Indian Journal of Fundamental and Applied Life Sciences ISSN: 2231– 6345 (Online)
An Open Access, Online International Journal Available at www.cibtech.org/sp.ed/jls/2015/01/jls.htm
2015 Vol. 5 (S1), pp. 57-62/Poor
Research Article

THE EFFECTS OF BUSINESS CLIMATE INDICATORS ON THE FOREIGN DIRECT INVESTMENTS AMONG SELECTED ISLAMIC COUNTRIES

***Rasool Sadegh Poor**
Development and Planning, Islamic Azad University, Department of Economy, Yazd, Iran
**Author for Correspondence*

ABSTRACT
Nowadays, most of the countries are willing to attract foreign investments due to insufficiency of internal resources for investment. Therefore, numerous studies have been done on foreign investment the results of which show that foreign investment can have a significant effects upon the macroeconomic variables such as economic development, employment, reinforcement of national currency rate, and business. Therefore, due to significance of this problem, the present study endeavors to determine the effects of selected indicators of business climate on foreign direct investment (FDI) through panel data and during 2006-2012. The results of present study show that cross-border trade index, obtaining bank credit and tax have significant effects upon foreign direct investment.

Keywords: *Foreign Direct Investment, Panel Data Model, Business Climate, D8 Countries*

INTRODUCTION
In the new conditions of global economy, foreign direct investment plays a significant role. The period of dealing with foreign investment and denying they have turned into a discussion of useful types of investment and ways of attracting these types of investments. Foreign investors, especially multinational companies (MNCs), are interested in investing in high-potential and advantageous regions to enhance their competitiveness and obtain higher profit. Cross-border operation and foreign direct investment can influence economic, social and political development of host countries in different ways and from different perspectives. This issue is highly significant for host countries. On the other hand, business climate indicators can significantly affect foreign direct investment. Therefore, the present study endeavors to determine the effects of business climate indicators on foreign investment in selected countries.

Theoretical Principles
Different economic trends and schools are always looking for primary factor of creation and distribution of wealth; in other words, the main factor of generation of economic value in the society. Therefore, the improvement of economic conditions of countries in 1990s led to attention of international institutions and countries to reduction of unemployment, economic development, etc. so that a part of major objectives of countries is related to business. Among the most important new theories which led to radical economic changes in economy of undeveloped countries, one can point to that of Hernando de Soto, the famous Peruvian economist, who published two books of "The Other Path" and "Mystery of Capital" in which improvement of business climate through setting up activities with little capitals is paid attention to. He also states that existence of business climate in developing countries has led private sector to underground, unofficial and unproductive economy. In this case, the capitals get caught in administrative system or move to developed countries (Midari and Ghodjani, 2009). To find the background and origins of the concept of business climate and propose solutions, two procedures should be followed:
A- A review of different theories and schools which analyze the increase of production and capital and determine environmental factors of firms
B- A review of different theories and schools which analyze environmental barriers of boosting economic activities of firms and propose solutions for improvement and regulation of business climate
One could claim that institutionalism (1947-1975) is the first school to discuss the business problems of a firm which analyzed economic activity environments from an institutional viewpoint. The institutionalists

© Copyright 2015 | Centre for Info Bio Technology (CIBTech)

believed that economy should be regarded as an organization or a unique and complete complex in which all constitutive parts are associated with each other. In this school, the role of organizations and institutes in economic life is emphasized. An institution is not only an organization for achieving objectives such as training, cooperation, provision of economic services or even a union but a pattern made of collective and group-based behavior which is regarded as a fundamental part of the culture. In this school, individual behaviors are emphasized more than absolute individualism.
Numerous factors might be influential upon business climate of which foreign investment is an important one. Since 1970s, foreign investment has had a significant role in national economies and it has exceeded business development. Therefore, all countries seek to determine the types of useful investments and ways to attract them.

The improvement of business climate can provide suitable conditions for economic development of countries by which increase of internal and foreign investment results and employment increases to a proper level. Reports of The World Bank under the title of "business climate" can be regarded as the most important reports of business climate.

These reports, annually published since 2004, investigate the global indicators of ease of business. This report is the reference for analysis of business climate in different countries and its improvement in different studies of this subject inside and out of the countries.

Tari and Baghi (2009) in a paper called "Challenges of Business Climate Business of Business Sector and Ways of Their Disposal" endeavored to express different components of economic business climate and development of official section of economy to introduce commercial business climate which was regarded as the fundamental indicators of business space and simultaneously took the position of Iran in global trade into account.

Rahmani (2009) in a paper called "Capital Market: Necessity of Modification and Improvement of Business Climate" initially reviewed the significance of financial system and development. Then, he described capital market and analyzed influential factors on capital market such as legal, economic, socioeconomic environment, information technology and communications.

At last, the status of a developed capital market in terms of capital accessibility, liquidity, risk distribution and capital market was described and the conditions of these variables in capital market of Iran was discussed.

Tobin and Rose in a paper called "Foreign Direct Investment the Business Environment in Developing Countries: the Impact of Bilateral Investment Treaties" investigated the effects of bilateral investment treaties (BIT) on foreign direct investment (FDI) and domestic private investment climate. The authors found out that there is an insignificant association among bilateral investment treaties (BIT), foreign direct investment (FDI) and domestic investment climate. In risk-taking countries, these treaties lead attraction of high amounts of foreign direct investment.

Dremer and Perchet (2010) in a study called "How Business is Done and the Doing Business Indicators: The Investment Climate when Firms Have Climate Control" evaluated the three indicators of authorized time of operation, time of operation generation and time of product importation and compared investment climate in more than 100 countries.

They found out that in business climate, time is an important and influential factor and it is affected by political reformations in each country.

Influential Factors upon Business Climate

For economic success of the market and empowerment of private sector emphasized in two approaches of developing business climate and privatization in 1980s, existing institutions and mechanisms play a significant role. In 2005 report of The World Bank, results of a survey of business owners regarding the most important business barriers is shown in the following conceptual model.

© Copyright 2015 | Centre for Info Bio Technology (CIBTech)

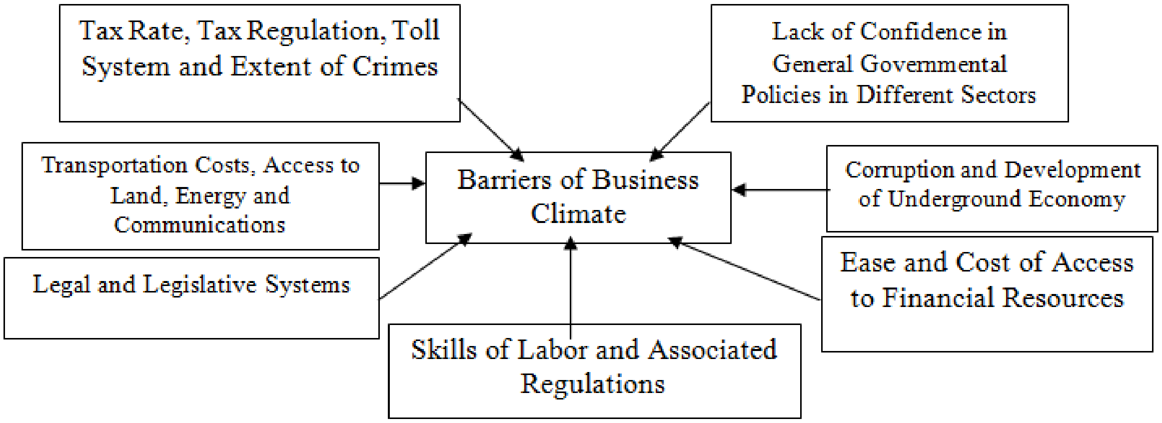

Figure 1: Barriers of Business Climate
Source: Research Findings

The governments which consider the economic health and creation of opportunities for their citizens should evaluate macroeconomic conditions along with regulations with influence daily economic activities. Study of micro factors affecting business does not have long background. The first instances of such studies date back to 1980s by interview with experts who were ignored in the present study due to contradictions in conceptual understandings and exclusion of poor countries.
As a result, influential factors upon business climate can be observed in Figure 2.

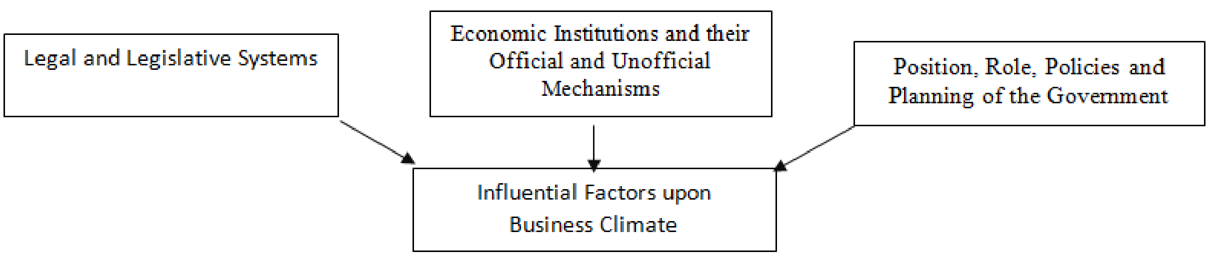

Figure 2: Influential Factors upon Business Climate
Source: Research Findings

Challenges of Job Market and Business Climate
Undoubtedly, one of the challenges of job market is closed, changeless and non-liberalized climate enforced by market regulations which makes market demands inflexible and problematic. This has led to consistent reduction of Iran's position in regard to business climate. This is while resolution of production and investment barriers through regulation of national business climate, reduction of investment risk through providing economic and political security and generation of coordination between educational system and demands of job market can regulate and improve job market and employment. The performance of private sector is influential upon market regulations so that unemployment rate as caused by existing disorders of regulations of job market and other markets are undeniable. Reformation of existing laws is an essential condition for improvement of employment status in Iran. As experts of The World Bank admitted, reformation in for indexes of obtaining license, support of investors, and employment of labor as well as registration of ownership and liquidation of corporate operations might help Iran to improve its position.
It is evident that consistent and stable economic development through proper economic policies has a significant role in realization of economic potentials, full employment and proper conditions of production factors. This will certainly be accompanied by suitable job opportunities. Without productive

© Copyright 2015 | Centre for Info Bio Technology (CIBTech)

and efficient investments, significant economic development is impossible. In fact, employment is the output of an economic cycle in which low unemployment rate and creation of stable employment are impractical without attention to the whole economic cycle.

Experimental Results

Statistical Data

Due to the fact that present study aims to investigate selective affects of business climate indicators upon foreign direct investment in D8 countries (i.e. Iran, Indonesia, Bangladesh, Pakistan, Turkey, Malaysia, Egypt and Nigeria), combined data method is used.

Combined data is a set of data through which cross-sectional data (N) of a definite period of time (T) is evaluated. The number of observations is N*T. So, cross-sectional data of present study includes the data of 8 countries (i.e. Iran, Indonesia, Bangladesh, Pakistan, Turkey, Malaysia, Egypt and Nigeria) and the desired period of time in 2006-2012.

Appropriate Model Selection Tests

F-Limer Test

To select among methods of panel data and Ordinary Least Squares (OLS) combined method, F-Limer test is used. When possibility statistic of F-Limer is less than 5 percent, H_0 is denied. So, panel data should be the primary criterion.

Table 1: F-Limer Test

Test	Test Statistic	Value of Possibility
Cross-section F	14.36	0.0000
Cross-section Chi-square	17.60	0.0000

Source: Findings of Present Study

Hausman Test

If panel data is the primary criterion based on results of F-Limer test, Hausman test is used to determine which model (fixed or random effects) is more suitable for estimation.

Table 2: Results of Hausman Test

Test	Test Statistic	Value of Possibility
Cross-section Random	9.92	0.04

Source: Software Calculations

Specification and Estimation of Model

The present study intends to analyze the role of desired effects of business indicators on foreign direct investment. Indicators of starting a business, cross-border trade, reception of bank credit and tax payment were regarded as dependent variables of present model and then, the effects of foreign investment on each one of above-mentioned variables were tested in the following equation.

$$IF_{it}==\alpha_0+\alpha_1 start_{it}+ \alpha_2 trade_{it}+ \alpha_3 credit_{it}+ \alpha_4 tax_{it}+u_{it} \quad (1)$$

Table 3: Estimation Results of Combined Data

Variable	Coefficient	Std. Error	t-Statistic	Probability
C	15.702	1.282	12.241	0.000
Trade	-0.035	0.013	-2.629	0.011
Credit	-0.047	0.023	-2.062	0.044
Tax	-0.126	0.018	-6.838	0.000
Start	-0.010	0.020	-0.51	0.60
R-squared	0.75	Adjusted R-squared		0.69

Source: Software Calculations

© Copyright 2015 | Centre for Info Bio Technology (CIBTech)

In which “start”, “trade”, “credit”, “tax” and “IF” refer to indicators of starting a business, cross-border trade, obtaining bank credit, tax payment and foreign direct investment.
In the above equation, “i” represents the country and “t” refers to time. The above regression equation is estimated based on panel data. To do so, F-test and Hausman test has been done. Final estimation of the above-mentioned tests is summarized in table 3.
As shown in table 3, all of the coefficients are statistically significant with exception of starting business. The adjusted coefficient is 0.69 which means that 69 percent of IF changes can be explained by model variables. So, one can rewrite the above equation as the following:

$$IF_{it}=15.70 - 0.01start - 0.03Trade - 0.04Credit - 0.12Tax \quad (2)$$
$$(12.24)^{**} \quad (-0.51) \quad (-2.62)^{*} \quad (-2.06)^{*} \quad (-0.83)^{**}$$

The numbers inside parentheses represent t-statistic. Significance of coefficients in level of 5 percent is shown by (*) while it is represented by (**) in level of 1 percent.
The results of estimating the second equation as shown in table 3 show that indicators of cross-border trade, obtaining bank credit and tax have significant effects upon foreign direct investment. Countries can increase foreign direct investment through planning for improvement of these indicators while starting business has no significant influence on foreign direct investment.

Conclusion

Nowadays, no country achieves proper development without active participation in the global business and economy. Therefore, the challenge facing majority of the countries is the way to improve business climate and increase their level of foreign direct investment. Due to significance of this subject in the present study, the role of selected effects of business climate indicators on foreign direct investment during 2006-2012 among desired Islamic D8 countries is analyzed through econometric model of panel data. The results of present study show that in D8 countries, indicators of cross-border trade, tax and receiving bank credit have significant effect upon foreign investment. So, improvement of the business indicators can be regarded as an economic strategy for attracting foreign investment in development of countries.

REFERENCES

Ahmadi SV (2009). Comparative Study of Indicators of Business Climate in Iran and the World, Collection of Economic Studies of Central Bank of Islamic Republic of Iran (30).

Ashrafzade SHR and Megregan N (2009). *Panel Data Econometrics*, Tavon Research Institute of Tehran University.

Driemeier MH and Pritchett L (2010). *How Business is Done and the Doing Business Indicators: the Investment Climate when Firms Have Climate Control*. The World Bank, Research Working.

Hosseinzade Bahraini MH, Falahi MA and Erfani Jahan Shahi F (2013). The Effects of Business Regulations on Economic Development in a Selection of Developed and Developing Countries, *Regional Development and Economy Magazine*, **19**(3).

Kaya H (2009). Unfavorable Business Environment and Foreign Direct Investment Activities of Turkish Manufacturing Firms, *Journal of BRSA Banking and Financial Markets* **3** 101-118.

Midari A and Ghodjani A (2009). *Measurement and Improvement of Business Climate* (University Jihad Publication of Tehran).

Rahmani A (2009). Capital Market: Necessity of Correction and Improvement of Business Climate, the First Conference of Business of Central Bank of Islamic Republic of Iran.

Saleh Abadi A (2010). The Role of Capital Market on Improvement of Business Climate, the First Conference of Business of Central Bank of Islamic Republic of Iran.

Tari F and Gholami Baghi S (2009). Challenges of Business Climate and Ways of Their Disposal, the First Conference of Business, Central Bank of Islamic Republic of Iran.

Tari F and Gholami Baghi S (2008). *General Policies of Article 44 and Business Climate with Emphasis on Business* (Job and Society Monthly Publication) No.115 4-21.

© Copyright 2015 | Centre for Info Bio Technology (CIBTech)

Tobin J and Rose-Akerman S (2003). Foreign Direct Investment the Business Environment in Developing Countries: the Impact of Bilateral Investment Treaties, *Yale Law & Economics Research Paper* **293**.
Tokuoka K (2012). Does the Business Environment Affect Corporate Investment in India?, IMF Working Paper.

© Copyright 2015 | Centre for Info Bio Technology (CIBTech)