

FOREIGN INVESTMENT IN SOUTHEAST ASIA: THE ROLE OF POLITICAL STABILITY, TRADE OPENNESS, REGULATORY QUALITY, AND GROSS DOMESTIC PRODUCT (2014–2023)



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Abstract

Foreign Direct Investment (FDI) plays a crucial role in promoting economic growth and development, particularly in developing regions such as Southeast Asia. This study aims to analyze the determinants of FDI by examining the effects of institutional and macroeconomic factors, namely political stability, regulatory quality, trade openness, and Gross Domestic Product (GDP) across 11 Southeast Asian countries during the period 2014–2023. Unlike previous studies that typically focus on limited variables or a single country, this research employs a panel data approach across countries and time to provide a more comprehensive analysis. The analytical method used is panel data regression with Common Effect Model (CEM), Fixed Effect Model (FEM), and Random Effect Model (REM), with the best model selected through Chow, Hausman, and Lagrange Multiplier tests. The results indicate that trade openness and GDP have a positive and significant effect on FDI, confirming that market size and international trade integration are key factors in attracting foreign investment. Meanwhile, political stability and regulatory quality do not have a significant effect on FDI.

Keywords: Foreign Direct Investment, Trade Openness, Political Stability, Regulatory Quality, GDP

INTRODUCTION

Foreign Direct Investment (FDI) plays a crucial role in promoting economic growth and sustainable development, particularly in developing countries. Beyond providing long-term capital, FDI facilitates technology transfer, enhances managerial capabilities, increases productivity, and creates employment opportunities, thereby strengthening the competitiveness of host economies (Wilantari et al., 2020; Kumari et al., 2023). Consequently, attracting FDI has become a strategic priority for many countries seeking to accelerate economic development and improve their integration into the global economy.

Southeast Asia has emerged as one of the world's most attractive destinations for FDI due to its large population, sustained economic growth, and increasing regional integration. The establishment of the ASEAN Economic Community (AEC) in 2015 further strengthened the region's investment attractiveness by promoting a single market characterized by the freer movement of goods, services, investment, skilled labor, and capital. Although Timor-Leste is included in this study as part of Southeast Asia, the regional integration promoted by the AEC has significantly influenced the investment climate across the region. Consequently, Southeast Asian countries have increasingly implemented policies aimed at improving competitiveness and attracting foreign investment.

The 2014–2023 period is particularly important because it captures the transition toward and the implementation of the ASEAN Economic Community (AEC), allowing an assessment of FDI determinants under a more integrated regional investment environment. This period also reflects changes in investment patterns following regional economic integration, making it appropriate for evaluating how institutional and macroeconomic factors influence FDI inflows across Southeast Asian countries.

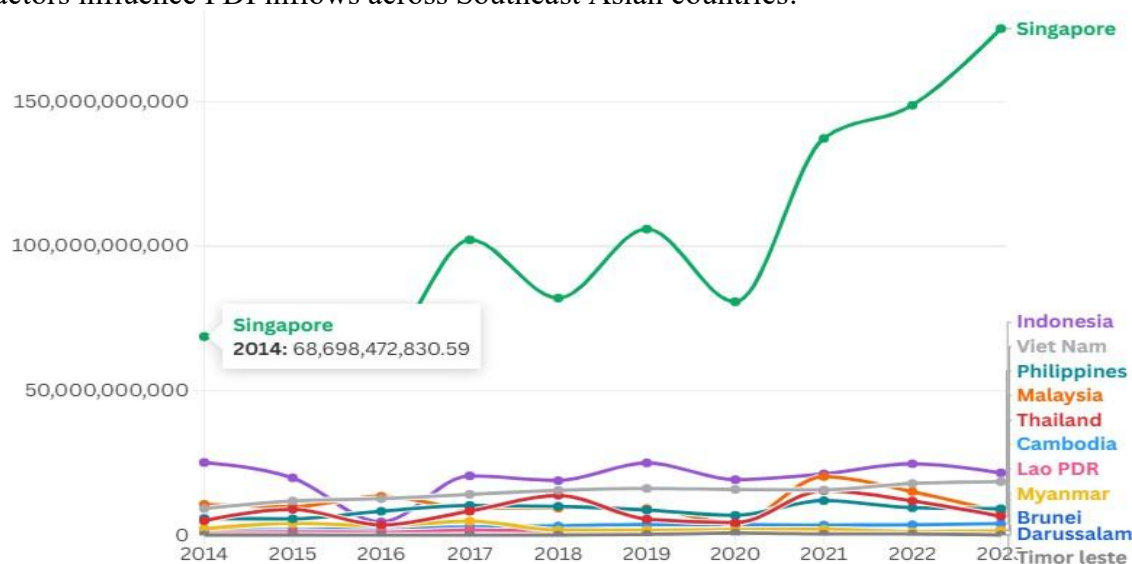


Figure 1.
Trends in FDI Inflows in Southeast Asian Countries, 2014–2023

Source: World Bank, processed

Figure 1 illustrates considerable disparities in FDI inflows across Southeast Asian countries during the 2014–2023 period. Singapore consistently attracted substantially higher FDI inflows than other countries, whereas Indonesia, Vietnam, Malaysia, and Thailand

experienced moderate investment growth, while smaller economies recorded relatively low and fluctuating inflows. These differences indicate that regional economic integration has not resulted in an equal distribution of FDI across Southeast Asia. This phenomenon raises an important research problem regarding the factors responsible for these disparities. Specifically, it remains unclear whether institutional factors, such as political stability and regulatory quality, or macroeconomic factors, such as Gross Domestic Product (GDP) and trade openness, play a more dominant role in attracting FDI across Southeast Asian countries (Behera & Sethi, 2022; Prasetyo et al., 2022).

To explain the determinants of FDI, this study adopts Dunning's OLI (Ownership–Location–Internalization) paradigm as its primary theoretical framework. According to this paradigm, multinational firms invest abroad not only because of firm-specific ownership advantages but also because of location-specific advantages and internalization benefits (Dunning, 2003). In this context, political stability and regulatory quality represent institutional characteristics that reduce investment risk and improve legal certainty, whereas GDP and trade openness reflect the economic attractiveness of a host country through market size and access to international trade. Therefore, the OLI paradigm provides a comprehensive framework for explaining how institutional and macroeconomic conditions jointly influence FDI decisions (Batschauer da Cruz et al., 2022).

Previous studies have identified both institutional and macroeconomic factors as important determinants of FDI. Tomayahu et al. (2021) found that countries with stable governance and accountable institutions tend to attract greater foreign investment, while Lee (2023) emphasized that political risk remains a critical consideration in multinational investment decisions. Meanwhile, Kumari et al. (2023) reported that GDP growth and trade openness positively affect FDI inflows by expanding market opportunities and facilitating international business activities. These findings suggest that both institutional quality and macroeconomic performance contribute to investment attractiveness; however, their relative importance remains inconclusive.

Although the literature on FDI determinants has expanded considerably, several research gaps remain. Most previous studies have focused either on institutional variables or macroeconomic variables separately, or have examined individual countries and broader groups of developing economies rather than Southeast Asia specifically. Moreover, limited studies have simultaneously analyzed political stability, regulatory quality, GDP, and trade openness using recent panel data covering the post-AEC period. Accordingly, empirical evidence explaining the combined influence of institutional and macroeconomic factors on FDI across Southeast Asian countries remains limited.

This study addresses these gaps by simultaneously examining the effects of political stability, regulatory quality, trade openness, and GDP on FDI across eleven Southeast Asian countries, including Timor-Leste, during the 2014–2023 period using panel data regression. By integrating institutional and macroeconomic perspectives within the OLI framework, this study offers a more comprehensive explanation of FDI determinants in Southeast Asia. The findings are expected to enrich the empirical literature on FDI determinants in developing countries while providing practical implications for policymakers in strengthening institutional quality and designing effective trade and investment policies to enhance the region's attractiveness to foreign investors.

REVIEW OF LITERATURE

Foreign Direct Investment

Foreign Direct Investment (FDI) refers to a cross-border investment in which investors acquire a lasting interest and a significant degree of influence over business activities in a host country. Unlike portfolio investment, FDI involves long-term capital commitments accompanied by the transfer of technology, managerial expertise, production techniques, and organizational knowledge, thereby contributing to economic development in host countries (Renaldo, 2020; Nisa & Juliprijanto, 2022). For developing economies, FDI is regarded as an important source of capital because it enhances productivity, creates employment opportunities, promotes industrial upgrading, and strengthens international competitiveness. Consequently, understanding the determinants of FDI has become an important topic in international business and development economics.

OLI Paradigm Theory

This study adopts Dunning's Ownership–Location–Internalization (OLI) paradigm as its primary theoretical foundation for explaining FDI decisions (Dunning, 2003). The OLI paradigm argues that multinational enterprises engage in foreign investment when three conditions are simultaneously fulfilled: ownership advantages, location advantages, and internalization advantages. Ownership advantages refer to firm-specific assets such as technology, innovation, and managerial capabilities. Internalization advantages explain why firms prefer direct investment over licensing or exporting to reduce transaction costs and protect proprietary knowledge. Meanwhile, location advantages describe the characteristics of host countries that make them attractive destinations for foreign investment.

Among these three dimensions, the present study focuses on location advantages because they directly represent country-specific characteristics influencing investors' location decisions. According to the OLI paradigm, countries with favorable institutional environments and strong macroeconomic performance provide greater investment attractiveness by reducing uncertainty, improving expected profitability, and facilitating business operations. Institutional quality, represented by political stability and regulatory quality, contributes to legal certainty, policy consistency, and lower investment risk. Conversely, macroeconomic conditions, represented by trade openness and Gross Domestic Product (GDP), indicate market size, purchasing power, and integration with international markets. Therefore, these four variables collectively reflect the location advantage component of the OLI paradigm and are expected to influence FDI inflows into Southeast Asian countries (Aberu, 2023; Darkwah et al., 2024; Uguru et al., 2023).

Hypothesis Development

The Effect of Political Stability on FDI in Southeast Asia

Political stability reflects the extent to which a country's political environment is predictable, secure, and free from violence or government instability. Within the OLI paradigm, political stability constitutes an important location advantage because it reduces investment uncertainty and enhances confidence among multinational enterprises. Stable political conditions enable firms to undertake long-term investment planning while minimizing risks associated with policy changes, political conflict, or institutional disruption.

Empirical evidence generally supports the positive relationship between political stability and FDI. Bohle and Regan (2021) found that stable political institutions significantly strengthen investment-led growth by encouraging multinational enterprises to undertake

long-term investment commitments. Likewise, Afif (2022) reported that political stability enhances investment competitiveness in developing countries by providing a more predictable business environment. These findings suggest that political stability serves as a signal of institutional reliability that encourages foreign investors to expand their investment activities.

Nevertheless, previous studies have also reported mixed findings regarding this relationship. In resource-rich or rapidly growing economies, foreign investors may continue investing despite relatively unstable political conditions because expected returns outweigh perceived political risks. Furthermore, multinational firms often employ various risk management strategies that reduce their sensitivity to political uncertainty. Consequently, the influence of political stability on FDI may differ depending on the institutional maturity, market potential, and economic characteristics of each country.

Although previous studies have been conducted in countries such as Ireland, Hungary, and several developing economies, their findings remain relevant to Southeast Asia because countries within the region similarly compete to attract foreign investment while pursuing institutional reforms and economic integration. Therefore, political stability is expected to positively influence FDI inflows in Southeast Asian countries.

H₁: Political stability positively affects Foreign Direct Investment in Southeast Asian countries.

The Effect of Regulatory Quality on Foreign Direct Investment

Regulatory quality refers to the government's ability to formulate and implement effective regulations that promote private sector development and create a predictable business environment. Within the OLI framework, regulatory quality represents a location advantage because transparent, consistent, and efficient regulations reduce transaction costs, strengthen legal certainty, and improve investors' confidence in conducting business activities.

Numerous empirical studies demonstrate that regulatory quality positively influences FDI. Kaushal (2021) found that improvements in regulatory quality significantly increased FDI inflows into India by enhancing institutional efficiency and reducing administrative barriers. Similarly, Yerrabati (2021) concluded that better regulatory quality encourages foreign investment while simultaneously strengthening economic growth in developing countries. These findings indicate that effective regulations create favorable business conditions that improve investment attractiveness.

However, previous literature also suggests that regulatory quality does not always produce significant effects on FDI. In several developing countries, improvements in regulations may not immediately attract foreign investors if implementation remains weak, bureaucratic inefficiencies persist, or enforcement lacks consistency. Moreover, investors may prioritize market size, labor availability, or natural resources over institutional quality when selecting investment destinations. These mixed findings indicate that the effectiveness of regulatory quality depends on broader institutional conditions and complementary economic factors.

Although much of the empirical evidence originates from India and other developing economies, the findings remain applicable to Southeast Asia because countries across the region have undertaken similar regulatory reforms to improve competitiveness and attract

international investment following regional economic integration. Therefore, higher regulatory quality is expected to increase FDI inflows into Southeast Asian countries.

H₂: Regulatory quality positively affects Foreign Direct Investment in Southeast Asian countries.

The Effect of Trade Openness on FDI in Southeast Asia

Trade openness reflects the degree to which a country is integrated into the global economy through international trade activities. It is commonly measured by the ratio of total exports and imports to Gross Domestic Product (GDP). Within the OLI paradigm, trade openness represents a location advantage because open economies provide multinational enterprises with easier access to international markets, lower trade barriers, more efficient supply chains, and greater opportunities to participate in global production networks. As a result, countries with higher levels of trade openness are generally considered more attractive destinations for foreign investment.

Previous empirical studies largely support the positive relationship between trade openness and FDI. Rathnayaka Mudiyanse et al. (2021) found that greater trade openness significantly increased FDI inflows into Romania by improving market accessibility and reducing trade-related constraints. Similarly, Soomro et al. (2022) reported that trade openness positively influenced FDI in BRICS countries by strengthening economic integration and facilitating international business activities. These findings indicate that liberal trade policies enhance investment attractiveness by providing multinational corporations with broader market access and production efficiency.

Nevertheless, the relationship between trade openness and FDI is not always consistent across countries. Several studies have reported insignificant or weaker effects, particularly in economies where trade liberalization is not accompanied by adequate infrastructure, institutional quality, or investment facilitation policies. In such cases, reducing trade barriers alone may be insufficient to attract foreign investors if the overall business environment remains unfavorable. These mixed findings suggest that the effectiveness of trade openness depends on complementary institutional and macroeconomic conditions that support business operations.

Although previous studies were conducted in Romania and BRICS countries, their findings remain relevant to Southeast Asia because countries throughout the region have increasingly adopted export-oriented development strategies and trade liberalization policies following regional economic integration. The implementation of the ASEAN Economic Community (AEC) has further encouraged member countries to reduce trade barriers and improve regional connectivity, making trade openness an important determinant of FDI. Therefore, countries with higher levels of trade openness are expected to attract greater FDI inflows.

H₃: Trade openness positively affects Foreign Direct Investment in Southeast Asian countries.

The Effect of Gross Domestic Product (GDP) on Foreign Direct Investment

Gross Domestic Product (GDP) reflects the size and overall performance of a country's economy and is widely regarded as an important indicator of market potential. Within the OLI paradigm, GDP represents a location advantage because larger economies provide greater consumer demand, stronger purchasing power, broader business opportunities, and higher expected returns for multinational enterprises. Consequently,

countries with higher GDP levels are generally more attractive destinations for foreign investment.

Numerous empirical studies have found that GDP positively influences FDI. Kumari et al. (2023) reported that rapid economic growth and increasing GDP significantly attracted FDI into India because foreign investors perceived the expanding domestic market as an opportunity for long-term business expansion. Likewise, Raza et al. (2021) found that GDP positively affected FDI among OECD countries, particularly when accompanied by effective governance and favorable institutional quality. These findings indicate that strong economic performance increases investor confidence by signaling higher market capacity and future profitability.

However, previous studies also suggest that GDP alone may not guarantee greater FDI inflows. Large market size does not necessarily attract multinational enterprises if institutional quality is weak, political conditions are unstable, or regulatory uncertainty remains high. In some developing countries, investors place greater emphasis on governance quality, legal certainty, and business climate than on market size itself. Therefore, the influence of GDP on FDI may vary depending on the interaction between macroeconomic performance and institutional conditions.

Although much of the existing evidence originates from India and OECD countries, the findings remain applicable to Southeast Asia because countries across the region similarly rely on economic growth to strengthen investment attractiveness. Rapidly expanding economies create larger consumer markets and greater production opportunities, making GDP an important consideration for multinational enterprises when selecting investment destinations. Accordingly, countries with higher GDP levels are expected to attract larger FDI inflows.

H4: Gross Domestic Product (GDP) positively affects Foreign Direct Investment in Southeast Asian countries.

RESEARCH METHOD

This study uses Southeast Asian countries as the research population. The sampling technique employed is purposive sampling, resulting in 11 countries selected as the sample, namely Brunei Darussalam, Cambodia, Indonesia, Laos, Malaysia, Myanmar, the Philippines, Singapore, Thailand, Vietnam, and Timor-Leste, observed over the period 2014–2023. The data used are secondary data obtained from the World Bank.

The selection of this period and country coverage is intended to obtain a sufficient number of observations and to capture the dynamics of FDI across countries more comprehensively. To achieve the research objectives optimally and meet the minimum data requirements, panel data regression analysis is employed as the main estimation method, as it is capable of accommodating variations across countries and over time simultaneously, as commonly applied in empirical FDI studies in the ASEAN region (Maharani & Setyowati, 2024). This study utilizes panel data analysis, which combines time series and cross-sectional data. The basic panel regression model in this study is formulated as follows:

$$FDI_{it} = \beta_0 + \beta_1 IPS_{it} + \beta_2 RQ_{it} + \beta_3 TO_{it} + \beta_4 GDP_{it} + \varepsilon_{it}$$

In this study, Foreign Direct Investment (FDI) is used as the dependent variable, while the Indicator of Political Stability (IPS), Regulatory Quality (RQ), Trade Openness (TO), and

Gross Domestic Product (GDP) are used as independent variables. Considering the differences in scale among variables, particularly FDI and GDP which are measured in monetary units, a natural logarithm transformation is applied to stabilize the variance and reduce potential heteroskedasticity. Therefore, to standardize the measurement scale and stabilize data variance, a natural logarithmic transformation is applied to the FDI and GDP variables. This transformation is commonly used in empirical studies in the ASEAN region as it improves estimation accuracy and facilitates the interpretation of elasticity relationships among economic variables (Safira & Setyowati, 2025). Thus, the regression model used in this study is as follows:

$$LOGFDI_{it} = \beta_0 + \beta_1 IPS_{it} + \beta_2 RQ_{it} + \beta_3 TO_{it} + \beta_4 LOG GDP_{it} + \varepsilon_{it}$$

Description :

FDI : Foreign Direct Investment(US\$)
IPS : Indicator Political Stability (Index Scale)
RQ : Regulatory Quality (Index Scale)
TO : Trade Openness (Index Scale)
GDP : Gross Domestic Product (US\$)
 β_0 : Constant
 $\beta_1 \beta_2 \beta_3 \beta_4$: Coefficients of independent variables
it : Cross Section and Time series
 ε : Error term

The panel regression model in this study is estimated using three approaches, namely the Common Effect Model (CEM), Fixed Effect Model (FEM), and Random Effect Model (REM). The selection of the best model is conducted using the Chow test and Hausman test, supported by the Lagrange Multiplier (LM) test. After determining the best model, further testing is carried out, including classical assumption tests, F-test, t-test, and the coefficient of determination (R^2).

Variable Definition

Table 1.
Operational Definition of Variables

Variable	Definition	Unit
Foreign Direct Investment (FDI)	The realized value of foreign direct investment in a country originating from foreign investors, either individuals or foreign companies, that directly enter the economies of Southeast Asian countries each year.	Nominal (Million USD)
Indicator of Political Stability (IPS)	The perception of political instability, referring to the likelihood that a government may be destabilized or overthrown through unconstitutional or violent means, including politically motivated violence and terrorism.	Scale ranging from -2.5 to 2.5
Regulatory Quality (RQ)	Reflects the ability of the government to formulate and implement sound policies and regulations that support private sector development.	Scale ranging from -2.5 to 2.5
Trade Openness (TO)	The sum of total exports and imports divided by Gross Domestic Product (GDP), representing the degree of trade openness.	Percentage (%)

Gross Domestic Product (GDP)	The total market value of all final goods and services produced within a country's borders over a specific period, typically one year.	Nominal (Million USD)
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RESULTS AND DISCUSSION

Estimation Results

This study employed panel data regression analysis using three estimation approaches, namely the Common Effect Model (CEM), Fixed Effect Model (FEM), and Random Effect Model (REM). The objective of estimating these three models was to identify the most appropriate specification for explaining the determinants of Foreign Direct Investment (FDI) across eleven Southeast Asian countries during the 2014–2023 period. The estimation results for each model are presented in Table 2.

Table 2.
Panel Data Estimation Model

Variable	CEM	FEM	REM
C	-4.086920	-2.300777	-5.703421
IPS	0.218697	0.371698	0.426815
TO	0.010974	0.002615	0.008146
RQ	-0.504496	-0.174768	-0.449964
LOG(GDP)	0.982593	1.769.221	1.059.661
R^2	0.884105	0.929544	0.599050
R^2 Adjusted	0.879690	0.919161	0.583775
F-Statistic	2.002.478	8.952.518	3.921.945
Prob.Statistic-F	0.000000	0.000000	0.000000

Model Selection Test

(1) Chow Test

Cross-Section $F(10,95)=6.126756$; Prob.F (10,95) = 0.0000

(2) LM Test (Breuch-Pagan)

Cross-section statistic = 34.23541 ; Prob = 0.0000

(3) Hausman Test

Cross-Section random X^2 (4) = 6.665180 ; Prob X^2 (4)= 0.1547

Source: Processed data using EViews, 2026

The appropriate panel data model was selected through the Chow test, Lagrange Multiplier (LM) test, and Hausman test. The Chow test compares the Common Effect Model and the Fixed Effect Model, while the LM test compares the Common Effect Model and the Random Effect Model. Subsequently, the Hausman test determines whether the Fixed Effect Model or the Random Effect Model provides more efficient and consistent estimates.

The Chow test produced a probability value of 0.0000, indicating that the Fixed Effect Model is preferred to the Common Effect Model. Similarly, the LM test yielded a probability value of 0.0000, suggesting that the Random Effect Model is superior to the Common Effect Model. Furthermore, the Hausman test generated a probability value of 0.1547, which exceeds the 5% significance level, indicating that the Random Effect Model is more appropriate than the Fixed Effect Model. Therefore, the Random Effect Model (REM) was selected as the final estimation model because it provides more efficient parameter estimates under the assumption that country-specific effects are uncorrelated with the explanatory variables.

Classical Assumption Tests

The classical assumption tests in this study include the multicollinearity test and the heteroskedasticity test to ensure that the regression model satisfies the BLUE (Best Linear Unbiased Estimator) criteria.

Multicollinearity Test

The multicollinearity test was performed by examining the correlation coefficients among the independent variables. The results are presented in Table 3:

Table 3.
Multicollinearity Test Results

	IPS	TO	RQ	GDP
IPS	1.000.000	0.608416	0.594522	-0.211758
TO	0.608416	1.000.000	0.734270	-0.026704
RQ	0.594522	0.734270	1.000.000	0.305247
GDP	- 0.211758	-0.026704	0.305247	1.000.000

Source: Processed data using EViews, 2026

The correlation matrix indicates that all correlation coefficients among the explanatory variables are below the commonly accepted threshold of 0.85. Therefore, no evidence of serious multicollinearity is detected, suggesting that each independent variable provides distinct information in explaining variations in Foreign Direct Investment (FDI).

Heteroskedasticity Test

The heteroskedasticity test was conducted using the Glejser method. The results are presented in Table 4:

Table 4.
Heteroskedasticity Test Results

Variable	Coefficient	Std. Error	t-Statistic	Prob.
GDP	-2.80E-13	2.88E-13	-0.972110	0.3332
IPS	0.099098	0.116022	0.854129	0.3950
RQ	-0.033643	0.145938	-0.230527	0.8181
TO	-7.48E-05	0.001482	-0.050484	0.9598

Source: Processed data using EViews, 2026

The probability values for all explanatory variables exceed the 5% significance level, indicating that the null hypothesis of homoskedasticity cannot be rejected. Therefore, the regression model does not exhibit heteroskedasticity, implying that the estimated coefficients satisfy one of the key assumptions required for reliable statistical inference.

Estimation Results of the Selected Model

Based on the model selection tests, the best model used in this study is the Random Effect Model (REM). The estimation results of the selected model are presented as follows:

Random Effect Model Estimation Results

$LOGFDI_{it} = -5.703421 + 0.426815 IPS_{it} - 0.449964 RQ_{it} + 0.008146 TO_{it} + 1.059661 LOG GDP_{it} + \varepsilon_{it}$				
	(0.05500)	(0.1009)	(0.0022)	(0.0000)
$R^2 = 0.59$; DW-Stat = 1,25 ; F-Stat = 39.21 ; Prob. F-Stat = 0.00				

The estimated model yields an R^2 value of 0.599, indicating that approximately 59.9% of the variation in Foreign Direct Investment (FDI) across Southeast Asian countries is explained by political stability, regulatory quality, trade openness, and Gross Domestic Product (GDP). The remaining 40.1% is attributable to other factors not included in the model.

The overall significance of the regression model was evaluated using the F-test. The estimated Random Effect Model produced a Prob(F-statistic) of 0.0000, indicating that the independent variables jointly have a statistically significant effect on Foreign Direct Investment. Accordingly, political stability, regulatory quality, trade openness, and GDP collectively contribute to explaining variations in FDI inflows among Southeast Asian countries.

Partial Significance Test (t-test)

The partial significance test was conducted to examine the individual effect of each explanatory variable on Foreign Direct Investment. The results are summarized in Table 5.

Table 5.
Partial Test Results (t-test)

Variable	Probability	Criteria ($\alpha = 0.05$)	Conclusion
IPS	0.0550	> 0.05	Not significant
TO	0.0022	< 0.05	Significant
RQ	0.1009	> 0.05	Not significant
LOG(GDP)	0.0000	< 0.05	Significant

Source: Processed data using EViews, 2026

The estimation results indicate that trade openness and Gross Domestic Product (GDP) significantly influence Foreign Direct Investment, whereas political stability and regulatory quality do not exhibit statistically significant effects at the 5% significance level.

Political stability has a positive regression coefficient ($\beta = 0.426815$) with a probability value of 0.0550. Although the estimated coefficient indicates a positive relationship, the effect is not statistically significant at the conventional 5% significance

level. Nevertheless, the probability value is close to the threshold, suggesting that political stability may still be associated with FDI, although the available evidence is insufficient to confirm this relationship statistically within the present sample.

Regulatory quality exhibits a negative coefficient ($\beta = -0.449964$) with a probability value of 0.1009, indicating that its effect on FDI is statistically insignificant. Consequently, no empirical evidence is found to support the hypothesis that improvements in regulatory quality significantly influence FDI inflows during the study period.

Trade openness has a positive and statistically significant coefficient ($\beta = 0.008146$, $p = 0.0022$). Because the dependent variable is expressed in natural logarithms while trade openness is measured in percentage points, the coefficient implies that, holding other variables constant, a one-percentage-point increase in trade openness is associated with approximately a 0.81% increase in Foreign Direct Investment.

Gross Domestic Product (GDP) also has a positive and highly significant coefficient ($\beta = 1.059661$, $p < 0.001$). Since both FDI and GDP are expressed in natural logarithms, the estimated coefficient represents an elasticity. Thus, holding other variables constant, a 1% increase in GDP is associated with approximately a 1.06% increase in Foreign Direct Investment. This finding indicates that larger economies tend to attract proportionally greater foreign investment than smaller economies.

Trade Openness and Foreign Direct Investment

The empirical results indicate that political stability has a positive coefficient but does not significantly affect Foreign Direct Investment (FDI) at the 5% significance level ($\beta = 0.426815$; $p = 0.055$). Accordingly, Hypothesis 1 is not supported. Although the estimated coefficient suggests that improvements in political stability are associated with higher FDI inflows, the statistical evidence is insufficient to confirm this relationship for the sample of eleven Southeast Asian countries during the 2014–2023 period. Nevertheless, the p-value is close to the conventional significance threshold, indicating that political stability may still play a role in attracting foreign investment, although its influence is not consistently observed across countries.

From the perspective of the OLI paradigm (Dunning, 2003), political stability constitutes an important component of location advantage, as stable political conditions reduce uncertainty, strengthen investor confidence, and improve the predictability of long-term business operations. However, the insignificant finding suggests that political stability alone may not adequately explain cross-country variations in FDI within Southeast Asia. Other economic characteristics, including market size and trade integration, may provide stronger signals for multinational enterprises when selecting investment locations.

This finding differs from previous studies conducted by Bohle and Regan (2021) and Afif (2022), which reported that political stability positively influences FDI by reducing investment uncertainty. One possible explanation is that Southeast Asian countries exhibit substantial heterogeneity in terms of institutional quality, economic development, and investment structures. During the study period, several countries continued to attract considerable FDI despite experiencing varying levels of political stability, whereas others with relatively stable political conditions received comparatively lower investment inflows. Consequently, the relationship between political stability and FDI appears to be less uniform than originally hypothesized.

The insignificance of political stability should therefore be interpreted cautiously. The regression results indicate only that the statistical relationship is not sufficiently strong within the observed sample and period; they do not imply that political stability is unimportant for investment decisions. Instead, the findings suggest that political stability may interact with other institutional and macroeconomic factors that were not explicitly incorporated into the present model.

Regulatory Quality and Foreign Direct Investment

The results further reveal that regulatory quality does not significantly influence Foreign Direct Investment ($\beta = -0.449964$; $p = 0.1009$). Therefore, Hypothesis 2 is not supported. Although the estimated coefficient is negative, the relationship is statistically insignificant, indicating that changes in regulatory quality cannot be associated with systematic changes in FDI inflows during the observation period.

Within the OLI paradigm, regulatory quality represents another important dimension of location advantage because effective regulations reduce transaction costs, improve legal certainty, and facilitate business operations. The absence of statistical significance suggests that regulatory quality alone may not be sufficient to explain investment decisions across Southeast Asian countries. Instead, investors may simultaneously consider broader economic opportunities, infrastructure, labor availability, market accessibility, and regional integration when evaluating investment destinations.

The present finding differs from those reported by Kaushal (2021) and Yerrabati (2021), who found that stronger regulatory quality significantly increased FDI inflows in developing countries. One possible explanation lies in the diversity of regulatory systems across Southeast Asia. Although several countries have introduced regulatory reforms to improve the investment climate, differences in policy implementation, institutional effectiveness, administrative efficiency, and governance practices remain substantial. Consequently, improvements in regulatory quality may not immediately translate into higher FDI inflows across all countries in the region.

Another possible explanation is that multinational enterprises frequently evaluate investment opportunities using multiple criteria simultaneously. Improvements in regulatory quality may therefore become more influential only when accompanied by favorable macroeconomic conditions, political certainty, or stronger market potential. Accordingly, the insignificant coefficient should not be interpreted as evidence that regulatory quality lacks importance, but rather that its independent contribution cannot be statistically confirmed within the present model.

Trade Openness and Foreign Direct Investment

The empirical results demonstrate that trade openness positively and significantly affects Foreign Direct Investment. Hypothesis 3 is therefore supported. Holding other variables constant, a one-percentage-point increase in trade openness is associated with approximately a 0.81% increase in FDI inflows. This finding indicates that economies with greater integration into international trade tend to attract higher levels of foreign investment.

The result strongly supports the location advantage component of the OLI paradigm. Countries with more open trade regimes provide multinational enterprises with broader market access, lower trade barriers, and greater participation in regional and global production networks. These conditions reduce transaction costs and improve production efficiency, thereby increasing investment attractiveness.

The findings are also consistent with the institutional and economic developments discussed in the Introduction. Since the implementation of the ASEAN Economic Community (AEC), Southeast Asian countries have progressively strengthened regional economic integration by facilitating the movement of goods, services, investment, and skilled labor. Such integration enhances market accessibility and creates a more favorable investment environment for multinational corporations seeking production and distribution hubs within the region.

This result is consistent with Xu et al. (2021), who argued that trade openness enhances market efficiency and encourages international investment. Similarly, Rakshit (2022) found that trade liberalization increases investor confidence by reducing tariff and non-tariff barriers, while Albab (2025) emphasized that greater market access encourages export-oriented FDI. Collectively, these findings reinforce the argument that trade openness represents one of the most important economic determinants of FDI in Southeast Asia.

Gross Domestic Product and Foreign Direct Investment

The estimation results further indicate that Gross Domestic Product (GDP) has a positive and highly significant influence on Foreign Direct Investment. Hypothesis 4 is supported. Specifically, a 1% increase in GDP is associated with approximately a 1.06% increase in FDI, holding other variables constant. Because both variables are expressed in natural logarithms, the estimated coefficient represents an elasticity between market size and foreign investment.

This finding is consistent with the OLI paradigm, which identifies market size as one of the principal components of location advantage. Larger economies generally provide stronger purchasing power, greater production capacity, and broader market opportunities, thereby increasing expected returns for multinational enterprises. Consequently, countries with larger GDP tend to become more attractive destinations for long-term foreign investment.

The result also aligns with previous empirical studies. Kumari et al. (2023) found that GDP growth significantly stimulates FDI by expanding domestic market potential, while Raza et al. (2021) reported that stronger economic performance encourages foreign investment, particularly when supported by effective governance. Similarly, Tomayahu et al. (2021) argued that countries experiencing sustained economic expansion are more likely to attract multinational enterprises seeking long-term business opportunities.

Nevertheless, the interpretation of this finding should consider the characteristics of the sample. Throughout the study period, Singapore consistently recorded substantially higher FDI inflows and GDP than most other Southeast Asian countries, potentially exerting considerable influence on the estimated coefficients. Although the Random Effect Model accounts for cross-country heterogeneity, the dominance of Singapore suggests that future studies should perform additional robustness analyses, such as excluding Singapore from the sample, estimating Fixed Effect models, employing robust standard errors, or using FDI as a percentage of GDP, to examine whether the estimated relationships remain consistent.

Overall, the findings suggest that macroeconomic factors, particularly trade openness and GDP, provide stronger empirical explanations for FDI inflows than institutional variables during the observation period. While political stability and regulatory quality remain theoretically important components of location advantage within the OLI paradigm, their independent effects were not statistically supported in this study. These results imply that

policies aimed at expanding market capacity and strengthening economic integration may generate more immediate impacts on attracting Foreign Direct Investment across Southeast Asian countries.

CONCLUSION

Based on the results of this study, it can be concluded that economic and institutional factors have different effects on Foreign Direct Investment (FDI) inflows in Southeast Asia during the 2014–2023 period. Political stability and regulatory quality do not have a significant effect on FDI, indicating that foreign investors tend to be adaptive to political risks and do not always consider regulatory aspects as the primary determinant, as long as economic profit potential remains high. In contrast, trade openness and Gross Domestic Product (GDP) are found to have a positive and significant effect on FDI, confirming that market size and the level of international trade integration are the main factors in attracting foreign investment in the region.

Based on these findings, governments in Southeast Asian countries need to strengthen trade openness through policy harmonization and improved logistics connectivity to enhance market efficiency and cross-border investment. In addition, economic growth should be supported through the development of physical and digital infrastructure to increase competitiveness, particularly for countries with lower economic capacity. Although political stability and regulatory quality are not found to be significant, efforts to maintain socio-political stability and strengthen legal certainty remain important to sustain investor confidence. Furthermore, regulatory reforms through the digitalization of licensing services, along with improvements in human capital quality and technological innovation, should become long-term priorities to enable Southeast Asia to attract higher-quality and more sustainable investment.

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