improvement in the foreign direct investment in Eastern Africa region. The overall regression model coefficient of determination  $R\text{-sq} = .5895$ ,  $Wald\ chi2(10) = 122.06$ ,  $Prob > chi2 = 0.000 < .05$  indicating there was a positive and significant relationship between institutional quality factors and foreign direct investment in Eastern Africa region. The findings showed that 58.95% of changes in the level of FDI inflow within the region can be predicted by institutional quality factors and the control variables (inflation, exchange, GDP growth rates and the trade openness).

## Discussion of Hypotheses

**H<sub>01</sub>** There is no statistically significant effect of voice and accountability on the level of foreign direct investments in selected East African countries.

Findings from the analysis revealed  $\beta_1 = 0.0351$ ,  $P > |z| = .001 < .05$  signifying there was a positive and significant effect of voice and accountability on the level of foreign direct investments in East African countries. Changing the level of voice and accountability will lead to an improvement in FDI by a factor of 0.0351.

**H<sub>02</sub>** There is no statistically significant effect of political stability on the level of foreign direct investments in selected East African countries.

The results of the study showed  $\beta_2 = -.0117$ ,  $P > |z| = -0.80 > .05$  signifying there was a negative and insignificant effect of political stability on the level of foreign direct investments in East African countries.

**H<sub>03</sub>** There is no statistically significant effect of government effectiveness score on the level of foreign direct investments in selected East African countries.

The results of the study showed  $\beta_3 = 0.0209$ ,  $P > |z| = 1.12 > .05$  signifying there was a positive and insignificant effect of government effectiveness on the level of foreign direct investments in East African countries.

**H<sub>04</sub>** There is no statistically significant effect of regulatory quality score on the level of foreign direct investments in selected East African countries.

The results of the study showed  $\beta_4 = -.0088$ ,  $P > |z| = -0.72 > .05$  signifying there was a negative and insignificant effect of regulatory quality on the level of foreign direct investments in East African countries.

**H<sub>05</sub>** There is no statistically significant effect of rule of law on the level of foreign direct investments in selected East African countries.

Findings from the analysis revealed  $\beta_5 = 0.0540$ ,  $P > |z| = .000 < .05$  signifying there was a positive and significant effect of rule of law on the level of foreign direct investments in East African countries. Changing the level of rule of law score will lead to an improvement in FDI by a factor of 0.0540.

**H<sub>06</sub>** There is no statistically significant effect of control of corruption score the level of foreign direct investments in selected East African countries.

The results of the study showed  $\beta_6 = -.0068$ ,  $P > |z| = -0.54 > .05$  signifying there was a negative and insignificant effect of control of corruption on the level of foreign direct investments in selected East African countries.



## CHAPTER FIVE

### DISCUSSION, CONCLUSION AND RECOMMENDATIONS

#### 5.1 Introduction

This chapter concludes the study and presents the study summary, a discussion of the main findings and the conclusions that were drawn from the study.

#### 5.2 Summary

Governments in developing economies are in constant competition for foreign investment which is considered a significant economic driver and an indicator of stability in business operations. Evidence from African states shows that while FDI has been increasing steadily in recent years, this effect is not uniform across as some countries can attract more investment than others. Moreover, there is evidence that some countries were experiencing negative inflows despite neighbouring countries reporting an increase in FDI inflows. This study sought to understand the factors that contribute to this difference in foreign inflows and focused on institutional quality factors while using macroeconomic factors as control variables. The study was grounded on the internalization theory and the Institutional FDI Fitness Theory and was guided by a correlational research design. The study collected secondary data and applied panel regression analysis.

Analysis of the secondary data revealed that there was a positive and significant relationship between institutional quality factors and foreign direct investment in the Eastern Africa region. The regression results revealed that individually, voice and accountability and the rule of law have positive and significant effects on FDI inflows, government effectiveness has positive but insignificant effects on FDI inflows while political stability, regulatory quality and control of corruption exerted a negative but insignificant effect on FDI inflows into the Eastern African region. Altogether, a unit change in the quality of these variables would explain an approximately 58.9% increase in foreign investment into the East African region.

#### 5.3 Discussion

##### 5.3.1 Voice and Accountability on the Level of foreign direct investment in Selected Eastern African Countries

The first objective of the study focussed on the effect of voice and accountability factors on the level of FDI inflows in East African countries and from the analysis, voice and accountability factors have a positive and significant effect. Semenas (2020) made similar observations in a study

which investigated FDI drivers in emerging economies. The research revealed that governance indicators as well as the macroeconomic factors all influence FDI inflows into emerging countries with improved voice and accountability, political stability, regulatory quality and control of corruption resulting in higher FDI inflows. In Pakistan, Nadeem, Jiao, Nawaz and Younis (2020) made the observation that voice and accountability encourage innovation which increases the attractiveness of developing countries to investors in more developed economies.

In China, Munjal, Varma and Bhatnagar (2022) revealed that guaranteeing free speech, media independence and high standards of accountability is one of the strategies that Asian countries have adopted to attract Chinese investors. The study established a strong link between governance variables, asserting that control of corruption works in tandem with voice and accountability factors to enhance a country's attractiveness to foreign investors. Bouchoucha and Benammou (2020) also concluded that African countries that can demonstrate the ability to guarantee freedom of speech, control corruption, design and implement effective policies and promote accountability are attractive investment destinations.

While these studies assert that voice and accountability variables have positive impacts on FDI inflows, Bosire (2019) casts doubt on the findings in a study that investigated FDI inflows into East Africa, finding that on their own, voice and accountability factors do not necessarily predict the flow of FDI into the region as factors such as natural resources, open markets and labour markets were identified as important considerations for investors. Elsewhere, Saha, Sadekin and Saha (2022) revealed that a high degree of accountability and rule of law has negative impacts on FDI inflows in lower-middle-income countries such as Kenya. Both of these studies examined data from more than ten countries and resource and material differences may skew the results from these studies.

### **5.3.2 Political Stability and Absence of Violence/terrorism on the Level of foreign direct investment in Selected Eastern African Countries**

The second objective of the study was on the effect of political stability and absence of violence/terrorism on the level of FDI in East African countries and analysis findings pointed to a negative and insignificant effect. Similar observations had been made in the analysis by Ari and Ibrahim (2021) which revealed that while in the short run, an increase in terrorism may not have a significant effect on FDI, sustained attacks and increased insecurity over longer periods discourage

FDI inflows. In Burkina Faso, Kambou and Khariss (2020) revealed that an increase in the number of extremist groups in the country resulted in significant negative impacts on FDI inflows into the country. These studies, however, presented evidence from countries which were suffering from an increased wave of extremism and terror while the current study focuses on countries with shorter periods of violence and terror.

In Kenya, Meah, Onono and Ocharo (2016) study revealed that while voice and accountability as an institutional quality factor has significant positive effects on private investment, a country's exposure to political risk, terrorism as well as its population's personal consumption levels moderate the relationship. Furthermore, in China, Shen (2020) asserted that the Chinese government's artificial devaluation, as well as its large consumer market, play a key role in attracting foreign investors. In Pakistan, while the country has been struggling to control corruption and protect against terrorism, the country's large market has emerged as the main attraction for foreign investors who are willing to risk their operations in the unstable country.

### **5.3.3 Government Effectiveness on the Level of foreign direct investment in East African Countries**

The third objective of the study was on the effect of government effectiveness on the level of FDI in East African countries and the results were that the degree of effectiveness has a positive and insignificant effect. Similarly, the analysis from Kayani and Ganic (2021) revealed that government effectiveness, political stability, and voice & accountability factors have insignificant effects on inward FDI in China. In the study by Paul and Jadhav (2019), government effectiveness, regulatory quality, political stability, and control on corruption as institutional quality factors are significant determinants of FDI in emerging markets. The researchers added that the quality of infrastructural development, as well as the cost of trade measured by tariff and non-tariff barriers, have significant impacts on FDI inflows.

In China, Li, Luo and De Vita (2020) revealed that the higher the differences in government effectiveness and control of corruption between China and an investment destination the lower the investment from China and called on the governments to align their policies and control systems with the country they seek investment from. Huang, Meng, Chen and Liu (2022), on the other hand, assert that the simplification of administrative procedures is one of the main factors influencing FDI outflows from the Chinese private sector. However, according to the findings from Shah, et al. (2019), the institutional differences between China and host countries have

insignificant effects on outward FDI while the resource capacity of recipient countries is a significant attraction factor for Chinese investors who are more likely to risk investing in resource-rich countries with weaker institutions.

Elsewhere, the findings from Muhammad and Khan (2022) were that G7 investors will invest in countries with or without resources as well as they have quality institutions. Japanese investors were also revealed to consider institutional freedom, corruption scores and the strength of financial systems before investing. Moreover, the study by Duanmu (2014) which investigated investment within the BRIC block of nations revealed that enforcement of labour laws, in addition to trading relations and capital mobility are key predictors of FDI outflows. In the study by Buitrago and Barbosa (2020), a country's inability to guarantee stability, tackle corruption, and follow through on contracts, as well as liberalize the economy and provide a stable regulatory environment discourages FDI inflows.

#### **5.3.4 Regulatory quality on the level of foreign direct investment in selected Eastern African countries**

The fourth objective of the study was on the effect of regulatory quality on the level of FDI in East African countries and analysis findings revealed that the regulatory quality in East Africa has a negative and insignificant effect. Appiah-Kubi et al., (2020) made similar observations in West Africa where, while ethical values and the ability to protect investor property through contract enforcement encourage FDI, regulations in securities and the stock exchange had insignificant impacts on FDI. Bhasin and Garg (2020) made similar observations in the study on FDI inflows into 26 emerging economies. The research revealed that while the rule of law and the normative institutional environment and negative impacts on FDI inflows, a higher degree of regulatory efficiency was associated with increased FDI. This suggests that while foreign investors will seek to take advantage of the weak laws, norms and values of emerging economies, they will also invest in economies with a basic enabling environment where the regulations are lax and tax collection and enforcement minimal.

However, the analysis by Peres et al. (2018) in the middle east revealed that institutional quality factors do not significantly influence FDI inflows since most of the study samples had weaker institutional frameworks. According to Aziz (2018), countries with a high degree of economic freedom, ease of doing business and low international country risk are attractive destinations. The researcher added that developing countries should develop quality policies and guarantee their

institutions a high degree of independence to encourage foreign investors. Likewise, Uddin, et al (2019) observed that the government's size, legal structure and property rights protection, and adherence to free trade practices and representation all influence FDI inflows. According to the study's conclusion, infrastructural quality and the developments of the financial sector have significant impacts on investors' decision-making.

### **5.3.5 Rule of law on the level of foreign direct investment in selected Eastern African countries**

The fifth objective of the study centred on the effect of the rule of law on the level of FDI in East African countries and the results were that the rule of law has a positive and significant effect. Contractor et al. (2020) also observed that multinational companies are attracted to and invest in countries with strong contract enforcement and more efficient international trade regulations. Chen and Jiang (2022) found similar results in China where higher-quality institutions were singled out as important determinants of market development. The study revealed that quality institutions encourage trade openness, development of quality industrial structures and facilitate technology and skills transfer which increases a country's productivity and attractiveness to investors.

Comi, Grasseni and Resmini (2021) revealed that countries which struggle to enforce contractual agreements will discourage investors from Italy who are conscious of contractual arrangements. The study, however, also showed that this consciousness does not apply to all types of investors since investors in the information and knowledge-intensive sectors were more responsive to efficient jurisdictions than those in the resource extraction as well as manufacturing sectors. Tag (2021) made inconclusive observations in research that revealed that while judicial independence and impartiality increase FDI net inflows, contract enforcement had insignificant impacts on FDI in developed economies. This could be because most developed nations have quality institutions and contract enforcement policies and procedures. Indeed, in Egypt, Karamali (2020) demonstrated that the country's poor transparency, a high degree of contractual breaching with minimal consequences and legal restrictions placed on foreign firms had made the operating environment unattractive to foreign investors, making the country unable to meet its investment objectives.

### **5.3.6 Control of Corruption on the Level of foreign direct investment in Selected Eastern African Countries**

The sixth objective of the study was on the effect of control of corruption on the level of FDI in East African countries and the analysis findings were that control of corruption has a negative and insignificant effect. This implies that investors may be attracted to the countries' inability to control corruption, an observation that had been made by Bhasin and Garg (2020) who revealed that certain foreign investors will look to take advantage of weak values as a profiteering strategy. Similarly, Nigerian investors were determined to be more attracted to the countries' weak internal controls in the study by Omodero (2019) whose findings were that investors were willing to invest in the country despite its inability to effectively control corruption. The study, however, reported that this effect may change in the future as foreign companies seek more stable economies.

In Zimbabwe, Muzurura (2016) revealed that the government's inability to control corruption was one of the most significant hindrances to FDI inflows into the country. The study also revealed that Zimbabwe's institutional weaknesses, lack of trade openness, inconsistent government policies, political instability and poor governance increased the country's attractiveness to foreign investors. Shisya (2021) was also of the opinion that corruption and bribery, absence of property rights protection, bureaucratic inefficiency, disregard for the rule of law and unpredictable policy variations have significant negative effects on FDI inflows into the country.

### **5.4 Conclusions**

The analysis of the research led to the conclusion that overall, institutional quality factors have a positive and significant effect on the volume of foreign direct investment in the Eastern Africa region. This finding showed that East African countries can increase their attractiveness to foreign investors by improving the level of accountability, government effectiveness, control of corruption, guaranteeing political stability, enforcement of the rule of law and improving the relevance of new regulations. Specifically, the process by which governments are selected, monitored, and replaced, the capacity of the government to effectively formulate and implement sound policies and the respect of citizens and the state for the institutions that govern economic and social interactions among them have significant impacts on foreign direct investment inflows into the country.

The findings confirm the propositions made in the Institutional FDI Fitness theory which postulates that institutions, policies and the degree to which countries implement these policies

give a country a competitive advantage in the global FDI market. The study concludes that institutional and governmental factors play a key role in attracting FDI, implying that reducing the obstacles relating to institutions would encourage foreign direct investors to increase their investment volume. The results of the regression analysis led to the conclusion that voice and accountability factors have significant impacts on the level of foreign direct investment into Eastern African states. This implies that the extent to which a country enables its citizens to participate in the selection of the government and freely express themselves, guaranteeing the freedom of association as well as a high degree of media freedom will attract a higher volume of foreign investment.

The regression findings led to the conclusion that political stability and the absence of violence/terrorism have a negative and insignificant effect on the level of foreign direct investments in East African countries. This suggests that while the relationship may be insignificant, a stable political environment with low levels of terrorism would attract a higher level of FDI inflow into Eastern African countries. The study concludes that Eastern African governments should have in place strong security forces to ensure stable environments and a reduction in violent threats given the regional instability witnessed.

The results of the analysis led to the conclusion that while the relationship is insignificant, the degree of government effectiveness has positive impacts on FDI inflows into Eastern African states. This implies that the quality of public services, the quality of the civil service and the degree of its independence from political pressures, the quality of policy formulation and implementation, and the credibility of the government's commitment to implemented policies do not have significant impacts on FDI inflows. Therefore, the conclusion is that improving a high degree of government effectiveness will encourage FDI inflows.

The regression results led to the conclusion that the regulatory quality in East African states has a negative but insignificant effect on the volume of FDI inflows into the region. This implies that although the ability of the government has not been able to formulate and implement sound policies and regulations that permit and promote private sector development, FDI inflows have remained consistent throughout the study period. The results of the analysis led to the conclusion that the rule of law in Eastern Africa has a positive and significant effect on the level of foreign direct investments in the region. This implies that governments that abide by the rules of society,

especially concerning the quality of contract enforcement, respect property rights, have accountable police, and courts, as well as minimize the likelihood of crime and violence will realize a higher level of foreign investment.

The results also led to the conclusion that control of corruption in East Africa has negative but insignificant effects on the volume of FDI inflows in the region. This implies that while a high degree of abuse of public power for private gain, petty and grand forms of corruption, as well as state capture by elites and private interests, may have insignificant effects on FDI inflows, the effect is more likely to be negative than not. The results of the research further led to the conclusion that country-specific variables including inflation rate, exchange rate, GDP growth rate and trade openness do not have a significant effect on the foreign direct investment flowing into the Eastern Africa Region. Lastly, the findings led to the conclusion that the degree of trade openness had an insignificant negative effect on FDI inflows into East Africa.

### **5.5 Recommendations**

The results of the analysis revealed that countries occupying the same region have crucial dissimilarities that may significantly affect FDI attractiveness. The study noted that the East African states all have different, unique features that might attract or discourage FDI. However, the study findings indicate that voice and accountability, and the rule of law were the only factors with significant effects on FDI inflows into all East African states. This study recommends that the countries apply differential implementation of policies while taking into account the country-specific uniqueness such as political stability which may impact foreign investors. The study calls on the East African countries to develop a better understanding and appreciation of the role of institutions and governance as well as economic factors in enhancing FDI inflows. Specifically, this study recommends that the states strive to improve voice and accountability, and the rule of law factors which have been ascertained to have significant impacts on FDI.

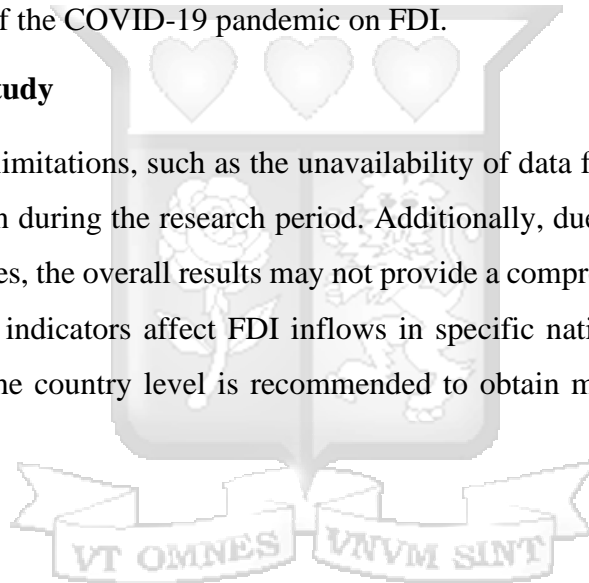
It is recommended that East African states can increase FDI inflows by formulating and implementing sound and relevant regulations that would encourage investment into the country's private sector. The study avers that East African governments should ensure they control corruption in all its forms and shapes. The research calls on the governments in the region to continuously reform institutions as this would improve the ability and efficiency of businesses operating in the region and attract more FDI inflows.

## **5.6 Areas for Further Research**

The study recommends research on the effect of institutional quality on FDI in individual sectors such as information and communication technology and manufacturing as well as extractive sectors which were revealed to respond to different institutional quality variables. Further, the study calls for more examination into the relationship between financial systems and FDI inflows considering these systems were identified as important determinants of FDI inflows. The study also calls for an examination of the relationship between institutional quality variables and FDI inflows from the perspective of multinational companies. Considering the study revealed that internal country-specific variables also impact FDI inflows, the study calls for further research into the effect of the existence of substitute economics on FDI in Eastern Africa. A further area of study would be on the impact of the COVID-19 pandemic on FDI.

## **5.7 Limitations of the Study**

The study faced various limitations, such as the unavailability of data for new member countries in the East African region during the research period. Additionally, due to volatile environments in some surveyed countries, the overall results may not provide a comprehensive understanding of how institutional quality indicators affect FDI inflows in specific national contexts. Therefore, further investigation at the country level is recommended to obtain more tailored and accurate results.



## REFERENCES

- Acquah, A. M., & Ibrahim, M. (2020). Foreign direct investment, economic growth and financial sector development in Africa. *Journal of Sustainable Finance & Investment*, 10(4), 315-334.
- Adeel-Farooq, R. M., Khan, J., Nawaz, A., & Akram, K. (2020). Governance and FDI in Selected SAARC Economies. *Pakistan Journal of Social Sciences (PJSS)*, 40(3) 1317-1327.
- Adeboye, F. B., Osabohien, R., Olokoyo, F. O., Matthew, O., & Adediran, O. (2020). Institutional quality, foreign direct investment, and economic development in sub-Saharan Africa. *Humanities and social sciences communications*, 7(1), 1-9.
- Alonso, J. A., Garcimartin, C., & Kvedaras, V. (2020). Determinants of institutional quality: an empirical exploration. *Journal of Economic Policy Reform*, 23(2), 229-247.
- Appiah-Kubi, S. N., Malec, K., Maitah, M., Kutin, S. B., Pánková, L., Phiri, J., & Zaganjori, O. (2020). The impact of corporate governance structures on foreign direct investment: A case study of West African countries. *Sustainability*, 12(9), 3715.
- Ari, Y. O., & Ibrahim, B. (2021). The Impact of Terrorism on Foreign Direct Investment: The Case of Turkey. *Third Sector Social Economic Review*, 56(3), 1781-1797.
- Aswata, M. B., Nnyanzi, J. B., & Bbale, J. M. (2018). Debt, corruption and investment in East Africa: a panel ARDL analysis. *Modern Economy*, 9(12), 2012-2038.
- Azam, M., Nawaz, M. A., & Riaz, M. (2019). Does corruption and terrorism affect foreign direct investment inflows into Pakistan. *Journal of Managerial Sciences*, 13(2), 85-97.
- Aziz, O. G. (2018). Institutional quality and FDI inflows in Arab economies. *Finance Research Letters*, 25, 111-123.
- Bahati, J. A., & Mbithi, M. L. (2022). Determinants of Foreign Direct Investment: A Comparative Study between Central and East Africa. *Open Journal of Social Sciences*, 10(6), 359-378.
- Bailey, N. (2018). Exploring the relationship between institutional factors and FDI attractiveness: A meta-analytic review. *International Business Review*, 27 (1), pp. 139–168.
- Bhasin, N., & Garg, S. (2020). Impact of institutional environment on inward FDI: A case of select emerging market economies. *Global Business Review*, 21(5), 1279-1301.

- Bildirici, M.(2004). Real Cost of Employment an Turkish Labour Market: A Panel Cointegration Tests Approach. *International Journal of Applied Econometrics and Quantitative Studies*.
- Bosire, E. M. (2019). Foreign Direct Investments into Eastern Africa region: The governance paradox. *International Journal of Economics and Financial Issues*, 9(1), 169.
- Bosire, E. M. (2020). Foreign Direct Investments into Eastern Africa Region: The Infrastructure Development Nexus. *International Journal of Economics and Financial Issues*, 10(5), 370.
- Bouchoucha, N., & Benammou, S. (2020). Does institutional quality matter foreign direct investment? Evidence from African countries. *Journal of the Knowledge Economy*, 11(1), 390-404.
- Bryman, A., & Bell, E. (2007). *Business Research Methods*, (3rd ed.). New York:: Oxford, University press.
- Buitrago R, R., & Barbosa Camargo, M. I. (2020). Home country institutions and outward FDI: An exploratory analysis in emerging economies. *Sustainability*, 12(23), 10010.
- Challe, E., Lopez, J., & Mengus, E. (2019). Institutional quality and capital inflows: Theory and evidence. *J. Int. Money Financ*, 96, 168–191.
- Chen, F., & Jiang, G. (2021). Investigating the Impact of Institutional Quality on FDI: Are There Promotional Effects in Economic Integration Regions? *Sustainability*, 13(20), 11309.
- Chen, F., & Jiang, G. (2022). The impact of institutional quality on foreign direct investment: empirical analysis based on mediating and moderating effects. *Economic Research-Ekonomska Istraživanja*, 1-21.
- Chiappini, R., & Viaud, F. (2021). Macroeconomic, institutional, and sectoral determinants of outward foreign direct investment: Evidence from Japan. *Pacific Economic Review*, 26(3), 404-433.
- Dar, A. A., Muhammad, T., & Siddiqi, M. W. (2020). Bureaucratic Quality and FDI Inflows Nexus: A South Asian Perspective. *Romanian Journal of Economic Forecasting*, 23(3), 149.

- Dobrowolska, B., Dorożyński, T., & Kuna-Marszałek, A. (2021). Institutional Quality and its Impact on FDI Inflow: Evidence from the EU Member States. *Comparative Economic Research. Central and Eastern Europe*, 24(4), 23-44.
- Duanmu, J. L. (2014). A race to lower standards? Labor standards and location choice of outward FDI from the BRIC countries. *International Business Review*, 23(3), 620-634.
- Erminio, F., & Rugman, A. (1996). A Test of Internalization Theory and Internationalization Theory: The Upjohn Company. *Management International Review*, 36(3): 199-213.
- Ghasemi, A., & Zahediasl, S. (2012). Normality tests for statistical analysis: a guide for non-statisticians. *International journal of endocrinology and metabolism*, 10(2), 486.
- Ghauri, P., Grønhaug, K., & Strange, R. (2020). *Research methods in business studies*. Cambridge University Press.
- Granath, M., & Sluiter, M. (2018). Do property rights matter to FDI?: A cross-sectional study of property rights, institutions and FDI in middle income countries. *Jonkoping University*.
- Hadri, K., & Kurozumi, E. (2012). A simple panel stationarity test in the presence of serial correlation and a common factor. *Economics Letters*, 115(1), 31-34.
- Hammami, H., Hammami, M., Coulibaly, S., & Marzouk, M. (2020). Determinants of FDI attractiveness: A MCI model approach. *Economics Bulletin*, 40(2), 1033-1048.
- Hausman, J. A., & Taylor, W. E. (1981). A generalized specification test. *Economics Letters*, 8(3), 239-245.
- Hayat, A. (2019). Foreign direct investments, institutional quality, and economic growth. *The Journal of International Trade & Economic Development*, 28(5), 561-579.
- Huang, X., Meng, X., Chen, M., & Liu, X. (2022). The impact of administrative simplification on outward foreign direct investment: Evidence from a quasi-natural experiment in China. *The Journal of International Trade & Economic Development*, 31(3), 375-393.
- Kalii, R. (2021). An Analysis of the Internationalization Process of Large Manufacturing Firms in Kenya. *Mba, University of Nairobi*.

- Kambou, P., & Khariss, M. (2020). Effect of Terrorism on Foreign Direct Investment in Burkina Faso. *International Journal of Accounting, Finance, Auditing, Management and Economics*, 1(3), 200-211.
- Karamali, I. (2020). Optimizing Foreign Direct Investment: Attracting High-Technology Multinational Corporations in the Arab Republic of Egypt. *Mba, University of Texas at Austin*.
- Kasasbeh, H. A., Mdanat, M. F., & Khasawneh, R. (2018). Corruption and FDI inflows: Evidence from a small developing economy. *Asian Economic and Financial Review*, 8(8), 1075-1085.
- Kayani, F. N., & Ganic, M. (2021). The Impact of Governance on Chinese Inward FDI: The Generalized Method of Moments Technique. *Humanities and Social Sciences Letters*, 9(2), 175-184.
- Kirovska, Z., Gjozinska, B., & Tanevska Jadrovska, L. (2022). The Impact of the Efficiency of the Judicial System in Attracting Foreign Direct Investments in the Republic of North Macedonia. *Zagreb International Review of Economics & Business*, 25(1), 21-32.
- Lee, M., Alba, J. D., & Park, D. (2018). Intellectual property rights, informal economy, and FDI into developing countries. *Journal of Policy Modeling*, 40(5), 1067-1081.
- Lestari, D., Lesmana, D., Yударuddin, Y. A., & Yударuddin, R. (2022). The impact of financial development and corruption on foreign direct investment in developing countries. *Investment Management and Financial Innovations*, 19(2), 211-220.
- Li, C., Luo, Y., & De Vita, G. (2020). Institutional difference and outward FDI: Evidence from China. *Empirical Economics*, 58(4), 1837-1862.
- Liu, H., Tang, Y., Chen, X., & Poznanska, J. (2017). The determinants of Chinese outward FDI in countries along “One Belt One Road”. *Emer. Mark. Financ. Trade*, 53, 1374–1387.
- Marandu, E. E., Mburu, P. T., & Amanze, D. (2019). An analysis of trends in foreign direct investment inflows to Africa. *International Journal of Business Administration*, 10(1), 20-32.

- Meah, D. O., Onono, P. A., & Ocharo, K. N. (2016). Foreign direct investment, institutional quality and economic growth in Kenya. *International Journal of Development and Sustainability*, 5 (7) 295-307.
- Melin, M. M. (2021). The business of peace: understanding corporate contributions to conflict management. *International Interactions*, 47(1), 107-134.
- Mosikari, T. J., Nthebe, T. C., & Eita, J. H. (2018). Does corruption hampers inward FDI in South Africa from other African countries? a gravity model analysis. *University of Johannesburg*.
- Moustafa, E. (2021). The relationship between perceived corruption and FDI: a longitudinal study in the context of Egypt. *Transnational Corporations Journal*, 28(2).
- Mugauri, T. (2019). Is Zimbabwe open for business? The protection of property rights within the legal framework of foreign direct investments. *Doctoral dissertation, University of Pretoria*.
- Muhammad, B., & Khan, M. K. (2022). Do Institutional Quality and Natural Resources Affect the Outward Foreign Direct Investment of G7 Countries? *Journal of the Knowledge Economy*, 1-22.
- Munjal, S., Varma, S., & Bhatnagar, A. (2022). A comparative analysis of Indian and Chinese FDI into Africa: The role of governance and alliances. *Journal of Business Research*, 149, 1018-1033.
- Musabeh, A. (2018). Main theories of Foreign Direct Investment. *Research gate*.
- Musavengane, R., & Zhou, Z. (2021). Political crises and tourism in Sub-Saharan Africa: destination recovery post-coup d'état. *International Journal of Tourism Policy*, 11(1), 52-72.
- Mutisya, A. N., Muturi, W., & Kemboi, I. (2019). Effect of tax incentives on foreign direct investment in Kenya. *International Journal of Business Management & Finance*, 3(2), 51-64.
- Muzurura, J. (2016). Determinants of foreign direct investment (FDI) in Zimbabwe: What factors matter? *Mba, Midlands State University*.

- Nadeem, M. A., Jiao, Z., Nawaz, K., & Younis, A. (2020). Impacts of voice and accountability upon innovation in Pakistan: Evidence from ARDL and Maki Cointegration approaches. *Mathematical Problems in Engineering*.
- Newby, P. (2014). *Research methods for education*. . Routledge.
- Nguyen, A. L. (2020). FDI inflows and intellectual property rights for MNEs in emerging markets: an alternative approach through the lens of trademarks in Vietnam (1986-2016). *Multinational Business Review*, 28 (4) 483-519.
- Nguyen, H. H. (2020). Impact of foreign direct investment and international trade on economic growth: Empirical study in Vietnam. *The Journal of Asian Finance, Economics and Business*, 7(3), 323-331.
- Nguyen, T. V., & Cao, T. H. (2015). The impact of institutional quality on foreign direct investment (FDI) inflows to Vietnam. *EADN Working Pap*, 86, 28.
- Njuguna, A. E., & Nnadozie, E. (2022). Investment Climate and Foreign Direct Investment in Africa: The Role of Ease of Doing Business. *Journal of African Trade*, 1-24.
- Nyakobo, E. H. (2021). The Effect of Corruption on the Productivity of Manufacturing Firms in Kenya. *Doctoral dissertation, University of Nairobi*.
- Omodero, C. O. (2019). Effect of corruption on foreign direct investment inflows in Nigeria. *Studia Universitatis Vasile Goldiş Arad, Seria Ştiinţe Economice*, 29(2), 54-66.
- Othman, A. (2022). The Role of Economic Freedom, Governance, and Business Environment in Attracting Foreign Direct Investment in the Arab Region. *Journal of Economics and Business*, 2, 1-19.
- Oxford Analytica. (2018). Corruption may undermine Kenyan government credibility. *Emerald Expert Briefings*.
- Pace, R. K., & LeSage, J. P. (2008). A spatial Hausman test. *Economics Letters*, 101(3), 282-284.
- Pamba, D. (2022). The Symmetric effects of Fiscal Policy on FDI Inflows. Evidence from South Africa. Evidence from South Africa. *University of KwaZulu-Natal*.

- Paroma, C. L., & Iwuoha, P. P. (2018). Power Struggle and Crisis in Africa: Implications for Foreign Direct Investment. *International Journal of Advanced Academic Research: Social & Management Sciences*, 4(7).
- Paul, J., & Jadhav, P. (2019). Institutional Determinants of Foreign Direct Investment Inflows: Evidence from Emerging Markets. *International Journal of Emerging Markets*, 15 (2), 245-261.
- Pedroni, P. (1999). Critical values for cointegration tests in heterogeneous panels with multiple regressors. *Oxford Bulletin of Economics and statistics*, 61(S1), pp. 653-670.
- Peres, M., Ameer, W., & Xu, H. (2018). The impact of institutional quality on foreign direct investment inflows: evidence for developed and developing countries. *Economic research-Ekonomska istraživanja*, 31(1), 626-644.
- Pessegueiro, D. M., Ferreira, M. A., Reis, N. R., & Pinto, C. S. (2018). The influence of arbitrary and pervasive corruption on FDI inflows and the moderating effect of corruption distance: evidence from Latin America. *Revista Eletrônica de Negócios Internacionais (Internext)*, 13(1), 50-62.
- Pickard, A. J. (2013). *Research methods in information*. . Facet publishing.
- Qumba, M. F. (2018). Safeguarding foreign direct investment in South Africa: Does the Protection of Investment Act live up to its name? *South African Journal of International Affairs*, 25(3), 341-364.
- Rahman, M. M., Rana, R. H., & Barua, S. (2019). The drivers of economic growth in South Asia: evidence from a dynamic system GMM approach. *Journal of Economic Studies*, 46(3), 564-577.
- Rautenbach, M. (2021). An analysis of the relationship between FDI and economic growth in selected East African countries. *Doctoral dissertation, North-West University (South Africa)*.
- Rwigema, P. C. (2022). Leadership and governance for economic development. Case of Rwanda. *The Strategic Journal of Business & Change Management*, 9(2), 1177-1192.

- Sabir, S., Rafique, A., & Abbas, K. (2019). Institutions and FDI: evidence from developed and developing countries. *Financial Innovation*, 5(1), 1-20.
- Saha, S., Sadekin, M. N., & Saha, S. K. (2022). Effects of institutional quality on foreign direct investment inflow in lower-middle income countries. *Heliyon*, 8(10).
- Satoglu, E. B. (2020). FDI into emerging markets: Do institutions really matter? *International Journal of Research in Business and Social Science*, 9(5), 200-211.
- Semenas, S. (2020). Governance and Foreign Direct Investments: A panel gravity approach on emerging markets. *Mba, Umea University*.
- Shah, M. H. (2018). Foreign direct investment and trade related intellectual property rights (TRIPS): The case of Latin American & Caribbean developing economies. *NICE Research Journal*, 1-17.
- Shah, S. H., Kamal, M. A., Hasnat, H., & Jiang, L. J. (2019). Does institutional difference affect Chinese outward foreign direct investment? Evidence from fuel and non-fuel natural resources. *Journal of the Asia Pacific Economy*, 24(4), 670-689.
- Shen, Y. (2020). Assessing the factors that promote foreign direct investment in China. *Mba, Wenzhou-Kean University*.
- Shisya, J. A. (2021). The right to information in Kenya and its potential impact on foreign direct investment (FDI). *Strathmore University*.
- Siddica, A., & Angkur, M. T. (2017). Does institution affect the inflow of FDI? A panel data analysis of developed and developing countries. *International Journal of Economics and Finance*, 9(7), 214-221.
- Sokang, K. (2018). The Impact of Foreign Direct Investment on the Economic Growth in Cambodia: Empirical Evidence. *International Journal of Innovation and Economic Development*, 4(5), 31-38.
- Tsegba, M., & Semberfan, J. (2020). International Financial Reporting Standards (IFRS) Adoption and Foreign Direct Investment (FDI) in Anglophone West African Countries: The Role of Institutional Qualities. *10th International Conference of Accounting and Finance Research*.

- Tulu, A. H. (2021). The Relation of Investment Incentives and Inflow of FDI: Case of Developing Countries and Ethiopia. *Journal of Economy*, 6(5), 98-103.
- Tulu, A. H. (2021). The Relation of Investment Incentives and Inflow of FDI: Case of Developing Countries and Ethiopia. *Journal of Economy*, 6(5), 98-103.
- Uddin, M., Chowdhury, A., Zafar, S., Shafique, S., & Liu, J. (2019). Institutional determinants of inward FDI: Evidence from Pakistan. *International Business Review*, 28(2), 344-358.
- Ullah, I., & Khan, M. A. (2017). Institutional quality and foreign direct investment inflows: evidence from Asian countries. *Journal of Economic Studies*.
- Ullah, M. I., Aslam, M., Altaf, S., & Ahmed, M. (2019). Some new diagnostics of multicollinearity in linear regression model. *Sains Malaysiana*, 48(9), 2051-2060.
- Walliman, N. (2010). *Research methods: The basics*. . Routledge.
- World Bank. (2020). Global Investment Competitiveness Report 2019/2020: Rebuilding Investor Confidence in Times of Uncertainty. *Washington, DC: World Bank Group*, doi:10.1596/978-1-4648-1536-2.
- World Bank. (2023). World Development Indicators. *Washington, DC: World Bank Group*.
- Xu, C., Han, M., Dossou, T. A., & Bekun, F. V. (2021). Trade openness, FDI, and income inequality: Evidence from sub-Saharan Africa. *African Development Review*, 33(1), 193-203.
- Yakubu, I. N. (2020). Institutional quality and foreign direct investment in Ghana: A bounds-testing cointegration approach. *Review of International Business and Strategy*, 30 (1) 109-122.

## APPENDICES

### Appendix I: Data Extraction Tool (for each country: Kenya, Tanzania, Uganda, Burundi, Rwanda, Ethiopia and South Sudan)

Variable/Year	05	06	07	08	09	10	11	12	13	14	15	16	17	18	19	20	21
Voice and accountability																	
Political Stability																	
Government effectiveness																	
Regulatory quality																	
Control of corruption																	
Rule of law																	
Inflation																	
GDP																	
Exchange rate																	
Trade openness																	
Foreign direct investment net inflow																	

## Appendix II: Ethical Review Committee Approval

Che Sangale Rd, Madaraka Estate,  
P.O. Box 59857 00200, Nairobi, Kenya,  
Cell: +254 703 414/6/7, Twitter: @SBSKenya  
Email: info@sbs.ac.ke or visit www.sbs.strathmore.edu



28<sup>th</sup> April 2023

Director General,  
National Commission for Science Technology and Innovation,  
P. O. Box 30623, 00100  
Nairobi.

Dear Sir,

**RE: FACILITATION OF RESEARCH – MUSILI, DANIEL MWANZAU**

This is to introduce Musili, Daniel Mwanzau who is a Master of Science in Development Finance (MDF) student at Strathmore University Business School, his admission number is MDF/52380/17. As part of our MDF Program, Musili is expected to do applied research and undertake a project. This is in partial fulfilment of the requirements of the MDF course.

Musili is undertaking a research paper on "Effect of Institutional Quality on Foreign Direct Investment: A Selected Case of East African Countries." The information obtained shall be treated confidentially and shall be used for academic purposes only.

Our MDF seeks to establish links with industry, and one of these ways is by directing our research to areas that would be of direct use to industry. We would be glad to share our findings with you after the research.

We appreciate your support and shall be willing to provide any further information if required.

Yours sincerely,

A handwritten signature in black ink, appearing to be "Alois Njenga".

Alois Njenga,  
Manager - Graduate Programmes.

Association of African  
Business Schools




Strathmore Business School is a Proud member of




AACSB

Appendix III: NACOSTI Research Approval

  
**REPUBLIC OF KENYA**  
National Commission for Science, Technology and Innovation

**Ref No: 714706** **Date of Issue: 18/May/2023**


**RESEARCH LICENSE**




**This is to Certify that Mr. Daniel Musili of Strathmore University, has been licensed to conduct research as per the provision of the Science, Technology and Innovation Act, 2013 (Rev.2014) in Nairobi on the topic: EFFECT OF INSTITUTIONAL QUALITY ON FOREIGN DIRECT INVESTMENT: A SELECTED CASE OF EAST AFRICAN COUNTRIES for the period ending : 18/May/2024.**

**License No: NACOSTI/P/23/25791**

**Applicant Identification Number**  
**714706**

  
**Director General**  
**NATIONAL COMMISSION FOR**  
**SCIENCE, TECHNOLOGY &**  
**INNOVATION**

**Verification QR Code**  


**NOTE: This is a computer generated License. To verify the authenticity of this document, Scan the QR Code using QR scanner application.**

**See overleaf for conditions**