

Does Corruption Dent Investment? Evidence from the 1MDB Scandal and Malaysian FDI Inflows in ASEAN-5, 2000–2024

Gde PutraDananjaya*
Universitas Udayana Indonesia
E-mail: * gdedananjaya@gmail.com

Submitted:
01 September 2026

Revised:
28 September 2026

Accepted:
16 October 2026

Abstract

This study examined whether the 1MDB scandal produced a detectable effect on Malaysian foreign direct investment (FDI) inflows relative to its ASEAN peers. Using an annual World Bank panel for ASEAN-5 economies over 2000–2024, this study identifies Malaysia as the treated unit against 2015's exposure of the scandal, estimated through a two-way fixed-effects DiD model that nets out GDP per capita growth, unemployment, and trade openness.. This paper contributed to the literature on corruption, governance shocks, and international investment by offering case-specific, quasi-experimental evidence on a major sovereign-wealth-fund scandal, rather than relying solely on aggregate corruption indices. The interaction term ($MALAYSIA \times POST2015$) remained positive but statistically insignificant across Pooled OLS, Fixed Effects, Random Effects, and TWFE specifications. The Hausman test supported Fixed Effects, while diagnostics indicated no heteroskedasticity, serial correlation, or multicollinearity. A placebo test using 2012 as a false treatment year likewise yielded an insignificant coefficient, reinforcing the credibility of the main finding. Overall, the results indicated no statistically detectable reduction in Malaysian FDI inflows relative to its ASEAN peers following the public exposure of the 1MDB scandal.

Keywords: 1MDB Scandal; Foreign direct investment; Difference-in-differences; Southeast Asia; Governance shock

1. INTRODUCTION

Foreign direct investment (FDI) remains a catalyst for growth in many emerging countries (Hayat, 2019). In ASEAN, FDI drives infrastructure development, technology transfer, industrial diversification, and labour market expansion (Bhujabal et al., 2024). In ASEAN countries such as Indonesia, Malaysia, Vietnam, Thailand, and the Philippines, FDI is treated as the barometer of global investors' trust and economic stability (Hayat, 2019). Over the last 2 decades, these 5 countries have adopted more liberal economic policies to attract regional and global investment (Asongu et al., 2018; Peres et al., 2018; Saini & Singhania, 2018). In many cases of ASEAN disorder, 1 Malaysia Development Berhad (1MDB) was one of the most recognised scandals in ASEAN governance history (Jones, 2020). The scandal was officially leaked in 2015 and has become one of the biggest corruption cases involving a modern sovereign wealth fund. According to many international investigators, millions of dollars were misused through complex shell companies across

multiple countries with no jurisdiction (Jones, 2020). Because the 1MDB scandal involves various Malaysian senior politicians, it attracted international media attention, even outside the ASEAN region (Maksum, 2020). Logically, a corruption episode like this should raise an empirical question: Does the 1MDB scandal significantly affect FDI inflows in Malaysia relative to other ASEAN countries? Or can the Malaysian macroeconomy absorb that disruption without long-term damage? Therefore, this paper will treat FDI as the main variable because it can be interpreted as an indicator of global investors' trust (Lee et al., 2024).

Many previous panel studies show that corruption and FDI inflows have a significant negative relationship. Corruption is perceived as a hidden cost that may create business uncertainty (Cuervo-Cazurra, 2006; Hakimi & Hamdi, 2017). So, corruption disorders will most likely influence the tendency of capital inflows in a country (Chih et al., 2023). Accordingly, these findings support the view that institutional quality plays a significant role in determining capital inflows (Bhujabal et al., 2024). However, much of the existing literature on corruption and FDI relies on aggregate, country-level corruption indices measured across countries and over time (Krifa-Schneider et al., 2022; Qureshi et al., 2021; Thede & Karpaty, 2023). For example, Hakimi and Hamdi (2017) used the International Country Risk Guide corruption index to examine the relationship between corruption and FDI across MENA countries. Thereby capturing average institutional differences rather than the effect of a specific corruption event. In contrast, this study treats the public exposure of the 1MDB scandal in 2015 as a discrete, country-specific governance shock and compares the subsequent change in Malaysian FDI with contemporaneous changes among its ASEAN peers. This event-based, quasi-experimental approach therefore examines whether a major corruption scandal produced a detectable change in international investment, rather than whether countries with different average levels of corruption receive different amounts of FDI.

Furthermore, this paper estimates the causal effect of the 1MDB scandal on Malaysian FDI, compared with peers in other ASEAN countries, including Indonesia, Vietnam, the Philippines, and Thailand, using the Difference-in-Differences (DiD) method over the 2000–2024 period (Callaway & Sant'Anna, 2021). Research using DiD methods to study the impact of corruption and capital inflows on peer countries remains limited. Also, many papers do not cover long enough time horizons, so turbulence arising from corruption scandals over medium- or long-term horizons cannot be captured properly. Specifically, this paper asks whether the 1MDB scandal significantly affected Malaysian FDI inflows relative to those of its ASEAN peers after 2015. Moreover, this study uses a two-way fixed-effects DiD model and controls for variables such as GDP per capita growth, unemployment, and trade openness (Goodman-Bacon, 2021). In short, this study aims to contribute to the FDI literature by applying a quasi-experimental method and an ASEAN study to examine one of the biggest investment scandals, namely 1MDB.

FDI is consistently recognised as a necessary catalyst for economic development in emerging markets, although its effect depends on the sector receiving the investment and host-country conditions. Theoretically, FDI decisions are shaped not only by institutional reputation but also by macroeconomic factors, connectivity reliability, and long-term investment commitments. Among these factors, the unemployment rate is a key indicator of business stability. From an investment perspective, a high unemployment rate indicates not only a social problem but also weaknesses in domestic demand, underutilised production capacity, and unstable political conditions. GDP growth per capita is another important determinant. GDP per capita growth is a proxy for the host country's purchasing power. According to many theories, multinational companies seek not only a low-cost production base but also a host country with robust growth, as this can translate directly into expanded domestic demand. For example, in the ASEAN context, countries like Indonesia and Vietnam often use their localised economic growth as one of many attractive factors for FDI. Therefore, GDP per capita growth in this paper serves not only as a control variable but also as a signal of localised economic growth in the host country.

Trade openness also plays an important role in capturing a country's fundamental FDI activities, because lower trade barriers and greater international integration can facilitate both market-seeking and export-oriented investment. In the ASEAN context, this signal is necessary to indicate a host economy's readiness for foreign investment (Dananjaya, 2026). A more globally integrated host is perceived as more dependable for foreign investment. Much of the literature on the cross-country relationship between corruption and FDI shows a predominantly negative relationship (Chih et al., 2023; Qureshi et al., 2021; Thede & Karpaty, 2023). The theoretical mechanism underlying these findings draws on the grabbing hand hypothesis, or sand in the wheels, in which corruption is described as an unexpected transactional cost borne by foreign investors, thereby delaying the inflow of funds (Hakimi & Hamdi, 2017). Corruption also signals inconsistent law enforcement. Instability in legal regulation for international investors is often the main obstacle to investment, and reducing investment risk is necessary (Cuervo-Cazurra, 2006). Given these points, research using the Corruption Perceptions Index generally finds that more corrupt countries receive far less investment than they should (Hakimi & Hamdi, 2017).

However, another perspective, called the grease-the-wheels hypothesis, argues that in certain institutional contexts, especially in more complex bureaucracies, corruption is needed to facilitate transactions and business activities. Although this view is in the minority, it is necessary to show that the effect of corruption on FDI is not uniform but depends on the channels through which corruption occurs (Aluko et al., 2024; Krifa-Schneider et al., 2022). Nevertheless, most corruption literature empirically shows that corruption scandals ultimately deplete investor trust, especially when they directly involve an institution that manages sovereign wealth, as happened with 1MDB (Jones, 2020; Poon, 2021).

In short, this 1MDB case raises a question: if a country-level corruption scandal such as 1MDB is expected to reduce investor trust, can the damage be reflected in Malaysian FDI inflows relative to its ASEAN peers? Although the empirical expectation is clear, evidence on how the governance shakeout affects FDI remains limited, especially in the ASEAN context (Aluko et al., 2024; Jones, 2020; Krifa-Schneider et al., 2022; Poon, 2021; Thede & Karpaty, 2023). Thus, the gaps in the empirical literature strongly motivate this paper's quasi-experimental approach to estimating the effect of the 1MDB scandal on Malaysian FDI.

In ASEAN and other emerging-market contexts, many studies have used event-based methods to examine how political instability and governance shake-ups may be transmitted to FDI decisions. According to previous studies, the shakeout often does not result in short-term gains; instead, it takes time for the turbulence to be absorbed and reflected in the market (Guo et al., 2021). Thus, a longer time is preferable to a short one for explaining the governance shakeout phenomenon. Interestingly, many studies also report null or non-significant results, indicating that, in some cases, institutions experiencing governance turbulence continue to accept FDI inflows (Callaway & Sant'Anna, 2021).

Most existing research on corruption and FDI either relies on broad cross-country corruption indices that do not isolate specific scandal events. Many 1MDB papers approach the case purely from a political science and governance perspective, without translating its consequences into quantifiable investment outcomes. Not to mention that studies applying quasi-experimental designs to corruption shocks in the ASEAN context remain comparatively limited, and those that do exist tend to use shorter post-treatment windows. Correspondingly, by applying a two-way fixed-effects DiD design to a 2000–2024 ASEAN-5 panel, this paper provides a causal estimate of the effect of the 1MDB scandal on Malaysian FDI inflows. Based on the theoretical framework and empirical literature that have been discussed, this research proposes the following hypothesis:

H₁: The 1MDB scandal has a significant negative effect on Malaysian FDI inflows relative to ASEAN peers after 2015.

2. RESEARCH METHOD

Foreign direct investment (FDI) remains a catalyst for growth in many emerging countries (Hayat, 2019). In ASEAN, FDI drives infrastructure development, technology transfer, industrial diversification, and labour market expansion (Bhujabal et al., 2024). In ASEAN countries such as Indonesia, Malaysia, Vietnam, Thailand, and the Philippines, FDI is treated as the barometer of global investors' trust and economic stability (Hayat, 2019). Over the last 2 decades, these 5 countries have adopted more liberal economic policies to attract regional and global investment (Asongu et al., 2018; Peres et al., 2018; Saini & Singhania, 2018). In many cases of ASEAN disorder, 1 Malaysia Development Berhad (1MDB) was one of the most recognised scandals in ASEAN governance history (Jones,

2020). The scandal was officially leaked in 2015 and has become one of the biggest corruption cases involving a modern sovereign wealth fund. According to many international investigators, millions of dollars were misused through complex shell companies across multiple countries with no jurisdiction (Jones, 2020). Because the 1MDB scandal involves various Malaysian senior politicians, it attracted international media attention, even outside the ASEAN region (Maksum, 2020). Logically, a corruption episode like this should raise an empirical question: Does the 1MDB scandal significantly affect FDI inflows in Malaysia relative to other ASEAN countries? Or can the Malaysian macroeconomy absorb that disruption without long-term damage? Therefore, this paper will treat FDI as the main variable because it can be interpreted as an indicator of global investors' trust (Lee et al., 2024).

Many previous panel studies show that corruption and FDI inflows have a significant negative relationship. Corruption is perceived as a hidden cost that may create business uncertainty (Cuervo-Cazurra, 2006; Hakimi & Hamdi, 2017). So, corruption disorders will most likely influence the tendency of capital inflows in a country (Chih et al., 2023). Accordingly, these findings support the view that institutional quality plays a significant role in determining capital inflows (Bhujabal et al., 2024). However, much of the existing literature on corruption and FDI relies on aggregate, country-level corruption indices measured across countries and over time (Krifa-Schneider et al., 2022; Qureshi et al., 2021; Thede & Karpaty, 2023). For example, Hakimi and Hamdi (2017) used the International Country Risk Guide corruption index to examine the relationship between corruption and FDI across MENA countries. Thereby capturing average institutional differences rather than the effect of a specific corruption event. In contrast, this study treats the public exposure of the 1MDB scandal in 2015 as a discrete, country-specific governance shock and compares the subsequent change in Malaysian FDI with contemporaneous changes among its ASEAN peers. This event-based, quasi-experimental approach therefore examines whether a major corruption scandal produced a detectable change in international investment, rather than whether countries with different average levels of corruption receive different amounts of FDI.

Furthermore, this paper estimates the causal effect of the 1MDB scandal on Malaysian FDI, compared with peers in other ASEAN countries, including Indonesia, Vietnam, the Philippines, and Thailand, using the Difference-in-Differences (DiD) method over the 2000–2024 period (Callaway & Sant'Anna, 2021). Research using DiD methods to study the impact of corruption and capital inflows on peer countries remains limited. Also, many papers do not cover long enough time horizons, so turbulence arising from corruption scandals over medium- or long-term horizons cannot be captured properly. Specifically, this paper asks whether the 1MDB scandal significantly affected Malaysian FDI inflows relative to those of its ASEAN peers after 2015. Moreover, this study uses a two-way fixed-effects DiD model and controls for variables such as GDP per capita growth, unemployment, and trade openness (Goodman-Bacon, 2021). In short, this study aims to contribute to the FDI literature by applying a quasi-experimental method and an ASEAN study to examine one of the biggest investment scandals, namely 1MDB.

FDI is consistently recognised as a necessary catalyst for economic development in emerging markets, although its effect depends on the sector receiving the investment and host-country conditions. Theoretically, FDI decisions are shaped not only by institutional reputation but also by macroeconomic factors, connectivity reliability, and long-term investment commitments. Among these factors, the unemployment rate is a key indicator of business stability. From an investment perspective, a high unemployment rate indicates not only a social problem but also weaknesses in domestic demand, underutilised production capacity, and unstable political conditions. GDP growth per capita is another important determinant. GDP per capita growth is a proxy for the host country's purchasing power. According to many theories, multinational companies seek not only a low-cost production base but also a host country with robust growth, as this can translate directly into expanded domestic demand. For example, in the ASEAN context, countries like Indonesia and Vietnam often use their localised economic growth as one of many attractive factors for FDI. Therefore, GDP per capita growth in this paper serves not only as a control variable but also as a signal of localised economic growth in the host country.

Trade openness also plays an important role in capturing a country's fundamental FDI activities, because lower trade barriers and greater international integration can facilitate both market-seeking and export-oriented investment. In the ASEAN context, this signal is necessary to indicate a host economy's readiness for foreign investment (Dananjaya, 2026). A more globally integrated host is perceived as more dependable for foreign investment.

Much of the literature on the cross-country relationship between corruption and FDI shows a predominantly negative relationship (Chih et al., 2023; Qureshi et al., 2021; Thede & Karpaty, 2023). The theoretical mechanism underlying these findings draws on the grabbing hand hypothesis, or sand in the wheels, in which corruption is described as an unexpected transactional cost borne by foreign investors, thereby delaying the inflow of funds (Hakimi & Hamdi, 2017). Corruption also signals inconsistent law enforcement. Instability in legal regulation for international investors is often the main obstacle to investment, and reducing investment risk is necessary (Cuervo-Cazurra, 2006). Given these points, research using the Corruption Perceptions Index generally finds that more corrupt countries receive far less investment than they should (Hakimi & Hamdi, 2017).

However, another perspective, called the grease-the-wheels hypothesis, argues that in certain institutional contexts, especially in more complex bureaucracies, corruption is needed to facilitate transactions and business activities. Although this view is in the minority, it is necessary to show that the effect of corruption on FDI is not uniform but depends on the channels through which corruption occurs (Aluko et al., 2024; Krifa-Schneider et al., 2022). Nevertheless, most corruption literature empirically shows that corruption scandals ultimately deplete investor trust, especially when they directly involve an institution that manages sovereign wealth, as happened with 1MDB (Jones, 2020; Poon, 2021).

In short, this 1MDB case raises a question: if a country-level corruption scandal such as 1MDB is expected to reduce investor trust, can the damage be reflected in Malaysian FDI inflows relative to its ASEAN peers? Although the empirical expectation is clear, evidence on how the governance shakeout affects FDI remains limited, especially in the ASEAN context (Aluko et al., 2024; Jones, 2020; Krifa-Schneider et al., 2022; Poon, 2021; Thede & Karpaty, 2023). Thus, the gaps in the empirical literature strongly motivate this paper's quasi-experimental approach to estimating the effect of the 1MDB scandal on Malaysian

FDI.

In ASEAN and other emerging-market contexts, many studies have used event-based methods to examine how political instability and governance shake-ups may be transmitted to FDI decisions. According to previous studies, the shakeout often does not result in short-term gains; instead, it takes time for the turbulence to be absorbed and reflected in the market (Guo et al., 2021). Thus, a longer time is preferable to a short one for explaining the governance shakeout phenomenon. Interestingly, many studies also report null or non-significant results, indicating that, in some cases, institutions experiencing governance turbulence continue to accept FDI inflows (Callaway & Sant'Anna, 2021).

Most existing research on corruption and FDI either relies on broad cross-country corruption indices that do not isolate specific scandal events. Many 1MDB papers approach the case purely from a political science and governance perspective, without translating its consequences into quantifiable investment outcomes. Not to mention that studies applying quasi-experimental designs to corruption shocks in the ASEAN context remain comparatively limited, and those that do exist tend to use shorter post-treatment windows. Correspondingly, by applying a two-way fixed-effects DiD design to a 2000–2024 ASEAN-5 panel, this paper provides a causal estimate of the effect of the 1MDB scandal on Malaysian FDI inflows. Based on the theoretical framework and empirical literature that have been discussed, this research proposes the following hypothesis:

H₁: The 1MDB scandal has a significant negative effect on Malaysian FDI inflows relative to ASEAN peers after 2015.

4. RESULTS AND DISSCUSSION

The first test is the unit root test, and the results are shown in Table 1 below.

Table 1. Panel Unit Root Test Results — Im-Pesaran-Shin (IPS) Test

Variable	Level W-stat	Level p-value	Decision	1st Diff W-stat	1st Diff p-value
	<i>IPS (intercept)</i>			<i>IPS (intercept)</i>	
FDI	-6.0407	0.0000*	Stationary I(0)	—	—
GDPPCGROWTH	-8.2199	0.0000*	Stationary I(0)	—	—
UNEMPLOYMENT	-0.5368	0.2957	Non-stationary	-9.6305	0.0000*
TRADE	-0.8701	0.1921	Non-stationary	-8.5644	0.0000*

Note: * denotes significance at the 5% level. Null hypothesis: the variable contains a unit root. Exogenous variable: individual intercepts. Maximum lag order (p_{max}) = 2. MALAYSIA and POST2015 are binary dummy variables and are excluded from unit root testing by construction

Source: Proceed Data, 2026

Does Corruption Dent Investment? Evidence from the 1MDB Scandal and Malaysian FDI Inflows in ASEAN-5, 2000–2024
Dananjaya, 2026

As shown in Table 1, FDI and GDP per capita growth are stationary at the base level, while unemployment and trade need to be differenced to be stationary.

Table 2. Descriptive Statistics

Variable	Mean	Std. Dev.	Min	Max	Skewness	Kurtosis	Obs
FDI	2.7366	1.7499	-2.7574	9.6630	0.4538	5.4359	125
Unemployment	2.9739	1.6762	0.2490	8.0600	0.8519	3.8071	125
GDPC Growth	3.5260	2.6238	-10.5489	7.7336	-2.3839	11.4991	125
Trade	109.9257	47.1367	32.9722	220.4068	0.1681	2.1341	125

Note: Sample covers ASEAN-5 countries (Indonesia, Malaysia, Philippines, Thailand, Vietnam) over the period 2000–2024. All variables are measured at the country level. FDI = foreign direct investment net inflows (% of GDP); Unemployment = unemployment rate (% of total labour force); GDP pc Growth = GDP per capita growth (%); Trade = trade openness (% of GDP).

Source: *Proceed Data, 2026*

Table 2 presents the descriptive statistics for the four continuous variables. FDI shows a mean of 2.7366, ranging from -2.7574 to 9.6630. Trade openness carries the widest dispersion, with a mean of 109.9257 and values ranging from 32.9722 to 220.4068, reflecting the heterogeneity of ASEAN-5 economies' export orientation.

Table 3. Correlation Matrix

Variable	FDI	Unemployment	GDPPC Growth	Trade
FDI	1.0000			
Unemployment	-0.4178	1.0000		
GDPPC Growth	0.3639	-0.0407	1.0000	
Trade	0.5362	-0.4709	0.0466	1.0000

Note: Correlation coefficients computed using the Pearson method at the level. The sample covers ASEAN-5 countries over 2000–2024 (N = 125).

Source: *Proceed Data, 2026*

Table 3 provides the Pearson correlation matrix. The strongest relationship is between FDI and Trade (0.5362), followed by FDI and Unemployment (-0.4178). None of the pairwise correlations approach a level that would indicate severe multicollinearity, which the VIF test later confirms in the post-estimation diagnostic results.

Table 4. Regression Results - Pooled OLS, Fixed Effects, Random Effects, and TWFE DiD

Variable	Pooled OLS	Fixed Effects	Random Effects	TWFE DiD
MALAYSIA	-0.7501 (0.5457)	—	-0.1775 (0.7364)	—
POST2015	-0.0478 (0.2883)	-0.1440 (0.2964)	-0.1797 (0.2781)	—
INTERACTION	1.0720 (0.6278)	0.4389 (0.7323)	0.8860 (0.6196)	0.7101 (0.7365)
UNEMPLOYMENT	-0.1681 (0.1047)	-0.2643 (0.1625)	-0.2960* (0.1187)	-0.4259* (0.1866)
GDPPCGROWTH	0.2178* (0.0469)	0.1624* (0.0449)	0.1763* (0.0451)	0.2849* (0.0782)
TRADE	0.0191* (0.0044)	0.0040 (0.0072)	0.0119* (0.0051)	0.0049 (0.0078)
Observations	125	125	125	125
R ²	0.4508	0.1355	0.2489	0.1604
Adj. R ²	0.4229	0.0679	0.2107	-0.1317
F / Chi ² stat	16.14*	3.606*	39.10*	4.393*
Country FE	No	Yes	No	Yes
Time FE	No	No	No	Yes

Note: Dependent variable is FDI net inflows (% of GDP). Standard errors in parentheses. * $p < 0.05$. INTERACTION = MALAYSIA $\times$ POST2015 (DiD term). MALAYSIA dropped in the FE and TWFE DiD due to its time-invariant nature. POST2015 is absorbed by time fixed effects in TWFE DiD. The sample covers ASEAN-5 countries, 2000–2024 (N = 125).

Source: *Proceed Data, 2026*

As shown in Table 4, across all four estimators, the INTERACTION term (MALAYSIA $\times$ POST2015), which indicates the coefficient of primary interest, is never statistically significant at the 5% level (Pooled OLS: 1.0720, SE = 0.6278; FE: 0.4389, SE = 0.7323; RE: 0.8860, SE = 0.6196; TWFE DiD: 0.7101, SE = 0.7365). GDPPCGROWTH

is consistently significant and positive across all four specifications, reinforcing its role as a robust driver of FDI. TRADE is significant in Pooled OLS and RE but loses significance once country fixed effects are introduced, suggesting its explanatory power is partly absorbed by unobserved, time-invariant country characteristics.

Table 5. Hausman Specification Test

Test Statistic	χ^2	df	p-value
Hausman Test	17.453	5	0.0037*

Note: Null hypothesis: Random Effects estimator is consistent and efficient. * $p < 0.05$. The result rejects the null hypothesis, indicating that the Fixed Effects estimator is the consistent and preferred model for this panel.

Source: *Proceed Data*, 2026

A Hausman test is conducted to determine the preferred estimator between FE and RE. The result ($\chi^2 = 17.453$, $p = 0.0037$) rejects the null hypothesis of no systematic difference between the two estimators, confirming Fixed Effects as the preferred estimator over Random Effects (Hausman, 1978). The TWFE model remains the main DiD specification because it incorporates both country and year fixed effects. The parallel trends assumption is assessed visually through a pre-treatment trend plot, which shows no divergent trajectory between Malaysia and the ASEAN-4 control group before 2015. Vietnam shows a visible FDI spike around 2008, attributable to its 2007 WTO accession, a country-specific shock rather than a violation of the parallel trends assumption (Hanh, 2011). The TWFE DiD model also reports a negative Adjusted R^2 (-0.1317). This is expected, given the specification absorbs 30 fixed-effect dummies (5 country + 25 year) across only 125 observations, and it does not undermine the validity of the coefficient estimates, since the Adjusted R^2 penalises model complexity rather than reflecting estimator bias. In short, the consistent insignificance of the INTERACTION term across all four estimators constitutes this paper's central empirical finding: the analysis found no statistically detectable effect of the 1MDB scandal on Malaysian FDI inflows relative to its ASEAN peers during the study period

Table 6. Post-Estimation Diagnostic Tests

Test	Statistic	df	p-value	Decision
<i>Panel A: Model-level tests</i>				
Breusch-Pagan (Heteroskedasticity)	BP = 10.863	6	0.0927	No heteroskedasticity
Wooldridge (Serial Correlation)	$\chi^2 = 35.231$	25	0.0841	No serial correlation
<i>Panel B: Variable-level test (Multicollinearity)</i>				
Variable	VIF			
UNEMPLOYMENT	2.161			

GDPPCGROWTH	1.061
TRADE	3.069
MALAYSIA	3.370
POST2015	1.411
INTERACTION	2.052

Note: Diagnostics were conducted on the Fixed Effects model (heteroskedasticity, serial correlation) and Pooled OLS (VIF). The null hypothesis for the Breusch-Pagan and Wooldridge tests is homoskedasticity and no serial correlation, respectively. All tests evaluated at the 5% significance level fail to reject the null. VIF values below 10 indicate no multicollinearity concern.

Source: *Proceed Data, 2026*

The Breusch-Pagan result ($p = 0.0927$) does not reject homoskedasticity at the 5% level. Similarly, the Wooldridge result ($p = 0.0841$) provides no evidence of first-order serial correlation at the same significance level. Variance Inflation Factors (VIF) are calculated for all regressors, with the highest value recorded at 3.370 (MALAYSIA), well below the conventional threshold of concern (O'Brien, 2007). Thus, the diagnostic results indicate no significant heteroskedasticity, serial correlation, or problematic multicollinearity at the 5% level.

Table 7. Placebo Test - Fixed Treatment Year (POST2012)

Variable	Coefficient	Std. Error	t-value	p-value
Unemployment	-0.0556	0.3463	-0.1605	0.8731
GDPPC Growth	0.3851	0.1273	3.0248	0.0039*
Trade	0.0203	0.0163	1.2426	0.2196
Interaction (Placebo)	0.4222	1.1479	0.3678	0.7145

Note: The dependent variable is FDI net inflows (% of GDP). Two-way fixed effects model estimated on the pre-treatment subsample (2000–2014, $N = 75$) using a fabricated treatment year (2012) in place of the actual 1MDB scandal year (2015).

* $p < 0.05$. POST2012 is absorbed by time fixed effects. INTERACTION_PLACEBO = MALAYSIA $\times$ POST2012. The coefficient is statistically insignificant at the 5% level, indicating no spurious treatment effect prior to the true 2015 event

Source: *Proceed Data, 2026*.

The placebo INTERACTION term (MALAYSIA $\times$ POST2012) yields a coefficient of 0.4222 (SE = 1.1479, $t = 0.3678$, $p = 0.7145$), which is not statistically significant at the 5% level. The insignificant placebo coefficient provides no evidence of a spurious treatment effect around the false 2012 cutoff. This result supports the credibility of the main specification by indicating that the estimated post-2015 pattern was unlikely to be driven by a comparable break immediately before the actual treatment period. However, the placebo result does not establish that the true effect of the 1MDB scandal was exactly zero.

The results show that the INTERACTION term (MALAYSIA $\times$ POST2015) is positive in all four estimators, Pooled OLS (1.0720), Fixed Effects (0.4389), Random Effects (0.8860), and TWFE DiD (0.7101), though never statistically significant at the 5% level. Thus, the data do not support H₁, which proposed a significant negative effect. Although the INTERACTION coefficient remains positive across all specifications, its statistical insignificance means that its direction should not be interpreted as evidence that the scandal increased Malaysian FDI. The main finding is instead that the analysis does not detect the negative FDI response predicted by the grabbing-hand or sand-in-the-wheels perspective, which views corruption as an additional transaction cost that discourages foreign investment (Cuervo-Cazurra, 2006; Hakimi & Hamdi, 2017; Thede & Karpaty, 2023). This result does not invalidate that theoretical perspective. Rather, it suggests that the predicted negative response is not statistically detectable in Malaysia's aggregate FDI inflows relative to its ASEAN peers during the period examined. One possible explanation is that broader macroeconomic conditions, existing investment commitments, or differences across economic sectors may limit the visibility of the shock in aggregate FDI data. However, these mechanisms are not directly tested in the present analysis and should therefore be interpreted as possible explanations rather than established causal channels.

The finding differs from Hakimi and Hamdi (2017), Thede and Karpaty (2023), and Osuma et al. (2024), who reported that corruption reduces the likelihood of foreign investment. However, this difference should be interpreted in light of the different research designs. Previous studies generally examined corruption as a persistent institutional condition using country-level indices or firm-level investment data, whereas the present study examines the public exposure of a specific corruption scandal as a discrete governance shock. Therefore, the absence of a statistically significant post-2015 effect does not contradict the broader evidence that persistent corruption can discourage foreign investment. Instead, it indicates that the public exposure of a major scandal does not necessarily translate into a statistically detectable change in aggregate national FDI during the period examined.

The control-variable results provide further context for the main finding. GDP per capita growth remains positive and statistically significant across all specifications, indicating that stronger economic performance is consistently associated with higher FDI inflows (Hayat, 2019; Lee et al., 2024). Unemployment remains negative across all specifications and is statistically significant in the Random Effects and TWFE specifications, suggesting that weaker labour-market conditions may reduce the host economy's attractiveness (Lee et al., 2024; Saini & Singhania, 2018). In contrast, trade openness is significant in Pooled OLS and Random Effects but becomes insignificant after including country fixed effects (Saini & Singhania, 2018). This indicates that its explanatory power may reflect persistent differences in trade integration across ASEAN countries rather than changes within each country over time. Together, these results indicate that observable macroeconomic conditions are more consistently associated with FDI movements during the

study period, while the model does not identify a statistically significant post-2015 governance-shock effect.

5. CONCLUSION

This study finds no statistically significant evidence that the public exposure of the 1MDB scandal reduces Malaysian FDI inflows relative to its ASEAN peers during the period examined. Although the INTERACTION coefficient remains positive across all specifications, its statistical insignificance prevents interpreting its direction as evidence of increased FDI. The finding also does not imply that corruption is irrelevant to international investment or that Malaysia's economic reputation fully absorbs the governance shock. Instead, it indicates that the analysis does not detect a statistically significant change in aggregate national FDI following the scandal within the present research design. The study therefore contributes to the literature by showing that the effects associated with persistent corruption conditions may not be equally visible when corruption is examined as a discrete governance event using aggregate FDI data.

The null result nevertheless raises a more nuanced possibility: Malaysia's established economic reputation may buffer the shock, preventing it from immediately translating into a measurable decline in aggregate FDI. However, economic reputation should be understood as a buffer rather than immunity. Reputational capital is accumulated gradually through economic performance, policy stability, and institutional credibility, but repeated governance failures can eventually weaken that capital and alter investor behaviour (Bhujabal et al., 2024; Cuervo-Cazurra, 2006). For the Malaysian government and policymakers, the stability of aggregate FDI should therefore be viewed as an opportunity to reinforce transparency and accountability, not as evidence that corruption carries no investment consequences. Strong macroeconomic performance may sustain investor attention, but credible governance is necessary to preserve that confidence over the longer term (Hayat, 2019; Hakimi & Hamdi, 2017; Tabash et al., 2024). Governance, in this sense, forms part of the institutional foundation on which a country's economic reputation is built. For investment-promotion authorities, the findings highlight the limitations of relying solely on headline FDI figures when assessing the consequences of a governance scandal. Stable aggregate inflows may coexist with changes in investment sectors, source countries, project quality, or investor risk perceptions. For investors, the results similarly suggest that national economic resilience should not be confused with the absence of governance risk. Macroeconomic strength and institutional credibility should be evaluated together because an economy may continue attracting capital while underlying regulatory, reputational, or sector-specific risks remain.

Several limitations qualify these conclusions. The sample contains 125 country-year observations across five countries, which may limit the statistical power to detect an effect.

FDI is measured as an aggregate percentage of GDP and therefore cannot capture changes in its sectoral or source-country composition. In addition, the POST2015 variable imposes a single treatment date on a scandal that developed gradually before and after its public exposure (Jones, 2020), while the model does not include a direct institutional-quality measure capable of identifying changes in governance or economic reputation. Future research could address these limitations using sectoral or project-level FDI data, alternative treatment dates, event-study specifications, or a synthetic-control design. Such extensions would provide a clearer assessment of whether the consequences of the 1MDB scandal appear in investment sectors or through governance and reputational channels that are not observable in aggregate FDI inflows.

REFERENCES

- Aluko, B., Garri, M., Owalla, B., Kim, J. Y., & Pickernell, D. (2024). Informal institutions' influence on FDI flows: A configurational fsQCA analysis of corruption as part of the MNEs' FDI motivation system. *International Business Review*, 33(6), 102327. <https://doi.org/10.1016/j.ibusrev.2024.102327>
- Asongu, S., Akpan, U. S., & Isihak, S. R. (2018). Determinants of foreign direct investment in fast-growing economies: evidence from the BRICS and MINT countries. *Financial Innovation*, 4(1), 26. <https://doi.org/10.1186/s40854-018-0114-0>
- Bhujabal, P., Sethi, N., & Padhan, P. C. (2024). Effect of institutional quality on FDI inflows in South Asian and Southeast Asian countries. *Heliyon*, 10(5), e27060. <https://doi.org/10.1016/j.heliyon.2024.e27060>
- Breusch, T. S., & Pagan, A. R. (1979). A Simple Test for Heteroscedasticity and Random Coefficient Variation. *Econometrica*, 47(5), 1287. <https://doi.org/10.2307/1911963>
- Callaway, B., & Sant'Anna, P. H. C. (2021). Difference-in-Differences with multiple time periods. *Journal of Econometrics*, 225(2), 200–230. <https://doi.org/10.1016/j.jeconom.2020.12.001>
- Chih, Y.-Y., Demir, F., Hu, C., Liu, J., & Shen, H. (2023). A spatial analysis of local corruption on foreign direct investment: Evidence from Chinese cities. *European Journal of Political Economy*, 79, 102443. <https://doi.org/10.1016/j.ejpoleco.2023.102443>
- Cuervo-Cazurra, A. (2006). Who cares about corruption? *Journal of International Business Studies*, 37(6), 807–822. <https://doi.org/10.1057/palgrave.jibs.8400223>
- Dananjaya, G. P. (2026). Trade Openness and Inflation Dynamics in Indonesia: Long-Run Evidence Across Four Structural Break Episodes (1969–2024). *Journal of Economics and Business UBS*, 15(3), 514–527. <https://doi.org/10.52644/aereze87>

- Drukker, D. M. (2003). Testing for Serial Correlation in Linear Panel-data Models. *The Stata Journal: Promoting Communications on Statistics and Stata*, 3(2), 168–177.
<https://doi.org/10.1177/1536867X0300300206>
- Eggers, A. C., Tuñón, G., & Dafoe, A. (2024). Placebo Tests for Causal Inference. *American Journal of Political Science*, 68(3), 1106–1121.
<https://doi.org/10.1111/ajps.12818>
- Goodman-Bacon, A. (2021). Difference-in-differences with variation in treatment timing. *Journal of Econometrics*, 225(2), 254–277.
<https://doi.org/10.1016/j.jeconom.2021.03.014>
- Guo, J., Wang, Y., & Yang, W. (2021). China's anti-corruption shock and resource reallocation in the energy industry. *Energy Economics*, 96, 105182.
<https://doi.org/10.1016/j.eneco.2021.105182>
- Hakimi, A., & Hamdi, H. (2017). Does corruption limit FDI and economic growth? Evidence from MENA countries. *International Journal of Emerging Markets*, 12(3), 550–571. <https://doi.org/10.1108/IJoEM-06-2015-0118>
- Hanh, P. T. H. (2011). Does WTO accession matter for the dynamics of foreign direct investment and trade? *Economics of Transition*, 19(2), 255–285.
<https://doi.org/10.1111/j.1468-0351.2010.00405.x>
- Hausman, J. A. (1978). Specification Tests in Econometrics. *Econometrica*, 46(6), 1251.
<https://doi.org/10.2307/1913827>
- Hayat, A. (2019). Foreign direct investments, institutional quality, and economic growth. *The Journal of International Trade & Economic Development*, 28(5), 561–579.
<https://doi.org/10.1080/09638199.2018.1564064>
- Im, K. S., Pesaran, M. H., & Shin, Y. (2003). Testing for unit roots in heterogeneous panels. *Journal of Econometrics*, 115(1), 53–74. [https://doi.org/10.1016/S0304-4076\(03\)00092-7](https://doi.org/10.1016/S0304-4076(03)00092-7)

- Jones, D. S. (2020). 1MDB corruption scandal in Malaysia: a study of failings in control and accountability. *Public Administration and Policy*, 23(1), 59–72.
<https://doi.org/10.1108/PAP-11-2019-0032>
- Krifa-Schneider, H., Matei, I., & Sattar, A. (2022). FDI, corruption and financial development around the world: A panel non-linear approach. *Economic Modelling*, 110, 105809. <https://doi.org/10.1016/j.econmod.2022.105809>
- Lee, S. J., Kang, S. J., & Lee, S. (2024). Economic, social and institutional determinants of FDI inflows: A comparative analysis of developed and developing economies. *Transnational Corporations Review*, 16(3), 200074.
<https://doi.org/10.1016/j.tncr.2024.200074>
- Maksum, A. (2020). 1MDB (1 Malaysia Development Berhad), Scandal, and Its Impact on Malaysian Domestic Politics. *Politika: Jurnal Ilmu Politik*, 11(2), 198–218.
<https://doi.org/10.14710/politika.11.2.2020.198-218>
- O'Brien, R. M. (2007). A Caution Regarding Rules of Thumb for Variance Inflation Factors. *Quality & Quantity*, 41(5), 673–690. <https://doi.org/10.1007/s11135-006-9018-6>
- Osuma, G., Ayinde, A., Ntokozo, N., & Ehikioya, B. (2024). Evaluating the impact of systemic corruption and political risk on foreign direct investment inflows in Nigeria: An analysis of key determinants. *Discover Sustainability*, 5, Article 432.
<https://doi.org/10.1007/s43621-024-00676-7>
- Peres, M., Ameer, W., & Xu, H. (2018). The impact of institutional quality on foreign direct investment inflows: evidence for developed and developing countries. *Economic Research-Ekonomska Istraživanja*, 31(1), 626–644.
<https://doi.org/10.1080/1331677X.2018.1438906>

- Poon, J. P. H. (2021). Regulating the global illicit economy: Singapore's role in United States' spatial financial surveillance. *Political Geography*, 91, 102493. <https://doi.org/10.1016/j.polgeo.2021.102493>
- Qureshi, F., Qureshi, S., Vo, X. V., & Junejo, I. (2021). Revisiting the nexus among foreign direct investment, corruption and growth in developing and developed markets. *Borsa Istanbul Review*, 21(1), 80–91. <https://doi.org/10.1016/j.bir.2020.08.001>
- Saini, N., & Singhania, M. (2018). Determinants of FDI in developed and developing countries: a quantitative analysis using GMM. *Journal of Economic Studies*, 45(2), 348–382. <https://doi.org/10.1108/JES-07-2016-0138>
- Tabash, M. I., Farooq, U., Matar, A., & Al-Absy, M. S. M. (2024). Role of governance in attracting foreign direct investment inflow: Empirical evidence from the South Asia region. *Cogent Economics & Finance*, 12(1), Article 2358930. <https://doi.org/10.1080/23322039.2024.2358930>
- Thede, S., & Karpaty, P. (2023). Effects of corruption on foreign direct investment: Evidence from Swedish multinational enterprises. *Journal of Comparative Economics*, 51(1), 348–371. <https://doi.org/10.1016/j.jce.2022.10.004>