

HOME BIAS ENDURANCE IN FOREIGN DIRECT INVESTMENTS

Abstract

The distribution of FDI over the years has been strongly linked to the geographical and cultural proximity between the countries involved; in that sense FDI resembles the home bias phenomenon in international portfolio flows. The purpose of this paper is to analyse the issues related to home bias and foreign direct investments. This paper finds strong empirical evidence of enduring near-home bias in FDI outflows, clear evidence that the much lauded globalization has a long way to go when it comes to foreign investments. Studies have found considerable evidence to suggest that distance, physical, institutional, and cultural play an important role in the distribution of FDI. However, the increased markets liberalization in the past two decades should have decreased if not erased any such non-economic factors in FDI. Using the “home bias” framework from the finance literature and the gravity model we utilise a large sample of bilateral FDI data for a large sample countries, including both developed and emerging markets, to examine the impact of physical, cultural and institutional distance on foreign direct investment flows of 3,136 unique bilateral county pairs over a 30 year period.

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1. Introduction

The term home bias (French and Poterba, 1991; Lewis, 1999) was initially used in the context of equity portfolio investments to describe the investors' tendency to overweight their domestic investments. Although investors can diversify their portfolios by holding assets in many foreign countries, they tend not to take full advantage of such opportunities (Coval and Moskowitz, 1999). More generally, the home bias puzzle in equity markets falls within the more general category of familiarity biases in behavioural finance (Huberman, 2001; Boyle, Garlappi and Uppal, 2011).

Familiarity biases, however, are not unique to equity portfolio investments. Johanson and Vahlne (1977) and Johanson and Wiedersheim-Paul (1975) introduced the notion of psychic distance in FDI management literature in the late 1970s through a series of case studies that described the factors that would influence managers when thinking about expanding their businesses abroad. At the time, there were plenty of factors that would make FDI location decisions difficult: too many barriers and costs of doing business abroad; various transport difficulties (both for commerce and technological and human know-how), inability to acquire information on foreign locations, etc. Understandably, all this would make corporate managers prone to invest in places where they have high degree of familiarity. Thus, we understand home country bias in the context of FDI as the preference to invest in close, familiar countries abroad based on three categories of such proximity: geographical, institutional and cultural.

More recently, however, in an era of capital markets liberalisation, foreign investment should not any more determined by forces other than economics and finance (Bekaert, 1995; Bekaert, Harvey and Lundblad, 2005; Levine, 2001). According to the OECD (2009) unrestrained flow of direct investment is indeed a measure of globalization. In spite, however, the overall FDI flows in the world have increased by around 150% over the past decade, there is still some evidence to suggest that the effect of globalisation on financial markets remains rather limited (Stulz, 2005; Errunza, 2001; Kho, Stulz and Warnock, 2008). Despite the strong reduction of barriers to trade and investment, these studies find that country-specific factors still play a very big role and drive cross-country investment.

Furthermore, Cummings and Dai (2010) and Nachum, Zaheer and Gross (2008) argue that a country's location determines its access to developed markets, resources, investment knowledge and general location familiarity. Furthermore, they find that proximity of one country to the rest of the world influences its choices of investment destination choices. In fact, FDI activity is considered as a natural and widely available indicator of globalization precisely because it measures the extent of international (cross-border) investments which are made with the objective to form a long lasting interest in a country different than that of the investor.

The objective of this study is to examine the role of distance from home, in terms of physical, cultural and institutional distances, on foreign direct investment decisions by MNCs and test whether the globalization of the past two decades has reduced their influence. Using a large dataset of bilateral investment flows we show that international corporate investments decisions are still very much influenced by the familiarity of the environment where investment opportunities arise. We provide evidence, using a sample of 34 OECD countries and a maximum of 190 bilateral pairs during the period 1981 to 2010 that the stylized home bias phenomenon exists in FDI: when investing in international destinations corporate managers show a strong preference for locations near their home country.

To the best of our knowledge this is the first study that provides a comprehensive account of the global trends and patterns of FDI over an extended time period. Our evidence suggests enduring presence of home bias in foreign direct investment outflows over the past three decade, despite significant liberalisation in the capital markets and increasing globalization in the world. These findings have policy implications and show that economic activity and the country trade openness aren't the only driving forces in direct investments but the sense of familiarity that investors have towards an investment destination country creates a home bias effect that has endured over time.

The paper is organised in the following way. Section 2 provides a review of the literature related to FDI investment; section 3 outlines the gravity model and its econometric adaptation for the purposes of this study while section 4 describes the dataset used in this study. Section 5 presents the results. Section 6 concludes.

2. Related Literature

Home bias has been studied for the equity markets (Kang and Stulz, 1997; Coval and Moskowitz, 1999; Chan, Covrig and Ng, 2005), personal consumption (Lewis, 1999), international trade (Ng 2010) but it hasn't been applied to FDI. This could be related to the perception that FDI are perceived as real investments that are permanent rather than short-term and as such they might be governed by different decision rules.

Behavioural aspects in the theory of the firm and FDI have been suggested since the 1960s in the work of Hymer (1960), Cyert and March (1963), Aharoni (1966) and Agarwal (1980) albeit only as a theoretical notion with scarce empirical supporting evidence. FDI literature started developing in the 1950s (Buckley, 2002) through several theories on the motives for FDI: monopolistic (Hymer, 1960; Kindleberger, 1969), oligopolistic (Knickerbocker, 1973; Kim et al., 1987; Caves, 1974; Severn and Laurence, 1974) and Dunning's (1980; 1988 and 1995) eclectic or OLI (ownership, location, internalisation) paradigm. Subsequent work on FDI, regardless of the geographical specification of the data or methodology seeks to test and establish different factors that influence FDI flows. Most studies feature measures of GDP as proxies for the economic pull of an economy and are important determinants of FDI flows for both emerging and developed countries (Hsiao and Shen, 2003; Hansen and Rand, 2006). This reflects the strong influence on FDI that the size of the markets of the partner countries have and the tendency of FDI towards larger economies. FDI literature also features some form of measurement for country openness as the second major determinant of FDI flows (Agarwal et al., 1991, Bevan and Estrin, 2004, and Janicki and Wunnava, 2004). Countries that are more 'open' with increased trade flows or portfolio investments would be more likely to engage in FDI. The standard measure for trade openness of a country is through the ratio of the sum of exports plus imports over GDP (Chakrabarti, 2001).

More recently, increased globalization has sparked interest in the geographic component of the firm investment choices (Alcacer, 2006). Financial globalization is defined as global linkages through cross-border financial flows (Yeyati, Williams, 2011). It is something that is especially significant and beneficial for emerging markets. The costs of doing business abroad have significantly dropped compared to some twenty years ago. Making an international telephone call or travelling isn't any

longer featured as a major expense to doing business at great distances. Therefore the FDI destination country choices shouldn't show a near-home bias.

One of the theories regarding FDI called psychic distance (Johanson and Wiedersheim-Paul, 1975, Johanson and Vahlne, 1977), developed in the mid-1970s, has proposed various factors that could influence managers' psyche when making an FDI decision. Psychic distance is defined as "...factors preventing or disturbing the flows of information between firm and market. Examples of such factors are differences in language, culture, political systems, level of education, level of industrial development etc..." (Johanson and Wiedersheim-Paul, 1975 p. 308). A range of psychic distance stimuli have been used in large data sets as significant predictors of trade flows (Dow and Karunaratna, 2006). Corporate managers prefer to invest in foreign destinations near home not only in terms of physical distance, but also in terms of institutional and cultural distance.

In FDI studies, cultural proximity is often also assumed through geographical distance or shared border (Galego, Vieira and Vieira, 2004, Benito and Gripsurd, 1992; Green and Cunningham, 1975; Grosse and Goldberg, 1991; Grosse and Trevino, 1996; Habib and Zurawicki, 2002; Di Giovanni, 2003; Sethi et al, 2003). We use three aspects of culture that are important aspects of familiarity: language, historical ties and organisational culture which in many instances are closely related to each other.

Speaking the language of the destination country has been found to be a significant variable in predicting the FDI flows. It might lower the degree of asymmetric information and give superior ability to international investors to identify good investment opportunities (West and Graham, 2004; Dow and Karunaratna, 2006). Similarly, historical ties are important determinants of cultural proximity and familiarity (Benito and Gripsurd, 1992). Countries sometimes change borders over time. Countries that were the parts of a single country in the past or that were in a colonial relationship have similar attitudes or values. Corporate investors would feel at home in their foreign direct investments if they can understand the spoken languages or if the countries had historical ties such as being different parts of the same country some time ago.

Foreign Direct Investors feel more familiar and near home in work environments where organisational cultures are similar (Gianetti and Yafeh, 2011; Solnik and Zuo, 2011). Kogut and Singh

(1988) use the Jemison and Sitkin (1986) definition of organisational fit as the match between administrative practices, cultural practices and personal characteristics of the target and parent firms to create a Cultural Distance Index, a composite index using deviations along Hofstede's (1980) indices on four cultural dimensions; the power distance, uncertainty avoidance, masculinity/femininity and individualism. The elements making up the dimensions are organisational and managerial in character.

Institutional distance is defined as the extent of similarity or dissimilarity between the regulatory, cognitive, and normative institutions of two countries (Xu and Shenkar, 2002; Kostova, Zaheer, 1999; Kostova, 1996). Institutional distance is linked to the establishment of legitimacy in the host country and the transfer of strategic operations and organisation practices from the parent firm to the subsidiary abroad. Being a member of the same economic union or having similar legal systems play a significant role in the investment decisions. Such similarities breed familiarity bias (Brainard, 1997) which makes it easier for corporate managers to make international investments if the destination markets have similar structure as the home market.

The home bias literature has attempted to explain the observed home bias effects as the consequence of, most frequently, asymmetric information and transaction costs (Portes and Ray, 2005; Ahearne et al, 2004). We include a number of variables to test if those explanations are going to reduce the observed home country bias for foreign direct investments thereby explaining why it appears that globalization hasn't taken full effect as one would expect.

Trust (Guiso, Sapienza and Zingales (2009); Johanson and Vahlne, 2009) towards the destination country creates a perception of a safe investment opportunity and reduced risks and thus entice FDI. The existence of bilateral tax treaties can reduce transaction costs directly and stimulate cross border deals. Differential taxation on a firm's international operations has impact on firm values (Errunza and Senbet, 1981).

Informational asymmetries are important in FDI decisions as investors might find it more difficult to gather information on more 'distant' investment possibilities. Studies show that more knowledgeable investors are also more prone to invest and diversify their assets abroad (Bailey, Kumar and Ng (2008); Graham, Harvey and Huang (2009)), however they also find that the observable bias effects remain present especially for less sophisticated investors, Information costs

and availability can play an important role for the investment decision of firms; (Gordon and Bovenberg, 1996). Portes and Rey (2005) and Di Giovanni (2005) use telephone usage as a proxy for information costs. We use the international phone calls per capita for the FDI host country as well as another similar indicator for the business information availability such as the availability of the Financial Times newspaper to proxy for the extent of informational asymmetries in the FDI receiving country for international investors.

Finally, country-specific governance is also an important factor for doing business in a particular location because it affects the availability of information in the FDI receiving country and making investments in places of low country governance costly. Kaufman et al. (2009) capture country specific factors of governance through accountability, political stability, government effectiveness, regulatory quality, rule of law and control of corruption. These indicators have been used in FDI literature (Globerman and Shapiro (2002); Bénassy-Quéré, Coupet and Mayer (2007), Habib and Zurawicki (2002)) and they are found to have a stimulating influence on FDI. Investors prefer locations where there is political stability and rule of law and governments work effectively regulatory quality and accountability are high and corruption is under control. We believe that those attributes of the business environments lower the costliness of the uncertainty of the investment process and thus increase foreign investments.

3. The Model

The basis for the model that will be developed to test home bias in FDI is the gravity model. Its origins are in physics, in the Newton's second law of gravity and it was first introduced in economics by Ian Tinbergen (1962). He developed the gravity model to explain international trade flows between bilateral country pairs. Although it has many variations (Bergstrand, 1985) the basic analogy of its two main parts, the mass of two objects and their distance are maintained in the basis for this model. It can be written as:

$$F_{i,j} = G \frac{M_i^\alpha M_j^\beta}{D_{ij}^\theta} \quad (1)$$

Where F_{ij} is the force of attraction between the two objects i and j ; M_i and M_j are the masses or sizes of the two objects, D_{ij} is the distance between them while G is a constant that represents Earth's gravity force. From the equation we can say that the bigger their mass the higher the force of attraction between them and the bigger the distance between them the lesser is the force of attraction. This basic relation between an object's mass and its distance from other objects was taken by Tinbergen (1962) as the basis for a natural relationship between two objects in economics. In economics these two objects can be any number of things that have an interaction - countries, cities, companies and people as well as in any number of relationships between them: general trade, imports, exports or direct investment. Following this general premise of two main factors, mass and distance we can say that the FDI flows are a function of the size of the respective economies in bilateral country pairs and the distance between them as well as other contributing factors. When we transform equation (1) into a logarithmic form we get the following simple functional form of the gravity model (Bergstrand, 1985) that can be used to explain the magnitude of FDI flows between two countries:

$$\log F_{i,j,t} = \log M_{i,t} + \log M_{j,t} - \log D_{i,j} + u_{i,j,t} \quad (2)$$

Where $F_{i,j,t}$ are FDI flows from country i towards country j at time t ; $M_{i,t}$ and $M_{j,t}$ are country's i and j 's GDP at time t , respectively; $D_{i,j}$ is the distance between the two countries that have an FDI relationship; $u_{i,j,t}$ stands for the error term. In the case of this study, the aim is to test near-home bias in FDI. Therefore we are interested in whether the distance between the FDI partners or being near-home geographically either being located in the same continent or by sharing a border increases FDI flows.

In addition to this physical proximity, psychic distance or familiarity is represented through a group of cultural or institutional proximity variables that will result in a near-home bias that can be observed. These variables capture any similarities that may exist between countries in several areas such as: their institutions or legal system similarity; their economic development through membership in political and economic unions and organisations, their cultural and lingual similarity or social similarity that may occur because of some past historical occurrence and similarities in organisational culture. Accordingly we estimate the following model:

$$FDI_{i,j,t} \text{ (outflows)} = \beta_0 + \beta_1(\gamma_1) + \beta_2(\gamma_2) + \beta_3(\gamma_3) + \beta_4(\gamma_4) + u_{i,j,t} \quad (3)$$

Where: $FDI_{i,j,t}$ is the FDI outflows from country i to j at time t ; γ_1 is for the macroeconomic variables that denote the economic pull or strength of the country. We use two macroeconomic variables: the GDP and the country trade openness; γ_2 is for the three geographical proximity variables, distance between the country pairs, a shared border dummy and a same continent dummy. The next set of variables, denoted by γ_3 is the institutional variables: same origin of the country's legal system and common membership to a political or economic union between the country pairs. The last set, γ_4 is the cultural familiarity group which includes the common language dummy and common history between the country pairs and the cultural distance index that measures culture in a sociological way. Finally, $u_{i,j,t}$ stands for the error term component and has a time and cross sectional component due to the fact that our analysis involves panel data. The variables used in the model will be discussed in greater detail in section 3.

To examine the impact of home bias on FDI we estimate the following regression specification for FDI outflows at level values of the variables using OLS panel estimators¹ with fixed effects as suggested by the Hausman test (Hausman, 1978). We cluster the standard errors in the cross-section of the panel using the (White, 1980) method in order to control for the heteroskedasticity that comes from the country variability (Wooldridge, 2002).

$$\begin{aligned} \text{Log} (FDI \text{ outflows}_{i,j,t}) = & \beta_0 + \\ & \beta_{11} \log (GDP_{rec}) + \beta_{12} \log (GDP_{send}) + \beta_{13} \log (Openness_{rec}) + \beta_{14} \log (Openness_{send}) + \\ & \beta_{21} \log (DIST_{i,j}) + \beta_{22} SAMECONT + \beta_{23} BORDER + \\ & \beta_{31} ECONORGD + \beta_{32} LEGALOR + \\ & \beta_{43} SAMEHIST + \beta_{44} COMLANG + \beta_{45} CDindex + \varepsilon_{i,j,t} \end{aligned} \quad (4)$$

where $\log (FDI \text{ outflows}_{i,j,t})$ is the logarithm of the levels of FDI outflows in millions of US dollars from country i to j at time t . $\log (GDP_{rec})$ is the logarithm of the GDP levels in millions of constant

US dollars for the FDI receiving country. $\text{Log}(GDP_{send})$ is the logarithm of the GDP levels in millions of constant US dollars for the FDI sending country. $\text{Log}(Openness_{rec})$ is the ratio of the exports plus imports over GDP for the FDI receiving country. $\text{Log}(Openness_{send})$ is the ratio of the exports plus imports over GDP for the FDI sending country. $\text{Log}(DIST)$ is the logarithm of the distances between the two countries i and j in the bilateral country pairs. *SAMECONT* is a dummy variable that takes the value of one if the two countries in the bilateral country pair are on the same continent. *BORDER* is a dummy variable if the two countries in the bilateral country pair share a border. *ECONORGD* is a dummy variable that has a value of one if the two countries in the bilateral country pair are members of an economic or political union (EU, OECD, Commonwealth or NAFTA). *LEGALOR* is a dummy variable that takes the value of one if the two countries in the bilateral country pair have the same legal system origin. *COMLANG* is a dummy variable that takes the value of one if the two countries in the pair share the same language and *SAMEHIST* is a dummy that has the value of one if the two countries in the bilateral country pair share history. *CDINDEX* is the cultural distance index by Kogut and Singh (1988) between country i and j .

Equation (4) is estimated in the full panel, by continent and by country as well as over time in two sub-periods from 1981-1995 and from 1996-2010 which roughly divides the sample into two equal sub-periods and it also takes into consideration the capital liberalization that happened in the early 90s (Bekaert 1995). Equation (5) does the same thing but it splits the sample into three parts according to the decades.

We conduct a number of additional tests and estimate the following model:

$$FDI_{i,j,t}(\text{outflows}) = \beta_0 + \beta_1(\gamma_1) + \beta_2(\gamma_2) + \beta_3(\gamma_3) + \beta_4(\gamma_4) + \beta_5(\gamma_5) + u_{i,j,t} \quad (5)$$

Where all the variable groups are as denoted above and γ_5 can denote any of the following variables: bilateral trust index, international phone minutes per capita for the receiving country, financial times circulation per capita for the receiving country, bilateral tax treaties for double tax avoidance and any of the six world governance indicators including voice and accountability, political stability, government effectiveness, regulatory quality, rule of law and control for corruption.

4. Data

We investigate home bias in FDI flows in a bilateral country framework across a large number of countries using data from the OECD database which provides bilateral FDI data. For our analysis we consider positive FDI outflows for the 30 OECD member countries² and their (maximum possible) 190 partner countries, from 1981 to 2010; the data is in constant millions of US dollars. We define an observation as the FDI outflow from country i to country j at a given year t . We only consider sovereign countries (not country territories) and require each bilateral country pair to have at least two consecutive time series observations. Therefore, the data is an unbalanced panel. The data set includes a total of 24,853 observations for FDI outflows which translates into 3,136 unique bilateral country pairs (without their time series). Initially, the total number of observations in the case of all FDI outflows (positive, negative and zero relationship) was 64,596 with 24,047 observations among bilateral pairs that do not have an FDI relationship (zero FDI outflows). Our sample is well diversified and only 1,050 (4.3%) observations (of the 24,853 FDI outflows) occur among the G7 member countries with the rest being spread out throughout the rest of the world.

Table 1 presents descriptive statistics. FDI outflows range from a maximum value of \$172 billion [FDI outflow from Germany to the UK in 2000] to a minimum value of just \$0.001 million [outflow of the Czech Republic to Argentina in 2003]. In such a wide range the average FDI outflow investment across the sample of country pairs and 25 year period is \$685 million and the median just \$31 million. The average GDP of the sending country is over \$1.4 trillion, which is more than twice the equivalent (\$548 billion) of its receiving counterpart.

[Insert Table 1 here]

We categorize all of the independent variables in 9 groups listed in the way we use them when building the model: economic size (GDP of the sending and receiving country), country openness (exports plus imports over GDP for both the sending and receiving country), physical distance (distance, border and continent), institutional distance (economic or political union and legal origin),

cultural distance (shared language, shared history and cultural distance index). In addition, for robustness we use bilateral trust, asymmetric information (international phone calls and Financial Times circulation in the FDI host country), bilateral tax treaties for double tax avoidance and a set of country governance indicators (voice and accountability, political stability, government effectiveness, regulatory quality, rule of law and control of corruption).

Starting with the variables that are central to this study, we use three variables to measure the *physical proximity* between the countries in order to capture the effects of the distance from different perspectives. The proximity itself is an indicator for a greater familiarity between countries since it's generally true that places that are closer together are also more similar to each other. The geographic proximity (*dist*) measures the real distance between the two countries in the bilateral pair (in kilometres) and is obtained from the CEPII³. To illustrate, the distance between France and the US is roughly the mean of the sample with about 5,000 km. New Zealand and France are approximately 20,000 km apart (the maximum in our sample). The smallest distance is around 60km [distance between Austria and the Slovak Republic]. The second proxy for distance is a dummy variable that shows if the two countries in the pair are located on the *same continent* (ContSame). In our data, 42% of the countries that have an FDI relationship are located on the same continent. The *shared border* (border) variable⁴ is a dummy variable that takes the value of one if the two countries in the bilateral country pair share a border. In the data, 6% of the country pairs share the same border. Although these variables are correlated we keep all of them in our regressions because they offer a unique perspective on different aspects of physical distance.

The *shared membership to an economic or political union* (*EconOrgD*) is a dummy variable (constructed by the authors) that takes the value of one if both countries in the bilateral country pair are members of either one of the following international organisations or unions: Organisation for Economic Cooperation and Development (OECD), the European Union (EU), the Commonwealth of Nations or North American Free Trade Association (NAFTA). This dummy variable will show if similar social establishment stimulates the investing preferences among countries. We expect it to have a positive influence on FDI flows. In our sample, 45% of the countries in the country pairs share such membership to an economic or a political union.

The *same origin of the legal system* (*LegOr*) is a dummy variable that takes the value of one if both countries in the bilateral country pair share the same type of legal system. Data on countries' origin of the legal system are taken from professor Rafael La Porta's⁵ datasets. It divides the legal systems of the world into 5 categories: British, French, German, Socialistic and Scandinavian. This kind of division establishes a proxy for social and cultural similarity between the countries and it will show whether these factors enhance FDI flows among them. In this sample, 26% of the bilateral country pairs have the same origin of their legal systems.

The *shared official language* or language spoken by a minority (*LangCom*) is a dummy variable⁶ that takes the value of one if the countries in the bilateral country pair have the same official language or if there is a minority of at least 14% that speaks the official language of the other country. The data on this dummy variable was taken from the CEPII as two individual dummies and merged together by the authors for the purpose of this study. This variable clearly establishes if greater familiarity with a certain country based on the most basic cultural similarity – the language has a stimulating effect on the FDI flows. In our data, 14% of the FDI flows are between such countries.

The *shared history* (*HistSame*) variable is a dummy variable⁷ that takes the value of one if there are certain shared historical events between the two countries in the bilateral country pair. It is a dummy variable that is comprised from five other dummy variables taken from the CEPII database and merged together by the authors. These dummies are: dummy if the countries have had a common colonizer after 1945, have ever had a colonial link, have had a colonial relationship after 1945, are currently in a colonial relationship or were/are the same country⁸. Eight percent of the bilateral country pairs in this sample share such a historical relationship.

The *cultural distance index* is calculated following Kogut and Singh (1988) and is based on the four cultural dimensions as proposed by Hofstede (1980). The data on these dimensions are taken from Hofstede's website⁹. The four dimensions are: power distance index (the extent to which the less powerful members of organisations and institutions accept and expect that power is distributed equally); individualism (the degree to which individuals are integrated into groups); masculinity (the distribution of roles between genders) and uncertainty avoidance index (society's tolerance for uncertainty and ambiguity). These are sociological circumstances in which individuals live and work

in different societies. The idea behind Kogut and Singh's index is to measure the difference in these cultural dimensions between the two countries involved in an FDI relationship. Therefore, the greater the difference between the two countries, the lesser the FDI flows between them. The index is calculated using the following formula:

$$CD_{ij} = \sum_{d=1}^4 \{(I_{d,i} - I_{d,j})^2 / V_d\} / 4$$

Where the $I_{d,i}$ and $I_{d,j}$ is the individual cultural dimension (d) for country i and j respectively and V_d is the variance of each of the cultural dimensions. The data is time-invariant and reduces the sample from 22,109 down to 17,462 observations. We expect this variable to have a negative coefficient indicating that corporate managers prefer destinations with similar organisational culture. The cultural dimensions range from 0-100 and we use the logarithm of the index for our analysis.

The fourth set of variables is *macroeconomic*. Data on the macroeconomic variables is from the World Bank. The *gross domestic product* of the FDI receiving and sending countries (GDP_{rec} , GDP_{send} respectively) measured like the FDI flows in constant \$US, are used to show the economic magnitude of the two markets involved in an FDI relationship, which is one of the main attracting factors between two economic entities. The GDP is a variable that also has a very wide range of values that go from as little as the minimum of \$US 121 million [Republic of Palau in 2003] to the maximum value of US\$ 11.7 trillion [USA in 2010]. We use a standard literature measure for a country's openness to trade as *the sum of exports and imports over GDP* for both the FDI outflows receiving and sending countries.

We obtained the bilateral trust index as used in Guiso et al. (2009). The index measures bilateral trust between citizens of two countries in a sample of 15 European countries¹⁰. It reduces our sample from 17,462 to 3,464 observations. The data is a set of surveys conducted by Eurobarometer and sponsored by the European Commission (Guiso et al, 2009). They were conducted on a representative sample of the total population over the age of sixteen and on about 1,000 individuals per country. The survey question asked them to rate how much they trust people from their own country and from other countries. They rate the trustworthiness on a scale from 1-4 (1 being not at all

and 4 being a lot of trust) and the index is an average of all answers. Because all countries are European this also makes the same continent and economic organisation dummies have the value 1 for each observation and therefore unusable in this regression. We expect a greater degree of trust to have a positive influence on FDI flows.

Asymmetric information is quite difficult to measure directly; studies most commonly use telephone communication and media as a proxy for the amount of information that's available to and for investors. We add two variables for asymmetric information: *the international phone calls* in the FDI receiving country measured in minutes and divided by the country's population (per capita). This data on international telephone calls is obtained from the International Telecommunications Union (www.itu.int). Data is from 1995-2010 and it reduces the sample from 17,462 to 13,289 observations. We've obtained all available data from the *Financial Times newspaper* on their newspaper circulation and are also using it as per capita for the FDI outflows receiving country. Data is from the Financial Times company and is on their annual world circulation available from: 1997-2010. This reduces the sample to 10,991 observations.

We've also constructed a dummy variable to denote one if the two countries in the bilateral country pair have a signed *bilateral treaty for double taxation avoidance*. The variable is constructed by the authors from data available in the UNCTAD's country profile database available on UNCTAD's website¹¹. The data is available for all the years of our sample and it reduces the sample to 11,118 observations.

For corporate governance we include six variables from the World Governance Indicators (WGI)¹² available for all countries between the 1996-2010 period. We include these in order to capture some country specific factors that have to do with doing business in one country and the costliness that might entail. We have obtained the WGIs from the World Bank as explained in Kaufman et al., (2009). Their data is compiled from a number of 441 variables, 35 different sources and 33 organisations that inform on aspects of governance. Then the authors assign each of the following six aggregate indicators with that information and use an unobserved components model to construct them. The six aggregate indicators are as follows. *Voice and Accountability* captures perceptions of the extent to which a country's citizens are able to participate in selecting their government, as well as

freedom of expression, freedom of association, and a free media. *Political Stability and Absence of Violence* captures perceptions of the likelihood that the government will be destabilized or overthrown by unconstitutional or violent means, including politically-motivated violence and terrorism. *Government Effectiveness* captures perceptions of the quality of public services, the quality of the civil service and the degree of its independence from political pressures, the quality of policy formulation and implementation, and the credibility of the government's commitment to such policies. *Regulatory Quality* captures perceptions of the ability of the government to formulate and implement sound policies and regulations that permit and promote private sector development. *Rule of Law* captures perceptions of the extent to which agents have confidence in and abide by the rules of society, and in particular the quality of contract enforcement, property rights, the police, and the courts, as well as the likelihood of crime and violence. *Control of Corruption* captures perceptions of the extent to which public power is exercised for private gain, including both petty and grand forms of corruption, as well as "capture" of the state by elites and private interests.

These indices range in our sample from a minimum of -1.85 to a maximum of +2.59. They're also highly correlated amongst themselves and we cannot therefore use them together in the same regression but rather adding them one by one in order to see their effect. The data is available for the following years only: 1996, 1998, 2000 and 2002-2010, which reduces our sample for each variable to 10,229 observations. We expect all of the variables to have a positive influence on FDI i.e. the higher the level of each of the indicators the better the country governance and the more the FDI flows to that country.

The correlation matrix in Table 2a shows that a pair of variables that exhibit high correlation of -0.80: the same continent dummy variable and the physical distance variable. This kind of correlation is to be expected for such variables since they show essentially the same information that the further away the countries are the less likely it is that they will be on the same continent but they show different aspects of the proximity relationship; thus we keep them both in our analysis. In our robustness checks the correlation is very high between the six indices of country governance. Even though they are part of the same variable group using them in the same regression isn't possible due to multicollinearity; we therefore put them one by one in the regression.

[Insert Tables 2a,b here]

5. Near-Home Bias in FDI

Table 3 reports the results for home bias in FDI outflows. The FDI sending country is an OECD member and the FDI receiving country is the partner country anywhere in the world. We start by estimating the basic gravity model and then add the other variables one by one.

[Insert table 3 here]

In column (1) we report results for the basic economic relation between FDI outflows and economic mass and distance, as established by the gravity model. The coefficient estimate for the GDP of the FDI sending and receiving countries is positive and significant indicating that FDI outflows increase the higher the wealth of the countries. The relatively higher coefficient of the GDP for the FDI sending country (0.83 vs. 0.68) is also consistent with the view that FDI moves from large towards small. As income in the FDI receiving country increases, FDI flows to that country increases. Consistent with previous literature, the coefficient estimate for distance is negative and significant, suggesting that FDI outflows are larger to countries that are geographically closer.

In column (2) we add the country openness to trade as an additional macroeconomic explanatory variable. The coefficient estimates for the trade openness of both the FDI sending and receiving countries are positive and significant. As expected, countries that are more prone to trade have higher FDI flows.

Columns (3) and (4) include two additional proxies for the physical proximity between the FDI host and source countries. In column (3) we add the dummy variable equal to one if the partner countries are in the same continent. The coefficient estimate for the same continent dummy is positive and significant. FDI outflows are more likely to occur between countries located on the same continent. In column (4) we use the dummy variable that measures if the FDI sending and receiving countries share a border. The coefficient estimate for the shared border dummy is positive. FDI outflows are higher to countries that share a border. Corporate managers prefer to invest into countries that are bordering their own country as they are usually more familiar with the investment climate of such neighbouring countries. Firms expand abroad to exploit the knowledge created within the firm,

including not only technical but also marketing and managerial know-how (Casson, 1987). This advantage is most powerful in an environment that is similar to the environment that they are already familiar with (Buckley and Casson, 1991).

In columns (5) through to (9) we incorporate one by one the different variables from the institutional and cultural proximity groups as described in the data section. In column (5) we report results with the dummy variable that measures if the FDI partner countries share membership to the same economic or political organisation. The coefficient estimate for the shared economic organisation dummy is positive¹³. The economic structure and institutional quality in FDI sending and receiving countries is a major competitive advantage when investments are channelled towards countries in the same economic organisation (Habib and Zurawicki, 2002). In other words, similarity of the economic structures of the host and source countries creates a familiar environment where firms prefer to invest.

Column (6) introduces a dummy variable that measures if the FDI sending and receiving countries have the same origin of legal system. The coefficient estimate for the same legal system dummy is positive indicating that FDI flows are higher towards countries that have a similar legal system. Similarity of institutional environments is important in FDI decisions (Xu and Shenkar, 2002). If a company is familiar with a certain legal framework, weather British, German or French, it might be better able to exploit its knowledge advantage in a country that operates under the same legal system. Other things being equal it would be more advantageous to penetrate into a foreign market whose legal system is familiar. The empirical work of Galindo et al. (2003) also shows that in the banking sector, foreign bank penetration is greater between countries that have legal and institutional similarities.

A dummy for common history is added in column (7); it takes the value of 1, if the FDI sending and receiving countries share a common history. The coefficient estimate for the shared history dummy is positive: firms invest more in countries where they share a past such as having been part of the same country in the past or having had colonial ties (Guiso et al., 2009). The informational advantage of expanding into an environment that is likely to be rather familiar culturally and institutionally, to the environment from which they come from is highly beneficial when investing. A

shared history implicitly provides familiarity with business climates, a common understanding of issues and ways of resolving them. Historical similarities encourage the firms' expansion across borders.

Column (8) introduces a dummy variable that measures if the host and source countries have a shared official language or a shared language spoken by a minority in either country¹⁴. The coefficient estimate for the shared language dummy is positive. Corporate investors prefer to invest in countries where they share a language at an official or minority level. Language is a major ingredient of cultural similarity (Dongmin et al., 2009; Guiso et al., 2009). "Speaking the same language" metaphorically and literally is important in finalising a business deal. Speaking the same language gives a competitive advantage to firms expanding abroad against their foreign competitors that do not speak the same language. It puts them into a level field with domestic firms that speak the same language.

Ultimately, in column (9) we add the Cultural Distance Index. The CD index measures the similarity in organisational cultures in country pairs as defined by Hofstede (1980) and calculated as suggested by Kogut and Singh (1988). We can see that the index has the expected negative sign indicating that the greater the distance in organisational cultures between the country pairs, the less FDI outflows between them. Corporate managers prefer to work with managers that have similar values to the ones in their home country in terms of their power distances to people with authority, uncertainty avoidance, masculinity femininity of jobs distributions and individualism. The coefficient estimates for shared border becomes insignificant when we include the cultural distance index in this estimation. Geographically distant countries in different continents and naturally that do not share a border such as Great Britain and New Zealand or Australia (very low CD index, between 0.12 – 0.16) have similar cultures. Once we account for cultural distance we see that foreign investors prefer destinations closer in cultural than physical distance.

While economic factors such as country openness and GDP have been found to effect FDI flows, much remains unexplained in terms of how familiarity or psychic distance helps or hinders FDI decisions by corporate investors. FDI decisions are difficult to reverse compared to portfolio investments in foreign destinations. The location decisions of foreign direct investors provide a good test of how familiarity breeds investments and the psychic distance measured via institutional and

cultural distances matters. Using bilateral data on a wide set of countries we show how a comprehensive set of factors of psychic distance and familiarity with the business environment are important in location decisions. We demonstrate empirically that foreign direct investors prefer to invest near home. They also prefer to invest in countries that are in the same economic union with their home country, and that use the same legal frameworks. Historical ties such as sharing the same home country some time in near history and linguistic ties such as being able to speak home language in a foreign country are also driving forces in foreign direct investors' location decisions. The cultural distance in corporate relations is important in that it corporate managers prefer countries where corporate cultures are similar.

5.1. *Near-Home Bias in FDI in Different Continents*

We analyse the role of home bias in foreign direct investments using the bilateral outflows from different continents, Europe, Asia-Pacific and Americas. Table 4 reports results for the three continents, i.e. Europe, Asia-Pacific and Americas. Again, the dependent variable is the logarithm of FDI outflows sending countries located in one of the three continents to any of their partner countries across the three continents.

[Insert table 4 here]

The overall pattern of results for each of the three continents is broadly similar to the aggregate patterns reported in Table 3. In the case for the 26 countries in Europe almost all the variables for macroeconomic, physical, cultural and institutional proximity are significant and with the expected sign with the exception of same continent and border. This affirms the findings from the previous global analysis on a regional level.

Given the large distances among the four Asian-Pacific countries (Australia, Japan, Israel Korea and New Zealand) physical proximity measured in nominal terms is a significant factor in their foreign investment decisions. However, the significant continent dummy clearly suggests that there is a strong preference for mutual foreign investments among the countries in that region. The coefficient for trade openness of the FDI sending country negative and significant which is contrary to the *a priori* expectation and it's only present as such for this continent compared to the other two. The

shared history variable is negative and significant indicating that for the Asian-Pacific region mutual investing does not take place between countries with shared past. The rest of the cultural and institutional proximity variables are significant and with the expected sign.

For the American continent that includes FDI outflows from Canada, Mexico, Chile and the US, the variables are predominantly consistent with the aggregate results in Table 3 with the openness of the sending country, the distance and the shared language variables insignificant. The shared border variable is negative and significant contrary to expectation. In this case identically to the Asian Pacific countries, the physical proximity ceases to be important due to the vast distances between the countries but they still prefer to invest a lot within the same continent.

5.2. *Near-Home Bias in FDI in Different Countries*

[Insert table 5 here]

To gain some further insights into the pattern of decision making of individual sending countries Table 5 replicates the global and continent analysis at the individual country level. The regression results show the pattern of FDI flows from each of the 29 countries for whom sufficient data is available for estimation. Although the bulk of the results remain broadly similar with the aggregate and continent evidence presented in Tables 3 and 4 there are nevertheless a number of important points to note. We find very strong supporting evidence across all countries for the gravity model factors: the GDP and distance with these variables being significant with the expected influence in over 80% of the cases. These results are consistent with previous literature findings namely, Green and Cunningham (1975) who find GNP to be a major FDI predicting force of US outflows.

Evidence of near-home bias is clearly more prominent among the largest FDI investors US, UK, Germany, France, Spain and the Netherlands. For these 5 countries, distance and the institutional factors (economic organisation, and shared legal origin) emerge as important determinants of their FDI outflows; with the exception of Germany, the legal origin is also a significant factor in foreign investment decisions by these countries. The cultural distance index is overall significant with the predicted negative sign. Luxembourg also falls within this group of countries despite its much smaller

size. This is most likely due to the favourable tax rates that other countries use to register a large number of firms and operate from Luxembourg.

There is also a small group of countries like Denmark, Portugal, Austria and Sweden whose foreign investment decisions are also affected by some of the variables. The remaining 16, relatively small countries, also display some evidence of near-home bias but limited across a narrow range of our familiarity characteristics. Benito and Gripsurd (1992) do not find supporting evidence of culture being influential in a study of Norway's direct investments in the manufacturing industry. Conversely, we find the cultural distance index for Norway to be significant and with the predicted sign. This is possibly because their sample of manufacturing firms only reflects resource-seeking investments which are least likely to be affected by psychic distance or familiarity preferences because the firms cannot always choose where they can go to find natural resources.

The economic union variable is predominantly of significance for the most developed of the EU countries indicating that they do most of their direct investments in countries of similar institutional organisation and business climate. The legal system origin is negative and significant for all countries in the OECD that have a Germanic origin of the system (Germany, Austria, Japan, Korea and Switzerland) indicating that there aren't many countries with this system and so they do not always have a choice to invest in such places. The language isn't significant overall with it being important in the case of Czech Republic, Denmark, Spain, Netherlands and France.

The cultural similarity between the countries is overall a significant predictor with 52% of the coefficients for this variable being statistically significant and with the predicted negative influence confirming the findings in previous literature (Kogut and Singh, 1988) and in spite of the findings in Dow and Karunaratna (2006) as well as Green and Cunningham (1975) who do not find this index to be a significant factor in their study.

It is worth noting, however, that foreign investment decisions by smaller countries are also not always consistent even with the better established economic determinants of FDI. Table 5, shows a negative and significant relation between the trade openness of, Japan, the Netherlands and Slovakia and their flow of foreign direct investment.

Overall across the 29 countries the most pertinent home bias variables in order of consistency are: distance, cultural distance, economic organisation, legal origin, shared history, common border and same continent common language. Overall, these variables suggest that familiarity for smaller countries may be case by case determined.

5.3. *Near-home bias across time*

[Insert tables 6a,b here]

To investigate the potential implications of the market liberalization in the world in the early and mid-1990s (Bekaert and Harvey, 2005), we split the 35-year period into two and three-year sub-periods. Table 6a covers the periods 1981-1992 and 1993-2005, while in table 6b we test for differences across three sub-periods, i.e. 1981-89, 1990-99 and 2000-10. This is important knowing that there was a significant capital market liberalization. One could argue that the liberalization would influence the home bias factors after the 90s in the sense that they might become less important due to greater capital mobility. The results of these regressions are shown in tables 6a,b and they support the general results in table 3. The physical distance remains significant through time (except between 1981-89). In table 6b it can be observed that while in the first period (column 2) the distance isn't significant while the border dummy is, in the later periods (3) and (4), the physical distance remains statistically significant while the border isn't. This indicates that the physical distance still remains as a factor, the FDI investments do not necessarily occur between immediate neighbours with whom a border is shared. The other types of proximity, cultural and institutional also remain a significant driving force of FDI outflows in all sub-periods. These results indicate that in spite the diminishing presence of traditional barriers to trade and capital flows, the importance of distance between countries remains a consistent and significant determinant of FDI over time.

5.4 Possible explanations for the observed home bias

The equity and international portfolio literature has looked for reasons and alternative explanations as to why we observe this home bias phenomenon. Similarly, the FDI studies have also controlled for country-specific political factors or informational availability in the FDI host country

(Green and Cunningham, 1975; Habib, Zurawicki, 2002). The home bias literature most frequently controls for asymmetric information and transaction costs (French and Poterba, 1991; Tesar and Werner, 1995; Coval and Moskowitz, 1999) when looking to explain and control for alternative possibilities as to why there is home bias if it is not due to the observed familiarity features among the country pairs. Indeed, it makes intuitive sense to see if countries invest in particular places because they simply can't obtain information (for political or technological reasons) about other places or whether it's simply too costly to invest somewhere where the managers cannot be trusted, where they would be subjected to double taxation or where there is poor country governance. In order to test for some of the proposed explanations for the existence of home bias we add few variables to the original model in (4). These results are presented in tables 7-10.

5.4.1. *Is home bias due to bilateral trust?*

[Insert table 7 here]

We begin by adding the bilateral trust between the two countries in the country pair. This variable is taken from Guiso et al. (2009) and because of the limited data for it, consisting of 15 European countries we lose two of the other variables: shared continent and economic and political union dummies. We can see that the bilateral trust index is both positive and significant. This confirms the findings in Guiso et al. (2009) in that bilateral trust plays a role in the cultural biases between countries and their subsequent economic relationship. The shared language becomes negative suggesting that the 15 European countries in this subsample invest more in destinations where they do not have a shared language once the trust between the nations is taken into account. The other variables follow the conclusions of the main regression in table 3.

5.4.2. *Is home bias due to asymmetric information?*

[Insert table 8 here]

In order to consider information availability as a possible explanation for home bias we add two proxy variables: international phone minutes per capita and Financial Times circulation per capita for the FDI outflows receiving country which reduce the sample to 13,289 and 10,991 observations

respectively. We can see that the international phone calls variable isn't significant. This isn't consistent with previous findings (Coval & Moskowitz, 1999; Choe, Kho and Stulz, 2001) in both home bias in equity markets and FDI literature and FDI literature. The FT circulation in the FDI host country is statistically significant. This means that increased informational availability in one country, increases the attractiveness of that country. Despite the additional explanatory power of information availability our home bias variables remain significant.

5.4.3. *Is home bias due to lack of bilateral tax treaties?*

[Insert table 9 here]

The regression in table 9 considers the influence of bilateral tax treaties for double taxation avoidance. This variable reduces the sample by few observations down to 11,118 out of 16,792, however data isn't available for five countries: Israel, Mexico, Korea, Slovenia and Turkey. Results show that this variable is a strong predictor of FDI flows but similarly to the case of the two asymmetric information variables in table 8, the home bias variables remain significant, suggesting that even though tax treaties play a role (Erunza and Senbet, 1981; Liljeblom and Löflund, 2005) in the choice of the destination countries it is not the sole explanatory factor along with the other macroeconomic variables in predicting the choice country for FDI.

5.4.4. *Is home bias due to country governance?*

[Insert table 10 here]

The results for the country governance factors in home bias in FDI outflows are presented in table 10. These variables reduce the sample to 10,229 observations. Results show that all of the six governance indicators are significant and positive except the government effectiveness indicator which is only significant at the 10% level. This suggests that the individual country governance in the FDI outflows receiving country plays a role in the choice country. FDI investors prefer to invest in countries where there is better governance. The voice and accountability indicator is positive and significant indicating that the greater the freedom of speech and expression of the citizens of one country, the greater the FDI flows to that country. The political stability indicator shows a positive and

significant influence on FDI outflows. The greater the political stability and absence of violence the more the FDI flows. This is one of the most commonly used factors in the literature (Green and Cunningham (1975); Grosse & Travino 1996) to control for country risk and country governance when investing at a particular location and our findings support the general findings in the literature. Regulatory quality shows the ability of the government to implement sound policies that promote the private sector, therefore the greater this quality the more FDI flows will be attracted. This variable is also positive and significant. The rule of law variable is positive and significant, the greater the rule of law i.e. the extent to which the rules of the society are abided the greater the FDI flows to that country. Finally, the control of corruption is also both positive and significant indicating that the investors prefer countries with greater control over corruption. Controlling for corruption is a common feature in FDI studies (Habib & Zurawicki, 2002) along with political stability. It always proves to have a significant effect on FDI flows.

The country governance quality in the FDI outflows receiving country plays a role in the potential costliness of investing in a particular country. Understandably, investors prefer to invest in countries that have better social governance. However this doesn't eliminate the other factors of near-home bias. All of them remain overwhelmingly significant and with the expected sign which shows that familiarity in the institutional and cultural sense still plays an important factor in the investment destination choices for FDI in addition to the macroeconomic and governance factors.

6. Conclusion

We investigate the location choices for foreign direct investments using data on the FDI outflows of 3,136 unique bilateral country pairs for the period 1981-2010. The literature on FDI has traditionally relied on a set of well defined economic factors including internationalisation to explain destination decisions of foreign direct investments. We contribute to this literature by testing the continuing impact of a comprehensive set of institutional and cultural factors, identified in the psychic distance literature, and show that they are still play a pivotal role in corporate foreign investment decisions. We show that familiarity in combination with geographical aspects of the location choices create a home bias effect in FDI flows. We test for the presence of near-home bias in FDI outflows at

a global, regional and country level. We show evidence that cultural and institutional similarities between host and source countries remain decisive factors across time and different geographical areas in corporate decisions on entering into a foreign market. We also show evidence that the near-home bias hasn't diminished across time in spite of the undisputable increase in globalisation.

More specifically, our evidence reveals that corporate investors prefer destinations near-home. We measure distance in terms of physical, institutional and cultural proximity. Institutional proximity is an important indicator for business climate familiarity. Direct investors prefer to invest in countries with similar economic and legal systems to their own. Cultural distances are also important indicators of investment choices. A commonly spoken language between the host and source countries, a shared history and organisational culture determine FDI decisions as they give a competitive advantage to the foreign investor relative to its international competitors. We control for other factors; bilateral trust and bilateral tax treaties increase FDI flows. Asymmetric information and bad corporate governance reduce FDI flows. The effect of physical, institutional and cultural distances on FDI remains. Stulz (2005) argues that one of the reasons for this persistence of home bias in the markets and the limited effect of globalisation is the twin agency problem (the fact that managers of corporations sometimes act in their own best interests and the fact that governments sometimes limit capital mobility to protect their interests). This can also be applied here as one of the possible reasons for the endurance of home country bias in FDI flows. As discussed earlier, managers suffer from various biases or simply don't have all the time and resources to look at all investment options. Various governments do not establish the same relationship with all of the countries in the world and this results in added perceived or real difficulties in the corporate managers' investment choices.

Our results are important from a policy perspective. We show that economic activity and country openness are not necessarily the only prerequisites to attract foreign investors. FDI's tend to have a beneficial impact on economic growth and many countries want to attract them. We show that FDI investors prefer destinations that are familiar to them. There is need for caution here. Being neighbours or having a shared language may not be the only prerequisites to attract foreign direct investments. Developing the legal frameworks, improving economic relations and corporate governance will also make the business environment more familiar to foreign direct investors. As such

our results suggest a further research agenda. One area of future research is to investigate in detail what host countries can do to make their institutional environments more welcoming to foreign investors.

NOTES

¹ We make alternative panel estimations using a static GMM (IV) estimation method. Conclusions do not change. Results are available from the authors upon request.

² OECD member countries: Australia, Austria, Belgium, Canada, Chile, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Iceland, Ireland, Israel, Italy, Japan, Korea, Luxembourg, Mexico, Netherlands, New Zealand, Norway, Poland, Portugal, Slovak Republic, Slovenia, Spain, Sweden, Switzerland, Turkey, United Kingdom, United States (34 countries)

³ [Centre D'Etudes Prospectives Et D'Informations Internationales (CEPII)] The distance is measured following Head and Meyer (2002) and the formula for the distances is not a simple air distance between two cities but it is calculated using the countries' area and the capitals' longitude and latitude: $[d_{ij} = .67 * \text{sqr}(\text{area}/\pi)]$.

⁴ There are five island countries among the OECD member countries: Australia, Iceland, Japan, Korea and New Zealand. For these countries the shared border dummy variable never takes the value of one and cannot be used in the estimation for these countries. The data we use is on South Korea, which only borders North Korea (for which there isn't any data) and therefore South Korea effectively becomes an island country in our data sample;

⁵ <http://mba.tuck.dartmouth.edu/pages/faculty/rafael.laporta/publications.html>

⁶ The common language dummy in our sample also never has a value of one for these countries: Czech Republic, Denmark, Greece, Iceland, Japan, Norway, Slovenia, Portugal and Poland because in our sample they don't share the same official or minority language with any of their FDI partners.

⁷ The history dummy variable doesn't have a value of one for: Denmark, Switzerland, Norway and Italy..

⁸ The shared history part of the dummy variable complements the common colonizer information setting to one if the countries were or are the same state or the same administrative entity for a long period (25-50 years in the twentieth century, 75 year in the ninetieth and 100 years before). This definition covers countries have been belong to the same empire (Austro-Hungarian, Persian, Turkish), countries have been divided (Czechoslovakia, Yugoslavia) and countries have been belong

to the same administrative colonial area. For instance, Spanish colonies are distinguished following their administrative divisions in the colonial period (viceroyalties). According to this definition, Argentina, Bolivia, Paraguay and Uruguay were thus a single country. Similarly, the Philippines were subordinated to the New Spain viceroyalty and thus the ‘same country’ equals to one with Mexico. Sources for this variable came from: www.worldstatesmen.org/.

⁹ The data for Hofstede’s cultural dimensions can be obtained from: www.geert-hofstede.com/

¹⁰ These countries are: Austria, Belgium, the UK, Denmark, the Netherlands, Finland, France, Germany, Greece, Ireland, Italy, Norway, Portugal, Spain and Sweden;

¹¹ UNCTAD: United Nations Conference on Trade and Development (www.unctad.org)

¹² www.govindicators.org

¹³ We constructed two alternative versions of the economic and political union dummy to reflect the shared customs union and shared currency union where in accordance with our dataset. The results of the alternative estimations support the findings for this variable.

¹⁴ We estimated this regression with an alternative language variable. It was created based on different language families and it shows broader similarities between the languages spoken between two countries. The findings remain the same.

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Table 1. Descriptive statistics for FDI outflows panel data

The table reports the main descriptive statistics of the variables used in the FDI outflows analysis. These variables are in their original units

	FDI Outflows (mil\$)	GDP of FDI Receiving country(mil\$)	GDP of FDI Sending country(mil\$)	Trade Openness of the FDI Rec. country (%)	Trade Openness of the FDI Send. Country (%)	Physical Distance (km)	Location on Same continent	Shared Border	Econ. or Political Union	Legal Syst. Origin	Shared History	Common Language	Cultural Distance Index
Mean	685	548000	1400000	0.87	0.81	5620	0.42	0.06	0.45	0.26	0.08	0.14	2.10
Median	31	120000	441000	0.70	0.62	5059	0.00	0.00	0.00	0.00	0.00	0.00	1.90
Maximum	172210	11700000	11700000	5.39	3.55	19630	1.00	1.00	1.00	1.00	1.00	1.00	10.16
Minimum	0.001	121	6520	0.09	0.12	60	0.00	0.00	0.00	0.00	0.00	0.00	0.00
St. Dev.	3328	1500000	2400000	0.67	0.63	4433	0.49	0.23	0.50	0.44	0.28	0.35	1.47
Observations	24853	24664	24201	22174	24829	24664	24853	24664	24853	24853	24664	24664	18000

Table 1b. Descriptive statistics for robustness variables for home bias in FDI outflows panel data

The table reports the main descriptive statistics of the additional variables used in the FDI outflows analysis. These variables in their original units.

	Bilateral Trust	International Phone Minutes for rec. Country per capita	FT circulation per capita for rec. country	Bilateral treaties	Voice and Accountability	Political Stability	Government Effectiveness	Regulatory Quality	Rule of Law	Control of Corruption
Mean	2.82	79.50	0.001	0.76	0.37	0.18	0.56	0.55	0.43	0.46
Median	2.75	28.30	0.000	1.00	0.55	0.36	0.54	0.63	0.49	0.28
Maximum	3.65	1909.79	0.008	1.00	1.83	1.66	2.37	2.23	2.01	2.59
Minimum	2.18	0.00	0.000	0.00	-2.22	-3.18	-2.25	-2.25	-2.09	-1.85
St. Dev.	0.32	151.43	0.001	0.43	0.96	0.91	0.99	0.92	1.01	1.09
Observations	3464	18075	14251	13820	15761	15758	15747	15748	15758	15747

Table 2. Correlations table for FDI outflows panel data

The table reports the correlation coefficients of the variables used in the FDI Outflows regression analysis.

	L FDI Outflows	L GDP of FDI Receiving country	L GDP of FDI Sending country	Trade Openness of the FDI Rec. country	Trade Openness of the FDI Send. country	L Distance	Location on Same continent	Shared Border	Econ. or Political Union	Legal Syst. Origin	Shared History	Common Language	Cultural Distance Index
L FDI Outflows	1.00												
L GDP of FDI Receiving country	0.41	1.00											
L GDP of FDI Sending country	0.32	-0.11	1.00										
Trade Openness of the FDI Rec. country	0.04	-0.30	-0.05	1.00									
Trade Openness of the FDI Send. country	-0.11	-0.08	-0.63	0.14	1.00								
L Distance	-0.17	-0.02	0.23	-0.11	-0.14	1.00							
Location on Same continent	0.15	0.04	-0.18	0.12	0.05	-0.80	1.00						
Shared Border	0.19	0.09	-0.04	0.01	0.00	-0.46	0.27	1.00					
Econ. or Political Union	0.33	0.48	-0.11	-0.06	-0.03	-0.36	0.42	0.18	1.00				
Legal Syst. Origin	0.05	-0.07	-0.03	-0.03	0.05	-0.06	-0.03	0.18	0.00	1.00			
Shared History	0.11	-0.09	0.03	-0.01	-0.05	-0.08	-0.06	0.17	0.02	0.33	1.00		
Common Language	0.17	-0.06	0.14	0.00	-0.07	0.04	-0.06	0.18	-0.01	0.35	0.41	1.00	
Cultural Distance Index	-0.14	-0.09	0.00	0.14	-0.02	0.14	-0.10	-0.18	-0.17	-0.27	-0.10	-0.16	1.00

Table 2a. Correlations table for FDI outflows panel data (continues from previous table)

The table reports the correlation coefficients with the robustness variables used in the FDI Outflows regression analysis.

	Bilateral trust	LInternational Phone Calls/cap	FT circulation per capita	Bilateral tax treaties	Voice and Accountability	Political Stability	Government Effectives	Regulatory Quality	Rule of Law	Control of Corruption
L FDI Outflows	0.12	0.22	0.21	0.34	0.27	0.19	0.33	0.33	0.31	0.30
L GDP of FDI Receiving country	-0.15	0.15	0.08	0.39	0.29	0.11	0.46	0.40	0.40	0.38
L GDP of FDI Sending country	-0.29	-0.12	-0.05	0.07	-0.12	-0.09	-0.12	-0.12	-0.11	-0.10
Trade Openness of the FDI Rec. country	0.17	0.42	0.46	-0.09	0.06	0.35	0.28	0.32	0.25	0.25
Trade Openness of the FDI Send. country	0.15	0.07	0.00	-0.10	0.00	0.01	-0.01	0.00	-0.01	-0.01
L Distance	-0.33	-0.29	-0.19	-0.17	-0.28	-0.26	-0.22	-0.24	-0.24	-0.19
Location on Same continent	NA	0.34	0.19	0.19	0.42	0.36	0.31	0.35	0.32	0.28
Shared Border	0.07	0.12	0.04	0.07	0.14	0.11	0.12	0.11	0.11	0.10
Econ. or Political Union	NA	0.50	0.25	0.36	0.68	0.51	0.65	0.64	0.66	0.61
Legal Syst. Origin	0.01	-0.06	-0.02	-0.08	-0.08	-0.07	-0.11	-0.11	-0.10	-0.09
Shared History	0.15	-0.06	0.03	0.00	-0.02	-0.02	-0.05	-0.05	-0.04	-0.04
Common Language	0.16	-0.01	0.08	0.05	0.00	-0.05	-0.02	-0.02	-0.01	0.01
Cultural Distance Index	-0.12	-0.07	-0.06	-0.06	-0.20	-0.08	-0.10	-0.10	-0.13	-0.11
Bilateral trust	1	0.24	0.13	-0.27	0.48	0.34	0.50	0.39	0.49	0.50
International Phone Calls/cap		1	0.52	0.10	0.62	0.65	0.73	0.73	0.72	0.74
FT circulation per capita			1	0.12	0.33	0.41	0.52	0.52	0.51	0.54
Bilateral tax treaties				1	0.32	0.21	0.33	0.28	0.31	0.26
Voice and Accountability					1	0.68	0.80	0.83	0.82	0.79
Political Stability						1	0.75	0.74	0.79	0.77
Government Effectives							1	0.94	0.96	0.95
Regulatory Quality								1	0.93	0.91
Rule of Law									1	0.96
Control of Corruption										1

Table 3. Near-Home Bias in FDI outflows

Dependant variable is log (FDI outflows_{ij,t}) which equals foreign direct investment flow from country i to country j at time t; The FDI outflows are from the FDI sending country towards the FDI receiving country. The explanatory variables are: Log of the GDP of the FDI receiving country; log of the GDP for the FDI sending country; trade openness (ratio of exports plus imports over GDP) for the FDI receiving country; trade openness (ratio of exports plus imports over GDP) for the FDI sending country; the log of the physical distance between the country i and j in kilometres; shared continent dummy (value of one if the two country i and j are one the same continent); shared border dummy (value of one if country i and j share a border); shared economic or political union dummy (value of one if country i and j share membership in the same economic or political union); same legal origin dummy (one if country i and j share the same origin of their legal systems); shared language (one if country i and j share the same official language or language of the minorities); shared history (one if country i and j share history with respect to having had a past colonial relationship or having been part of the same country). The t-statistics are based on standard errors that have been adjusted for heteroskedasticity using the White (1980) method; Fixed effects used; Note that *, **, *** stand for significant coefficients at the 10%, 5% and 1% level respectively;

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
	(Log)FDI Outflows	(Log)FDI Outflows	(Log)FDI Outflows	(Log)FDI Outflows	(Log)FDI Outflows	(Log)FDI Outflows	(Log)FDI Outflows	(Log)FDI Outflows	(Log)FDI Outflows
C	-4.04 ***	-7.19***	-7.53***	-7.93***	-7.99***	-8.48***	-8.48***	-8.12***	-8.39***
(Log) GDPrec	0.68***	0.82***	0.82***	0.81***	0.74***	0.76***	0.78***	0.78***	0.79***
(Log) GDP send	0.83***	1.12***	1.13***	1.12***	1.11***	1.12***	1.13***	1.10***	1.26***
Openness rec		0.31***	0.31***	0.31***	0.30***	0.31***	0.31***	0.31***	0.32***
Openness send		0.51***	0.52***	0.52***	0.52***	0.51***	0.54***	0.53***	0.64***
(Log) Distance	-0.72***	-0.70***	-0.62***	-0.49***	-0.47***	-0.45***	-0.37***	-0.42***	-0.60***
Same Continent			0.09***	0.14***	0.05**	0.10***	0.20***	0.17***	0.06***
Border				0.34***	0.34***	0.25***	0.19***	0.11***	-0.01
Shared Econ. Org.					0.24***	0.23***	0.20***	0.20***	0.14***
Same Legal System						0.26***	0.16***	0.10***	0.12***
Shared History							0.57***	0.42***	0.37***
Shared Language								0.34***	0.36***
Cul. Dist. Ind.									-0.04***
N	24,002	22,109	22,109	22109	22109	22109	22109	22109	15858
Adj. R ²	0.40	0.46	0.46	0.46	0.47	0.47	0.49	0.47	0.46

Table 4: Near-Home Bias in FDI outflows by sending continent calculated

Dependant variable is log (FDI outflows_{i,j,t}) which equals foreign direct investment outflow from country i to country j at time t, *for the FDI outflows sending country located on a particular continent* (Europe, Asia-Pacific and the Americas); The FDI flows are from the FDI sending country towards the FDI receiving. The explanatory variables are: Log of the GDP of the FDI receiving country; log of the GDP for the FDI sending country; trade openness (ratio of exports plus imports over GDP) for the FDI receiving country; trade openness (ratio of exports plus imports over GDP) for the FDI sending country; the log of the physical distance between the country i and j in kilometres; shared border dummy (value of one if country i and j share a border); shared economic or political union dummy (value of one if country i and j share membership in the same economic or political union); same legal origin dummy (one if country i and j share the same origin of their legal systems); shared language (one if country i and j share the same official language or language of the minorities); shared history (one if country i and j share history with respect to having had a past colonial relationship or having been part of the same country) and the cultural distance index based on Kogut and Singh (1988). The t-statistics are based on standard errors that have been adjusted for cross-sectional heteroskedasticity using the White (1980) method; Fixed effects used; Note that *, **, *** stand for significant coefficients at the 10%, 5% and 1% level respectively;

Variable	EUROPE (send)	ASIA-PACIFIC (send)	AMERICAS (send)
	Log (FDI outflows)	Log (FDI outflows)	Log (FDI outflows)
C	-8.93 ***	-6.46 ***	-7.75***
(Log) GDPrec	0.77 ***	0.82 ***	0.88***
(Log) GDP send	1.42 ***	0.75 ***	0.81***
Openness rec	0.29 ***	0.33 ***	0.47***
Openness send	0.71 ***	-0.56 ***	-0.12
(Log) Distance	-0.67 ***	-0.26 **	-0.11
Same Continent	-0.06	0.38 ***	0.8***
Border	-0.02	NA	-0.39***
Shared Econ. Org.	0.22 ***	0.19 ***	0.36***
Same Legal System	0.07 ***	0.15 ***	0.41***
Shared History	0.49 ***	-0.29 ***	0.28***
Shared Language	0.28 ***	0.35 ***	0.06
Cul. Dist. Ind.	-0.03 ***	-0.05 ***	-0.08***
N	13867	2,360	1,235
Adjusted R ²	0.48	0.43	0.64

Table 5. Near-Home Bias in FDI outflows by individual country

Dependant variable is log (FDI outflows_{i,j,t}) which equals foreign direct investment flow from country i to country j at time t; The FDI outflows are from the FDI sending country towards the FDI receiving country. The explanatory variables are: Log of the GDP of the FDI receiving country; log of the GDP for the FDI sending country; trade openness (ratio of exports plus imports over GDP) for the FDI receiving country; trade openness (ratio of exports plus imports over GDP) for the FDI sending country; the log of the physical distance between the country i and j in kilometres; shared continent dummy (value of one if the two country i and j are one the same continent); shared border dummy (value of one if country i and j share a border); shared economic or political union dummy (value of one if country i and j share membership in the same economic or political union); same legal origin dummy (one if country i and j share the same origin of their legal systems); shared language (one if country i and j share the same official language or language of the minorities); shared history (one if country i and j share history with respect to having had a past colonial relationship or having been part of the same country); cultural distance index (Kogut and Singh, 1988). The t-statistics are based on standard errors that have been adjusted for cross-sectional heteroskedasticity using the White (1980) method; Note that *, **, *** stand for significant coefficients at the 10%, 5% and 1% level respectively.

	<i>Const.</i>	<i>LGDP of FDI rec. country</i>	<i>LGDP of FDI send country</i>	<i>Openness rec. country</i>	<i>Openness of send. country</i>	<i>L distance</i>	<i>Same Cont.</i>	<i>Shared Border</i>	<i>Econ. Organs. Dummy</i>	<i>Legal origin dummy</i>	<i>Shared History</i>	<i>Shared Lang.</i>	<i>CD index</i>
Australia	-28.41 ***	0.64 ***	5.00 ***	0.17 ***	-4.15	-0.04	1.23 **	NA	-0.12	0.64 ***	0.54 ***	0.19 **	-0.03
Austria	-11.96	0.56 ***	2.03	0.17 ***	1.24 *	-0.49 ***	0.24 **	0.05	0.06	-0.52 ***	0.62 ***	0.59 ***	-0.04 *
Belgium	-47.11 **	0.92 ***	8.03 **	0.40 ***	0.54	-0.20	0.16	0.01	0.58 ***	0.15	0.81 ***	0.04	0.01
Czech R.	-29.50	0.45 ***	6.22	0.13	-0.02	-0.83 ***	-0.28	0.52 **	-0.02	0.43 ***	-0.05	NA	-0.01
Denmark	-43.61 ***	0.94 ***	7.99 ***	0.32 ***	-0.56	-0.34 ***	0.36 ***	-0.18 *	0.11	0.47 ***	NA	NA	-0.09 ***
Finland	-29.32 ***	0.88 ***	5.74 ***	0.35 ***	-0.87	-0.69 ***	-0.12	0.06	0.22 ***	0.13	0.19	0.32 *	-0.17 ***
France	-41.25 ***	0.94 ***	6.70 ***	0.36 ***	-0.79	-0.70 ***	-0.23 **	0.12	0.28 ***	0.29 ***	0.32 ***	0.10	-0.03
Germany	-24.48 ***	0.92 ***	3.49 ***	0.35 ***	0.27	-0.13 *	0.36 ***	0.10 *	0.16 ***	-0.38 ***	0.09	0.47 ***	-0.07 ***
Greece	-29.66 ***	1.02 ***	4.85 ***	0.43 ***	0.59	-0.47 ***	0.77 ***	1.80 ***	0.07	-0.10 ***	-1.50 ***	NA	-0.17 ***
Hungary	-20.85 **	0.83 ***	4.63 **	0.55 ***	0.88	-1.98 ***	-0.93 ***	1.06 ***	0.13	0.41 **	-0.89 ***	-0.11	-0.16 ***
Iceland	-4.71	0.41 ***	1.28	0.17	5.67 ***	-1.79 ***	-0.14	NA	-0.11	0.43 *	0.05	NA	NA
Ireland	-9.21	0.93 ***	1.56	0.36 ***	0.35	-1.13 ***	-0.33	NA	0.66 ***	1.02 ***	0.29	-0.39	-0.01
Italy	-1.54	1.11 ***	-0.59	0.40 ***	2.70	-0.31 **	0.84 ***	-0.01	-0.20 ***	0.32 ***	NA	0.07	-0.16 ***
Japan	-16.05 ***	1.19 ***	2.12 ***	0.48 ***	-3.87 ***	-0.47 **	0.23	NA	-0.06	-0.38 ***	0.06	NA	-0.03 *
Korea	-18.74 ***	0.89 ***	3.13 ***	0.28 ***	-0.78	-0.60 ***	0.08	NA	-0.23 ***	-0.54 ***	-0.60 ***	-0.03	0.06 **
Luxemb.	-16.59	1.19 ***	3.25	0.63 ***	0.41	-1.23 ***	-0.08	-0.75 ***	0.55 ***	0.59 ***	-0.08	0.06	-0.14 ***
Netherl.	-56.30 ***	0.92 ***	10.44 ***	0.38 ***	-2.40	-0.46 ***	-0.10	-0.58 ***	0.23 ***	0.08	0.31 ***	0.57 ***	-0.03 ***
New Zeal.	24.78	0.72 ***	-6.78 ***	0.62 ***	4.41	0.24 ***	1.98 ***	NA	-0.38 **	0.19	0.66 ***	-0.17 **	-0.17 **
Norway	-18.19 ***	0.72 ***	3.80 ***	0.49 ***	-0.24	-1.06 ***	-0.49 ***	-0.05	0.17	0.25	NA	NA	-0.13 ***
Poland	-12.09 **	0.96 ***	2.04 *	0.51 ***	2.55	-1.59 ***	0.00	-0.04	-0.09	0.01	0.28 *	NA	-0.09 ***
Portugal	2.14	0.83 ***	-0.66	0.53 ***	3.18	-1.62 ***	-0.27 *	0.19	0.24 **	0.58 ***	2.02 ***	NA	0.08 **
Slovakia	-37.33 ***	0.75 ***	8.11 ***	0.48 *	-1.75	-0.51 ***	-0.06	0.89 ***	-0.32	0.36	0.16	-0.29	0.08
Slovenia	-16.37	0.87 ***	4.48	-0.08 *	0.20	-2.20 ***	-1.30 ***	0.00	0.10	0.26	-0.09	NA	-0.03
Spain	-19.89 ***	0.83 ***	3.31 ***	0.41 ***	2.34	-1.03 ***	-0.01	0.12 **	0.17 **	0.42 ***	0.52 ***	0.65 ***	-0.09 ***
Sweden	-11.27	0.84 ***	1.73	0.26 ***	1.43	-0.53 ***	0.14	0.24	0.24 ***	-0.06	0.70 ***	-0.53 ***	-0.14 ***
Switzerl.	-4.85	0.78 ***	0.45	0.33 ***	1.05	-0.17	-0.03	0.17	0.18 ***	-0.37 ***	NA	-0.07	-0.09 ***
Turkey	-12.20	0.41 ***	2.77	0.10	-3.04	-0.95 ***	-0.27	-0.32 *	0.06	0.30 ***	-0.49 **	0.77 **	0.18 ***
UK	-23.57 ***	0.93 ***	3.57 ***	0.38 ***	-1.29	-0.15 **	0.06	0.24 **	0.12 **	0.09	0.25 ***	0.03	-0.05 ***
USA	0.89	1.00 ***	-0.76	0.55 ***	3.89	0.04	0.83 ***	-0.49 ***	0.40 ***	0.30 ***	0.15 ***	0.11 **	-0.06 ***

Table 6a. Home Bias in FDI outflows in two sub-periods;

Dependant variable is log (FDI outflows $_{i,j,t}$) which equals foreign direct investment flow from country i to country j at time t; the time is split in two sub-periods: 1981-1995 (2) and 1996-2010 (3). The FDI outflows are from the FDI sending country towards the FDI receiving country. The explanatory variables are: Log of the GDP of the FDI receiving country; log of the GDP for the FDI sending country; trade openness (ratio of exports plus imports over GDP) for the FDI receiving country; trade openness (ratio of exports plus imports over GDP) for the FDI sending country; the log of the physical distance between the country i and j in kilometres; shared continent dummy (value of one if the two country i and j are one the same continent); shared border dummy (value of one if country i and j share a border); shared economic or political union dummy (value of one if country i and j share membership in the same economic or political union); same legal origin dummy (one if country i and j share the same origin of their legal systems); shared language (one if country i and j share the same official language or language of the minorities); shared history (one if country i and j share history with respect to having had a past colonial relationship or having been part of the same country); cultural distance index (based on Kogut and Singh (1988)); The t-statistics are based on standard errors that have been adjusted for cross-sectional heteroskedasticity using the White (1980) method; Fixed effects used; Note that *, **, *** stand for significant coefficients at the 10%, 5% and 1% level respectively;

	(1)	(2)	(3)
	(Log)FDI Outflows 1981-2010	(Log)FDI Outflows 1981-1995	(Log)FDI Outflows 1996-2010
C	-8.39***	-10.53***	-8.6***
(Log) GDPrec	0.79***	0.76***	0.81***
(Log) GDP send	1.26***	1.25***	1.35***
Openness rec	0.32***	0.42***	0.3***
Openness send	0.64***	1.64***	0.67***
(Log) Distance	-0.60***	-0.11**	-0.72***
Same Continent	0.06***	0.26***	0.04***
Border	-0.01	0.07**	-0.03
Shared Econ. Org.	0.14***	0.3***	0.07**
Same Legal System	0.12***	0.12***	0.12***
Shared History	0.37***	0.33***	0.39***
Shared Language	0.36***	0.34***	0.37***
Cul. Dist. Index	-0.04***	-0.07***	-0.03***
N	16,792	5289	12173
Adj. R²	0.46	0.54	0.49

Table 6b. Home Bias in FDI outflows in three sub-periods;

Dependant variable is log (FDI outflows $_{i,j,t}$) which equals foreign direct investment flow from country i to country j at time t ; the time is split in three sub-periods: 1981-1989 (2); 1990-1997 (3) and 1998-2005 (4). The FDI outflows are from the FDI sending country towards the FDI receiving country. The explanatory variables are: Log of the GDP of the FDI receiving country; log of the GDP for the FDI sending country; trade openness (ratio of exports plus imports over GDP) for the FDI receiving country; trade openness (ratio of exports plus imports over GDP) for the FDI sending country; the log of the physical distance between the country i and j in kilometres; shared continent dummy (value of one if the two country i and j are one the same continent); shared border dummy (value of one if country i and j share a border); shared economic or political union dummy (value of one if country i and j share membership in the same economic or political union); same legal origin dummy (one if country i and j share the same origin of their legal systems); shared language (one if country i and j share the same official language or language of the minorities); shared history (one if country i and j share history with respect to having had a past colonial relationship or having been part of the same country); cultural distance index (based on Kogut and Singh (1988)); The t -statistics are based on standard errors that have been adjusted for cross-sectional heteroskedasticity using the White (1980) method; Fixed effects used; Note that *, **, *** stand for significant coefficients at the 10%, 5% and 1% level respectively;

	(1)	(2)	(3)	(4)
	(Log)FDI Outflows 1981-2010	(Log)FDI Outflows 1981-1989	(Log)FDI Outflows 1990-1999	(Log)FDI Outflows 2000-2010
C	-8.39***	-11.35***	-9.82***	-8.67***
(Log) GDPrec	0.79***	0.83***	0.78***	0.81***
(Log) GDP send	1.26***	1.25***	1.27***	1.39***
Openness rec	0.32***	0.56***	0.37***	0.29***
Openness send	0.64***	1.58***	1.44***	0.67***
(Log) Distance	-0.60***	0.02	-0.33***	-0.76***
Same Continent	0.06***	0.27***	0.15***	0.05*
Border	-0.01	0.1***	0.07***	-0.05*
Shared Econ. Org.	0.14***	0.21**	0.24***	0.06*
Same Legal System	0.12***	0.13***	0.12***	0.13***
Shared History	0.37***	0.33***	0.37***	0.37***
Shared Language	0.36***	0.31***	0.34***	0.38***
Cul. Dist. Index	-0.04***	-0.08***	-0.05***	-0.03***
N	16,792	2442	5246	9774
Adj. R²	0.46	0.53	0.52	0.49

Table 7. Bilateral Trust and Home Bias in FDI outflows;

Dependant variable is log (FDI outflows $_{i,j,t}$) which equals foreign direct investment flow from country i to country j at time t; The FDI outflows are from the FDI sending country towards the FDI receiving country. The explanatory variables are: Log of the GDP of the FDI receiving country; log of the GDP for the FDI sending country; trade openness (ratio of exports plus imports over GDP) for the FDI receiving country; trade openness (ratio of exports plus imports over GDP) for the FDI sending country; the log of the physical distance between the country i and j in kilometres; shared continent dummy (value of one if the two country i and j are one the same continent); shared border dummy (value of one if country i and j share a border); shared economic or political union dummy (value of one if country i and j share membership in the same economic or political union); same legal origin dummy (one if country i and j share the same origin of their legal systems); shared language (one if country i and j share the same official language or language of the minorities); shared history (one if country i and j share history with respect to having had a past colonial relationship or having been part of the same country); cultural distance index (based on Kogut and Singh (1988)); bilateral trust between the citizens of two countries (from Guiso et al., 2009)The t-statistics are based on standard errors that have been adjusted for cross-sectional heteroskedasticity using the White (1980) method; Fixed effects used; Note that *, **, *** stand for significant coefficients at the 10%, 5% and 1% level respectively;

	(1)	(2)
	(Log)FDI Outflows	(Log)FDI Outflows
C	-8.39***	-11.19***
(Log) GDPrec	0.79***	1.01***
(Log) GDP send	1.26***	1.25***
Openness rec	0.32***	0.62***
Openness send	0.64***	0.64***
(Log) Distance	-0.60***	-0.68***
Same Continent	0.06***	NA
Border	-0.01	0.04
Shared Econ. Org.	0.14***	NA
Same Legal System	0.12***	0.24***
Shared History	0.37***	0.72***
Shared Language	0.36***	-0.37***
Cul. Dist. Index	-0.04***	-0.05***
Bilateral Trust		0.71***
N	16,792	3464
Adj. R²	0.46	0.64

Table 8. Asymmetric Information and Home Bias in FDI outflows;

Dependant variable is log (FDI outflows_{i,j,t}) which equals foreign direct investment flow from country i to country j at time t; The FDI outflows are from the FDI sending country towards the FDI receiving country. The explanatory variables are: Log of the GDP of the FDI receiving country; log of the GDP for the FDI sending country; trade openness (ratio of exports plus imports over GDP) for the FDI receiving country; trade openness (ratio of exports plus imports over GDP) for the FDI sending country; the log of the physical distance between the country i and j in kilometres; shared continent dummy (value of one if the two country i and j are one the same continent); shared border dummy (value of one if country i and j share a border); shared economic or political union dummy (value of one if country i and j share membership in the same economic or political union); same legal origin dummy (one if country i and j share the same origin of their legal systems); shared language (one if country i and j share the same official language or language of the minorities); shared history (one if country i and j share history with respect to having had a past colonial relationship or having been part of the same country); cultural distance index (based on Kogut and Singh (1988)); international telephone calls in minutes per capita for the FDI receiving country; financial times circulation per capita for the FDI outflows receiving country. The t-statistics are based on standard errors that have been adjusted for heteroskedasticity using the White (1980) method; Fixed effects used; Note that *, **, *** stand for significant coefficients at the 10%, 5% and 1% level respectively;

	(1)	(2)	(3)
	(Log)FDI Outflows	(Log)FDI Outflows	(Log)FDI Outflows
C	-8.39***	-8.56***	-8.71***
(Log) GDPrec	0.79***	0.81***	0.79***
(Log) GDP send	1.26***	1.28***	1.38***
Openness rec	0.32***	0.33***	0.24***
Openness send	0.64***	0.65***	0.68***
(Log) Distance	-0.60***	-0.62***	-0.69***
Same Continent	0.06***	0.08***	0.06**
Border	-0.01	-0.02	0
Shared Econ. Org.	0.14***	0.1***	0.03
Same Legal System	0.12***	0.13***	0.13***
Shared History	0.37***	0.37***	0.39***
Shared Language	0.36***	0.35***	0.32***
Cul. Dist. Index	-0.04***	-0.03***	-0.03***
L(Int. Phone Calls/capita)		0.02	
(FT/capita)			64.94***
N	16,792	13289	10991
Adj. R²	0.46	0.49	0.49

Table 9. Bilateral Tax Treaties and Home Bias in FDI outflows;

Dependant variable is log (FDI outflows i,j,t) which equals foreign direct investment flow from country i to country j at time t ; The FDI outflows are from the FDI sending country towards the FDI receiving country. The explanatory variables are: Log of the GDP of the FDI receiving country; log of the GDP for the FDI sending country; trade openness (ratio of exports plus imports over GDP) for the FDI receiving country; trade openness (ratio of exports plus imports over GDP) for the FDI sending country; the log of the physical distance between the country i and j in kilometres; shared continent dummy (value of one if the two country i and j are one the same continent); shared border dummy (value of one if country i and j share a border); shared economic or political union dummy (value of one if country i and j share membership in the same economic or political union); same legal origin dummy (one if country i and j share the same origin of their legal systems); shared language (one if country i and j share the same official language or language of the minorities); shared history (one if country i and j share history with respect to having had a past colonial relationship or having been part of the same country); cultural distance index (based on Kogut and Singh (1988)); bilateral tax treaties for double taxation avoidance. The t-statistics are based on standard errors that have been adjusted for cross-sectional heteroskedasticity using the White (1980) method; Fixed effects used; Note that *, **, *** stand for significant coefficients at the 10%, 5% and 1% level respectively;

	(1)	(2)
	(Log)FDI Outflows	(Log)FDI Outflows
C	-8.39***	-8.81***
(Log) GDPrec	0.79***	0.8***
(Log) GDP send	1.26***	1.21***
Openness rec	0.32***	0.36***
Openness send	0.64***	0.7***
(Log) Distance	-0.60***	-0.47***
Same Continent	0.06***	0.09***
Border	-0.01	-0.03
Shared Econ. Org.	0.14***	0.14***
Same Legal System	0.12***	0.13***
Shared History	0.37***	0.38***
Shared Language	0.36***	0.37***
Cul. Dist. Index	-0.04***	-0.04***
Bilat. tax treaties		0.14***
N	16,792	11118
Adj. R²	0.46	0.51

Table 10. Country Governance Factors and Home Bias in FDI outflows;

Dependant variable is log (FDI outflows_{i,j,t}) which equals foreign direct investment flow from country i to country j at time t; The FDI outflows are from the FDI sending country towards the FDI receiving country. The explanatory variables are: Log of the GDP of the FDI receiving country; log of the GDP for the FDI sending country; trade openness (ratio of exports plus imports over GDP) for the FDI receiving country; trade openness (ratio of exports plus imports over GDP) for the FDI sending country; the log of the physical distance between the country i and j in kilometres; shared continent dummy (value of one if the two country i and j are one the same continent); shared border dummy (value of one if country i and j share a border); shared economic or political union dummy (value of one if country i and j share membership in the same economic or political union); same legal origin dummy (one if country i and j share the same origin of their legal systems); shared language (one if country i and j share the same official language or language of the minorities); shared history (one if country i and j share history with respect to having had a past colonial relationship or having been part of the same country); cultural distance index (based on Kogut and Singh (1988)); voice and accountability index; political stability and absence of violence index; government effectiveness; regulatory quality; rule of law; control of corruption. The t-statistics are based on standard errors that have been adjusted for cross-sectional heteroskedasticity using the White (1980) method; Fixed effects used; Note that *, **, *** stand for significant coefficients at the 10%, 5% and 1% level respectively;

	(1)	(2)	(3)	(4)	(5)	(6)
	(Log)FDI Outflows	(Log)FDI Outflows	(Log)FDI Outflows	(Log)FDI Outflows	(Log)FDI Outflows	(Log)FDI Outflows
C	-8.61***	-8.48***	-8.49***	-8.43***	-8.49***	-8.43***
(Log) GDPrec	0.82***	0.82***	0.8***	0.79***	0.8***	0.79***
(Log) GDP send	1.36***	1.36***	1.36***	1.36***	1.36***	1.36***
Openness rec	0.3***	0.27***	0.29***	0.25***	0.29***	0.27***
Openness send	0.67***	0.67***	0.66***	0.67***	0.66***	0.67***
(Log) Distance	-0.75***	-0.75***	-0.74***	-0.75***	-0.74***	-0.74***
Same Continent	0.03	0.03	0.05*	0.04	0.05*	0.05
Border	-0.04	-0.05*	-0.03	-0.03	-0.03	-0.03
Shared Econ. Org.	-0.05	-0.01	0.05	-0.02	0.04	0.01
Same Legal System	0.14***	0.13***	0.12***	0.14***	0.12***	0.13***
Shared History	0.39***	0.38***	0.38***	0.38***	0.38***	0.39***
Shared Language	0.35***	0.38***	0.37***	0.35***	0.37***	0.36***
Cul. Dist. Index	-0.03***	-0.03***	-0.03***	-0.03***	-0.03***	-0.03***
Voice and Acc.	0.11***					
Polit. Stab.		0.08***				
Gov. Effect.			0.02*			
Regulat. Quality				0.1***		
Rule of Law					0.02***	
Control of Corr.						0.05***
N	10229	10229	10229	10229	10229	10229
Adj. R²	0.49	0.49	0.49	0.49	0.49	0.49