THE INFLUENCE OF
GOVERNMENT POLICY AND NGOS
ON CAPTURING PRIVATE INVESTMENT

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Breakfast Session 1: New frontiers in investment promotion

The Influence of Government Policy and NGOs on Capturing Private Investment

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ABSTRACT

Our paper applies new institutional economics theory to a unique data set of the world's low-income economies to examine the association between host governments' social policies and their ability to attract foreign direct investment. We add to this another new data set to explore the direct and indirect role of nongovernmental organizations (NGOs) in the business-society-government interface. We find that a host government's social inclusion policies are strongly associated with a country's FDI inflows. NGOs, however, obtain no statistically significant indirect effect on this relationship and only weak statistical significance as a direct influence on FDI inflows. Despite these mixed results, the findings of this exploratory study suggest future directions of research of interest to policy makers and business scholars.

Key words: foreign direct investment, globalization, nongovernmental organizations (NGOs), social policies

Globalization, the "ongoing process of integration and interconnection of states, markets, technologies, and firms," (Barkema, Baum, and Mannix, 2002) appears to be here to stay. Increased levels of trade and foreign direct investment worldwide, a cause or effect of the closer interdependence of world economies, are a reality. One of the most striking trends of recent increases in private investment is the emergence of nongovernmental organizations (NGOs) as important conduits for aid and as providers of development services in low-income economies. According to the United Nations Development Program, by the end of the 20th century more than 50,000 NGOs were working at the grass-roots level in developing countries, and their activities were affecting the lives of 250 million individuals (Besley and Ghatak, 1999). The increasingly important role of NGOs as they have advanced from mere service-providers to major players with the funds and potential to influence policy and institutions has received ample empirical and theoretical attention (Besley and Ghatak, 1999; Doh and Guay, 2006; Eden, 2004; Keim, 2003; Nancy and Yontcheva, 2006; Teegen, Doh, and Vachani, 2004). Further, as the civil society counterparts of multinational enterprises (MNEs) and governments, NGOs have become "major new organizational forms and vehicles to deliver social services such as poverty relief and environmental protection" (Teegen *et al.,* 2004: 475). They have influenced corporate strategy by inducing firms to seek a competitive advantage through reputational assets or by responding to pressures from the "moral marketplace" (Hess, Rogovsky, and Dunfee, 2002), and they have caused many corporate executives to internalize their commitment to social objectives and corporate social responsibility "even when there is no apparent economic benefit to the firm or other individual" (Doh and Guay, 2006: 58). In the international arena NGOs often create and institutionalize new norms in the societies where they operate (Keck and Sikkink, 1998; Lawrence, Hardy, and Phillips, 2002).

Private investment, NGOs, and the latter's role in the ability of host governments to promote private investment into their local economies, are the focal point of this paper and new institutional economics provides the underpinning rationale that guides its logic. We start with the premise that NGOs (civil society organizations) influence the institutional context in which they operate; the same context that defines the choice sets of multinational firms (the private sector) when they invest in host governments (the public sector). The institutional environment provides the framework in which an NGO operates, but an NGO can also establish formal rules and informal norms of its own that in turn influence, over time, other actors in society. What is the relationship among these private, public, and civil society sectors? Do NGOs modify the impact of host government policies (as manifestations of formal institutions) on the private sector? What is the influence of NGOs when they act alone in the institutional setting as compared to their influence when they act in tandem with host government policy? How do they affect the local environment that is perceived by foreign investors?

We seek to answer these questions as we examine the relationship among actors in three sectors of society: NGOs, host governments, and business. Building on the elements of new institutional theory highlighted above, this paper examines NGOs and host government policy, the former as "agents of globalization" (Teegen *et al.,* 2004) and the latter as promoters of social welfare and inclusion (wealth distribution). It then tests the direct effect of each as well as the moderating role of NGOs in influencing firm-level private investment.

This paper purports to shed light on the interconnectedness of a society's business, public and civil society sectors across developing countries. It empirically tests the effectiveness that a host government's social policies have in attracting private investment as well as the emerging role of NGOs in today's globalized world. Its main contribution is to add to the public policy/NGO research stream a new set of data and an understanding of how the main forces in society operate and *co*operate in promoting foreign direct investment. It is hoped that scholars will conduct further research to refine our understanding of the dual role of host government policy and NGOs in the

"ongoing process of integration and interconnection of states, markets, technologies, and firms," (Barkema, Baum, and Mannix, 2002).

The paper takes the following format. First, we present background information on nongovernmental organizations. We then develop our theoretical rationales and propose hypotheses grounded in these theories. Finally, we present our data, explain the methodology used to test our hypotheses empirically and provide the results of our tests. We close the paper with a discussion of the results and concluding remarks.

NONGOVERNMENTAL ORGANIZATIONS (NGOs)

Non-governmental organizations (NGOs) are non-profit, voluntary citizens´ groups that are organized on a local, national or international level. They may be of three types: 1) advocacy NGOs, that promote before governments or in international for the interests of groups who do not have either voice or access to do so themselves; 2) operational NGOs, that provide goods and services to needy clients; and 3) "hybrid" NGOs, which perform both of the previous functions (Doh and Teegen, 2003). Generally, they are organized around specific issues (some of their most visible and most successful work has been in the areas of human rights, health and environmental protection), and in their areas of concern they can serve as early warning mechanisms or monitors of official agreements. NGOs have operated in areas such as social services for decades, often in collaboration with governments or private partners. The United States has a particularly rich history of these types of partnerships (Salamon 1987).

In the academic literature, NGOs have been categorized as membership or "club" NGOs and social purpose NGOs (Teegen *et al.,* 2004). The former refers to those nongovernmental organizations that "tend to promote the material, social, or political interests of their own members" (Putnam, 2002: 11), while the latter refers to those NGOs that have exclusively social (including human rights and environmental) agendas (Teegen *et al*., 2004: 466). In the remainder of this paper, we follow Teegen *et al*.'s (2004) definition and use of the term NGO to mean social purpose NGOs:

> NGOs are private, not-for-profit organizations that aim to serve particular societal interests by focusing advocacy and/or operational efforts on social, political and economic goals, including equity, education, health, environmental protection and human rights. (Teegen *et al.,* 2004: 466)

NGOs offer a number of distinct advantages that can enhance the provision of social services or the promotion of social needs, whether on their own or in cooperation with business or government. They include the following (Nancy and Yontcheva 2006; Yaziji 2004):

- They generally enjoy a great degree of legitimacy in the eyes of the public;

- They are well attuned to public concerns, and to the needs of specific groups that might not be represented by the market or defended by the government;

- Their dense, extensive networks are different from those of the typical MNE or government;

- Their members and representatives have technical expertise in the issue at hand, often due to having worked in difficult settings or with underserved populations;

- They are often more cost-effective than their private or public partner.

Although NGOs also suffer from some drawbacks –chief among them their relative immunity from transparency and accountability and their dependence on donors for funds, which are often scarce (Kapstein, 2000) -- their strengths have led governments and multilateral institutions to direct more and more funding through them. Although precise figures are difficult to obtain, the OECD noted that

the funds that industrialized economies channelled through NGOs rose from 0.2% of their total bilateral official development aid (ODA) in 1970 to 17% in 1996 (Wood, 2003). In Africa, by 1994 already 12% of foreign ODA was being funnelled to the region through NGOs, and the number has continued to rise (Chege, 1999). Transfers of official developed-country aid to NGOs in 2006 totalled more than $2bn of total ODA, about 123% more than in 2002 (OECD.Stat and Epstein and Gang, 2006).

The OECD figures in Appendix A demonstrate how significant aid through NGOs has become as a percentage of all bilateral ODA for the member nations in the Development Assistance Committee (DAC)[1], especially Ireland and the Netherlands, where it represents about 20% of the total. Italy, the United Kingdom, New Zealand, Sweden, Denmark, Canada and Switzerland also direct a large proportion of their development aid through NGOs. In cases like the Netherlands, New Zealand or the United Kingdom, this proportion has risen steadily over the 2000-2006 period, partly in response to a conscious government decision to direct more aid through these channels in order to increase aid effectiveness. In the United States, Congress mandated in the late 1980s that 13.5% of US funding of international development efforts should be passed through PVOs (Private Voluntary Organizations), and USAID stated in its latest report that PVOs receive about a third of USAID´s development assistance budget.[2] Unfortunately, since the United States does not make NGO aid flows publicly available, it is not possible to determine how much ODA goes through this conduit.

THEORY AND HYPOTHESES

Host governments have always been concerned about how to position themselves in an increasingly competitive market for a limited supply of investment resources. Why should a multinational firm choose one host country over another when many of these countries offer similar attractions (tax breaks, profit repatriation, low domestic content requirements, etc.)? How can one country strategically position itself against others in the chase after cash inflows in the form of FDI?

More important, does this competition for funds involve the way a recipient country treats its citizens? Do multinational corporations (and their FDI) respond to the institutional environment of a host country on a social policy level? At the firm level, recent empirical research has corroborated the association between "good" companies and higher profit levels (Mackey, 2007) and, conversely, "bad" companies and decreasing bottom lines (Harris and Bromiley, 2007). We ask whether the same relationship applies at the country level: that is, are "good" countries rewarded with more private investment. Is there an association between pro-social public policy and levels of global private investment? We are particularly interested in those economies in earlier stages of development, where pro-social policies are a rarer phenomenon, as they provide a fertile empirical testing ground for our hypotheses. We can then restate our question thus: What is the relationship between the ability of an emerging country (host country) to attract private investment and the quality of public policies affecting the life of its citizens? Are pro-social host government policies in emerging countries linked to higher inward flows of foreign direct investment to that country?

To answer these questions, we rely on the theoretical underpinnings of the new institutional economics. Beginning with the premise that institutions matter (North, 1990; Williamson, 2000), the institutional environment refers to the set of fundamental political, social, and legal ground rules that establishes the basis for production, exchange, and distribution (Davis and North, 1971) and defines the conditions under which business occurs (North, 1990). Institutions are the humanly devised rules of the game, both formal and informal norms of behaviour. Formal institutions are explicitly created,

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[1] The percentages in the table are calculated using the data available in OECD.Stat. However, the DAC Development Co-operation Report gave substantially higher estimates of Commitments support to/through NGOS as a share of total bilateral commitments for the 2001-2002 period, ranging from a high of 14.1% for Sweden to a low of 0.6% for France.

[2] USAID Chapter 6: Sources and amounts of private aid, p. 13 (http://www.usaid.gov/fani/ch06/privateaid12.htm).

usually by law and government (North, 1990) and include the formal written rules, regulations, laws and contracts that represent the choices made by a society to give structure to its relations with others.

Implicit in the theoretical tenets of this theory is that formal institutions lessen uncertainty. They spell out in written form what is acceptable and what is not and thus promote more cost-efficient transactions to take place. Assuming that transaction costs are everywhere (Coase, 1937) and that institutions mitigate the costs associated with carrying out transactions in a society, it follows that efficient markets depend on market-based supporting institutions (North 1990). Therefore, the formal institutions of a society, those political, *social*, and legal rules of the game that a country has in place (Davis and North, 1971), have important consequences for foreign investors.

While the components of the institutional environment of most interest to social scientists in the management field have typically been those legal and political constraints that encourage or discourage a multinational firm in the daily operations of its businesses overseas (Click, 2005; (Delios and Beamish,1999; Delios and Henisz, 2003; Hill, 1998; Kobrin, 1979, 1982; Moran, 2004; Oxley, 1999; Yu and Cannella, 2007), there has been a dearth of studies exploring the *social* ground rules in place in a host country's institutional environment. We ask whether host governments that proactively promote pro-social policies for their citizens are in a better position to reap the benefits of globalization. Do those host countries that devote resources to social policies and institutions compete more effectively for multinational firms' foreign direct investment projects? Does FDI flow toward environments that have better distributions of wealth and more broadly shared benefits of growth and development for citizens?

Institutional theory posits that institutions mitigate transaction costs by reducing uncertainty and establishing a stable structure to facilitate interactions, thus enhancing efficiency. Consequently, those host governments that have put into place pro-social, formal institutions that embrace sound policies would help investors to see them as more efficient, would send positive signals to the marketplace --that is, private investment--, and would, therefore, enhance the host government's chances of capturing foreign direct investment. We would expect such policies to underpin a country's ability to attract multinational firms to invest there and thus increase its levels of foreign direct investment. We thus posit the following hypothesis:

H1: Ceteris paribus, host government social policies will be positively associated with a country's ability to capture private investment.

We now introduce the role of nongovernmental organizations into the conversation. NGOs have changed the way that governments and corporations do business and have altered the dyadic relationship between government and business. If we view NGOs as organizations, we can continue to apply new institutional economics logic. Organizations, embedded within the institutional framework, are supported and constrained by institutional forces (Scott, 1995) and it is the interaction between organizations and institutions that shapes economic activities across borders (North, 1990; Scott, 1995). Indeed, management scholars have long noted the importance of non-market, institutional factors for multinational firms' strategic decisions, such as choosing a foreign location for their direct investment (Boddewyn and Brewer, 1994; Dunning, 1998).

NGOs are organizations embedded in the institutional fiber of a society. As "new organizational forms" they influence how business is carried out in countries where they have a presence because they are attuned to specific groups' needs and wants. They are often able to influence public opinion and have been successful in getting governments and multilateral institutions to direct more and more funding through them. Further, as "agents of globalization," nongovernmental organizations demand attention not only from governments and multilateral institutions but also from multinational corporations that look overseas for potential foreign direct investment locations. They form an integral part of the institutional context of a country and are often a third party in the business-government interface. We therefore posit that a country that has high levels of NGO presence will

more likely to attract private investment in an increasingly competitive market of recipient countries. Thus:

H2: Ceteris paribus, the presence of NGOs in a host country will be positively associated with a country's ability to capture private investment.

The impact of NGOs on private investment may not only be a direct one, however. It is possible that as two important components of a society's institutional environment, NGOs work in tandem with a host government to secure better outcomes for the greater good. As we predict a positive direct association between "good" government social policy, i.e., one that is beneficial to citizens, and levels of inward foreign direct investment (H1), we further predict that the presence of NGOs in a host country will increase the intensity of that relationship. We therefore state the following hypothesis:

H3: Ceteris paribus, the presence of NGOs in a host country will increase the direct effect of that country's social policies on its ability to capture private investment.

METHODS

Sample

Our sample of 59 countries was drawn from the group of countries that are the poorest and least creditworthy in the world, and as such are eligible for International Development Assistance loans from the World Bank. To determine how much to lend to each country, the World Bank staff has developed a Country Policy and Institutional Assessment (CPIA) that scores these countries on the quality of their policy performance in four basic areas: Economic Management, Structural Policies, Policies for Social Inclusion/Equity, and Public Sector Management and Institutions. Three of these areas are not new to empirical analysis, since numerous rankings have been developed to assess the quality of institutions and performance in economic management, structural policies and public sector management. What is new and interesting to researchers about the CPIA is that it includes numeric scores to reflect the quality of pro-social policies, and that those detailed scores were recently made public for the first time, in 2006.

In this study, we use as independent variables the CPIA rankings, in particular those that refer to pro-social policies or policies promoting social inclusion (explained more fully below). Since the scores are only recently available, it is not possible to compare 2005 scores with those obtained in previous years to determine whether major policy changes have occurred. The World Bank, however, states that little change is likely in the overall CPIA rankings from year to year, since the criteria focus on the quality of policies and institutions, which tend to be longer-term in nature. This should mean that the single year for which full numerical scores have been made available -- 2005 -- should serve as an adequate reflection of the policy and institutional environment for each country in recent years. To ensure that the single score does reflect a fairly stable institutional environment, we compared the overall 2005 CPIA score with the quintile rankings for 2002-2004, which are publicly available. As a result, of the original pool of 77 countries ranked in 2005, ten were dropped because they had been ranked on fewer than two quintiles or because their quintile ranking on the CPIA had varied by more than one position between 2002 and 2005 (e.g., a move from 1st to 2nd quintile was considered to reflect a fairly stable institutional environment over the period but a move from 1st to 3rd was not). A further four countries were dropped due to lack of homogeneous GDP or FDI data from the World Bank. This left a pool of 62 countries with adequate data and stable CPIA rankings for the empirical analysis. We later had to drop three more countries due to other missing data, however. Appendix B provides a list of the countries in our final sample.

Data

To empirically test the role of NGOs in low-income countries and their contribution to private investment, a data set had to be obtained that reflected the presence of NGOs in the individual recipient countries. Obtaining this data was a major challenge. The OECD, in its excellent reporting of data on private and official development aid from member nations, does not offer a breakdown of NGO aid by recipient country. The alternative of searching for the data from the NGOs themselves was not only daunting --tens of thousands of NGOs are present in developing countries— but it also turned out to be impossible since many do not report their expenditures by country. The only alternative to was to approach each of the countries in the DAC for data on how much of their development aid to the countries in our study was channelled through NGOs. Since some donor countries report data only by region, they were excluded from our data set; and the biggest donor of all, the United States, declined to release any of its NGO data by recipient country or region. The sheer size of U.S. giving, combined with the preference for private and voluntary channels for ODA in that donor nation, makes this omission especially serious for a study of this type[3].

There are additional reasons why the data we were able to obtain represent very low estimates of actual NGO development spending and other important omissions in the NGO and private aid data. The figures reported by those governments that do publish them normally reflect only the official aid given to or channelled through these agencies, and not the NGO spending funded by autonomous sources such as private volunteer giving, which is substantial and surpasses public-sector contributions in many cases. (A 2007 USAID report estimated that PVOs in the United States received only 10% of their funding from the government (USAID), with 80% coming from private donations and 10% from other sources[4]). As a result of these factors, the official NGO figures used in this report are very low estimates of the total.

Measures

Dependent variable. FDI flows to emerging market economies have increased dramatically over the past 15 years, despite the financial market setbacks in many countries (Brukoff and Rother, 2007). In fact, multinational firms provide the largest proportion of worldwide FDI monies and are the single largest source of emerging markets' net capital inflows (IMF 2003). It can be expected that these multinational firms would be selective about the host countries where they choose to invest, particularly when they are selecting among the world's poorest developing countries.

As a proxy for private investment by MNCs worldwide, we use levels of foreign direct investment as our dependent variable. We measure it by using the natural log of FDI net inflows (**LNFDI**) to a recipient country, averaged for two years, 2000 and 2005. FDI net inflows serve as a reflection of the confidence that foreign investors have in the local economy and their expectations of growth, economic success and company profits on an aggregate level. We follow the IMF's definition of FDI: *international investment that reflects the objective of a resident in one economy (the direct investor) to obtain a lasting interest in an enterprise resident in another economy (the direct investment enterprise). A direct investment relationship is established when the direct investor has acquired ten percent or more of the ordinary shares or voting power of an enterprise abroad (5th Edition of the IMF's Balance of Payments Manual (BPM5).*

Independent variables. The construct of host government social policies (**SOCIALPOL**) is operationalized by the social policy (a formal institution) used by host governments in our sample of 59 developing countries. The construct of societal formal institutions is measured by using social

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[3] There is much speculation over why NGO figures are so difficult to come by. One source that has worked with the data for several decades alleges that the sheer size of the flows has created opportunities for corruption and misuse of funds that officials are reluctant to reveal.

[4] 2007 Volag Report of Voluntary Agencies.

welfare as a proxy for the policies of a host government that address the well-being of its citizen. This measure is a numerical score encompassing five distinct dimensions that together measure the extent to which a country's policies for social inclusion and equity support sustainable growth and poverty reduction. The World Bank's Country Policy and Institutional Assessment (CPIA) was the source for this measure. Appendix C gives a detailed description.

Our measure for the influence of NGOs **(NGOs)** in each of the 59 developing countries in our sample is the data set we compiled from each of the countries in the DAC that report the development aid channelled through NGOs to the countries in our sample. (See Appendix D for a list of the developed countries that use NGOs.) Despite the limitations and inevitable measurement error in our new series, it is the first set of its kind and therefore has merit on its own. We therefore decided to use this measure as the main variable representing NGOs in the empirical portion of our paper.

To check the robustness of our results, however, we compiled a second data set with a simple count of the number of NGOs operating in each of the recipient countries in our sample, taken from *The Directory of Development Organizations 2008*. The Directory is published by a not-for-profit organization located in The Netherlands, with the objective of facilitating "international cooperation and knowledge sharing in development work, both among civil society organizations, research institutions, governments and the private sector" (http://www.devdir.org/index.html). Starting in 1997 (although available online since only 2000), the directory now lists 53,750 development organizations in 228 countries. It is divided into six geographical sections (Africa, Asia and the Middle East, Europe, Latin America and the Caribbean, North America, and Oceania) and uses nine classifications to categorize the development organizations around the world: (1) international organizations; (2) government institutions; (3) private sector support organizations (including fair trade); (4) finance institutions; (5) training and research centers; (6) civil society organizations; (7) development consulting firms (including references to job opportunities and vacancy announcements); (8) information providers (development newsletters/journals); and, (9) grant makers. After consulting with the head economist at *The Directory of Development Organizations,* we determined that for our research purposes we should focus exclusively on group 6: civil society organizations (CSOs). For the 62 countries in our sample, one country is not included in the directory (Lao PRD), and the Republic of Congo and the Democratic Republic of Congo have 23 between them. In order to include both countries in our final sample without double counting, we allocated 11 CSOs to the Republic of Congo and 12 to the Democratic Republic of Congo (for a total of 23 between the two countries). Among the remaining countries in our sample, the number of civil society organizations totals 9028.

It should be added that while The Directory of Development Organizations data suffers from obvious limitations, since it gives no idea of the relative magnitude of the different NGO projects, it at least gives an idea of how active NGOs are in different countries. Again, we used these results as a robustness check on those obtained from our preferred data set. We do not report the results of the analyses we conducted with the second measure of NGOs.

Control variables. Several alternative explanations for an increase in a recipient country's level of inward FDI flows are possible. The attractiveness of a host country for investing firms depends, in great part, on the size of its market (Contractor, 1991; Delios and Henisz, 2003; Dhanaraj and Beamish, 2004; Loree and Guisinger, 1995). We therefore control for the size and attractiveness of the host country's macro economy as an alternative explanation for multinational firms' choices to channel FDI there. To that end we include as control variables three country-level macroeconomic indicators to represent different facets of size: host country economic growth rate, host country population, and the host country's rate of inflation.

- GDP growth, the annual % change of output in real terms (**%GDPGROW**), reflects the strength of the local economy and the increase in the size of the domestic market, opening the

door to larger sales and higher profits. Thus higher GDP growth should generally be associated with larger FDI inflows.

- Population (**LNPOP**) is another indicator of market size. FDI is most likely to be attracted to economies with both large populations *and* higher GDP per capita. Following previous researchers, we use the natural log of the host country's population.

- Inflation (**INFLA**) enters the regression as a proxy for macroeconomic stability and as a reflection of the internal or external shocks suffered by the economy during the period under study, which may affect potential direct investors. A high and/or variable rate of inflation is a sign of internal economic instability and of the host government's inability to maintain consistent monetary policy. It also may boost costs, making exports from the region less competitive on international markets (Grosse and Trevino, 2005).

Two other control variables were included to reflect possible alternative explanations in a host economy that might influence a foreign investor's decision.

- If a host country produces oil (**OIL**), it may favorably skew its chances of receiving large FDI projects. We controlled for this possibility by using a dummy variable for oil producing countries (1=oil-producing; 0=otherwise).

- The openness (**OPENNESS**) of the host country, that is, its exports + imports/GDP, is controlled for because an economy more deeply integrated into the world trade system is more likely not only to receive FDI inflows but also to experience higher rates of GDP growth and per-capita GDP growth, all other things being equal (Maddison, 2001).

For the control variables, except oil, a simple average of the values for the 2000-2005 period was used in order to represent the period immediately prior to and coinciding with the CPIA social policy score. The only exception was the "count" variable for NGO, which could only be obtained for the year 2007.

An overview of all variables, their measurements, definitions, and sources is reported in Table 1.

TABLE 1

Data Labels, Measurements, Definitions and Sources

Label	Variable	Measurement	Definition	Source
LNFDI	Dependent	Natural log of FDI net inflows, averaged over two years (2000 and 2005)	Net foreign direct investment inflows, or the net inflows of investment to acquire a lasting management interest (10 percent or more of voting stock) in an enterprise operating in an economy other than that of the investor.	*World Development Indicators 2000 and 2005 (The World Bank)*
%GDPGROW	Control	5 year average (2000-2005) annual real GDP percentage growth rate	How fast output/income is growing in host country.	*World Dev. Indicators 2000-2005 (The World Bank)*
POP	Control	The natural log of 5 year average (2000-2005) of host country population	How large the host country is in terms of its population.	*World Dev. Indicators 2000-2005 (The World Bank)*
INFLA	Control	Change in annual consumer price level, average 2000-2005	Average annual increase in price level; reflection of internal and external shocks.	*World Development Indicators 2000-2005 (The World Bank)*
OIL	Control	Dummy variable: 1 = oil-producing country; 0 = otherwise	Whether the host country is an oil-producing nation.	*The Energy Information Agency website (http://eia.doe.gov/)*
OPENNESS	Control	(Imports plus exports)/GDP	The weight of trade (imports plus exports) in the national economy.	Penn World Tables
SOCIALPOL	Independent	Score 1-6, with higher numbers reflecting more pro-social policies	The extent to which a host government has policies for social inclusion in place. The overall score is based on five dimensions of social inclusion: gender equality, equity of public resource use, building human resources, social protection and labor, and policies and institutions for environmental sustainability.	*Country Policy and Institutional Assessments Questionnaire, World Bank 2005*
NGOs	Independent	The amount of official aid from DAC countries that was channeled through NGOs to development projects in the sample countries between 2000 and 2005, as % of recipient GDP.	Official aid to development channeled through NGOs	Compiled from each of the donor countries in the DAC that report the development aid channelled through NGOs to the countries in our sample

Modeling and Analysis

The relationships among these variables were assumed to be linear; an ordinary least-squares regression was used. Specifically, the four models we test take the following forms:

Model 1: $LNFDI_i = \beta_o + \beta_{i1-5} CONTROLS + \varepsilon$

Model 2: $LNFDI_i = \beta_o + \beta_{i1-5} CONTROLS + \beta_{i6} SOCIALPOL + \varepsilon$

Model 3: $LNFDI_i = \beta_o + \beta_{i1-5} CONTROLS + \beta_{i7} NGOs + \varepsilon$

Model 4: $LNFDI_i = \beta_o + \beta_{i1-5} CONTROLS + \beta_{i6} SOCIALPOL + \beta_{i8} SOCIALPOL*NGOs + \varepsilon$

where $LNFDI_i$ is the dependent variable (the natural log of FDI inflows in $country_i$), β_{i1-5} represents the set of control variables described above, β_6 represents the social inclusion policies in $country_i$, $\beta 7$ represents the level of NGO presence in $country_i$, β_{i8} represents the moderating effect of NGOs in $country_i$, and ε is the error term for the regression.

We ran our statistical tests using SPSS software and conducted robustness checks for heteroskedasticity and multicollinearity.

RESULTS

This study proposed a) to explore the association between pro-social policies and private investment in the form of FDI flows (H1); and b) to test whether the emerging international actors, NGOs, played an important role in that process (H2 and H3). The correlation and descriptive statistics matrix is provided in Table 2; the results are reported in Table 3.

TABLE 2

Correlation Table and Descriptive Statistics

Variable	Mean	Std. Deviation	1	2	3	4	5	6	7
1 LNFDI	18.0992	2.0413	1						
2 %GDPGROW	4.2157	3.1919	.447(**)	1					
3 LNPOP	15.6974	2.0047	.597(**)	.261(*)	1				
4 INFLA	14.7625	48.1228	.025	-.369(**)	.096	1			
5 OIL	.29	.457	.603(**)	.241	.501(**)	-.019	1		
6 OPENNESS	76.1712	40.9777	-.045	-.084	-.555(**)	-.180	-.157	1	
7 SOCIALPOL	3.2763	.5066	.324(*)	.311(*)	.065	-.343(**)	-.022	.094	1
8 NGOs	.2368	.2890	-.303(*)	.074	-.108	-.023	-.308(*)	-.083	-.162

* $P < .05$; ** $P < .01$

TABLE 3

Results of OLS Regression

Dependent Variable: Natural log FDI inflows	Model 1	Model 2	Model 3	Model 4
Control Variables				
% GDP growth	0.320***	0.263**	0.346***	0.283*
	(0.060)	(0.057)	(0.059	(0.057)
Population	0.541***	0.49***	0.529***	0.449***
	(0.119)	(0.111)	(0.116)	(0.11)
Inflation rate	0.161*	0.23**	0.163*	0.224**
	(0.004)	(0.004)	(0.004)	(0.004)
Oil producer	0.314**	0.354***	0.260**	0.312***
	(0.433)	(0.404)	(0.443)	(0.43)
Open economy	0.360**	0.321***	0.335**	0.306***
	(0.005)	(0.005)	(0.005)	(0.005)
Independent Variables				
Social inclusion policies	0.267**		0.254**	
			(0.339)	(0.339)
NGOs	-0.160*			
	(0.610)			
Soc. inclusion policies*NGOs		-0.105		
		(0.198)		
N	59	59	59	59
Constant	6.720	4.224	7.266	4.817
R^2	0.643	0.701	0.665	0.710

As the correlation table illustrates, multicollinearity does not appear to be a severe problem in this dataset. The maximum variance inflation factor (VIF) obtained was 2.059 and the overall mean VIF was 1.5031, substantially below the rule-of-thumb cut-off of 10 for multiple regression models (Neter, Wasserman, and Kutner, 1985: 392).

As Table 3 indicates, all control variables performed largely as expected. One of the key variables of interest in this study, host government social policies, was strongly and statistically significant. The positive association that we predicted between pro-social government policies and private foreign direct investment was confirmed. Hypothesis 1 therefore found support. NGO presence in the countries in our sample yielded mildly statistically significant coefficients when it entered the model directly, giving marginal evidence to support Hypothesis 2. When we tested the moderating effect of NGOs on the role of host government social inclusion policies, however, the statistical significance evaporated. Hence, our prediction of a positive indirect effect of the presence of NGOs (indicating that NGOs work in tandem with government policy to attract private investment) was not confirmed. This implies that while NGOs on their own play a small role in the levels of inward FDI flows to a developing country, this role is not as important as the policies themselves to send a positive signal to the market place. No moderating effect further indicates that the supplementary relationship that we expected between social policies and private investment in the poorest developing countries is simply not there.

The results for the NGO variable were corroborated when we tested Models 2 and 4 using our second measure of NGO presence (a simple count measure) in the 59 sampled countries. No statistical significance was achieved either as a direct or indirect effect.

DISCUSSION AND CONCLUSION

While our results seemed to confirm the role of the institutional environment in attracting private investment insofar as a host government's social policies are concerned, the role of NGOs was not as strong as we had expected. The most obvious reason behind NGO´s poor showing is the preliminary nature of the two data sets that we compiled for the study. Figures on NGO activity are still very difficult to obtain, and our series could contain enough omissions and measurement error, as discussed above, to distort the coefficients. Other than the count mesure we used as a second measure, we could discover no alternative data set on NGO presence to provide more robustness checking on our results. We are aware of only one other paper which has attempted to empirically test NGOs' role in the aid and development process (Nancy and Yontcheva, 2006), and that paper relied on figures provided by the EU Commission on the matching aid channelled through European NGOs. The figures they used are no longer publicly provided because the Commission considers them to be unreliable.[5] If better data were available, the results of our regressions might have been different and could have confirmed a more crucial role for NGOs in developing countries and in the process of private investment flows..

Another possible explanation for the lack of strong positive associations between NGO activity or FDI flows and policies promoting social inclusion in development countries is a simple question of sample selection. By choosing to focus on the poorest and least creditworthy developing countries, we biased our sample toward countries that had lower GDP per capita and were therefore likely to have poorer social policies and institutions than those found in more developed countries. FDI is less likely to flow to countries like those in our sample simply because they are poorer. To wit, some international business scholars have highlighted the regional as opposed to global pattern of FDI these past thirty years as more than 75% of FDI occurs among the triad nations of the world, namely the U.S. the E.U., and Japan (Rugman, 2000). This phenomenon could predispose the data toward a weak association (such as the one we found) or even a negative association between FDI and the policy variables. A similar effect could bias the NGO results: the countries where NGO aid is most needed

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[5] Commission representatives say that a reasonable data set reflecting the activities of European NGOs in developing countries could be available later in 2008.

may naturally be those that are least attractive for foreign investors. At the same time, donor countries may be more likely to use NGOs as investment channels for the countries with poorer institutions and worse social policies, in an effort to bypass corrupt or inefficient governments and make their own aid more effective. Hence there could be a tendency to find more NGO activity in countries with less socially inclusive policies. This selection bias could play a large role in our results.

Another consideration about the poor showing by our NGO variables is that the surge of NGO activity in developing countries is relatively recent. As we compiled the NGO series, we noted that for some large donor countries like Japan, the decision to channel aid through NGOs was made in the middle of the 2000-2005 period covered by our study. Clearly the role of NGOs will be larger and more observable in the future, but at the time of this study, NGO involvement in development aid was still in its infancy in many countries.

The greatest drawback of this study, therefore, was that we could not avoid serious understatement of the size and scope of NGOs in some of the lowest-income countries. As data improve, it will become easier to measure and evaluate the role of NGOs, and to test our hypotheses about the importance of their role in the developing world.

Nevertheless, despite this study's data limitations and mixed empirical results, we believe it takes an important preliminary step forward toward providing supporting evidence on the role and effectiveness of host government social policy and the role of NGOs in fostering direct investment. We positioned NGOs both as sole contributors to the process of global value creation (as proxied by private investment) and as collaborators with host governments' social inclusion policies to promote the attractiveness of a country for private investment funds. In this sense, this paper makes a contribution by providing a first attempt at laying the foundations for a fruitful research agenda for social scientists, economists, political scientists, public policy makers, and multinational corporations as they go forward in trying to understand the expanding role of NGOs on the world stage.

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NET DISBURSEMENTS OF BILATERAL OFFICIAL DEVELOPMENT AID (ODA) AND FLOWS THROUGH PRIVATE ORGANIZATIONS, AVERAGE 2000-2006

	Bilateral ODA ($US mn, current prices)	Debt forgiveness as % bilateral ODA	Aid flows through NGOs as % ODA*	Aid through international private organizations as % ODA*	Contributions to PPPs+ as % ODA*
All DAC Countries	53,625.22	18.15%	3.50%	0.98%	0.71%
Australia	1,086.04	0.11%	4.38%	0.11%	0.39%
Austria	569.114	57.64%	0.32%	0.40%	n.a.
Belgium	961	31.23%	3.57%	0.63%	n.a.
Canada	1,794.73	9.13%	4.93%	1.48%	2.91%
Denmark	1,164.49	4.81%	5.02%	n.a.	0.11%
Finland	350.66	12.89%	1.98%	1.24%	n.a.
France	4,996.89	37.88%	1.06%	0.32%	0.40%
Germany	4,461.6	33.54%	n.a.	0.26%	0.38%
Ireland	354.47	n.a.(a)	19.70%(a)	7.63%(a)	5.92%(a)
Italy	1,123.07	57.93%	8.98%	1.89%	n.a.
Japan	7,698.43	21.68%	2.85%	1.88%	0.25%
Netherlands	2,911.45	8.41%	21.37%	1.08%	1.04%
New Zealand	139.46	n.a.	6.97%(a)	1.70%(a)	0.11%(a)
Norway	1,463.97	n.a.	n.a.**	0.92%(a)	2.57%(a)
Portugal	290.4	11.79%	1.26%	0.10%	0.02%
Spain	1,339.23	23.10%	0.55%	0.13%	1.15%
Sweden	1,811.39	5.92%	6.78%	0.18%	0.84%
Switzerland	975.28	9.21%	4.79%	5.70%	0.13%
United Kingdom	4,988.09	22.94%	7.58%	3.64%	1.19%
United States	14,844.44	8.57%	n.a.***	n.a.	0.82%

Source: OECD.Stat; own calculations.

*The denominator is ODA less debt forgiveness, except in cases where debt forgiveness figures are not reported by the donor (a).

**The government of Norway does not publish its figures, but the percentage in 2000 was estimated at 25% (Lunde, 2002).

***While the U.S. government did not release its figures for use in OECD.Stat, the USAID´s 2007 Volag report estimates that support to private voluntary organizations in the United States channelled through USAID totalled $2,363mn in 2005, and to international private voluntary organizations the total was $93mn. (These organizations include only those registered with USAID as PVOs.) If these figures were divided by US ODA less debt relief, the percentage channelled through NGOs would total 18.1.

+Public-Private Partnerships.

(a) Debt forgiveness figures not reported separately by donor

APPENDIX B
58 Countries in Sample

Albania	Lesotho
Armenia	Madagascar
Azerbaijan	Malawi
Bangladesh	Mali
Benin	Moldova
Bolivia	Mongolia
Burkina Faso	Mozambique
Burundi	Nepal
Cambodia	Nicaragua
Cameroon	Niger
Cape Verde	Nigeria
Central Afr. Rep.	Pakistan
Chad	Papua New Guinea
Comoros	Rwanda
Congo, Dem. Rep.	Sao Tome and Principe
Congo, Rep.	Sierra Leone
Djibouti	Solomon Islands
Ethiopia	St. Lucia
Gambia, The	
	St. Vincent & The Grenadines
Ghana	Sudan
Grenada	Tanzania
Guinea	Togo
Guinea-Bissau	Tonga
Guyana	Uganda
Haiti	Uzbekistan
Honduras	Vanuatu
India	Vietnam
Indonesia	Zambia
Kenya	Zimbabwe

APPENDIX C
World Bank's Country Policy and Institutional Assessment (CPIA)

The CPIA has been used since the mid-1970s to assess the quality of a country's policies and institutional arrangements, in an effort to determine whether they lend support to sustainable growth and poverty reduction. (Country rankings in quintile format for the CPIA have been available since 2000, without specific scores; before that date, not even the quintile rankings were disclosed publicly.) The purpose of the assessment was to identify environments in which development assistance was most likely to be used effectively, following the World Bank's conviction that development "cannot be imported to a country from the outside; rather, it is largely a function of a country's own efforts." he Bank has used the scores in combination with per capita gross national income (GNI) to determine concessional lending and grants to low-income countries. Countries that emerge as "good performers" on the CPIA receive a higher allocation of concessional lending from the World Bank Group's International Development Association (IDA). The Bank also uses the scores internally to guide its risk assessments and interventions.

The CPIA ratings are produced for 136 IDA-eligible countries on an annual basis by World Bank staff, who assess each country's performance on individual criteria and assign a rating on a scale of 1 (low performance) to 6 (high). Country teams that are familiar with each country prepare ratings proposals based on data and diagnostic studies, and these are reviewed within each of the Bank's operational regions by the chief economist and then submitted to Bank wide review, to ensure objectivity of the scores. Bank staff meet with country authorities to ensure that all relevant available information has been used, but not to negotiate over the scores. The ratings depend on actual policies and performance rather than promises or intentions. The scores are averaged to yield a cluster score for each of the four categories defined below; and then to determine a composite country rating as the simple average of the four clusters. Over time, the criteria have been revised as thinking about development has changed. The general trend has been to move from strictly macroeconomic criteria to aspects of governance and social and structural dimensions.

The 16 criteria currently used for assessing country policy/institutional performance are grouped into four broad, equally weighted clusters: Economic Management, Structural Policies, Policies for Social Inclusion/Equity and Public Sector Management and Institutions. The specific items included in each of these categories in the current version of the CPIA are as follows:

1. Economic Management (**ECONMGMT**):
    a. Macroeconomic Management (**MACRO**)
    b. Fiscal Policy (**FISCAL)**
    c. Debt Policy (**DEBT**)
2. Structural Policies (**STRUCTURE**):
    a. Trade (**TRADE**)
    b. Financial sector (**FINANCE**)
    c. Business Regulatory Environment (**REGULATE)**
3. Policies for Social Inclusion/Equity (**SOCIALINCLUSION**)
    a. Gender equality (**GENDER**)
    b. Equity of public resource use (**EQUITY**)
    c. Building human resources (**HUMANRES**)
    d. Social protection and labor (**SOCPROT**)
    e. Policies and Institutions for Environmental Sustainability (**ENVIRONMENT**)
4. Public Sector Management and Institutions (**PUBSECTMGMT**)
    a. Property rights and rule-based governance (**PROPERTY**)

b. Quality of budgetary and financial management (**BUDGET**)
c. Efficiency of revenue mobilization (**REVENUE**)
d. Quality of Public Administration (**ADMIN**)
e. Transparency, accountability and corruption in the public sector (**CORRUPTION**).

APPENDIX D
12 DAC Countries included in NGO flow data (NGOs)

Australia	Netherlands
Austria	Portugal
Canada	Spain
Denmark	Sweden
Italy	Switzerland
Japan	United Kingdom

Finland reports NGO data only by the geographic region of the recipient, so its figures could not be included. The United Kingdom for some years does the same. The United States declined to release data for any of the period covered by this report, by recipient nation.