Foreign Direct Investment and Growth:

A Study in the Context of Kuwait

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Abstract

Foreign Direct Investment is considered an encouraging impetus for economic development of an economy by enhancing competitiveness through offering employment, transferring sophisticated technologies, boosting productivity and promoting infrastructure, etc. In the recent times, the downtrend of oil prices has affected adversely the GDP of GCC regions as revenue from oil has been major source of inflow of funds for them. This economic turmoil has caused a serious concern among these countries and attracted immediate attention of the government and policy makers. This has led the members to focus on non-oil units in order to get revenues by promoting FDI, abolishing subsidies, proposal to impose tax, cost cutting and downsizing of employment especially in public sectors to accentuate the drivers of growth. Kuwait is not an exception to it. In the light of above mentioned facts, present study examines the role of FDI to the economic rise of Kuwait. Here, the trends of FDI and GDP in GCC have been explained in general; and for Kuwait, in particular. The statistical tools such as correlation, Analysis of Variance (ANOVA) and regression have been employed to glean the desired results. The result shows a positive relationship between FDI and GDP of Kuwait.

Keywords: FDI, GDP, economic growth, GCC, Kuwait

1. Introduction

The subject of Foreign Direct Investment and economic growth both theoretically and empirically has been well discussed by scholars in economic contexts. With the inception of endogenous growth theories, FDI has been considered among influential elements of economic growth in the long run (Barro, 1991; Barro & Sala-I-M, 1995). The substantial and promising surge in the flow of FDI which started during 90s has attracted many researchers for exhaustive research in this field.

In spite of the studies done in this research area, there seems to be a conflict in thoughts about the nexus between FDI and economic growth. There is a two-pronged direction of opinions. FDI is considered as an important determinant for strengthening local capital and low productivity in developing economies (De Mello, 1999; Eller, et. al, 2005). The flow of FDI is recognized as growth-driving stimulus in a host country. However, this thought has been challenged by other authors who opine differently. Some of them claim that there is no robust effect of FDI on economic maturation if other factors i.e. country wise differences, volume of FDI inflow and convergent impacts are taken into consideration (Carkovic & Levine, 2002).

It is not only the significance of FDI to growth which is of consequence, but growth also has been pinpointed as one of the most inspiring components out of various others. The rapid pace of development would bring more FDI by MNCs as they explore new ventures for business (Hansen and Rand, 2006).

Presently, FDI plays a vital role in country's capital formation in totality. It motivates the level of investment in a host country. FDI contributes a lot in creating employment opportunities and magnifies the level of income and savings that enhance economic prosperity. Further, FDI is deemed as a channel for transmitting knowledge and technology. The socio-economic issues in developing countries in the shape of unemployment, balance of payment deficit, foreign exchange and poor technological potential can be well addressed through the advent of FDI inflow.

According to IMF World Economic Outlook Report, Kuwait's economic growth reached 1.7% in 2015 before rising to 1.8% in 2016. However, in its World Economic Outlook released in October, the organization revised its forecast slightly downward to 1.2% in 2015, but an expectant growth of 2.5% might take place its following year in due course accordingly.

The slowdown is largely attributed to falling oil prices. Still, the government continues to benefit from relatively high financial buffers which are enabling increased public investment in infrastructure: a key factor to emerge as a strong support to non-oil growth in 2016, and beyond. The landmark of the country's economic blossoming ahead is associated with the release of regulations in December 2014 clarifying the Direct Investment Law 2013. The final step in the implementation of law contains attempts to trim the red tape and lengthy procedures to smoothen the process of licensing for business. Following this progress, the US tech giant IBM got license to set up a 100% foreign-owned Kuwaiti company. This has added to the approach of government attracting FDI which is already the source of paid dividends. Thus, researchers have found it quite a lucrative prospect to study or analyze the trend of GDP and FDI in Kuwait extracting and citing data from 2000 to 2014.

1.1 GDP Trends in GCC

GDP in GCC nations from the year 2000 to the year 2008 shows a flourishing trend. After that, the GDP tumbled down in 2009 due to economic slump and recession. A strangely unexpected trend surfaced into picture during the post-recession period of 2010 to 2015.

Table 1. Trends of GDP in GCC

Year	GDP Growth in %
2010	6.4%
2011	7.7%
2012	5.4%
2013	3.6%
2014	3.6%
2015	3.4%
2016 (projected)	3.2% (projected)

Source: IMF Report 2015

GDP growth trend shows a clear fall in the GCC nations from 2010 to 2016. The GDP growth (%) witnessed an increase from 6.4% in 2010 to 7.7% in 2011. There was a sharp decline in the GDP from 7.7% in 2011 to 5.4% in 2012. Its downward flow continued further from that 5.4% in 2012 to 3.6% in 2013. The year is increasing and the growth rate is on constant descent. It is here for a year 2013 to 2014 that we see a static 3.6% GDP. From 3.6% of 2014 it fell farther to 3.4% in 2015. The prediction for 2016 as per last recordings of GDP is expected to go down by 3.2% in the current year 2016.

We therefore, see that the GCC economy is going through a crucial phase of crisis as continuous deterioration in the oil price is evidenced as the main reason for its crash of GDP graph. It is a known fact that the GCC members are chiefly dependent on their oil revenues which is being one of the major determinants of inflow of funds in them. Hence, the diminishing oil price awakened an alarming concern for the GCC member nations who have taken prudent step to create non-oil revenue sources for obtaining more and more funds i.e. abolishing subsidies, proposing to impose tax, pushing forth FDI, cost cutting, reducing public sector employments, etc in order to propel the growth drivers.

1.2 FDI Trends in GCC

Foreign Direct Investment (FDI) in GCC countries has worked as a vital source for development of infrastructure, job creation, diversification of revenue and investment in new enterprises beside adding strength to the local economy. According to the World Bank Report (2005), there are only few countries in the world which have manifested prosperous growth in their economies without being involved in trading activities. The inflow of FDI in GCC countries witnessed a positive development from the year 2000 to 2008. Larger share of the FDI was mostly attracted by three major economies of GCC i.e. Saudi Arabia, UAE and Kuwait.

Table 2. Trends of FDI in GCC

Year	FDI inflow (US$ Billions)
2009	51.4
2010	42.1
2011	29.8
2012	27.0
2013	22.6
2014	21.7

Source: UNCTAD 2015, World Investment Repor

However, there has been change in the inflow trend and it started sinking from the year 2009. GCC counties awakened to the fact that FDI is not only a salient source of inflow of long term funds into any country, but also it is significantly responsible for the economic stability of a country. FDI inflows displayed a downward trend in GCC countries as the inflow decreased to 42.1 US$ Billions in 2010 compared to 51.4 US$ Billions in 2009. This sort of financial collapse continued from 2010 to 2011 where FDI inflow got slashed to 29.8 US$ Billions. The FDI inflow reached to 27.0 US$ Billions in 2012 and it further got reduced into 22.6 US$ Billions in the year 2013. Despite a number of initiatives taken by the GCC countries to open up the GCC market for foreign investors, the FDI in GCC countries still saw a decline from 22.6 US$ Billions in 2013 to 21.7 US$ Billions in the year 2014.

1.3 Trends of GDP in Kuwait

Kuwait's GDP growth too, follows a sinking trend in the map of GCC economies during the early phase of the year 2000. The FDI flow was positive in Kuwait from 2011 to 2012.

Table 3. Trends of GDP in Kuwait

Year	GDP Growth in %
2011	6.3%
2012	6.6%
2013	1.5%
2014	1.3%
2015	1.7%

Source: IMF Report 2015

The GDP in Kuwait declined to 1.5% percent in the year 2013 from 6.6% of its previous year 2012. It further cascaded to 1.3% in the year 2014 compared to 1.5% of the year 2013. GDP growth rates are predicted to remain unresponsive in near future due to slump in oil price and other economic factors.

1.4 Trends of FDI in Kuwait

Table 4. Trends of FDI in Kuwait

Year	Share of World FDI	Foreign Direct Investment, percent of GDP
2000	0.002	0.04
2001	-0.015	-0.32
2002	NA	0.01
2003	-0.012	-0.14
2004	0.003	0.04
2005	0.015	0.29
2006	0.006	0.12

2007	0.004	0.1
2008	NA	NA
2009	0.086	1.05
2010	0.075	1.13
2011	0.149	2.12
2012	0.153	1.65
2013	0.074	0.82
2014	0.032	0.3

The Foreign Direct Investment trends in Kuwait from year 2000 to year 2014 depict a rollercoaster ride (Kuwait's FDI in share of world FDI and FDI in Kuwait as a percent of GDP of Kuwait). In the year 2001 to 2003, Kuwait's FDI compared to its share of world FDI was negative (as Kuwait invested more funds in other countries and received less investment from other countries as FDI). The FDI inflow started to gain momentum and became positive in the year 2004 and 2005. The FDI percent went down (re-elects a decreasing trend) in the year 2006 and 2007. It fell from 0.086 percent in the year 2009 to 0.075 percent in the year 2010. Again it got momentum in the year 2011 and 2012 when the data shows that FDI share of Kuwait increased from 0.149 percent to 0.153 percent. It demonstrated a decreasing trend when Kuwait's FDI share in the world FDI toppled down from 0.074 in the year 2013 to 0.032 percent in the year 2014. Kuwait's FDI as a percent of GDP illustrates the trend similar to the trend of Kuwait's FDI share in world FDI. Kuwait replaced its old FDI law of 2001 in the year 2013 which came into force in December 2014. Efforts were made by Kuwaiti government like giving tax holidays, 100% ownership by foreign investors to streamline the FDI approval process and to attract more FDI.

2. Review of Literature

Multinational enterprises are defined as giant companies with impressive control or market power replacing international trade with international production. The elements of Foreign Direct Investment have been classified into three types— International Capital Market Theory, Theory of International Trade and Theory of Firm (Vasyechoko, 2012). The inference has been drawn from the research that FDI is a channel for the transfer of know-how and technology to the developing economies (Balasubramanyam &Vidya Mahambre, 2003). It is concluded from a study that flow of FDI into different sectors of the economy such as primary, secondary and tertiary, foster economic growth (Laura Alfaro, 2003). A study conducted into Indian context explains that Foreign Direct Investment in post-reformed India is largely supposed to boost economic growth in the country (Chandana C. & Peter N., 2008). GDP per capita positively contributes to FDI inflows in the long run (Chew Ging Lee, 2009). Flow of FDI helps in filling the gap between anticipated investments and domestically mobilized saving (Todaro & Smith, 2003, Hayami, 2001). Further, FDI may provide strength to the country to come out of vicious cycle of underdevelopment (Hayami, 2001). The investigation on the impact of FDI via technology spillovers on the total productivity for the nations like Oman, Morocco, Saudi Arabia, Jordan, Egypt and Tunisia taking the data of 20 years concludes that FDI does not pose the positive spillovers on technology and productivity in comparison with other forms of capital formation (Sadik & Bolbol 2001). The contribution of FDI to the economic growth is severely affected by economic and social conditions in the beneficiary country also (Buckley et. al, 2002). A study across 69 nations taking into consideration the measures of FDI and other factors of economic maturation during 1975-2000, found that the relationship between GDP and FDI is moulded by the factors like financial market development, human capital endowment, trade openness and endowment of natural resources (Beatrice Farkas, 2012). Qaiser (2011) examines the effect of FDI on growth (GDP) of the SAARC countries. The result shows a positive and significant relationship between GDP and FDI and an insignificant relationship between GDP and inflation. Umeora (2013) investigated the impact of FDI on different chosen macroeconomic variables— GDP, inflation, Exchange Rate, etc. It was found that FDI affects GDP, Exchange Rate and inflation by 46.5%. Thus, FDI does cause the GDP to grow, raises inflation and affects Exchange Rate negatively.

3. Objectives of the Study

The present study is based on the following objectives:

- To study the trends of FDI and GDP in Kuwait.
- To investigate if there is any impact of FDI on GDP of Kuwait.

4. Hypotheses of the Study

In order to obtain the desired outcomes from the study, the following hypotheses have been proposed:

H$_0$:   There is no significant correlation between GDP and FDI.

H$_1$:   There is significant correlation between GDP and FDI.

5. Methodlogy

5.1 Research Design

The quantitative technique of research has been employed by the scholars in the present study. A quantitative research displays assessing the connection between variables using different statistical tools for given descriptive data analysis and framing proposed hypotheses (Creswell, 2008).

5.2 Sources of Data

The scholars have used the secondary data for the present study. The data has been collected from various sources such as IMF Report, UNCTAD World Investment Report, Global Economy Report, World Bank Report, Mundi Index Report, etc.

5.3 Research Tools

For the desired outcomes and analyzing data, scholars have applied different statistical tools such as correlation & ANOVA and regression analysis using SPSS (Version 19).

6. Empirical Results and Discussion

- **CONTRIBUTION OF FDI TO GDP OF KUWAIT**

Table 5. Correlation analysis

		GDP	FDI
Pearson Correlation	GDP	1.000	.566
	FDI	.566	1.000
Sig. (1-tailed)	GDP	.	.014
	FDI	.014	.
N	GDP	15	15
	FDI	15	15

The above correlation Table 5 shows that the correlation between GDP and FDI is 0.566 which is a moderately positive correlation between these two variables and gives an indication that we can reject the H0 (null hypothesis) taken in this research. The p value in the correlation is 0.014 which is below 0.05 that results in its being statistically significant. This p value (0.014) suggests us to reject H0 as p ≤ 0.05. "N" shows the number of pairs in the sample which is 15 in this case. It is found in the above analysis that correlation coefficients for GDP and FDI result in positive values leading to a true relationship which indicate that increase in one variable (GDP) corresponds to increase in the other variable (FDI); and the vice-versa.

Table 6. Model summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	R Square Change	F Change	df1	df2	Sig. F Change	Durbin-Watson
1	.566[a]	.320	.268	14.36360	.320	6.127	1	13	.028	.359

a. Predictors: (Constant), FDI
b. Dependent Variable: GDP

The above Model Summary table 6 provides information about the changes in variable scores. The R value represents the simple correlation which is 0.566 (the "R" Column). It indicates a high degree of correlation. The R2 value (the "R Square" column) indicates how much of the total variation in the dependent variable (GDP) is due to the independent variable (FDI). The correlation coefficient (r) is 0.566 and the coefficient of determination (r2) is 0.320 in the Model Summary indicate a positive strength of the linear trend between GDP and FDI when the Standard Error is 14.36360.

Table 7. ANOVA

	Model	Sum of Squares	df	Mean Square	F	Sig.
1	Regression	1264.167	1	1264.167	6.127	.028[a]
	Residual	2682.071	13	206.313		
	Total	3946.237	14			

a. Predictors: (Constant), FDI
b. Dependent Variable: GDP

The Sum of Squares column gives the sum of squares for each of the estimates of variance where in this case Regression is 1264.167 and Residual is 2682.071. The total shows 1264.167+2682.071= 3946.237 and the Sum of Squares corresponds to the numerator of the variance ratio. The third column displays the degrees of freedom for each estimate of variance which is 14 – 13= 1. The fourth column manifests the estimates of variance (the mean squares 1264.167 / 1= 1264.167 and 2682.071/ 13 = 206.313). F ratio is reflected in the fifth column which is calculated by dividing mean square between-groups by mean square within-groups (1264.167 / 206.313= 6.127). The exact significance level is .028 as marked in the above ANOVA table 7. The sig value is less than (α) alpha 0.05, hence the results are statistically significant depicting that null hypothesis would be rejected and alternate hypothesis would be accepted.

Table 8. Coefficients (Regression analysis)

	Model	Unstandardized Coefficients		Standardized Coefficients	T	Sig.
		B	Std. Error	Beta		
1	(Constant)	75.550	4.497		16.799	.000
	FDI	8.770	3.543	.566	2.475	.028

a. Dependent Variable: GDP

Coefficients table 8 shows that the Constant value (75.550) together with FDI values (8.770) and the p-value (0.028) is applied to check their significance. We reject Ho if p≤ .05. In our case also, the p value (0.028) is less than 0.05. This supports the relationship which is reliable and can be used to make predictions. In this case, our regression equation [y'= bx + a] becomes y = 8.770 (x) + 75.550. The same p value you see on the correlation matrix for these two variables.

7. Conclusion

The result of the present study indicates a significant and positive relationship between Foreign Direct Investments and the GDP in Kuwait resulting into a positive contribution to the economic flourishing of the country. Along the years, the FDI inflows have underwent constant ebb and flow sort of trends, albeit FDI influx recorded as USD 2.3 billion in 2013. The Foreign Direct Investment trends in Kuwait from year 2000 to year 2014 depict a rollercoaster ride (Kuwait's FDI in share of world FDI and FDI in Kuwait as a percent of GDP of Kuwait). During the years 2001 to 2003, Kuwait's FDI compared to its share of world FDI was negative (as Kuwait invested more funds in other countries and received less investment from other nations as FDI). In the beginning of 2003, a new law for FDI was commenced allowing foreign investors 100% ownership in a number of sectors in Kuwait. This law also provided tax relaxation and other benefits to new investors who in turn were to ensure the reservations in employment to the nationals of Kuwait.

The FDI inflow started to gain momentum and became manifold in the years 2004 and 2005. The percentage of FDI shrank (re-elects a decreasing trend) during the years 2006 and 2007. It fell from 0.086 percent in the year 2009 to

0.075 percent in the year 2010. It gained pace again in the years 2011 and 2012 when the data shows that FDI share of Kuwait increased from 0.149 percent to 0.153 percent. Further, it demonstrated a decreasing trend when Kuwait's FDI share in the world FDI went down from 0.074 in the year 2013 to 0.032 percent in the year 2014. Kuwait's FDI as a percentage of GDP illustrates the trend similar to the trend of Kuwait's FDI share in world FDI. Kuwait replaced its old FDI law of 2001 in the year 2013 which came into force in December 2014. The government made another Foreign Investment Law enacted in 2013 and implemented in 2015 along with a series of laws governing business to encourage the joint venture of private and public sectors. Through the 2015-2020 National Development Plan, the government tends to make cautious efforts to allure more of FDIs in order to develop the infrastructure of the country.

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