CIT Rate and Tax Holiday as Tax Competition Tools to Attract Inward FDI in ASEAN-6

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Abstract

This study examines how tax competition, through statutory Corporate Income Tax (CIT) rates and tax holiday schemes, affects inward foreign direct investment (FDI) in the ASEAN-6 countries: Indonesia, Singapore, Malaysia, Thailand, the Philippines, and Vietnam. Using panel data from 2014 to 2023, the analysis employs a feasibility test, complemented by T-tests, F-tests, R² tests, path analysis, and hypothesis testing to assess the direct and indirect effects of tax competition instruments on FDI. The findings reveal that tax competition via the CIT rate significantly influences FDI in partial and simultaneous models. Conversely, tax holidays demonstrate a significant impact only when examined simultaneously, not individually. When both instruments are analyzed, they exert a statistically significant combined effect, with a total impact value of 0.472. These results suggest that while CIT reductions are more effective as standalone tools, the coordinated use of both CIT cuts and tax holidays can enhance the effectiveness of tax competition in attracting FDI. However, the effectiveness of such incentives depends on policy design and institutional readiness. Therefore, policymakers in ASEAN-6 are encouraged to adopt a multidimensional strategy that integrates well-targeted fiscal incentives with broader institutional and structural reforms to foster investor confidence and support a more resilient investment climate.

Keywords: foreign direct investment (FDI), corporate income tax (CIT) rate, tax holiday, international financial data.

1.   INTRODUCTION

The advancement of globalization, driven by rapid technological progress, has transformed the global economic landscape. One key feature of this transformation is the increased flow of foreign capital through investment, particularly Foreign Direct Investment (FDI). FDI is often associated with long-term contributions across management, technology transfer, joint ventures, and capacity-building

(Mahadiansar et al., 2021). It is widely considered as a positive outcome of globalization since it brings numerous benefits to host countries in the form of employment, knowledge transfer, and improved business practices (Damanhuri, 2008).

While global FDI inflows to developed countries declined by 12% to USD 1.3 trillion in 2022, the ASEAN region experienced a surge in inward FDI, reaching USD 229 billion, the highest figure recorded to date (ASEAN Secretariat, 2023). This sharp contrast illustrates ASEAN's growing appeal as a major investment destination, especially during the post-pandemic recovery. Figure 1 below illustrates the trends in inward FDI to ASEAN countries from 2014 to 2023.
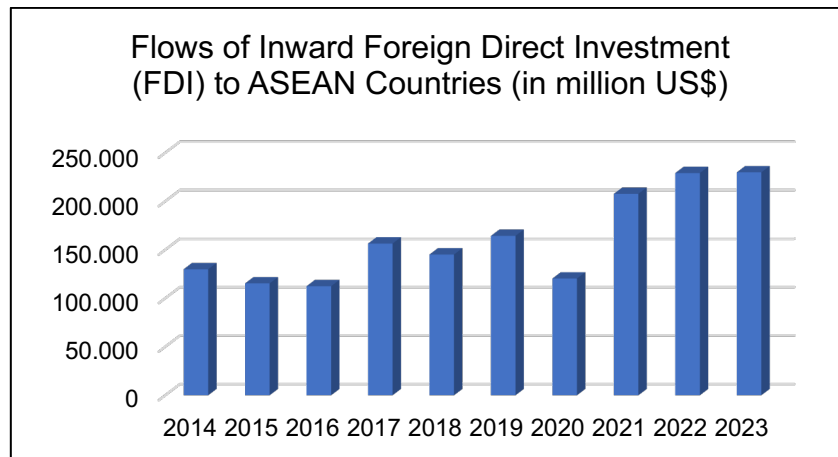

Figure 1. Flows of Inward FDI to ASEAN Countries

This study focuses on ASEAN-6, which comprises Indonesia, Singapore, Malaysia, Thailand, the Philippines, and Vietnam. These six countries are ASEAN's largest economies and the region's primary recipients of FDI. As shown in Figure 2, Singapore consistently ranks first, contributing over 60% of total ASEAN FDI, followed by Indonesia, Vietnam, the Philippines, Malaysia, and Thailand.
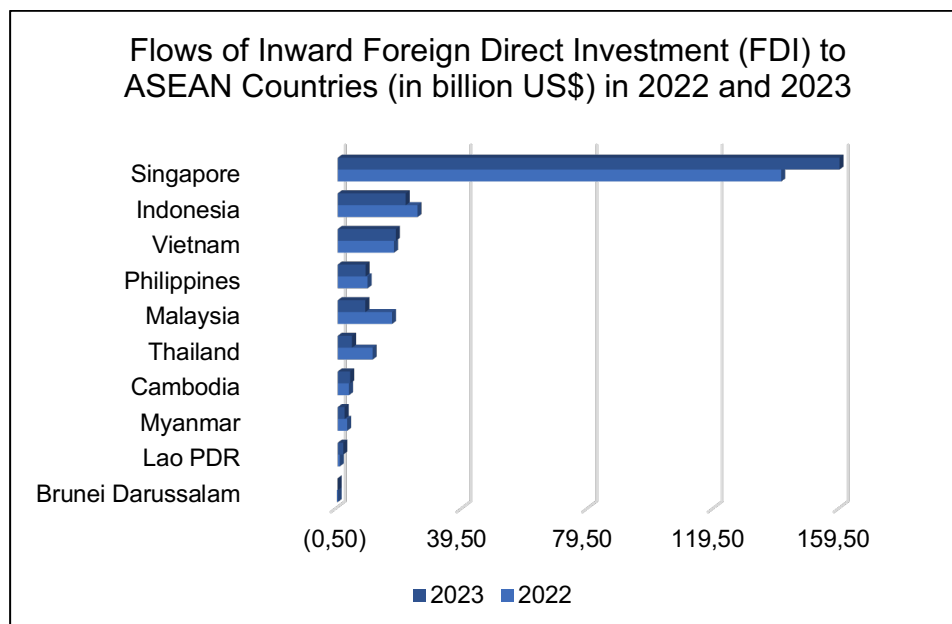

Figure 2. Comparison of Inward FDI to ASEAN Countries in 2022 and 2023

Various determinants, including economic fundamentals, institutional quality, and fiscal policy, influence variations in FDI inflows across countries. According to Kearney's 2019 FDI Confidence Index, factors such as "tax rate" and "ease of tax payment" were among the top considerations for investors when selecting host countries (Kearney, 2019). However, the 2024 edition highlights a notable shift in investor priorities, with "technological and innovation capabilities" emerging as the most critical determinant, reflecting the rising emphasis on digital readiness and innovation in global business (Kearney, 2024). Tax policy plays a pivotal role in shaping FDI decisions despite this shift, particularly in competitive regional markets such as ASEAN.

Tobing and Mukarromah (2015) argue that taxation constitutes a cost of business practice. Thus, the Corporate Income Tax (CIT) level and the availability of tax incentives, particularly tax holidays, are crucial for attracting foreign investors. These instruments are commonly employed by governments in the ASEAN-6 to promote investment, resulting in, what is widely known as, tax competition. Bella and Yudianto (2021), have found that lower CIT rates and generous tax holidays positively influence FDI inflows. However, other research, by Sunaryo and Nurhayati (2023), suggests that the relationship is statistically insignificant, indicating the need for further investigation.

Given these conflicting findings, this study analyzes how tax competition, operationalized through statutory CIT rates and tax holiday schemes, affects the inflow of FDI in ASEAN-6 countries from 2014 to 2023. Secondary data are collected from the ASEAN Stats Data Portal, the World Bank's World Development Indicators, KPMG, OECD, PwC, and other reputable sources. A panel data approach using multiple linear regression is applied to assess the impact of tax policy on FDI inflows. Hypothesis testing, model feasibility assessment, and path analysis are conducted to evaluate the independent variables' statistical significance and explanatory power through direct causal pathways and indirect effects mediated by intervening variables. Including mediating pathways that enable the identification of potential structural relationships between tax instruments and investment outcomes beyond linear associations.

Preliminary findings indicate that tax competition through reductions in statutory CIT rates tends to have a more consistent and statistically significant effect on attracting inward FDI than tax holidays. However, when both instruments are implemented in a coordinated and complementary manner, their combined effect enhances the overall effectiveness of tax competition strategies. These insights underscore the importance of crafting well-calibrated fiscal policies that boost investment attractiveness while preserving fiscal sustainability. Accordingly, this study aims to examine the effect of tax competition, through CIT rates and tax holiday schemes, on inward FDI in ASEAN-6 countries from 2014 to 2023. The findings are expected to inform regional policymakers in formulating integrated, data-driven tax policies that foster long-term economic growth.

2.   LITERATURE REVIEW

2.1. Foreign Direct Investment (FDI)

Numerous theoretical and empirical studies have sought to explain the nature, motivations, and determinants of Foreign Direct Investment (FDI), which is central to this research. FDI is a cross-border investment in which an investor from one economy acquires a lasting interest and significant influence over a business entity in another economy (OECD, 2014). It, typically, involves investors' active participation in the management and operations of the host enterprise, often through full ownership or equity participation in a joint venture (Ambarsari & Purnomo, 2005; Prawira et al., 2022). FDI is, thus, characterized by a long-term commitment by foreign entities to exert substantial control over productive activities in the host country (Mahadiansar et al., 2021).

Experts have developed various theories to construct a comprehensive conceptual framework for understanding FDI. Below are several key theories based on some experts:

1. Stephen Hymer's Theory (1960, published 1965) – Ownership Advantage Theory

    Hymer (1960) developed the theory known as the Ownership Advantage Theory. This theory is a pioneer in FDI studies, explaining why foreign companies from a source country invest abroad in a host country and emphasizing the importance of competitive advantages in international expansion.

2. Raymond Vernon's Theory (1966) – Product Life Cycle (PLC) Theory

    Vernon (1966) introduced the Product Life Cycle (PLC) theory, which explains FDI by suggesting that firms from developed countries invest in foreign markets based on the stages of a product's life cycle. As Rahajeng (2016) outlined, this model comprises three main stages: initial development and marketing in the home country, an export phase, and a standardization phase. In the final stage, as the product becomes more mature and cost efficiency becomes essential, firms often relocate production to countries with lower labor and production costs, thereby driving FDI

3. Peter Buckley and Mark Casson's Theory (1976) – Internalization Theory

    Buckley and Casson (1976) expanded Hymer's theory into the Internalization Theory, which explains why companies (source country) choose to internalize production activities abroad (host country). This theory suggests that companies may invest overseas in response to market imperfections. Through FDI, companies can internalize their operations, improve risk management, and maximize profits.

4. John H. Dunning's Theory (1977, 1981, 1988) – OLI (Ownership, Location, Internalization) Paradigm

    Dunning (1977, 1981, 1988) introduced the OLI Paradigm, also known as the Eclectic Paradigm, by offering a more holistic approach to explain the

factors influencing FDI. This theory explains that companies (source country) engage in FDI when there are additional advantages to gain by investing abroad (host country) after considering three main components: ownership (ownership advantages), location (location advantages), and internalization (internalization advantages).

5. Wilhelms and Witter's Theory (1998) – Institutional FDI Fitness Theory

Wilhelms and Witter (1998) emphasize that a host country's institutional quality, including government policies, market conditions, education systems, and socio-cultural factors, determines its attractiveness to foreign investors (Fachrulloh & Mawardi, 2018)

While these theories provide a strong conceptual foundation, some have limitations. For instance, the ownership advantage theory has been criticized for underestimating host country institutional factors, while the OLI model may overlook cultural and regional integration dynamics, particularly relevant in ASEAN.

FDI is central to development strategies by fostering capital accumulation, technology transfer, and job creation (OECD, 2022; UNCTAD, 2018). From the host country's perspective, it enhances competitiveness through productivity gains, while for source countries, it supports expansion into cost-effective markets (Khafidzin, 2021; Listikarini & Wijaya, 2023). In recent years, fiscal tools, particularly corporate tax rates and investment incentives have been increasingly recognized as key factors influencing FDI decisions (Xu & Wu, 2021). These elements form the foundation of what is commonly referred to as tax competition, which is further examined below.

2.2. Tax Competition

Building upon the foundational role of FDI in economic development, tax competition has become a key policy strategy, especially among emerging economies. Tax competition has been widely examined in theoretical and empirical studies, particularly its impact on foreign direct investment (FDI). It refers to the strategic behavior of governments in designing favorable tax regimes, primarily by reducing corporate income tax (CIT) rates or offering tax incentives, to stimulate economic activity and attract FDI. Bella and Yudianto (2021) describe tax competition as a fiscal tool to enhance business competitiveness and promote national welfare by lowering tax burdens to appeal foreign investors. Similarly, Tobing and Mukarromah (2015) suggest that tax competition not only attracts cross-border capital but also responds to tax policy changes in other jurisdictions, thereby mitigating potential spillover effects and preserving national economic interests.

The Standard Tax Competition Theory, pioneered by Zodrow and Mieszkowski (1986), conceptualizes this process by assuming that capital is highly mobile across borders while labor is relatively immobile. As a result, governments face a trade-off: setting high tax rates may drive capital outflows, while excessively low rates can lead to revenue shortfalls and underfunded public services. Wilson and Wildasin (2004) further argue that competition can push tax rates and public spending below optimal levels, harming long-term development goals.

In practice, tax competition has led to a global decline in statutory CIT rates (UNCTAD, 2022). However, this trend does not equally affect all countries. Xu and

Wu (2021) find that nations with better infrastructure and institutional frameworks benefit more from tax competition, while others may struggle to compete despite the offer of aggressive incentives. Moreover, modern tax competition strategies extend beyond simply cutting statutory CIT rates. Many countries now implement targeted incentives, such as tax holidays and geographic-based exemptions, to attract investment in priority sectors (Klemm & Liu, 2019; OECD, 2022).

In ASEAN-6, tax competition has intensified amid regional integration. Governments actively adjust their fiscal tools to attract general FDI and direct capital toward strategic industries and underdeveloped regions. Understanding how these instruments, CIT rates and tax holidays function in different national contexts is essential in evaluating their effectiveness and policy implications.

2.3. Corporate Income Tax (CIT) rate

Among various tax instruments, the statutory Corporate Income Tax (CIT) rate is one of the most visible and comparable tools in international tax competition. Host countries often reduce CIT rates to increase their attractiveness to multinational enterprises (MNEs), as lower tax burdens reduce the cost of capital and improve investment returns. Buckley and Casson (1976) suggest that competitive tax rates can incentivize firms to internalize production in low-tax jurisdictions. Dunning (1977b) also includes tax policy under location advantages in the OLI framework, affirming its relevance in FDI decisions.

Empirical evidence supports this perspective. Countries with relatively low CIT rates tend to receive higher FDI inflows, especially with macroeconomic stability and strong legal institutions (UNCTAD, 2022; World Investment Report 2022: International Tax Reforms and the Digital Economy, 2022). Furthermore, lower tax rates can provide financial flexibility for reinvestment and long-term expansion, particularly in capital-intensive industries. In the ASEAN context, variations in CIT rates across member countries reflect economic strategies and efforts to remain competitive.

2.4. Tax Holiday

A tax holiday is a time-bound exemption from corporate income tax granted to qualifying investments, often used by emerging economies to reduce the initial tax burden and attract FDI (UNCTAD, 2000). Within the OLI framework, tax holidays are part of location-specific advantages that make host countries more attractive to multinational enterprises (Dunning, 1988b).

In the ASEAN-6 context, tax holidays are among the most widely adopted fiscal incentives. They are particularly targeted toward capital-intensive or export-oriented sectors and are intended to complement broader tax competition strategies, including CIT rate reductions. Governments often utilize these incentives to stimulate early-stage investment and foster regional development.

However, the effectiveness of tax holidays is still debated. Empirical studies suggest that while they can boost short-term investment inflows, their economic significance is often lower than that of reductions in the CIT rate. For instance, Parys (2012) finds that tax holidays have only a modest effect on FDI decisions compared to broader statutory tax cuts. Overreliance on such incentives may also create fiscal

risks, especially in countries with limited revenue capacity or weak administrative oversight (Klemm & Liu, 2019)

The global tax environment is also undergoing a significant shift due to the implementation of Base Erosion and Profit Shifting (BEPS) 2.0, which introduces a 15% global minimum tax rate. In Indonesia. This is operationalized through a top-up tax imposed on multinational enterprises (MNEs) whose effective tax rate falls below the global threshold. According to the Directorate General of Taxes, this measure could neutralize the benefit of tax holidays for eligible MNEs, thereby reduce their attractiveness and raise concerns about their future role in tax competition (Fakultas Ilmu Administrasi Universitas Indonesia, 2023).

Given these developments, this study includes tax holidays as a core variable to evaluate their relative effectiveness in attracting inward FDI across ASEAN-6 countries within the evolving global tax framework compared to CIT rate adjustments.

3.   METHODOLOGY

This study aims to examine the extent to which tax competition, intervening through Corporate Income Tax (CIT) rates and tax holidays, affects Foreign Direct Investment (FDI) inflows in ASEAN-6 countries throughout the 2014–2023 period. A quantitative approach is employed by utilizing panel data collected from secondary sources, including the ASEAN Stats Data Portal, the World Bank's World Development Indicators (WDI), KPMG, OECD, PwC, and respective national authorities.

The data analysis process involves several stages. First, after data compilation, a classical assumption test is conducted, including normality tests, multicollinearity tests, heteroscedasticity tests, and autocorrelation tests, to ensure that the regression model meets the necessary assumptions. Subsequently, a model feasibility test is conducted through the regression coefficient test (t-test) for individual variable significance, the reliability test (F-test) for overall model validity, an evaluation of the path diagram based on F-test results, and the coefficient of determination (R^2) to assess the explanatory power of the model.

Afterwards, path analysis is used to estimate both direct and indirect effects of tax competition on FDI, mediated by CIT rate and tax holiday. Path analysis is particularly suitable when dealing with theoretical causal relationships, especially in the presence of multicollinearity or when parameters cannot be estimated simultaneously, as it allows a more robust interpretation than the standard regression models (Mishra & Min, 2010).

The final stage involves hypothesis testing, using the results of the coefficient of determination, t-tests, and F-tests to assess the statistical significance and explanatory strength of each variable pathway (Hutauruk et al., 2022).

All statistical procedures are conducted using IBM SPSS software, which supports both parametric and non-parametric comparisons, that allows diagnostic testing (e.g., normality and outlier detection), and provides efficient tools for frequency and regression analysis (Sarker et al., 2024). While AMOS or SmartPLS

may offer more advanced structural equation modeling (SEM) capabilities, SPSS is considered adequate for this study.

A conceptual representation of these relationships is presented in Figure 3 (Conceptual Framework), illustrating how tax competition may influence FDI directly or indirectly through the CIT rate and tax holiday as intervening variables.
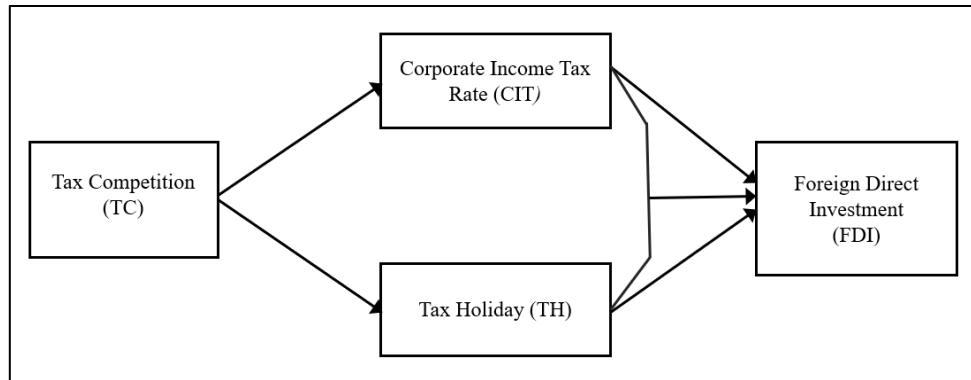

Figure 3. Conceptual Framework

3.1. Hypothesis

The hypotheses of this study are formulated as follows:

H_{01}: Tax competition through Corporate Income Tax (CIT) Rate does not significantly influence Foreign Direct Investment (FDI).

H_{a1}: Tax competition through the Corporate Income Tax (CIT) rate significantly influences Foreign Direct Investment (FDI)

H_{02}: Tax competition through tax holiday incentives does not significantly influence Foreign Direct Investment (FDI).

H_{a2}: Tax competition through tax holiday incentives significantly influences Foreign Direct Investment (FDI).

H_{03}: Tax competition through the CIT rate and/or tax holiday does not jointly have a significant influence on Foreign Direct Investment (FDI).

H_{a3}: Tax competition through the CIT rate and/or tax holiday jointly has a significant influence on Foreign Direct Investment (FDI).

3.2. Variable

This study uses three variables to understand and explain the relationships and interactions between the aspects of the research object. First is the exogenous variable (X) or independent variable. This variable is not influenced by other variables and is considered the starting point or input in the path analysis model. The exogenous variable in this study is tax competition. Second is the endogenous variable (Y) or dependent variable. This variable is influenced by other variables, either directly by the exogenous variable or indirectly through the intervening

variable. The endogenous variable in this study is Foreign Direct Investment (FDI). Third, the intervening variable (Z) or mediating variable. This variable explains the mechanism or process through which the exogenous variable affects the endogenous variable. The intervening variables in this study are the Corporate Income Tax (CIT) rate and the tax holiday. The definitions of each variable can be found in Table 1.

Table 1. Variable operational

Code	Desc.	Variable	Indicator	Scale	Source
FDI	Foreign Direct Investment	Y	Foreign direct investment, net inflows (% inward FDI to GDP)	Percentage	World Development Indicator (WDI) from World Bank DataBank and ASEAN Stats Data Portal from ASEAN Statistics Web Portal
TC	Tax Competition	X	Taxes on income, profits, and capital gains relative to total tax revenue (% taxes on income, profits, and capital gains to tax revenue)	Percentage	World Development Indicator (WDI) from World Bank DataBank and ASEAN Stats Data Portal from ASEAN Statistics Web Portal
CIT	Corporate Income Tax rate	Z_1	Statutory CIT rate of each country	Percentage	KPMG, OECD, and PwC
TH	Tax Holiday	Z_2	Tax holiday period (% longest tax holiday period in country X to longest period in ASEAN-6)	Percentage	KPMG, OECD, and PwC

Source: Processed by the author (2024).

3.3. Path Analysis

Path analysis assesses the causal relationships among variables and decomposes the direct and indirect effects of tax competition on Foreign Direct Investment (FDI). Hamid et al. (2019) explain that path analysis is used to measure the pattern of relationships that indicate the extent of the influence of several causal (exogenous) variables on the effect (endogenous) variable.

In this study, tax competition is hypothesized to influence FDI both directly and indirectly through two intervening variables: the statutory Corporate Income Tax (CIT) rate and tax holiday. The model structure is constructed based on the theoretical and empirical literature supporting the mediating roles of these tax policy instruments. The diagram in Figure 4 illustrates the conceptual path model used to test these relationships.
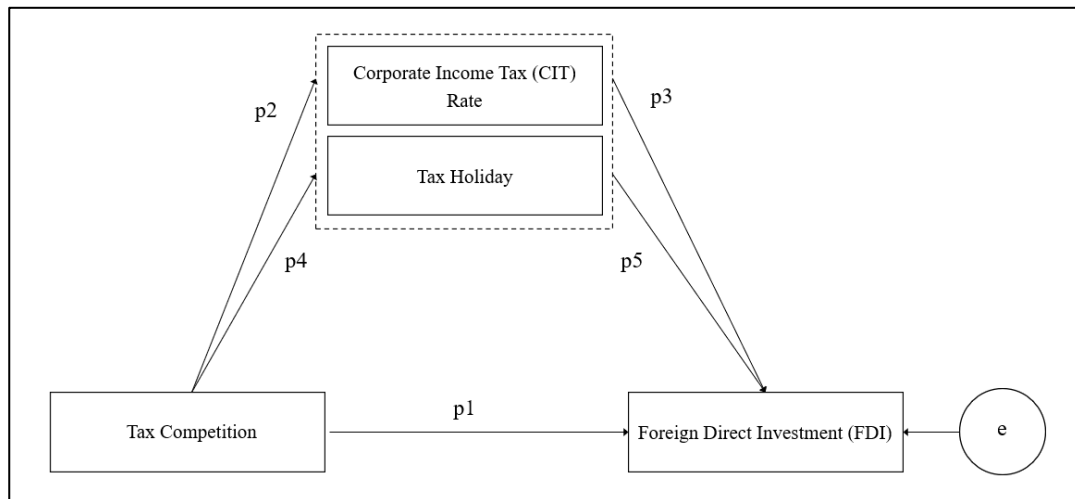
Figure 4. Path Analysis

Based on this model, the relationship between variables is based on the theory that tax competition directly impacts FDI (p1). Then, tax competition has an indirect effect through the CIT rate (p2) on FDI (p3). Tax competition also has an indirect impact through tax incentives (p4) on FDI (p5). Therefore, the total impact of each variable is as follows:

The direct effect of TC on FDI	= p1
The indirect effect of TC on CIT to FDI	= (p2xp3)
The indirect effect of TC on TH to FDI	= (p4xp5)
Total effect (correlation of TC to FDI)	= p1+(p2xp3)+(p4xp5)

Explanation:
FDI = Foreign Direct Investment
TC = Tax competition
CIT = Corporate Income Tax (CIT) rate
TH = Tax holiday

This analysis assumes linear relationships between variables, which is in line with classical path modeling principles. While the present model does not incorporate non-linear effects or moderating variables, future research may explore these dimensions to capture more complex interactions. Additionally, although the study emphasizes tax-related determinants, macroeconomic control variables, such as GDP growth, political stability, or infrastructure quality, are acknowledged as influential factors that can be incorporated into extended models for a more comprehensive understanding of FDI behavior.

4.   RESULT AND DISCUSSION

4.1. Descriptive Statistics

Table 2. Descriptive statistics

	N	Minimum	Maximum	Mean	Standard Deviation
FDI	60	- 0.9986	31.8351	6.597087	9.057104
TC	60	24.3936	70.9586	41.873758	12.5016918
CIT	60	17.00	30.00	22.40	3.8978
TH	60	25.00	100.00	53.25	22.3763

Source: Processed by the author using SPSS (2024).

The Foreign Direct Investment (FDI) variable reflects net inward FDI as a percentage of GDP. The mean FDI is 6.60% with a standard deviation of 9.06%, indicating substantial variation in FDI inflows across the ASEAN-6 countries. The minimum value is -0.99%, and the maximum is 31.84%, demonstrating wide fluctuations during the observation period.

The Tax Competition (TC) variable is represented by the share of taxes on income, profits, and capital gains relative to total tax revenue (percent). The mean is 41.87%, with a standard deviation of 12.50%. The minimum value recorded is 24.39%, and the maximum is 70.96%, indicating notable differences in reliance on income-based taxes among these countries.

The Corporate Income Tax (CIT) rate variable is measured by each country's statutory rate (percent). The average CIT rate is 22.40%, with a standard deviation of 3.90%, reflecting modest variability across ASEAN-6 countries. The rates range from 17.00% to 30.00%.

The Tax Holiday (TH) variable is expressed as the percentage of the most extended tax holiday period in a given country relative to the most extended period observed within ASEAN-6. The mean is 53.25%, with a standard deviation of 22.38%. Values range from 25.00% to 100.00%, illustrating substantial differences in tax holiday policies across countries.

4.2. Classic Assumption Test

The data used in this classical assumption test have been preprocessed through transformation to meet the analysis requirements. According to Ghozali (2018), data transformation is one technique to correct deviations from normality and other violations of classical assumptions. In this study, the natural logarithm (Ln) transformation is applied to stabilize variance and normalize the distribution of variables. This approach is also supported by J and Eric (2013), who highlight the effectiveness of logarithmic transformation in converting multiplicative patterns into additive ones, thereby improving model specification.

Table 3. Classic Assumption Test

Test	Model	Variable	Result	Decision	Conclusion
Normality test	Kolmogorov-Smirnov test	Z_1-X	Exact. Sig 0.256	0.256>0.05	Data is normally distributed

Test	Model	Variable	Result	Decision	Conclusion
		Z_2-X	Exact. Sig 0.170	0.170>0.05	
		Y	Exact. Sig 0.215	0.215>0.05	
Multicollinearity test	Tolerance and VIF test	Z_1-X	Tolerance 1.000 VIF 1.000	Tolerance 1.000>0.100 VIF 1.000<10.000	No multicollinearity symptoms
		Z_2-X	Tolerance 1.000 VIF 1.000	Tolerance 1.000>0.100 VIF 1.000<10.000	
		X-Y	Tolerance 0.771 VIF 1.297	Tolerance 0.771 >0.100 VIF 1.297<10.000	
		Z_1-Y	Tolerance 0.637 VIF 1.570	Tolerance 0.637 >0.100 VIF 1.570<10.000	
		Z_2-Y	Tolerance 0.743 VIF 1.345	Tolerance 0.743 >0.100 VIF 1.345<10.000	
Heteroscedasticity test	Glejser test	Z_1-X	0.805	0.805>0.05	No heteroscedasticity symptoms
		Z_2-X	0.570	0.570>0.05	
		X-Y	0.723	0.723>0.05	
		Z_1-Y	0.637	0.637>0.05	
		Z_2-Y	0.529	0.529>0.05	
Autocorrelation test		Z_1	1.807	dU (1.6518) < Durbin-Watson (1.807) < 4-dU (2.193)	No autocorrelation symptoms
		Z_2	1.694	dU (1.6518) < Durbin-Watson (1.694) < 4-dU (2.406)	
		Y	1.689	dU (1.4797) < Durbin-Watson (1.689) < 4-dU (2.255)	

Source: Processed by the author using SPSS (2024).

4.3. Model Feasibility Test

Table 4. Regression coefficient test (T-test)

Model	Variable (Code)	Independent Variable (Code)	Dependent Variable (Code)	Coef.	t Stat.	Sig.
1	TC – CIT – FDI	TC	FDI	0.278	2.856	0.006
		CIT	FDI	-0.646	-6.632	0.000
2	TC – TH – FDI	TC	FDI	0.338	2.496	0.015
		TH	FDI	0.077	0.565	0.575
3	TC – CIT & TH – FDI	TC	FDI	0.277	2.437	0.018
		CIT	FDI	-0.645	-5.783	0.000
		TH	FDI	0.003	0.028	0.978

Source: Processed by the author using SPSS (2025).

The t-test examines each independent variable's partial or direct effect on the dependent variable. The impact of Tax Competition (TC) on Foreign Direct

Investment (FDI) results in a t-statistic of 2.856, which indicates that this effect is significant (>1.96). Furthermore, the significance value (0.006) is smaller than the significance level (0.05), meaning there is a substantial effect of TC on FDI. The coefficient result of TC on FDI is 0.278, indicating a positive impact. Meanwhile, the effect of the CIT rate on FDI results in a t-statistic of -6.632, which shows that this effect is significant (<-1.96). The significance value (0.000) is smaller than the significance level (0.05), indicating a substantial impact of CIT on FDI. The coefficient of CIT on FDI is -0.646, indicating a negative effect. Therefore, reducing the CIT rate due to tax competition will increase inward FDI.

The effect of Tax Competition (TC) on Foreign Direct Investment (FDI) results in a t-statistic of 2.496, indicating that the effect is significant (>1.96). Furthermore, the significance value (0.015) is smaller than the significance level (0.05), indicating a substantial impact of TC on FDI. The coefficient result of TC on FDI is 0.338, indicating a positive impact. Meanwhile, the effect of Tax Holiday (TH) on FDI results in a t-statistic of 0.565, indicating that the effect is not significant (<1.96). The significance value (0.575) is greater than the significance level (0.05), indicating no significant impact of TH on FDI. The coefficient of TH on FDI is 0.077, indicating a positive impact. Therefore, the increase in tax holiday due to tax competition may enhance inward FDI, although it is not significant.

The effect of Tax Competition (TC) on Foreign Direct Investment (FDI) results in a t-statistic of 2.437, indicating that the effect is significant (>1.96). Furthermore, the significance value (0.018) is smaller than the significance level (0.05), indicating a substantial effect of TC on FDI. The coefficient result is 0.277, showing a positive effect of TC on FDI. Meanwhile, the effect of the CIT rate on FDI results in a t-statistic of -5.783, indicating that the effect is significant (<-1.96). The significance value (0.000) is smaller than the significance level (0.05), indicating a substantial effect of CIT on FDI. The coefficient is -0.645, indicating a negative effect of CIT rate on FDI. Additionally, the effect of the tax holiday (TH) on FDI results in a t-statistic of 0.028, indicating that the effect is not significant (<1.96). The significance value (0.978) is greater than the significance level (0.05), indicating no significant effect of TH on FDI. The coefficient is 0.003, showing a positive effect of TH on FDI. Therefore, reducing the CIT rate and increasing the tax holiday due to tax competition can enhance inward FDI in a country. However, the tax holiday policy is not significant.

Table 5. Reliability test (F-test)

Model	Independent Variable	Dependent Variable	Sig.
1	TC, CIT	FDI	0,000
2	TC, TH	FDI	0,013
3	TC, CIT, dan TH	FDI	0,000

Source: Processed by the author using SPSS (2024).

The F-test helps determine the influence of exogenous or independent variables (X) on endogenous or dependent variables (Y) through intervening variables (Z_1 and Z_2). Through CIT and/or TH, TC has a significance value smaller than the significance level (0.05). It indicates that tax competition, through CIT rate, tax holiday, or both, significantly affects inward FDI. The following path diagram, based on the F-Test, is presented to facilitate understanding of this study's indirect relationships among variables.
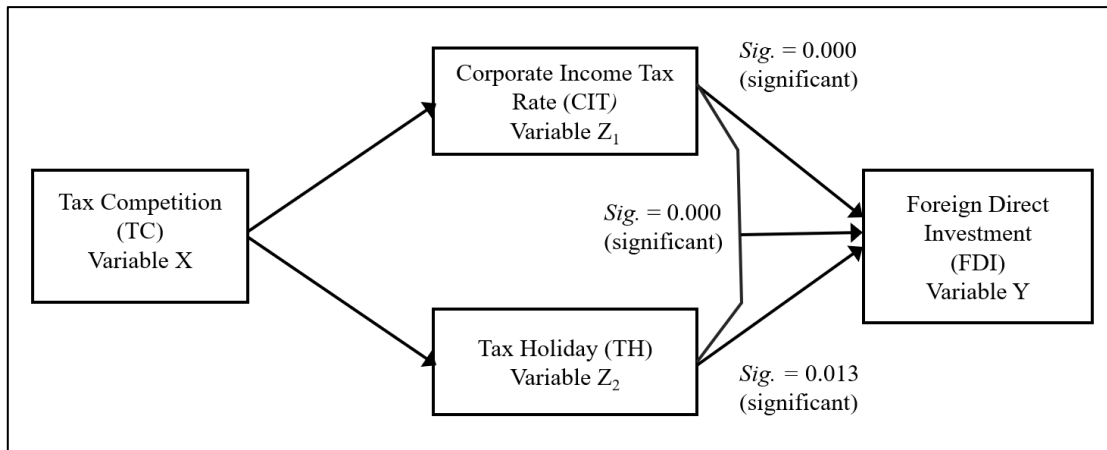
Figure 5. Path diagram based on F-test

Figure 5 illustrates that CIT, TH, or both simultaneously have a significant influence on FDI, indicating that CIT and TH can mediate the effect of TC on FDI. The dominant influence test can be identified through the total sum of coefficients. This total coefficient represents the overall effect of the exogenous variable in the model on the endogenous variable, both directly and through intervening variables. Below are the results of the indirect coefficient calculations:

$$p (X \rightarrow Z_1 \rightarrow Y) = -0.134$$

$$p (X \rightarrow Z_2 \rightarrow Y) = 0.002$$

The total coefficient is calculated as follows:

Table 6. Total coefficient

Model	Variable (Code)	Independent Variable (Code)	Intervening Variable (Code)	Dependent Variable (Code)	Direct Coef.	Indirect Coef.	Total Coef.
1	TC – CIT – FDI	TC	-	FDI	0.278	-	0.278
		TC	CIT	FDI	-0.646	-0.134	-0.780
2	TC – TH – FDI	TC	-	FDI	0.338	-	0.338
		TC	TH	FDI	0.077	0.053	0.130
3	TC – CIT dan TH – FDI	TC	-	FDI	0.277	-	0.277
		TC	CIT	FDI	-0.645	-0.134	-0.779
		TC	TH	FDI	0.003	0.002	0.005

Source: Processed by the author using SPSS (2024).

Based on the data in Table 6, the variable with the most dominant influence on FDI, regardless of the direction of the effect (positive or negative), is CIT, with a value of 0.780. It indicates that the CIT rate has the most significant impact on inward FDI.

Table 7. The coefficient of determination

Model	Variabel Independen	Variabel Dependen	Adjusted R Square
1	TC, CIT	FDI	0.444
2	TC, TH	FDI	0.112
3	TC, CIT, dan TH	FDI	0.434

Source: Processed by the author using SPSS (2024).

Based on the data in Table 7, the first model has a coefficient of determination of 0.444 or 44.4%, indicating that Tax Competition (TC) through the Corporate Income Tax (CIT) rate simultaneously contributes 44.4% to Foreign Direct Investment (FDI). In comparison, the remaining 55.6% is explained by other variables outside the scope of this study. The second model has a coefficient of determination of 0.112 or 11.2%, indicating that Tax Competition (TC) through Tax Holiday (TH) simultaneously contributes 11.2% to Foreign Direct Investment (FDI). In comparison, the remaining 88.8% is explained by other variables outside the scope of this study. The third model has a coefficient of determination of 0.434 or 43.4%, indicating that Tax Competition (TC) through the Corporate Income Tax (CIT) rate and Tax Holiday (TH) simultaneously contribute 43.4% to Foreign Direct Investment (FDI). In comparison, other variables outside the scope of this study explain the remaining 56.6%.

4.4. Path Analysis Test

Path analysis aims to measure the direct and indirect relationships among the variables and to understand how the independent variables influence the dependent variable, either directly or through intervening variables. The following are the results of the calculations and path analysis for this study:
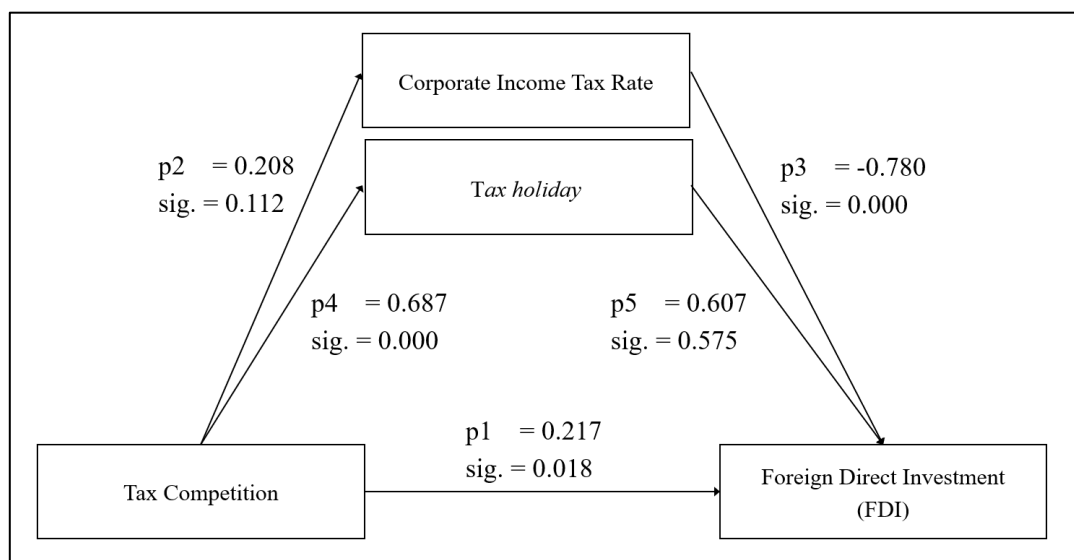

Figure 6. Path analysis

The total impact of each variable can be calculated as follows:

Direct effect of TC on FDI	= 0.217
Indirect effect of TC through CIT on FDI	= (0.208x(-0.780))
Indirect effect of TC through TH on FDI	= (0.687x0.607)
Total impact (correlation of TC to FDI)	= 0.472

Thus, the total impact of tax competition (TC) through corporate income tax rate (CIT) and tax holiday (TH) on inward Foreign Direct Investment (FDI) is 0.472. This figure indicates that tax competition substantially impacts foreign investors' decisions (source countries), although other factors largely influence it.

4.5. Hypothesis Test

The first hypothesis (H_{01}) examines whether tax competition through the Corporate Income Tax (CIT) rate has a significant influence on Foreign Direct Investment (FDI). The results show that the significance values for both the partial test (0.000) and the simultaneous test (0.000) are below the 0.05 threshold. These findings provide statistical evidence that tax competition through the CIT rate significantly influences FDI, both individually and jointly. Therefore, H_{01} is rejected, and H_{a1} is accepted.

The second hypothesis (H_{02}) assesses the influence of tax competition through tax holiday on FDI. The partial test yields a significance value of 0.575, which exceeds the 0.05 threshold, indicating no significant individual influence. Conversely, the simultaneous test produces a significance value of 0.013 below 0.05, indicating a significant joint influence. Thus, H_{02} is accepted, and H_{a2} is rejected for the partial test, but H_{02} is rejected, and H_{a2} is accepted for the simultaneous test.

The third hypothesis (H_{03}) evaluates the joint influence of tax competition through the CIT rate and tax holiday on FDI. The significant values for the partial tests are TC (0.018) and CIT (0.000) below the 0.05 threshold, indicating significant individual effects. In contrast, the TH variable shows a significance value of 0.978, which exceeds 0.05, suggesting no significant individual effect. The simultaneous test result is 0.000, indicating a significant joint influence. Therefore, for the partial test, H_{03} is accepted, and H_{a3} is rejected concerning the tax holiday variable. In contrast, H_{03} is rejected, and H_{a3} is accepted for the simultaneous effect of tax competition through the CIT rate and/or tax holiday on FDI.

4.6. Analysis of Research Results

ASEAN has emerged as a strategic foreign direct investment (FDI) hub due to its rapid economic growth, demographic advantages, and improving business climate. Dewi et al. (2023) highlight the region's increasing appeal to global investors. Dang and Nguyen (2021) attribute this attractiveness to ASEAN's dynamic and steady economic growth, while Khafidzin (2021) emphasizes the region's large population and low production costs as important location advantages. Similarly, Sunaryo and Nurhayati (2023) underscore ASEAN's access to vast markets, raw materials, services, and capital as key motivations for foreign investors seeking efficiency gains, market expansion, or portfolio diversification.

Since the 1990s, FDI inflows to ASEAN have grown substantially (Dang & Nguyen, 2021), cementing the region's role as a key investment destination. ASEAN has surpassed China as the top recipient of investment in the developing world for two consecutive years (ASEAN Secretariat, 2023). Mu`adzah and Sukarniati (2024) argue that this growth reflects investors' confidence in ASEAN's long-term prospects. Meanwhile, Irawan and Fachrezzy (2021) interpret it as a signal of strengthened economic performance across member states. Within ASEAN, the six largest economies, Singapore, Indonesia, Malaysia, Thailand, the Philippines, and Vietnam, account for the majority of inward FDI.

The following chart displays a comparison of the inward FDI (in million US$) in the ASEAN-6 countries from 2014 to 2023.
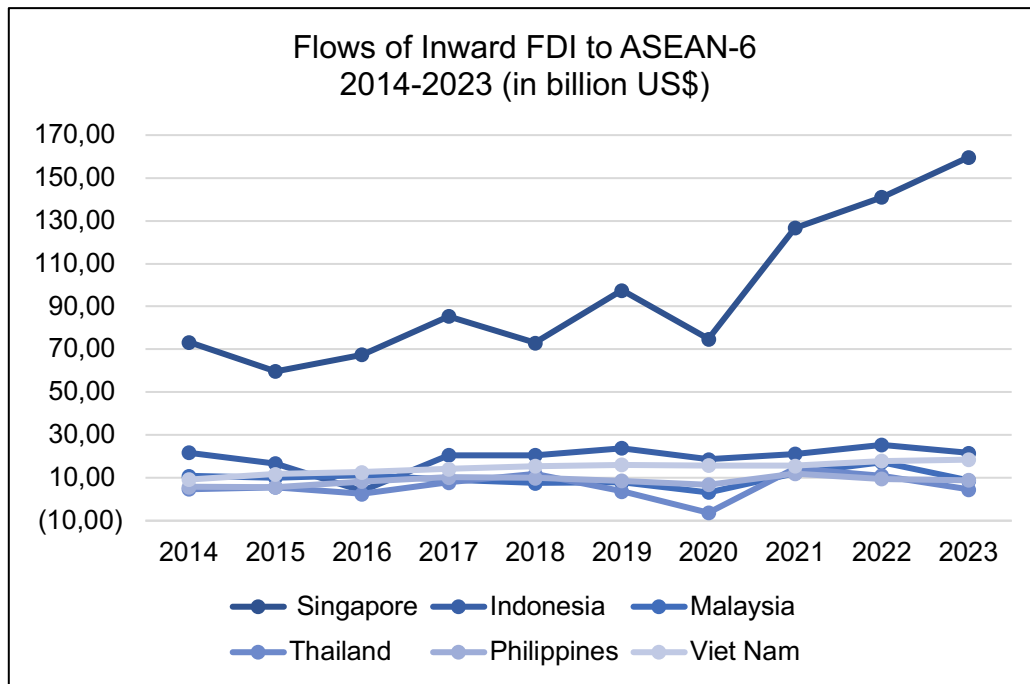
Figure 7. Flows of Inward FDI to ASEAN-6 in 2014-2023

Figure 7 displays the flows of inward FDI (in million USD) to ASEAN-6 from 2014 to 2023. It shows Singapore as the dominant recipient, followed by consistent growth in Indonesia and Vietnam. Malaysia and the Philippines have experienced moderate trends with some fluctuations, whereas Thailand has shown greater volatility, including sharp declines and quick recoveries.

The results of the path analysis indicate that tax competition, through the corporate income tax (CIT) rate and tax holiday policies, collectively explains 47.2% of the variation in inward FDI. It underscores the strategic importance of fiscal instruments in influencing capital inflows. These findings are consistent with the standard tax competition theory of Zodrow and Mieszkowski (1986), which builds on the Tiebout model by suggesting that jurisdictions compete for mobile capital by adjusting tax rates and incentives.

However, the differing explanatory power across models offers key insights. The CIT-only model yields a relatively high adjusted R² of 44.4%, suggesting that CIT rates alone significantly explain FDI variation. In contrast, the tax holiday model produces a low adjusted R² of 11.2%, indicating that tax holidays are relatively weak as standalone instruments. Meanwhile, the combined CIT and tax holiday model achieves an adjusted R² of 43.4%, which is slightly below the CIT-only model, suggesting possible overlaps and reaffirming the dominant role of CIT in influencing FDI. These patterns support Rahutami (2008) observation that structural heterogeneity in fiscal capacity, development levels, and institutional quality hinders ASEAN's integration efforts.

The hypothesis testing, further, clarifies these dynamics. The CIT rate has a significant negative correlation with FDI, implying that lower tax rates are associated with higher FDI inflows. This finding is aligned with standard models of tax competition. It reflects the classic "race to the bottom" phenomenon, as warned by Abbas and Klemm (2012, cited in Tobing & Mukarromah, 2015). However, such

aggressive competition can erode fiscal space and create long-term uncertainty. Babeth Ngoc Han Lefeur (in THE PRAKARSA, 2020) highlights how excessive tax competition in ASEAN, driven by repeated tax cuts and overlapping incentives, risks undermining public revenue, encouraging tax avoidance, and weakening regulatory capacity.

The second hypothesis suggests that tax holidays simultaneously affect FDI but have no significant partial effect. While tax holidays may enhance investment attractiveness when bundled with other policies, they are insufficient on their own. Investors prioritize a broader set of factors, such as macroeconomic stability, infrastructure, and ease of doing business (Nuryani et al., 2022; Sunaryo & Nurhayati, 2023). Nuryani et al. (2022), furthermore, argue that tax incentives must be supported by transparent rules and efficient implementation to reduce uncertainty and improve credibility.

The third hypothesis confirms that the simultaneous effect of CIT and tax holidays has a significant influence on FDI. However, only the CIT variable remains individually significant. It supports the idea that while combinations of tax policies may signal pro-investment orientation, their effectiveness depends heavily on complementary economic fundamentals. Studies by Shara et al. (2024) and Hossain et al. (2024) emphasize the importance of trade openness, macroeconomic growth, and streamlined regulations. Furthermore, Yusuf (2023) highlights that FDI can contribute to sustainable development, such as reducing deforestation, if accompanied by substantial budget allocations and good governance. These broader implications suggest that tax policy alone is not sufficient to ensure sustainable and inclusive investment growth.

These findings also resonate with the OLI Paradigm (Dunning, 1977a, 1981, 1988b), which classifies tax instruments as part of location-specific advantages that must be complemented by institutional and infrastructural supports. Dahliah et al. (2022), likewise, conclude that tax holidays and allowances, when implemented in isolation, are often ineffective due to the more decisive influence of labor productivity, market size, political stability, and interest rates on investor decisions.

Finally, tax competition must also be considered within the context of corporate governance and transparency. Natalia et al. (2021) argue that corporate governance mechanisms can strengthen the enforcement of tax policies and reduce tax avoidance. This insight reinforces the notion that governance quality plays a critical moderating role, ensuring that tax incentives are used as intended and that fiscal competition does not devolve into regulatory arbitrage.

All things considered, this study finds that tax competition through lower CIT rates significantly influences inward FDI, whereas tax holidays show a limited standalone impact. Policymakers across ASEAN need to avoid overreliance on tax incentives and, instead, pursue a coordinated fiscal strategy that integrates sound tax policy, strong governance, macroeconomic stability, and institutional reforms. Such a balanced approach will enhance competitiveness in attracting FDI and safeguard long-term fiscal sustainability and economic resilience.

5.   CONCLUSION

The flow of inward Foreign Direct Investment (FDI) in ASEAN-6 consistently places Singapore as the largest recipient, followed by Indonesia, Vietnam, Malaysia, the Philippines, and Thailand, based on the average inflows over the past decade (2014-2023). This study finds that tax competition through Corporate Income Tax (CIT) rate and tax holiday policies collectively accounts for 47.2% of the variation in inward FDI across ASEAN-6, underscoring the strategic role of fiscal instruments in shaping investment decisions. The analysis of three different intervening variable conditions leads to the following key conclusions:

1. Tax competition through the CIT rate significantly influences inward FDI in ASEAN-6, both partially and simultaneously. It confirms that reductions in the statutory CIT rate, driven by competitive pressures, are associated with increased inward FDI.

2. Tax competition through tax holiday incentives contributes to increases in inward FDI when considered simultaneously, but fails to show a statistically significant effect when evaluated partially. Tax holidays may help support FDI growth only when combined with other policy measures. Their standalone appeal is limited due to issues such as a lack of transparency, administrative complexity, or investor hesitation in the implementation.

3. When examined simultaneously, the combined implementation of CIT rate reductions and tax holiday policies contributes to an increase in inward FDI. However, similar to the previous finding, only the CIT rate shows a significant partial effect. It suggests that although tax holidays may enhance a country's overall attractiveness, their standalone influence remains relatively weak compared to CIT rate adjustments. The influence of a tax holiday remains relatively weak unless strong macroeconomic fundamentals and effective governance support it.

In summary, while both tax tools play a role in the broader strategy of attracting FDI, CIT rate reductions are more consistently impactful. Policymakers are, therefore, advised to design balanced and well-coordinated tax policies that prioritize effective CIT structures while ensuring that tax incentives such as holidays are complemented by strong governance, economic stability, and institutional clarity to maximize their effectiveness in attracting sustainable foreign investment.

5.1. Managerial Implication

The findings of this study suggest that tax competition through the Corporate Income Tax (CIT) rate has a statistically significant impact on inward Foreign Direct Investment (FDI) in the ASEAN-6. In contrast, tax holiday incentives fail to show significant effects when assessed individually. However, when considered simultaneously, both tax instruments collectively influence FDI. These results imply that statistical significance does not always translate into practical significance, especially when the effect is insignificant or context-dependent.

From a policy standpoint, this highlights two key implications. First, tax incentives such as CIT reductions may be more effective as part of a broader fiscal strategy. However, their implementation should be balanced with fiscal sustainability

to avoid undermining public service provision and long-term economic stability. Second, the limited individual effect of tax holidays underscores the need for caution when using them as standalone tools. They may still be helpful, but only when supported by complementary reforms.

More importantly, the results emphasize that fiscal incentives alone are insufficient to attract sustainable and high-quality FDI. To enhance their effectiveness, tax policies need to be integrated with institutional and structural reforms, including improvements in regulatory transparency, policy consistency, simplification of business licensing procedures, legal protection for investors, and improved governance in public finance administration. It aligns with existing literature that stresses the importance of infrastructure development, skilled labor availability, political and economic stability, and ease of doing business as key determinants of investor decisions.

Thus, policymakers in ASEAN-6 are encouraged to adopt a multidimensional approach: fiscal incentives should be well-targeted and efficiently administered while simultaneously investing in institutional capacity-building and structural reforms. This integrated strategy would strengthen investor confidence, improve the credibility of tax competition policies, and foster a more resilient investment climate.

5.2. Research Limitation

This study has several limitations. It focuses solely on the Corporate Income Tax (CIT) rate and tax holidays as indicators of tax competition without considering other factors that may influence Foreign Direct Investment (FDI), such as macroeconomic stability, workforce quality, infrastructure, or technological innovation policies. Additionally, the geographical scope of the study is limited to ASEAN-6 countries, meaning the findings may not fully reflect the dynamics present in other regions with differing economic characteristics. The data covers only the period from 2014 to 2023, which may not entirely capture long-term changes or structural trends in FDI flows.

5.3. Further Research

Future research can expand the current study by incorporating additional explanatory variables, such as ease of doing business, workforce quality, infrastructure availability, and technological innovation, to achieve a more comprehensive understanding of FDI determinants. Methodologically, future studies are encouraged to employ advanced panel data techniques such as Fixed Effects, Random Effects, or the Generalized Method of Moments (GMM) to address potential endogeneity or omitted variable bias and to improve the robustness of causal inference. Researchers may also enhance analytical depth by combining quantitative models with qualitative approaches, such as interviews, focus groups, or policy document analyses, to capture the contextual, political, and socio-cultural dimensions that influence tax policy and investment decisions. Moreover, extending the geographical coverage to developing regions beyond ASEAN, such as Africa, Europe, or Latin America, could support cross-regional comparisons and improve external validity. Conducting long-term studies that span broader economic cycles would also allow researchers to capture the delayed or compounding effects of tax competition and policy reforms. By integrating these methodological and thematic

enhancements, future research can provide more profound and more generalizable insights into the complex interplay between tax policy and foreign investment behavior.

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