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Macroeconomic Factors and Foreign Direct Investment in Kenya

Leah Njenga[1], Dr. Fredrick Wafula[2], Dr. Joshua Matanda[3]
[1](MScEconomics Candidate, Jomo Kenyatta University of Agriculture and Technology, Kenya)
[2,3](Lecturer, Jomo Kenyatta University of Agriculture and Technology, Kenya)

Abstract:
Over the years, foreign direct investment has become one of the major sources of capital flow connecting diverse country economies thus becoming key catalyst towards growth of economies in developing countries including Kenya. Despite their significance in economic development, foreign direct investments in Kenya have been changing over the years. Macroeconomic factors considerably influence decisions of foreign investors to invest or inject capital in different businesses. It is therefore essential to understand whether the macroeconomic factors in Kenya have an effect on foreign direct investment. The general objective of on-going study was to evaluate the effects of macroeconomic factors on foreign direct investment in Kenya. Moreover, the on-going study sought to establish effect of inflation, interest rate, foreign exchange rate and economic growth on foreign direct investment in Kenya. The study used explanatory research design. Moreover, target population was the period of 1960 to 2020. While data on some variables like economic growth is available from 1960, data on other variables (foreign direct investment, inflation, foreign exchange rate, and interest rate) was available from 1985. The study therefore captured the period between 1985 and 2020. This study employed secondary time-series data and was gathered using data extraction checklist. The quantitative data was gathered, edited and also coded into Stata version 2016, for statistical analysis. Moreover, quantitative data was analyzed based on inferential as well as descriptive statistics. The study found inflation has an inverse, but insignificant effect on foreign direct investment in Kenya. In addition, interest rate has an inverse and insignificant effect on foreign direct investment in Kenya. Also, the study found that there is an inverse and significant relationship between Foreign Exchange Rate and foreign direct investment in Kenya. Further, economic growth has positive and significant effect on foreign direct investment in Kenya. The study recommends that the central bank of Kenya should review policies in order to lower interest rates to make borrowing cheaper, which as a result encourages spending on credit and investment and hence enhance FDI. The government of Kenya should come up with successful strategies such as increasing the availability of credit and simplifying regulation related to exports such as bureaucracy procedures to help boost the country's exports and decrease imports. In addition, the government should facilitate economic growth by developing policies to help cut taxes and interest rates as well as increase efficiency and productivity through privatization and deregulation.

KeyWord: *Macroeconomic Factors,Inflation, Interest Rate, Foreign Exchange Rate, Economic Growth, Foreign Direct Investment*

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I. Introduction

Foreign direct investment (FDI) is a key catalyst to growth and an essential part of an effective as well as open global economic system. As such, FDI can assist to meet the economic expectation of developing in various ways. First, FDI acts as basis for development finance (Kangogo, 2015). The FDI helps to finance various investments in the country's economy. Second, in the host country it heightens the level of technical advancement and consequently plays an essential role in economic growth (EG) process. Third, besides being the basis of development finance as well as a channel for transfer of technology, FDI has numerous proven features. It enhances efficiency in productivity as well as managerial skills and knowledge. It further provides broad array of goods as well as services to an economy. Additionally, exports are promoted by FDI and therefore influence the balance of payment of a country positively (Asiamah, Ofori & Afful, 2019).

Over the years, FDI has become an essential source of private finance for various developing countries. However, benefits of FDI are not automatic as well as uniform across sectors, countries and also local communities (Rengasamy, 2017). National policies as well as global investment architecture influence the attraction of FDI to larger number of developing countries and hence affect the ability of a country to get full FDI benefits for development. However, developing countries have been experiencing a decrease in FDI inflows

over the years. For instance, between 2016 and 2020, FDI inflows in developing countries decreased by 42 percent. Foreign direct investment is seen as a major source of getting the required funds for investments in most African countries and hence its decrease leads to a decrease in levels of investments. In most African countries, inadequate resource to finance long-term investment is a major problem. This lack of investible funds is a big setback to economic growth and this is making it increasingly difficult to achieve the sustainable development goal by 2030 as set by the United Nations. Therefore, host countries, including developing countries, require to establish an effective, transparent and broad favorable policy environment for purposes of investment and to create institutional and human capacities to execute them. Therefore, macroeconomic factors perform a key role in attracting FDI inflows. Various macro-economic elements differ with time and impacts practices, outputs as well as economic processes in an economy and hence they are key to investment decisions.

Oniore, Gyang and Nnadi (2016) indicate that macroeconomic factors can promote or impede the performance of investments. Zardashty (2014) argues that in regard to real interest rate (INR), two schools of thought tried to explain the relationship with investment. The neoclassical investment model treats real INR as an element of user cost of capital, hence it influences investments inversely. Another argument is that when real INR is high, bank credits inflow increases as people want to save more this tends to complement savings and increase investment.

Theoretically real exchange rate can influence level of FDI either positively or negatively. The effect can be negative as it is among the elements that determines real cost of imports (Iqbal & Jamil, 2015). When a currency is devalued, real cost of purchasing imported capital goods tends to increase, this reduces profitability and a fall in investment resorts (Shah & Batley, 2009). Conversely, devaluation of real currency can influence investment positively in sectors generating globally traded goods, since it increases export volumes and competitiveness (Aftab, Jebra & Ullah, 2016).

Inflation rates (IR) can impact investment in long-term. Moreover, variable as well as high inflation create more confusion as well as uncertainty, with doubts over future cost of investment (Masoudi, 2016). At the final cost of investment, firms will be uncertain if inflation is volatile and high, they may as well fear that high inflation could result to economic uncertainty as well as future downturn. Countries with lengthy period of stable and low inflation have frequently experienced higher investment rates.

Macro-economic variables are relevant factors to wider economy at national or regional level and influence wider population instead of few individuals (Ayeni, 2020). Macroeconomic factors include, but not limited to economic output, inflation, savings, exchange rate, unemployment rate, trade openness, and are main economic performance indicators monitored by businesses, governments as well as consumers (Moshi & Kilindo, 2013).

According to Kasapi, Lampo and Economakis (2019), key macroeconomic factors such as trade balance, real unit labor costs (ULC), exchange rate, trade balance, exports' sectoral distribution affect inward FDI in Slovakia, Romania, and Greece while economic complexity and interest rates had no significant effect on FDI. Among members of Association of ASEAN, Rengasamy (2017) indicate that the trend as well as growth of FDI inflow was progressive and positive. Macro-economic factors of inflation and GDP influence FDI inflow significantly, however, exchange rate (ER) is insignificant and there has no influence on FDI inflow.

African countries gradually employ alternative strategies to mobilize development finance as one remarkable strategy effort to attract modern inflows of FDI. However, FDI inflow in African countries is influenced by different macroeconomic factors. Enu, Havi and Attah-Obeng (2013) indicate that macroeconomic factors in Ghana play an important role in FDI, and while trade openness, economic growth as well as exchange rate positively influence the inflows of FDI, inflation and interest rates negatively influences the inflows of FDI. In a different study, Asiamah, Ofori and Afful (2019) argue that short-run and long-run findings showed statistically significant but negative influence of inflation rate, interest rate and exchange rate on FDI in Ghana whereas GDP, telephone usage (TU) and electricity production influence FDI positively. In Nigeria, Obidike and Uma (2013) argue that selected macroeconomic variables; inflation, INR, and EG considerably influence FDI.

Studies conducted in Kenya show mixed findings on the influence of different macroeconomic factors on FDI. For instance, Kangogo (2015) argue that money supply as well as interest rate has a significant influence on FDI in Kenya, but ER as well as inflation had no significant influence on FDI inflow. In addition, Kwoba and Kibati (2016) indicated that exchange rate, GDP as well as inflation rate (IR) had negative insignificant influence on FDI inflows. Further, Otieno (2016) observed a positive and significant association between development expenditure and FDI and a negative effect of real INR, inflation, real ER on FDI.

In Kenya, FDI is covered in all sectors; banking, telecommunications or automobile sector. Operations in Kenya have been set up by different multinational companies which include Coca-Cola, Car and General and communication firms for instance Airtel. FDI is experienced in goods as well as services that are utilized in every aspect of our lives, (Kwoba & Kibati, 2016). FDIs are not however in exclusion since they have offered employment and provide technical knowledge because they train workers to uphold standards that are present in

other forms of investments across the world. Moreover, they are main sources of a country's foreign exchange. Over the years, FDI has been inconsistent with certain periods indicating low inflows. FDI inflow in 1980s and 1990s was low because of increasing challenges of poor infrastructure, decline in economic performance and high cost of living which significantly influenced negatively the FDI inflows. There are greater than 200 Kenyan multinational industries throughout the sectors with Germany, Britain, USA, Netherlands, South Africa, Switzerland, India as well as China being major traditional centers of FDI (Asiamah, Ofori & Afful, 2019).

Kenya acts as business hub within East Africa for numerous global businesses which translates to FDI dependence for capital inflow that consequently signals creation of jobs as well as an economy assisted to develop by investments from foreign countries. In Kenya, between 2007 and 2015, FDI average percentage growth was 40 percent with inflows mainly directed into consumer as well as retail goods, technology, telecommunications, media, minerals, natural gas as well as oil sector primarily from USA, UK and also India (Kangogo, 2015). The rate of growth enable Kenya to earn the category of FDI hotspot entering other Countries within Africa countries like Ghana, Tanzania, Uganda, Zambia, Nigeria, Rwanda as well as Mozambique. In 2015, FDI inflows was USD 1076.9 million or KES 105.29 billion, from previous USD 670 million KES 65.51 billion in 2014 which is 60 per cent improvement. Moreover, this capital was channeled to manufacturing, oil and gas industries

Statement of the Problem

Over years, FDI has become one of major bases of capital flow joining different country economies thus becoming key catalyst towards economies' advancement of diverse developing countries including Kenya (Edmiston, Mudd & Valev, 2004). Despite the importance of FDIs in Kenyan EG, they have been changing over the years. In addition, Kenya has experienced a sharp decline in FDI compared to inflows in Uganda and Tanzania (The World Bank, 2016. As a percent of the GDP, foreign direct investment (FDI) inflows in Kenya decreased from 3.46% in 2011 to 2.74% in 2012, 2.03% in 2013, 2014% in 1.34%. In addition, foreign direct investment (FDI) inflows, as a percent of the GDP, decreased to 0.97%, but increased to 0.98% in 2016, 1.60% in 2017 and 1.85% in 2018. However, foreign direct investment (FDI) inflows decreased to 1.40% in 2019 and 0.87% in 2020 (World Bank, 2020). Over the years, foreign exchange rate in Kenya has been increasing reaching a figure of 104 shillings against the dollar in 2017. In addition, foreign exchange rate increased from 98.69 to 104.12 between the year 2015 and 2017. In 2018, foreign exchange rate was 101.29, which increased to 102.01 in 2019 and 108.83 by October 2020. Inflation, measured in terms of consumer price index in Kenya increased from 114.02 in 2011 to 159.64 in 2016, but this reduced to 148.78 in 2018 (Central Bank of Kenya, 2019). Trade openness in Kenya has been on the decrease. It decreased from 37.7% in 2016 to 37.39% in 2017, 36.15% in 2018 and 33.4% in 2019 (World Bank, 2019). Before interest rate capping in 2016, Kenya had been portraying high interest rates when compared with both developed countries and some developing countries. The lending IR in Kenya was 16.51%, which reduced to 13.5% after interest rate capping. However, a law was signed in November 2019 cancelling a cap on banks' commercial lending rates, which means that commercial banks were at liberty to increase or reduce interest rates (Central Bank of Kenya, 2019). Various studies have been conducted on macroeconomic factors in Kenya. For instance, Otieno and Njuguna (2016) assessed the effect of macro-economic factors on FDI flows (2002-2013); and Kwoba and Kibati (2016) examined the impact of macro-economic variables on FDI in Kenya (2005-2014). However, these studies were conducted during different periods of time, had mixed findings and used a descriptive research design. In addition, there has been a considerable change in the macroeconomic environment in Kenya and most of the studies hence, the findings are not up-to-date. This study therefore sought to establish the influence of macroeconomic factors on foreign direct investment in Kenya.

Objectives of the Study

i) To establish the influence of inflation on foreign direct investment in Kenya.
ii) To assess the influence of interest rate on foreign direct investment in Kenya.
iii) To evaluate the influence of foreign exchange rate on foreign direct investment in Kenya.
iv) To assess the influence of economic growth on foreign direct investment in Kenya.

II. Literature Review

Theoretical Framework

This study covered theories related to macroeconomic factors and FDI in Kenya. Specifically, the study was anchored on the Purchasing Power Parity Theory, Eclectic paradigm of dunning, International Fisher Effect (IFE) Theory and Keynesian Economic Theory.

The PPP theory by Cassel was coined in 1920s to establish the association between exchange rates of various nations. The theory starts with PPP also known as inflation theory of exchange rates (Dutt & Ghosh,

2018). PPP states that if and also when the rate of exchange moves to offset rate of inflation creates differentials between nations (Hyrina & Serletis, 2013). The PPP has another definition based on "law of one price" which states that ER between 2 currencies must be equivalent to ratio of price level of similar products in two nations (Iyke & Odhiambo, 2017). The PPP theorem shows the association between product's relative prices and exchange rate. PPP can be referred back in 16th century in Spain as well as early 16 century in England however, Cassel was the first to refer this theory as the PPP. Moreover, Cassel once stated that without the PPP theory, it could be somehow impossible to discuss overvaluation and undervaluation of a currency due to lack of meaningful way (Morgan, 2012). The PPP theory was used in this research to establish the association between inflation and foreign exchange rates. As per the theory, foreign exchange rates (FXR) need to be assessed by relative cost of similar products between two nations. Inflation rate in one country should be inversely proportional to the country's exchange rate so as to ensure balance. This means that if the price levels of one country increase as a result of inflation, rate of exchange of the country should go down so as to return

John H. Dunning developed the eclectic paradigm in 1979 for global production through incorporating market imperfection structures, location theory and trans-cost market imperfections. The theory considers the nature of a country's involvement in international relations by analyzing two types of involvement (Young, 2017). The basic assumption of the eclectic paradigm is that the returns to FDI, and hence FDI itself, can be explained by a set of three factors: the ownership advantages of firms 'O', indicating who is going to produce abroad 'and for that matter, other forms of international activity'; by locational factors 'L' 'influencing the where to produce' and by the internalization factor 'I' that 'addresses the question of why firms engage in FDI rather than license foreign firms to use their proprietary assets' (Young, 2017). This paradigm assumes that institutions will avoid transactions in the open market if the cost of completing the same actions internally, or in-house, carries a lower price. The eclectic paradigm assumes that companies are not likely to follow through with a foreign direct investment if they can get the service or product provided internally and at lower costs. The Dunning's eclectic paradigm was used to explain the effect of inflation on foreign direct investment. The theory indicates that, increase in globalization, ownership and location advantages will lead to integration of entry modes by companies for example FDI or joint ventures, against licensing or export. However, an increase in inflation increases the cost of production hence decreasing the suitability of a country for investment.

Irving Fisher (1930) is the developer of this theory. He did this in his publication entitled the theory of interest. The theory gives an explanation as to why the rate of exchange varies from time to time. This is done through the use of market rates of interest rather than the rate of inflation (Baiashvili & Gattini, 2019). The theory holds that exchange rate varies due to change in interest rate. Furthermore, the theory indicates that the real interest rate in various nations is equal. This is as a result of possible simultaneous opportunities occurring between the financial markets in form of capital flows (Fornah & Yuehu, 2017). The IFE provides for the assumption that countries with lower interest rates will likely also experience lower levels of inflation, which can result in increases in the real value of the associated currency when compared to other nations. By contrast, nations with higher interest rates will experience depreciation in the value of their currency (Emmanue, Criscent & Alhasan, 2019). The IFE theory was adopted in this research to assess the association between interest rate and FDI. In accordance to this theory, the difference of the nominal interest rate for two nations is approximately equal to the exchange rate between the two countries at that specific time.

British economist John Maynard Keynes developed the Keynesian Economic Theory in the 1930s. Keynes holds that the total economic expenditure strongly influences the economic output in the short run and especially during the recession periods. According to the theory, the total demand does not necessarily add up to the economy's productive capacity. The macroeconomic study of Keynesian economics relies on three key assumptions--rigid prices, effective demand, and savings-investment determinants. First, rigid or inflexible prices prevent some markets from achieving equilibrium in the short run (Emmanue, Criscent & Alhasan, 2019). Second, effective demand means that consumption expenditures are based on actual income, not full employment or equilibrium income. Lastly, important savings and investment determinants include income, expectations, and other influences beyond the interest rate (Fornah & Yuehu, 2017). These three assumptions imply that the economy can achieve a short-run equilibrium at less than full-employment production. This theory was adopted to establish how economic growth influences FDI in Kenya. As indicated by the theory, decrease in demand leads to inefficient macroeconomic results in the economy. Keynes does not mean that savings and investments are influenced by similar factor; interest rate, which would run on money market as price of investments and savings. Keynes categorized consumption to autonomous consumption as well as induced consumption.

Conceptual Review

Egbert (2015) argues that conceptual framework refers to diagrammatic representation of a relation between independent and dependent study variables as depicted in Figure 2.1. The purpose of on-going study was to determine the association between macroeconomic factors and FDI in Kenya. Independent variables were

exchange rates, EG, IR as well as IN. Dependent variable was FDI in Kenya. Inflation occurs where by the general product prices in the economy go up over a certain time period. Increase in price levels leads to fewer goods and services being purchased by each currency unit. Consequently, increase in inflation indicates a low purchasing power of the currency – a negative growth in real currency value and unit of account in the economy (Alshamsi, Hussin & Azam, 2015).Interest rate refers to proportion of total amount loaned which is charged as interest by lender to the borrower, generally expressed as yearly percentage (Kiptanui, 2017). It refers to the rate at which the bank or any other lender charges on the money borrowed or rate at which the bank pays its savers for saving money in the account. According to Mokuolu (2018), interest rate is expressed as percentage of principal and refers to the amount that is charged by the lender for use of assets. Interest rate is normally noted on yearly basis referred to as the annual percentage rate (APR).

Exchange rate is the value of a country's currency in terms of another country. Components of exchange rate include the local currency as well as foreign currency. Therefore, exchange rate can be expressed directly or indirectly (Sharifi-Renani & Mirfatah, 2012). In direct expression, price of the foreign currency is given in terms of local currency. While on indirect expression, price of the local currency is given in terms of foreign country (Doorn, 2016).Economic growth refers to an increase in production of economic services and goods, compared from one period to another (Melnyk, Kubatko & Pysarenko, 2014). It can be measured in nominal or real (change in inflation) terms. EG implies rise in real GDP that is, rise in value of income, national output as well as expenditure (Muhammad, Imran Umer & Ahmed, 2012). Essentially the advantage of economic growth is better living standards –ability to allocate more resources to sectors like education and health care as well as higher real incomes. FDI refers to an investment to business entity in a certain country which is being controlled by the investor from another country (Obidike & Uma, 2013). In general, FDI occurs when potential investors make investments on another country's firm operations or gain foreign firm assets, with inclusion of ownership establishment or control of firms' interest in another country. FDI assets determine the overall level of investments done directly in a certain period of time, usually the end of three months or one year (Kasapi Lampou & Economakis, 2019).

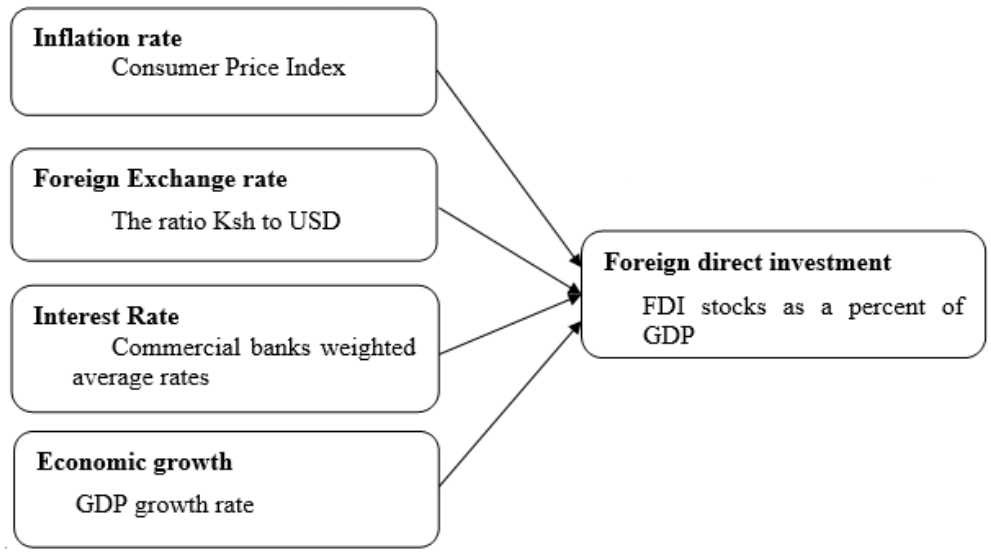

Figure1.0:ConceptualFramework

Empirical Review

Mustafa (2019) examined the association between inflation and FDI in Sri Lanka from 1978 to 2017. A long-term association was noted between variables. Inflation (dependent variable) is inversely associated with FDI (independent variable). Moreover, one-way causal association from FDI to inflation is assured. This study affirms the significant impacts of inflation on FDI. Mansoor and Bib (2019) evaluated the influence of inflation on FDI in Pakistan. Moreover, the study employed the Pakistan time series data obtained between 1980 and 2016 from indicator of world advancement. Overall findings showed that inflation influences FDI negatively as well as insignificantly. Additionally, inflation influences the economy directly. The association between economic growth and inflation is either negative or positive. In Ghana, Asiamah, Ofori and Afful (2019) assessed the determining factor of FDI between 1990 and 2015. The study revealed that short-run and long-run results had statistically significant as well as negative influence of inflation rate on FDI whereas GDP, telephone

usage (TU) and electricity production influenced FDI positively. Musyoka (2018) examined the effect of inflation on FDI in Kenya. The study revealed that inflation has insignificant influence on FDI in Kenya. However, this study covered the period between 1970 and 2016, which is more than five years ago and Kenya has experienced considerable changes in the last five years related to FDI and inflation.

Fornah and Yuehu (2017) performed a research to assess the influence of interest rate (INR) on foreign Direct investment (FDI) in Sierra Leone. The study found that interest rate influences foreign direct investment in Sierra Leone. In Nigeria, Emmanue, Criscent and Alhasan (2019) examined how interest rates influenced FDI between 2006- and 2018. The study found that negative association exit between INR and FDI. In addition, long run co-assimilating equation indicates that negative association exists between INR and FDI and the finding is not statistically significant. Mokuolu (2018) examined the influence of interest rate on FDI in developing countries: a case study of Nigeria. Result revealed that INR has negative influence on FDI flows. Moreover, IN with negative symbol as expected earlier means that FDIs in Nigeria happen regardless of whether IN is progressing as required or not. However, INR, with negative symbol as expected earlier as lower INR would promote FDI ceteris paribus indicated that encouragement observed level was insignificant. Ocharo and Musyoka (2018) conducted a research to establish how interest rates influence FDI. The results showed that INR have significant as well as negative effect on FDI inflows.

Cambazoğlu and Güneş (2016) examined the correlation between (ER) level and FDI inflows in Turkey. Results indicate that in long run, levels of (ER) and direct investment inflows relate however, in short run, the results could not discover any statistically significant association between levels of (ER) and foreign direct inflows. Rise in real (ER) level represents appreciation of Turkey domestic currency. Moreover, estimation results found that real (ER) appreciation decreases foreign direct inflows. Doorn (2016) carried out a study to examine the association between (ER) and FDI in Eurozone. The study used quarterly data obtained from top investor countries from1999 to second quarter of 2016 split in industry specifications. Therefore, between 4 January 1999 and 30 June 2016 was the period of interest in this study. Study results showed insignificant influence (ER) in investor country. Nevertheless, country-specific findings showed significant positive relationship between ER and FDI.In Kenya, Njuguna (2015) researched on the association between exchange rates and FDI. The results revealed that exchange rates impacts FDI levels in Kenya. FDI is attracted by a strong currency that can grow. It was noted that increase in FDI was due to increase in exchange rates.

Baiashvili and Gattini (2019) assessed the impact of economic growth on FDI. The study was focused on 111 countries, starting from developed countries to emerging as well as developing markets from 1980. The study found positive relationship between income levels of the countries and economic growth on FDI. The effect enlarges from low to middle-income countries. However, it reduces again moving to countries with high income. Sokang (2018) examined the impact of economic growth on FDI in Cambodia. The results noted that economic growth has positive influence on FDI of Cambodia. Sarker and Khan (2020) carried out a research to determine the association between economic growth and FDI from African countries. The study found positive effect of EG on FDI. In Kenya, Doorn (2016) carried out a study to examine the degree to which economic growth in infrastructure sector, agricultural sector and manufacturing sector influences FDI inflows. Results show that EG in infrastructure as well as manufacturing sector had positive significant effect on FDI.In addition, Gachunga (2019) examined how economic growth influences FDI in Kenya. The study found that economic growth in infrastructure and manufacturing sector had positive significant influence on foreign direct investment.

III. Material and Methods

The presents study employed the explanatory research design because it sought to establish causal relationship between independent study variables (inflation, interest rate, foreign exchange rate and economic growth) and dependent variable (foreign direct investment).Target population of the present study was the period of 1960 to 2020. However, the accessible population is data between 1985 and 2020. Sampling in this study was done by use of convenience sampling and was done along the years.Secondary time-series data was deployed in present study between1985 and 2020. Data on FDI, inflation, interest rates, foreign exchange rate and economic growth was obtained from KNBS, CBK and World Bank.Quantitative data analysis included descriptive as well as inferential statistics which emphasized on computation of percentage, standard deviation, mean as well as frequencies. In addition, trend analysis was used to show pattern of the data over the years. Additionally, inferential statistics paid emphasis on multivariate as well as correlation regression analysis. Multiple regression models were used in present study to model linear association between dependent (foreign direct investment) and independent study variables (economic growth, foreign exchange rate, interest rate and inflation).

Regression model was;

$$FDI_t = \beta_0 + \beta_{1t}FX_t + \beta_{2t}IR_t + \beta_{3t}In_t + \beta_{4t}EG_t + \varepsilon_t$$

FDI_t is dependent variable (Foreign Direct Investment), B_0 is y intercept (Constant), β_1- β_4 and coefficients of determination, $FX_{1t}$is Foreign Exchange Rate, IR_t is Interest Rate, In_t is Inflation, and EG_t is Economic Growth, t represents time and ε_t is an error term.

IV. Result and Discussion

Descriptive Analysis

Descriptive statistics involved computation of percentage, standard deviation, frequencies and mean of the dependent variable (Foreign direct investment) and the independent variables (inflation, interest rate, foreign exchange rate and economic growth). From the results, it can be seen that, the average in foreign direct investment for the country was approximately 0.6331389 between year 1985 and 2020. The indication in this case is that, on average, the country experienced an increase in foreign direct investment for the indicated period. During the same period, the minimum and maximum amount ever recorded in the foreign direct investment was 0.05 and the maximum was 2.532.

Inflation was another macroeconomic variable under consideration. For the period between 1985 and 2020, the mean value for the variable was approximately 70.1775 with a standard deviation of about 62.56551. In the same period, the minimum and maximum values of the variable were 5.17 and 208.03 respectively. Interest rate was the other macroeconomic variable under consideration in the current study. The variable was captured in terms of commercial banks weighted average rates for the indicated study period. The study found out that, the mean value for the variable was approximately 18.60103 with a standard deviation of 6.510982. The study further found out that, the minimum value for the interest rate in the period was approximately 11.996 per cent. The maximum value ever recorded in the period under consideration was 36.24. The average value for the foreign exchange rate for the period under consideration was approximately 65.87922 with a standard deviation of 28.07087. The study further found out that, the minimum and maximum values for foreign exchange rate in the country was 16.23 and the maximum was 106.451 respectively.

The study further found out that, the economic growth captured in terms of GDP growth rate for the period under consideration was 4.015956 percent with a standard deviation of 2.396238 percent. The results further showed that, the minimum and maximum values recorded for the variable was -0.7995 percent and was 8.4057 percent respectively.

Table 1: Descriptive Statistics

Variable	Obs	Mean	Std. Dev.	Min	Max
FDI	36	.6331389	.5930527	.005	2.532
In	36	70.1775	62.56551	5.17	208.03
IR	36	18.60103	6.510982	11.996	36.24
FX	36	65.87922	28.07087	16.23	106.451
GDP	36	4.015956	2.396238	-.7995	8.4057

Inferential Analysis

Inferential analysis entailed correlation and regression analysis. The purpose also conducted stationarity test using Philips-Perron and choice of model using Hausman test.

Unit Root Test

The research adopted ADF for testing stationarity of the data. The null hypothesis is that the variables are not stationary or they got unit root and hence if the p-value is less than the significance level (0.05) the variables are stationary. The null hypothesis for the ADF unit root test is that unit root is present in the variables. The p-values for the variables FDI and economic growth were 0.0000 and 0.0148 respectively. This implies that FDI, inflation, interest rate, foreign exchange rate and economic growth had no unit root and hence there was no need of running co-integration. However, inflation, interest rate, foreign exchange rate had a unit root as p-value was 1.0000, 0.6072, 0.7341 respectively.

Table 2: Unit Root Test

Variable	No of obs	Test Statistic	p-value for z(t)	Interpooled Dickey-Fuller 1% critical value	5% critical value	10% critical value
FDI	35	-4.923	0.0000	-3.682	-2.972	-2.618
Inflation	35	5.706	1.0000	-3.682	-2.972	-2.618
Interest Rate	35	-1.347	0.6072	-3.682	-2.972	-2.618
Foreign exchange rate	35	-1.051	0.7341	-3.682	-2.972	-2.618
Economic Growth	35	-3.302	0.0148	-3.682	-2.972	-2.618

Hausman Test

Hausman Test was used to detect the presence of endogenous repressors in a particular regression model. The presence of endogenous repressor leads to failure of OLS estimator. Hence, it is assumed that there is absence of correlation between error terms and predator variables. The null hypothesis in this study was that random influence was the preferred model while fixed influence model was alternative hypothesis. The Hausman Test was conducted and the results were as presented in Table 3. As illustrated in Table 3, Hausman specification test p value (0.000) was less than the alpha value of 0.05 (at 95% confidence interval). This implied that the null hypothesis was rejected implying that the study need to use fixed effects model.

Table3: Hausman Test

	Coefficients			
	(b) fixed	(B) random	(b-B) Difference	sqrt(diag(V_b-V_B)) S.E.
In	.08853	-.0031626	.0916926	.053723
FX	.9864781	1.805983	-.8195048	.7253833
IR	1.174765	1.851857	-.6770918	.6589835
EC	.0735228	.0596108	.0139121	.1162925

b = consistent under Ho and Ha; obtained from xtreg
B = inconsistent under Ha, efficient under Ho; obtained from xtreg

Test: Ho: difference in coefficients not systematic

chi2(4) = (b-B)'[(V_b-V_B)^(-1)](b-B)
= 35.18
Prob>chi2 = 0.0000

Correlation Analysis

From the findings as shown in Table 4, there is an inverse and insignificant relationship between inflation and foreign direct investment in Kenya (r = -0.008, p-value=0.965). These findings are in line with Alshamsi, Hussin and Azam (2015) findings that inflation has insignificant influence on FDI inflows. Moreover, the findings agree with Mohammed and Mansur (2014) findings that there exists a long-run inverse association between inflation level and FDI inflow in South Africa. Further, the findings indicated that interest rate had an inverse and insignificant relationship with FDI in Kenya (r = -0.302, p-value=0.074). The findings conform to Anna (2012) findings that INR had insignificant influence on FDI inflows in Zimbabwe. Moreover, the study findings conform to Kiptanui (2017) arguments that interest rate influences FDI inflows negatively. In addition, the results show that there exists an inverse and significant relationship between foreign exchange rate and FDI in Kenya (r= -0.428, p-value=0.009). The findings are contrary to Sharifi-Renani and Mirfatah (2012) findings that (ER) has a positive association with FDI in Iran. In addition, these findings concur with Kyereboah- Coleman and Agyire- Tettey (2008) discoveries that ER influences FDI inflow negatively in small and developing country such as Ghana.Also, economic growth had a positive, and significant relationship with the FDI in Kenya (r=0.500, p-value=0.002). These findings agree with Sokang (2018) argument that economic growth has positive influence on FDI of Cambodia. In addition, the findings conform to Melnyk, Kubatko and Pysarenko (2014) arguments that economic growth has positive influence on FDI in Cameron.

Table 4:Correlation Coefficients

		FDI stocks as a percent of GDP	Inflation (Consumer Price Index)	Interest Rate (Commercial banks weighted average rates)	Foreign Exchange Rate (Ratio of Ksh to USD)	Economic Growth (GDP Growth Rate)
FDI stocks as a percent of GDP	Pearson Correlation	1				
	Sig. (2-tailed)					
	N	36				
Inflation (Consumer Price Index)	Pearson Correlation	-.008	1			
	Sig. (2-tailed)	.965				
	N	36	36			
Interest Rate (Commercial banks weighted average	Pearson Correlation	-.302	-.248	1		
	Sig. (2-tailed)	.074	.145			

rates)	N	36	36	36		
Foreign Exchange Rate (Ratio of Ksh to USD)	Pearson Correlation	-.428**	.849**	-.196	1	
	Sig. (2-tailed)	.009	.000	.252		
	N	36	36	36	36	
Economic Growth (GDP Growth Rate)	Pearson Correlation	.500**	.214	-.422*	.058	1
	Sig. (2-tailed)	.002	.209	.010	.737	
	N	36	36	36	36	36

**. Correlation is significant at the 0.01 level (2-tailed).

*. Correlation is significant at the 0.05 level (2-tailed).

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Linear Regression Analysis

To establish the effect of macroeconomic variables on FDI in Kenya, multiple regression analysis was undertaken where the independent variables included economic growth, interest rate, inflation and foreign exchange rate and the dependent variable was FDI.

The regression model was expressed as follows;

$$Y_t = \beta_0 + \beta_1 X_{1t} + \beta_2 X_{2t} + \beta_3 X_{3t} + \beta_4 X_{4t} + \varepsilon_t$$

Y_t is the dependent variable (FDI), B_0 is the y intercept (Constant), β_1- β_3 and coefficients of determination, $X_{1t}$is the inflation, $X_{2t}$is the interest rate, X_{3t} is foreign exchange rate,X_{4t} is economic growth, t represents time and ε_t is an error term.

The r-squared for the relationship of the four independent variables (interest rate, economic growth, foreign exchange rate and inflation) and the dependent variable (FDI in Kenya) was 0.3860. This indicates that the four independent variables (interest rate, economic growth, inflation and foreign exchange rate) can help in explaining 38.60% of FDI in Kenya. Moreover, the p-value for the F-statistic was 0.0036, which shows that the model can be used in predicting the influence of interest rate, economic growth, inflation and foreign exchange rate on FDI in Kenya. After adjusting for the errors, the r-squared was 0.3068 implying that 30.68% of the FDI in Kenya can be explained factors such as interest rate, economic growth, inflation and foreign exchange rate. The results show that the F-calculated (4.87) was greater than the F-critical (2.68) and the p-value (0.0036) was less than the significance level (0.05) showing that the model could be used in predicting the effect of the four independent variables on the dependent variable.

The results show that inflation has a positive and insignificant effect on FDI in Kenya as indicated by a regression coefficient of 0.0039019. The p-value (0.196) was more than the significance level (0.05) and hence the influence was insignificant. This implies that an increase in inflation would lead to a 0.0039019 increase in FDI. These findings agree with Omankhanlen (2011) findings that inflation has insignificant influence on FDI in Nigeria. In addition, these findings concur with Musyoka (2018) arguments that inflation has insignificant influence on FDI in Kenya

In addition, the results revealed that interest rate has an inverse and insignificant effect on FDI in Kenya as indicated by a regression coefficient of -0.0067511. The p-value (0.676) was more than the significance level (0.05) and hence the effect was insignificant. This shows that an increase in inflation would lead to a 0.0067511 decrease in FDI in Kenya. The findings agree with Emmanue, Criscent and Alhasan (2019) findings that a negative and insignificant association exists between INR and FDI in Nigeria. In addition, the findings concur with Mokuolu (2018) findings that INR has negative influence on FDI flows.

Further, the results show that foreign exchange rate has an inverse and significant effect on FDI in Kenya as shown by a regression coefficient of -0.0134452. The p-value (0.034) was less than the significance level (0.05) and hence the effect was significant. This implies that an increase in interest rates would lead to a 0.0134452 decrease in FDI in Kenya. The findings agree with Njuguna (2015) findings that exchange rates impacts FDI levels in Kenya negatively. However, the findings are contrary to Otieno (2015) findings that exchange rate had insignificant relationship with the FDI inflows in Kenya.

The results show that economic growth has a positive and significant influence on FDI in Kenya as indicated by a regression coefficient of 0.1033672. The p-value (0.012) was less than the significance level (0.05) and hence the influence was significant. These findings disagree with Baiashvili and Gattini (2019) findings that there exists a positive relationship between economic growth and FDI in both developing and developed countries. Moreover, these findings are in line with Pantina and Zogjani (2015) arguments that economic growth has positive influence on FDI in Europe.

Table 5: Regression Coefficients

Source	SS	df	MS		
				Number of obs	= 36
				F(4, 31)	= 4.87
Model	4.75221696	4	1.18805424	Prob > F	= 0.0036
Residual	7.55768535	31	.243796301	R-squared	= 0.3860
				Adj R-squared	= 0.3068
Total	12.3099023	35	.351711494	Root MSE	= .49376

FDI	Coef.	Std. Err.	t	P>|t|	[95% Conf.	Interval]
In	.0039019	.0029516	1.32	0.196	-.002118	.0099217
IR	-.0067511	.0159771	-0.42	0.676	-.0393367	.0258345
FX	-.0134452	.0060614	-2.22	0.034	-.0258074	-.001083
EC	.1033672	.0387657	2.67	0.012	.024304	.1824305
_cons	.955534	.4471318	2.14	0.041	.0436026	1.867465

V. Conclusion and Recommendation

The research further concludes that there is an inverse and insignificant relationship between inflation and FDI in Kenya. This shows that an increase in consumer price index in Kenya leads to an insignificant decrease in FDI. The study concludes that interest rate has an inverse and insignificant effect on FDI in Kenya. This implies that high INR reduce FDI inflows within the country although not significantly. The interest rates are more likely to rise with higher inflation rate. The study concludes foreign exchange rate has an inverse and significant effect on FDI in Kenya. This implies that an increase in foreign direct investment leads to a significant decrease in FDI in Kenya. Normally, increase in exchange rate decreases the balance of trade of a country while decreasing exchange rate lowers purchasing power of income and capital gains resulting from total returns.The study also concludes that economic growth has a positive and significant effect on FDI in Kenya. This implies that an increase in economic growth would significantly increase FDI in Kenya.

The study recommends the central bank of Kenya should review policies in order to lower interest rates to make borrowing cheaper, which as a result encourages spending on credit and investment and hence enhance FDI in the country. This study also recommends that the government of Kenya should come up with successful strategies such as increasing the availability of credit and simplifying regulation related to exports such as bureaucracy procedures to help boost the country's exports and decrease imports. The government of Kenya should come up with policies to reduce budget deficit, control money being created by the government and increase interest rates to reduce inflation. Moreover, this study recommends that the government should develop supply-side policies, fiscal policy and policies control wages to help reduce inflationary pressures. The study recommends that the government should facilitate FDI by providing economic and political stability as well as investing in infrastructure such as new roads, railways lines and broadband internet to increase productive capacity and reduce congestion. In addition, the government should develop policies to help cut taxes and interest rates as well as increase efficiency and productivity through privatization and deregulation in order to improve FDI of the country.

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