MAKERERE UNIVERSITY

THE IMPACT OF FOREIGN DIRECT INVESTMENT ON ECONOMIC GROWTH IN KENYA: (1995-2015)

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ABSTRACT

FDI forms part of capital inflows to the host country and therefore a main contributor to economic growth in developing nations. This is because in addition to it contributing to the level of capital stock increment, it is accompanied by new technology and managerial expertise, which are key accelerators of economic growth. Statistics indicate that Kenya's FDI inflows ratio to GDP is low as compared to that of entire Sub-Saharan Africa and this gives worrying signs of FDI contribution to the economy. Kenya has also been experiencing political unrests especially during election periods like the 2007/2008 postelection violence. This motivated the study to investigate whether FDI has any impact on the Economic growth of Kenya.

Owing to non-stationarity of the macroeconomic variables ADF technique was used to transform the variables to be stationary at first difference; Cointegration test showed there is a long run relationship among the variables; Granger causality test showed that we cannot use histories of all the other variables to predict one variable than we can, using its lagged variable; regression results showed that FDI has a positive impact on economic growth in the short run, with a 1% increase in the level of FDI causing a 0.014% increase in GDP. The model was tested for heteroscedasticity, serial correlation, multicollinearity and omitted variables to validate it.

The study recommends that policy makers should develop policies which will initiate more FDI inflow into the country. This can be achieved through balanced improvement of all the other macroeconomic variables to attain a sustainable economic development. However, proper measures should be undertaken to protect local infant industries, minimize MNC's divestments and excess profit repatriation.