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Abstract:

With the rising elimination of trade and investment barriers the world over there has been a growing interest in the question of the role of differential environmental regulations in the location decisions of multinational enterprises (MNEs) and trade flows. A dominant hypothesis addressing this question is the pollution haven hypothesis (PHH) that purports that trade liberalization results in a relocation of dirty goods production to jurisdictions with lax environmental regulation. The PHH calls into question the efficacy of domestic environmental standards especially with respect to climate policy, because the location of emission of greenhouse gasses is irrelevant to the problem of climate change. More generally, the PHH is at the heart of the trade and environment debate. This paper examines whether UK's outbound investment flows (FDI) is influenced by the host countries' environmental regulations. We employ a general empirical model of the determination of FDI flows that captures interactions between country and industry characteristics in determining industry location. We use data on UK based multinational activity in 64 countries and 23 industries over the period between 2002 and 2006. We find a statistically and economically significant effect of environmental policy on the pattern of UK outbound FDI - a pollution haven effect.

Keywords:

pollution-haven, competitiveness, environmental-regulation, industry-location, FDI

JEL Classification: Q56, R11