PalArch's Journal of Archaeology of Egypt / Egyptology

THE IMPACT OF FOREGIN DIRECT INVESTMENT IN EMERGING MARKETS

Mawadah Lutfi Felemban[1], *Rozina Shaheen*[2]

[1,2] Effat College of Business, Effat University Qasr Khuzam St.,Kilo. 2, Old Mecca Road.

P.O.BOX 34689 Jeddah 21478 Saudi Arabia

Email: [1]mlflemban@effat.edu.sa, [2]roshaheen@effatuniversity.edu.sa

Mawadah Lutfi Felemban, Rozina Shaheen. The Impact of Foregin Direct Investment in Emerging Markets -- Palarch's Journal of Archaeology of Egypt/Egyptology 18(13), 1170-1181. ISSN 1567-214x

Keywords: Investment, Foreign Direct Investments, Stock Market, Finance, Saudi Arabia

ABSTRACT

Foreign direct investment (FDI) has become an important source of funding for emerging countries as a result of effective economic reflection. This study examined the impact of FDI on emerging markets. The impact of FDI in emerging markets is different from country to country depending on the factors of each country. In this study, sample data from year 1991-2018 for 7 emerging countries was used to estimate the statistical significance of the relation between the FDI and GDP the economic growth. The seven countries are Saudi Arabia, Brazil, China, Egypt, India, Australia, and Kenya. In this work, the analysis was done based on five variables, which are gross domestic product (GDP), are foreign direct investment (FDI), labor force (LF), trade openness (TO) and employment. The data used for this work was attained from World Bank. The results of the study have shown that FDI does not have a significant impact on some emerging countries. Moreover, the result of having insignificant effects for Saudi Arabia is due to being new to the involvement of FDI.

CCS Concepts

• Information systems→Database management system engines • Computing methodologies→Massively parallel and high-performance simulations.

INTRODUCTION

Foreign direct investment has played a role in the world economy since the 1990s and many investors have moved to emerging markets as a result of effective returns [1]. In addition, foreign direct investment (FDI) has a significant potential for transforming economies through innovation, creating better-paying and more stable jobs in host countries, and increasing productivity [2]. Importantly, foreign investors are becoming increasingly prominent players in delivering global public goods, improving working conditions, setting global industry standards, and delivering infrastructure to local communities [3].

Emerging markets (EMs) are when the country becomes a developed nation and its economy progresses to become more advanced [4]. Emerging economies and their governments want to boost their standards of living and bring dramatic improvements to a more developed society [4]. In addition, these countries are willing to grow rapidly and adopt a capitalist economy or a mixed economy that is crucial to global economic growth [5]. In contrast, the emerging market does not have stricter regulations of performance, as advanced countries such as the United States and Europe do [5]. This is the reason on why some investors are trying to invest in EMs. In addition, investments in emerging markets will, however, be at high risk due to economic instability, but some investors are looking to invest in EM due to high returns [6].

Foreign direct investment (FDI) is a kind of global venture carried out by a firm or an individual in a business intrigue situated in another state [7]. It also means that when one company owns a business in another state, the company not only contributes money but also participates in a business operation [7]. Thus, the key to FDI is the element of control. FDI decisions to invest or move abroad in host countries may have many impacts that may affect or change the aspect of doing business in foreign countries [8]. The economies of host countries and the financial, legal and natural conditions of developing countries are considerations that may influence or draw FDI decisions. Furthermore, FDI was used by developed economies to enter developing markets for competitive advantages [9].

The potential effects of foreign direct investment on emerging markets have been studied in different contexts and in different natures in various previous studies. Ayyagari et al. [10] examined the involvement of FDI in emerging markets and found that in order to maximize profits from FDI, local companies must take economic strategic choices. Kayalvizhi and Thenmozhi [11] scrutinized the factors that drive FDI in emerging markets and found that technology, corporate governance and culture to be a significant factor in magnetizing FDI flows in emerging markets. Wang et al. [12] analyzed the role of government commitment in FDI in emerging markets and found that government engrossment impacts the level of foreign investment. Park et al. [13] analyzed the impact of FDI on the supermarket industry in emerging markets and found that FDI has created more job opportunities for local community, which has benefited economic development. Piperopoulos et al. [14] examined the impact of outward FDI on emerging markets and found that this type of FDI improves the innovation aspects of the emerging markets. Cai et al. [15] assessed the determinants of FDI in emerging economies in terms of sovereign credit ratings, and found that developing business sector beneficiaries with a more grounded institutional status can draw more FDI from other developing markets.

The impact of FDI on economic growth is linked to the level of economic development. In addition, the link between FDI and subsequent growth varies considerably when host economies are categorized according to local host country characteristics such as gross domestic product (GDP), trade openness, labor force, employment and education. Thus, this work was done to examine the impact of foreign direct investment in emerging markets in terms of economic growth for the mentions GDP, trade openness, labor force, and employment.

METHODOLOGY

This study was conducted based on quantitative research method. This study has used quantitative data sample for 7 emerging countries. The countries are chosen random, which are Saudi Arabia, Brazil, China, Egypt, India, Australia, and Kenya. The analysis was done based on five variables, which are gross domestic product (GDP), are foreign direct investment (FDI), labor force (LF), trade openness (TO) and employment. GDP represents the economic growth of the country and it is used as dependent variable. The independent variables are foreign direct investment (FDI), labor force (LF), trade openness (TO) that calculated as the sum of import and export as a percentage of GDP, and employment, which will be affecting in the economic growth. The period of data is from 1991-2018. The source of data is from the World Bank. The aim of the research is to find if the FDI have significant effects on the economic growth of the emerging country. The analysis provides the estimated statistical significance of the relation between the variables and GDP in terms of the economic growth of the emerging countries. In this work, Equation 1 was used for the analysis and is shown as follow:

$$GDP_{it} = \beta_0 + \beta_1 FDI_{it} + \beta_2 TO_{it} + \beta_3 LF_{it} + \beta_4 Emplo_{it} \quad (1)$$

Where i for country and t for year. GDP is for growth rate, FDI is the inflow rate of foreign direct investment, TO is trade openness and it is the sum of import and export as % of GDP, LF is the rate of labor force, and Emplo is the rate of employment.

RESULT AND DISCUSSION

Analysis

The respondents were Table 1 shows the analysis for Saudi Arabia. Based on Table 1, FDI has a negligible impact since Saudi Arabia has recently begun to open up to foreign investment since before, they were dependent on and foxing on oil exports. Also, labor force has insignificant affect. However, the trade openness (TO) is significant in Saudi economic growth and it has the highest affect. Employment is also a significant variable that affecting in economic growth.

Table 1. Analysis for Saudi Arabia

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	182.3438	126.0285	1.446846	0.1614
FDI	-0.740352	0.423673	-1.747458	0.0939
TO	0.228680	0.103555	2.208303	0.0375
LF	-0.265238	0.339800	-0.780571	0.4430
Employment	-1.915742	1.227204	-1.561062	0.1322
R-squared		0.343804	Mean dependent var	3.267049
Adjusted R-squared		0.229683	S.D. dependent var	4.294598
S.E. of regression		3.769270	Akaike info criterion	5.652072
Sum squared resid		326.7700	Schwarz criterion	5.889966
Log likelihood		-74.12901	Hannan-Quinn criter.	5.724799
F-statistic		3.012630	Durbin-Watson stat	2.122798
Prob(F-statistic)		0.038978		

Table 2 shows the analysis for Brazil. Based on Table 2, FDI and trade openness (TO) have insignificant effect in Brazil economic growth. However, labor force (LF) and employment have a significant effect. In addition, based on Table 2, LF have the highest rate in Brazil economic growth.

Table 2. Analysis for Brazil

Variable	Coeffici	Std.	t-	Prob.

	ent	Error	Statistic	
C	-102.4140	36.45105	-2.809631	0.0099
FDI	-0.095122	0.394771	-0.240955	0.8117
TO	0.877763	0.391239	2.243546	0.0348
LF	-0.044990	0.155008	-0.290242	0.7742
Employment	0.536936	0.307252	1.747541	0.0939
R-squared		0.316478	Mean dependent var	2.421017
Adjusted R-squared		0.197604	S.D. dependent var	2.647729
S.E. of regression		2.371744	Akaike info criterion	4.725561
Sum squared resid		129.3789	Schwarz criterion	4.963454
Log likelihood		-61.15785	Hannan-Quinn criter.	4.798287
F-statistic		2.662307	Durbin-Watson stat	1.942598
Prob (F-statistic)		0.058362		

Table 3 shows the analysis for China. Based on Table 3, the trade openness is insignificant variable. FDI is also regarded as an insignificant variable because it has a low impact on economic growth in China. This small rate is because with foreign investors, China is strict in its rules. Labor and employment, however, are important variables that affect growth. Employment is the highest rate in economic growth, as shown in the Table 3.

Table 3. Analysis for China

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	-851.7950	141.0596	-6.038545	0.0000
FDI	0.006920	0.251419	0.027525	0.9783
TO	-0.051311	0.038774	-1.323330	0.1987
LF	0.257384	0.094220	2.731743	0.0119
Employment	8.839149	1.500458	5.890968	0.0000
R-squared		0.811514	Mean dependent var	9.671854
Adjusted R-squared		0.778734	S.D. dependent var	2.258640
S.E. of regression		1.062439	Akaike info criterion	3.119445
Sum squared resid		25.96189	Schwarz criterion	3.357339
Log likelihood		-38.67223	Hannan-Quinn criter.	3.192171
F-statistic		24.75630	Durbin-Watson stat	0.463565
Prob (F-statistic)		0.000000		

Table 4 shows the analysis for Egypt. Based on Table 4, the trade openness and labor force have insignificant effect in Egypt economic growth. However, foreign direct investment (FDI) and employment are significant variables. As shown in the Table 4, Egypt has a huge rate in affecting the economic growth.

Table 4. Analysis for Egypt

Variable	Coefficient	Std. Error	t-Statisti	Prob.

			c	
C	-851.7950	141.0596	-6.038545	0.0000
FDI	0.006920	0.251419	0.027525	0.9783
TO	-0.051311	0.038774	-1.323330	0.1987
LF	0.257384	0.094220	2.731743	0.0119
Employment	8.839149	1.500458	5.890968	0.0000
R-squared		0.811514	Mean dependent var	9.671854
Adjusted R-squared		0.778734	S.D. dependent var	2.258640
S.E. of regression		1.062439	Akaike info criterion	3.119445
Sum squared resid		25.96189	Schwarz criterion	3.357339
Log likelihood		-38.67223	Hannan-Quinn criter.	3.192171
F-statistic		24.75630	Durbin-Watson stat	0.463565
Prob (F-statistic)		0.000000		

Table 5 shows the analysis for India. Based on Table 5, foreign direct investment and employment have insignificant effect in India economic growth. However, trade openness and labor force have significant effect. As shown in the Table 5, highest rate that affect India economic growth is the trade openness.

Table 5. Analysis for India

Variable	Coefficient	Std. Error	t-Statistic	Prob.

C	-189.4134	195.7382	-0.967687	0.3433
FDI	-0.300120	0.804718	-0.372951	0.7126
TO	0.141014	0.066830	2.110044	0.0459
LF	0.434938	0.342374	1.270360	0.2167
Employment	1.728755	1.866923	0.925992	0.3641
R-squared		0.234753	Mean dependent var	6.692439
Adjusted R-squared		0.101667	S.D. dependent var	4.436406
S.E. of regression		2.052479	Akaike info criterion	4.436406
Sum squared resid		96.89138	Schwarz criterion	4.674300
Log likelihood		-57.10968	Hannan-Quinn criter.	4.509132
F-statistic		1.763918	Durbin-Watson stat	1.735579
Prob (F-statistic)		0.170560		

Table 6 shows the analysis for Australia. Based on Table 6, foreign direct investment and labor force have insignificant effect in Australia economic growth. However, the trade openness and employment are significant and affecting in the economic growth of Australia.

Table 6. Analysis for Australia

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	35.0395	18.266	1.9182	0.0676

	7	19	75	
FDI	0.013258	0.123778	0.107114	0.9156
TO	0.117742	0.107565	1.094613	0.2850
LF	-1.112827	0.378486	-2.940210	0.0074
Employment	0.371591	0.226731	1.638906	0.1148
R-squared		0.292207	Mean dependent var	3.041806
Adjusted R-squared		0.169112	S.D. dependent var	1.203892
S.E. of regression		1.097384	Akaike info criterion	3.184168
Sum squared resid		27.69780	Schwarz criterion	3.422062
Log likelihood		-39.57836	Hannan-Quinn criter.	3.256895
F-statistic		2.373843	Durbin-Watson stat	1.106327
Prob (F-statistic)		0.081931		

Table 7 shows the analysis for Kenya. Based on Table 7, the results showed that all variables are insignificant. However, FDI and trade openness affect economic growth a little, but they are not significant, as Kenya is risky and not so attractive to investors.

Table 7. Analysis for Kenya

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	93.78566	67.02532	1.399257	0.1751
FDI	0.611236	3.621341	0.168787	0.8674

TO	0.020171	0.028352	0.711462	0.4840
LF	-0.389772	0.170600	-2.284713	0.0319
Employment	-0.717764	0.830280	-0.864484	0.0319
R-squared		0.494394	Mean dependent var	3.830958
Adjusted R-squared		0.406463	S.D. dependent var	2.445409
S.E. of regression		1.883976	Akaike info criterion	4.265079
Sum squared resid		81.63543	Schwarz criterion	4.502972
Log likelihood		-54.71110	Hannan-Quinn criter.	4.337805
F-statistic		5.622503	Durbin-Watson stat	1.957605
Prob (F-statistic)		0.002624		

OVERALL DISCUSSION

Thus overall, based on the analysis done, it was found that FDI has different impact from country to another. It depends on the investors ' regulation of the country, location, or attractiveness. Moreover, as shown in the findings, FDI affects developed countries economic growth, but in all seven countries, the effect is not significant. Furthermore, there are also different factors in the country that may be more important than FDI, such as labor force, employment, and trade openness. Egypt, however, is the only country with significant FDIs for economic growth. This shows that Egypt is a good location and a good as investors are investing in their country, so the return reflected their economic growth's effectiveness. This is agreed by the work of Elshamy [16] where it was reported that Egypt has good location and Chinese investors are investing in Egypt. However, because of the nature and the region, Kenya and Australia have less impact on FDI in their economic growth. Moreover, Saudi Arabia has a negative impact as it has recently begun to open up foreign investment. China was negative because China is very stringent with foreign investors.

CONCLUSION

This work has examined the effect of FDI in economic growth of the emerging countries. The study has used data from 1991-2018 for 7 countries, which were Saudi Arabia, Brazil, China, Egypt, India, Australia and Kenya. Key findings of this work have shown that some countries have had a negative effect on their economic growth. In addition, the results have shown that it was an effective economic reflection for Egypt. This shows that if a country is working to improve its market and attract investors, it will increase its FDI inflow and reflect well on economic growth.

REFERENCES

Boghean, C., & State, M. (2015). The relation between foreign direct investments (FDI) and labour productivity in the European Union countries. *Procedia Economics and Finance*, *32*, 278-285.

Erdal, L., & Göçer, İ. (2015). The effects of foreign direct investment on R&D and innovations: panel data analysis for developing Asian countries. *Procedia-Social and Behavioral Sciences*, *195*, 749-758.

Arun, K., & Yıldırım, D. Ç. (2017). Effects of foreign direct investment on intellectual property, patents and R&D. *Queen Mary Journal of Intellectual Property*, *7*(2), 226-241.

Kostova, T., & Marano, V. (2019). Institutional theory perspectives on emerging markets. In *the Oxford Handbook of Management in Emerging Markets* (p. 99). Oxford University Press.

Korinek, A. (2018). Regulating capital flows to emerging markets: An externality view. *Journal of International Economics*, *111*, 61-80.

Ghysels, E., Plazzi, A., & Valkanov, R. (2016). Why invest in emerging markets? The role of conditional return asymmetry. *The Journal of Finance*, *71*(5), 2145-2192.

Nielsen, B. B., Asmussen, C. G., & Weatherall, C. D. (2017). The location choice of foreign direct investments: Empirical evidence and methodological challenges. *Journal of World Business*, *52*(1), 62-82.

Hlavacek, P., & Bal-Domanska, B. (2016). Impact of foreign direct investment on economic growth in Central and Eastern European countries. *Inžinerinė ekonomika*, 294-303.

Seker, F., Ertugrul, H. M., & Cetin, M. (2015). The impact of foreign direct investment on environmental quality: a bounds testing and causality analysis for Turkey. *Renewable and Sustainable Energy Reviews*, *52*, 347-356.

Ayyagari, M., Dau, L. A., & Spencer, J. (2015). Strategic responses to FDI in emerging markets: Are core members more responsive than peripheral members of business groups? *Academy of Management Journal*, *58*(6), 1869-1894.

Kayalvizhi, P. N., & Thenmozhi, M. (2018). Does quality of innovation, culture and governance drive FDI? Evidence from emerging markets. *Emerging Markets Review*, *34*, 175-191.

Wang, C., Hong, J., Kafouros, M., & Wright, M. (2018). Exploring the Role of Government Involvement in Outward FDI from Emerging Economies. In *State-Owned Multinationals* (pp. 75-109). Palgrave Macmillan, Cham.

Park, B. I., Kim, C. H., & Choi, S. B. (2016). Knowledge spillovers through inward FDI in emerging markets: an empirical examination in the supermarket industry. *European Journal of International Management*, *10*(3), 314-342.

Piperopoulos, P., Wu, J., & Wang, C. (2018). Outward FDI, location choices and innovation performance of emerging market enterprises. *Research Policy*, *47*(1), 232-240.

Cai, P., Kim, S. J., & Wu, E. (2019). Foreign direct investments from emerging markets: The push-pull effects of sovereign credit ratings. *International Review of Financial Analysis*, *61*, 110-125.

Elshamy, H. (2017). The economic determinants of Chinese foreign direct investment in Egypt. In *China and Africa* (pp. 189-198). Palgrave Macmillan, Cham.