THE IMPACT OF FOREIGN DIRECT INVESTMENT
ON SAUDI ARABIA

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Jawaher Abdulrahim
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AUTHOR: Jawaher Abdulrahim

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Economics Department

Dr. Bruce Brown
Project Committee Chair
Professor of Economics

Dr. Greg W. Hunter
Graduate Coordinator
Professor of Economics
ABSTRACT

This paper investigates the impacts of foreign direct investment on Saudi Arabia. This examination seeks to find the degree to which foreign firms benefit Saudi Arabia and their impact on other aspects such as language and culture. In addition, the study went further to review the influence of foreign firms on the FDI inflows in the country, the examination of the determinants of FDI in comparison to other developing countries, and to see how Saudi Arabia’s heavy dependence on oil revenue affects the nation’s FDI. Foreign direct investment is a crucial discussion term in the paper as it is a very important resource when it comes to economic development. This is because it cuts the gap between domestic mobilized savings and desired investments. Furthermore, FDI facilitates tax revenues of the host country, improves technological knowhow, and labor skills. Thus, a country such as Saudi Arabia with ample natural resources in terms of oil and numerous foreign workers is better placed to take advantage of such benefits. Also, the paper touches on Turkey’s FDI that is propelled by the country’s political stability as well as the foreign-friendly and accommodative culture that has contributed positively in facilitating an investor friendly environment. Turkey was used to demonstrate comparison with Saudi Arabia in terms of FDI and other economic aspects. Despite the favorable factors, it is worth mentioning that the Turkish economy was negatively influenced by the euro crisis of 2012, but thereafter, started to improve again. All in all, FDI contributes a large amount of the Saudi Arabia’s economy and foreign firms have a significant impact on the general Gross Domestic Product as they contribute a massive 34 % of the total GDP.

Key Words: FDI, Exports, Imports
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CHAPTER 1
INTRODUCTION

Statement of the Problem

Foreign investment normally denotes any investment in another nation carried out by private entities or individuals as opposed to government aid. Notably, most of foreign direct investments in the developing nations are usually performed by large multinational corporations. Due to advancement in technology, direct investments play an integral role in filling the resource gap between targeted and desired investment and locally mobilized savings. FDI also contribute, to filling the gap between targeted foreign exchange needs and those derived from net export earnings plus net foreign aid. In addition, FDI play a crucial role in supplementing government tax revenues and locally raised taxes since the operating companies pay taxes and resources can be mobilized.¹ It is important to note that the driving force behind investment in other countries such as Saudi Arabia is due to new emerging markets and potential for growth in those regions due to availability of resources. Other driving forces include competition and changes in market dynamics.² It is also important to mention that the multinational corporations (MNCs) help fill the gap in management entrepreneurship and skill providing resources in the form of management experience, entrepreneurial capabilities, and technological skills that can be conveyed to the local citizens through training programs and learning by doing.³ A report by UNCTAD showed that developing economies had attracted FDIs totaling to $334 billion in the year 2005, a number that has increasingly grown over time.⁴ As a

² Ibid.
result, Foreign Direct Investment (hereby abbreviated as FDI) has emerged as a global phenomenon eliciting research interest.⁵

FDI can play a crucial role when it comes to economic growth and development process and is considered a vital instrument through which economies are being integrated at the phase of production into the globalization world economy by bringing a package of assets, including capital, technology, managerial skills, and access to foreign markets.⁶ Importantly, one should bear in mind that a number of questions remain beyond the common language.⁷ On the investor side, for instance, FDI may be primarily to gain access to natural resources or other strategic assets such as research and development.⁸

Just like any other country, Saudi Arabia has both favorable and unfavorable factors when it comes to foreign direct investments. For instance, the availability of oil is a major contributing factor when it comes to investment while poor business policies and high levels of unemployment make up the negative side.⁹ All in all, it is important to note that Saudi Arabia has executed a new foreign investment code that avails foreign investors the same benefits, incentives, and guarantees offered to Saudi Arabians and companies. The statute permits foreigners to own property either independently or with a Saudi partner. Moreover, it permits investors to remit funds abroad and reduces taxes by 15% for foreign entities with an annual profit in excess of 100,000 saudi riyal.¹⁰ In reference to the above code, the Saudi Arabian General Investment Authority (SAGIA) must make decisions within 30 days after receiving

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⁷ Hussein, Impacts of foreign direct investment, 367
⁸ Ibid.
¹⁰ Hussein, Impacts of foreign direct investment, 369.
the needed documents. Through these efforts together with other policies such as sponsorship of foreign investors and issue of licenses by SAGIA for various activities has seen a remarkable increase of FDI in the last two decades. It is important to note that SAGIA was founded under the Council of Ministers Resolution No. 2 dated 1421/1/5 H corresponding to 2000/10/2 G. Its main role is to manage investment affairs in the kingdom, including foreign investment. Other roles entail the preparation of state policies that facilitate local and foreign investments, improving investment climate through plans proposal, checking and assessing the activities of local and foreign investments, and steering studies on investment prospects, among other roles.

**Definition of Key Terms**

The key terms for the study are: FDI, economic growth, multinational corporations, and determinants of FDI. Foreign Direct Investment (FDI) refers to the control of business ownership in one country by an enterprise that is based in another country. There are two types of FDIs. Green Field Investment is where a parent company setting up an associate or subsidiary company in the overseas country, sharing acquisition of a foreign business enterprise, and through Joint Venture or a merger its an agreement between parties to develop for a long-term by contributing equity, sharing profits. According to previous research, it depends on the type of industries and services to decide which of the foreign direct investments is efficient.

Economic growth refers to the increase in the productive capacity of a country reflected in the enhanced market values of the services and goods that are produced by that economy in a given period of time. Economic growth occurs when people utilize the available resources by rearranging them in a manner that makes

11 Ibid, 370.
12 Ibid.
these resources more valuable. Büthe and Milner (2008) define multinational
corporations (MNC) as an entity that controls or owns production of services and
goods in more than one nation other than its home country. Finally, determinants of
FDI refer to the factors that determine the rate of business ownership control by an
enterprise in a country other than its home country.14

CHAPTER 2

BACKGROUND

The Importance of Undertaking the Study

Foreign Direct Investment (FDI) has been regarded as a dominant tool for development to the receiving countries.\(^\text{15}\) FDI has not only improved the country’s capital formation, but also enhanced the balance of payments and creates employment within the host nation.\(^\text{16}\) In addition, FDI has had other spillover effects like the advancement of technology and business skills that enhance the efficiency and competition dynamism.\(^\text{17}\) Despite the implied significance of FDI on countries, little research has been undertaken regarding the impact of FDI in Saudi Arabia. As a result, there exists a gap in research that this study aimed to fill. The little research undertaken on the subject matter has shown that speculation by foreign firms has a positive effect on Saudi’s economy.\(^\text{18}\) Hegger’s (2003) findings showed that FDI helped bring some soundness to the Saudi economy, which engineered development in various industries. Rachdi and Saidi (2011) also acknowledged the fact that FDI in developing nations has shown to spur economic growth in these countries. They pointed out that countries that receive a large volume of foreign capital inflow are better positioned to experience faster economic growth than those that do not have high volumes of FDI.\(^\text{19}\) Alshareef (2013) also added that the concept of FDI and its impact on the Saudi Arabian society has not been widely analyzed. He pointed out that it has been widely accepted that investment by foreign firms has an impact on a country’s economy.\(^\text{20}\) Owing to limited studies on how foreign investment impacts the

\[\text{References:}\]
\(^{16}\) Ibid.
\(^{17}\) Isabel Álvarez and Raquel Marin. “FDI and technology as levering factors of competitiveness in developing countries.” *Journal of International Management* 19, no. 3 (2013): 236.
society in Saudi Arabia, it was important for this study to be undertaken. This study provided vital theoretical insights concerning the role that firms play in the economy, which is an emerging point of interest within the International Economics and Business field.

**Study Objectives and Aims**

This study seeks to find out whether foreign firms benefit Saudi Arabia, and the extent to which they do so. Bellak (2004) identified the need for analyzing the impact of foreign investment in other aspects of the society such as language and culture to be analyzed. Therefore, this study shall also be looking into the determinants of FDI in Saudi Arabia from the socio-cultural, economic and political perspective. In summation, this study aimed at fulfilling the following aims and objectives:

- To identify the impact of the foreign firm on the Saudi Arabian society.
- To critically review how foreign firms affect foreign direct investment inflows in Saudi Arabia given that the country is a major oil exporter.
- To examine the determinants of FDI in Saudi Arabia in relation to other developing countries.
- To determine how Saudi Arabia’s heavy dependency on oil revenue affects the country’s FDI.

**Current Issues and Historical Issues**

Participation of foreign firms in Saudi Arabia goes back to the 1960’s, but the increase started in 2000 following the passing of laws that allowed foreign companies to own 100% of their investment.21 It thus follows that foreign firms may impact the country economically, culturally and socially. In the world today, there is an increase

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in globalization as the technology continues to develop rapidly (Critchlow, 2009). Globalization has encouraged the growth of interdependence among different countries in the world. The business climate in the world and the growing competition has encouraged different companies to seek new markets elsewhere apart from the home countries where they are located.\(^{22}\) The motives of the different companies in the world to expand to new markets have been triggered by the internal and the external factors of the companies. The internal factors that influence expansion include the need to have marketing advantages, economies of scale, risk diversification and excess resources (Critchlow, 2009). The external factors that lead to the expansion of the companies to new regions include the foreign market opportunities, declining or stagnating home market and unsolicited orders (Varriale, 2012).

Saudi Arabia offers a good opportunity for the foreign companies as proposed by the UNCTAD’s investment report of 2007 that identified Saudi as having embarked on the creation of policies that helped the country to diversify its revenues and to reduce the dependency on the resources such as oil and gas that are subject to the global markets that are very volatile. The government initiatives resulted in the rise of foreign direct investments in the Saudi Arabian country (Smith, 2008). The foreign investments have mainly focused on the expansion of the manufacturing industries and have led to the development of the infrastructure and the improvement of services. The foreign companies have also focused on banking services and oil production. The oil production in the country is restricted to the domestic companies only, but the foreign companies are eager to obtain permission of oil drilling from the Saudi government (Smith, 2008). The foreign companies aimed at increasing the oil

production in the country to 4 million barrels a day by the year 2020. The country also has good opportunities for the expansion and the growth of the foreign investments. The establishment of the 2000 foreign investment act that was established by the Saudi Arabian General Investment Authority (SAGIA) has enhanced the business attractiveness of the country.\textsuperscript{23} The purpose of SAGIA was to help in the establishment of a one-stop shop that is authorized to issue licenses and to incorporate the new foreign and joint venture companies (Lohade, 2014).

However, despite the improvements in the business environment, the Saudi market still remains a big challenge for the new investors, especially the western investors (MacKinnon, 2000). More progress is needed in terms of the investment freedom and the property right protection and transparency.\textsuperscript{24} Saudi Arabia is one of the fastest growing countries in the Middle East region, and it possesses about 18\% of the total oil reserves that have been proven to the world. The government has a huge economic control on the drilling and export of oil. Most of the workers in the private sector are foreigners who are about 9 million. The private sector of the Saudi Arabia country accounts for about 40\% of the gross domestic product. Recently, the government of Saudi Arabia permitted the foreign investors to venture into sectors of the economy that include the power generation and Telecom. The foreign companies are encouraged to employ the workers who have the Saudi origin in order to help in the process of training them and increasing their skills in various sectors of the economy. The standards of living in Saudi Arabia are already high because of the status of the economy and the degree of transparency in the country. The corruption rate is very low in the country, and most of the funds are channeled to the relevant

\textsuperscript{23} Hegger, Investment in Saudi Arabia, 37.
\textsuperscript{24} Ibid.
areas such as education, development and health. The country is very stable politically, and this attracts foreign investments.

**Research Question**

The following research questions were asked:

- What impact do the foreign firms have on the Saudi Arabian society?
- Given that Saudi Arabia is a major oil exporter, how do foreign firms affect foreign direct investment inflows?
- Is Saudi FDI affected by similar determinants as other developing countries?
- How does Saudi Arabia’s heavy dependency on oil revenue affect the country’s FDI?

**Expected Outcomes**

The current study’s findings are expected to show a positive correlation between the nature of investment by foreign firms and the impact of foreign firms on the society. The study findings are also expected to show that Saudi Arabia has benefitted from FDI.
CHAPTER 3
LITERATURE REVIEW

Globalization and Foreign Investment

According to Abdel-Rahman (2015), the major source of income for Saudi is oil. The author argues that there is increased pressure on the country of Saudi Arabia to lessen its dependence on oil and to reform and liberalize its economy (Abdel-Rahman, 2015). In order to achieve the required liberalization and restructuring of the economy, the Kingdom has adopted various policies that encourage privatization and the promotion of investment. The author says that the adoption of the FDI policy by the Saudi Arabian country could see the development of the economy by enhancing foreign investment in the country and by diversifying the productive base of the economy of Saudi Arabia. The green field investments are expected to grow significantly in Saudi Arabia after the creation of the new investment law that permits these types of investments.

Fischer (2003) undertook a study to analyze the challenges of globalization in relation to FDI. He argued that the issue of globalization has widely been discussed by scholars as well as professionals alike. He described globalization as the interdependence between countries and points out that it has been increasing over the past years, brought out by various complex, impacting aspects of the society. Fischer (2003) also argued that the impact of globalization on the world economy is reflected in the increased cross-border trade between different countries in the world. He contended that globalization and its impacts are evident in the increased labor and capital flow among the countries in the world. Further, he identified increased capital flow to developing countries as one of interesting result of increased globalization

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activities (Fischer, 2003). Fischer (2003) argued that the capital inflow process occurred in stages and that not until recently did it take the form of foreign direct investment.

Fischer (2003) also explained the various impacts that globalization has had on foreign direct investment. He argued that the average rate of FDI around the globe has grown, which has had an impact on both the developing and the developed nations. He added that the volume of international capital inflows have exceeded the levels achieved in 1993. Fischer (2003) also identified the flow of capital across international boundaries and the economic activities that foreign firms controlled by other governments carry out in a country as the two concepts related to FDI. He also noted that activities carried out by foreign firms include employment, utilization of fixed capital, research and utilization of intermediate goods. Fischer (2003) recommended that all these activities have an implication on the economy and the society at large.

**Role that Foreign Investment Plays in the Local Economies**

According to Smith and Pamela (2008), the foreign direct investments play a huge role in the growth of the Arab world economies with the region reaping about 60 billion US dollars per year from the investments. The main beneficiaries of the foreign investments are the Saudi Arabia, Jordan UEA, Morocco, and Tunisia. Smith and Pamela (2008) further argued that the country of Saudi Arabia has topped the Arab world in reaping from the foreign direct investments with an income of 18 billion US dollars per year from the investments. Smith and Pamela (2008) also added that the foreign direct investments can bring the funds that are needed to boost areas such as education, health, utilities, telecoms, tourism, housing, infrastructure, and

26 Stanley Fischer, Globalization and Its Challenges, 4.
construction. FDI helped create new jobs in the country and new goods and services (Smith and Pamela, 2008). The country also benefitted from the improvement in technology, marketing and the access to export markets that the foreign direct investments facilitate.

In a more recent study, Alshareef (2013) investigated the benefits as well as the costs that foreign direct investment has had on the Saudi Arabian financial sector. He argued that Saudi Arabia has experienced an increased inflow of capital from foreign direct investment, a factor that motivated the study. He further added that an increase in studies that reveal the impact of FDI on local economies and the desire to investigate other impacts of FDI on the host nation are the factors that motivated the study.\textsuperscript{27} The paper acknowledged the fact that FDI in Saudi Arabia has been studied to some extent, but there still exists a wide gap in terms of literature that discuss the impact FDI has had on Saudi Arabia as a nation. Alshareef (2013) also analyzed how previous studies have handled the topic and found that FDI is an important driver of economic development and that many countries around the globe have strived to attract foreign investors. Even though Alshareef (2013) regarded the research on the impact of FDI in the Saudi context as not a new concept, he argued that the data and findings from this study would contribute to the understanding of the general trends and the impact of FDI on the financial institutions around the country. Regardless of its significance and contribution to this study, Alshareef ‘s (2013) research the overlooked the overall impact of FDI on the Saudi Arabian economy by restricting its analysis to financial institutions.

Bellack (2004) outlined a number of interesting facts about FDI and the role of multinationals in local economy. It was pointed out that multinational industries have

\textsuperscript{27} Nasser Alshareef, \textit{The Opportunities And Limitations}, 23.
higher levels of labor productivity compared to other firms in the national industries. Additionally, it is stated that multinational companies employ a higher number of administrative personnel compared to other types of firms. Bellack (2004) also stated that between 1965 and 1969, studies revealed that foreign firms in the UK were more profitable than domestic firms. He argued that descriptive analysis couldn’t be accurately used to explain the performance gap between foreign-owned firms and domestic firms. The main reason behind this is that there are often few foreign firms compared to domestic firms, most of which are middle and small-sized. Bellack (2004) further analyzed why researchers are increasingly interested in comparing the performance of domestically owned firms and foreign-owned firms and found that empirical evidence comparing foreign-owned firms and domestic firms are still scarce, but the available evidence revealed that foreign firms perform better than domestic firms.

In a similar study to that of Bellack, Haskel and his colleagues investigated whether domestic firms gain productivity spillovers from foreign firms. They also explored the extent to which firms would go to pay in order to obtain foreign direct investment. Their study findings showed that the presence of foreign firms in a country raises the total productivity levels of the industries in which the firms operate in. Just like Fischer, Haskel and his colleagues identified the rising level of FDI as an important phenomenon in globalization. They argued that for many governments, decisions on whether to give multinational firms or local firms incentives have been a major policy issue. Haskel et al. (2007) also stated that over the past few years, most governments across the globe have reviewed their laws in order to encourage more

29 Ibid
foreign firms to invest there. The tendency of governments to come up with policies has not only become common in developing countries, but also developed countries are offering attractive incentives to foreign firms.

**Impact of Foreign Firms on Local Investors**

According to Mahmoud Haddad and Sam Hakim (2015), the banking sector of Saudi Arabia experienced the problem of the global liquidity crisis because the government is trying to manage inflation, and at the same time lend the private-sector banks (Hakim, 2015). The liquidity management problem has resulted partially from the foreign banks in the country that are greatly affected by the global financial crisis. The two authors argue that the foreign-owned banks have suffered from the crisis more than the domestic bank because the process of lending from the international markets is more difficult. On the contrary, the foreign firms have boosted the local investors significantly. The foreign banks are well endowed financially, and they provide the local investors with loans to boost their businesses. The loans usually have a low interest rate, and this favors the local investors significantly. The foreign firm also makes partnerships with the local investors and they help them to expand and to market their goods and services.

Bellack (2004) made a comparison between the impact of foreign firms and that of local firms and made the argument that when foreign and domestic firms are compared, performance gaps are evident. In his article, Bellack (2004) analyzed a number of selected studies and reported what these studies found in regard to the gap in performance of foreign and domestic firms. He argued that the gaps in performance between the domestic and foreign-owned companies are visible in a number of areas such as technology, productivity levels, skills, wages and profitability. Bellack (2004) also discussed the factors that led to differences in the performance of foreign and
local firms, pointing out that the better performance exhibited by foreign-owned firms can be explained by multinational theory which argues that the better performance of foreign firms is attributed by these firms being multinationals as opposed to being from a different country.

Unlike Bellack (2004) who focused on both the impact of FDI on both developing and developed countries, Seyoum and his colleagues focused only on the impact that FDI has had on developing economies, mostly the African countries. Their findings showed that exogenous components that characterize a foreign direct investment do not have a significant impact on economic growth. The study identified the existence of a stable and strong industrial base as one of the major determinants of foreign investment. Additionally, countries that have financial systems that are better established were found to benefit from foreign investment more than those that do not.

In their analysis of the impact of foreign forms in local economies, Haskel and his colleagues examined the relationship between multinationals and the theory of productivity spillover (Haskel et al. 2007). They argued that most of the multinationals hold the assumption that they have knowledge assets, which can be transferred to other firms outside the parent country. The deploying of this knowledge impacts the performance of the firm in the host country as well as the general economy. Additionally, Haskel et al. (2007) are of the view that the knowledge transferred may also spill over to domestic firms, thus impacting the performance of domestic firms as well. The article is of the view that FDI inflow to a particular industry increases the productivity of domestic firms.

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31 Ibid.
Rachdi et al. (2011) examined the impact of foreign investment on both developing and developed economies. They identified liberalization of capital inflow has emerged as one of the important ways through which both the developed and the developing nations can spur their economic growth. The study found that financial liberalization has a positive impact on economic growth and that there is need for governments to ensure that their financial systems are liberalized.

Social and Cultural Impact of Foreign Firms on Local Communities

FDI has created avenues for foreign firms to introduce the western products in Saudi, and they have brought their culture in the country through the interaction of the foreign employees with the people of Saudi Arabia. The foreign investments have contributed greatly to the development of the local communities through financing of various sectors such as the education sectors and health sectors (Wrampelmeier, 2006). Sponsorship programs that are funded by the foreign investors are also very common to the local communities. Metra and Golder (2002) also identified knowledge levels as well as cultural differences between the host country and firm’s parent country as some of the reasons that influence market entry by foreign firms.

Challenges Faced by Investors in Foreign Countries

The foreign investments have faced various challenges in Saudi Arabia. The major challenges have been the lack of understanding of the cultural practices of the Saudi Arabia citizens by the foreign investors (Wrampelmeier, 2006). Saudi Arabia is a Muslim country, and there are various religious restrictions that are imposed on business activities such as interest rates that are charged when taking business loans. Marketing is also hindered because of various restrictions.

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Local Culture and how it shapes the Operations of Foreign Firms

The local culture of the Saudi Arabian people has influenced the way business is conducted in the country significantly (Wrampelmeier, 2006). The firms have to adapt to the Muslim religion rules and they have to give the employees the right to practice their faith and to observe the important days in the religious calendar of the Muslims (Varriale, 2012).

Foreign Firms in Saudi Arabia and their History

Metra and his colleagues analyzed the factors that shape the foreign market entry strategies that firms employ. They argued that a number of studies have investigated the impact of experience and learning on the market entry strategies that foreign firms employ, but studies on how the firms’ operations impact their entry into foreign firms still remain uninvestigated. The study analyzed the market entry strategies of 19 multinational firms, pointing out the barriers and the general impact that the strategies had on how the firms are perceived in the host countries. To analyze the impact of market knowledge, cultural variables and economic variables on the market entry strategy, the study utilized a hazard model with 722 observation entries. The study findings showed that one of the most important determinants of market entry by foreign firms is the cultural similarity between the domestic market and the parent country for the foreign company. Metra et al. (2002) also added that for countries that share similar culture, entry and acceptance of the firm by the local populations, it would be much easier to comparer countries with different cultural backgrounds. They reported that when the economic and cultural factors are

34 Ibid.
compared, economic factors emerge as having a greater impact on the foreign firm’s market entry (Metra and Golder, 2002).

**Role of Foreign Firms in Saudi Arabia**

Saudi Arabia, just like other developing countries, has highly benefitted from FDI. The foreign firms in Saudi Arabia include large multinational banks such as the Gulf International Bank and the Qatar bank. Other companies include foreign manufacturing companies and telecom companies. Ramady and Saee (2007) analyzed the role of FDI in the Saudi economic with a focus on how foreign direct investments have transformed Saudi’s economic growth. They pointed that Saudi Arabia has made major milestones towards increasing their efforts to attract foreign investors. Their study findings showed that foreign direct investment has led to the creation of employment increased the GDP of Saudi Arabia as well as that of the domestic firms that have benefited from new technologies and production techniques those foreign firms have introduced in Saudi Arabia. The study also reported that the inflow of capital from FDI has also increased in Saudi Arabia. It further investigated how managers and leaders in Saudi Arabia perceive foreign firms, pointing out that managers as well as leaders in Saudi Arabia welcome the whole concept of FDI but have ambivalent attitudes towards the benefits that FDI may bring to the country. The study also argued that foreign firms have an impact on the consumer behavior in host countries, especially when the firms introduce new products. Ramady and Saee (2007) also noted that FDI has led to the creation of new infrastructure and employment opportunities for a sizeable number of the county’s population.

Similarly, Roberts and Abdulaziz (2009) examined the recent trends in the inflow of FDI to Saudi Arabia. They argued that it has widely been expected that FDI

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35 Mohamed Ramady and John Saee, Foreign Direct Investment, 40.
activities should contribute to the development of the host nation. The study found that FDI in Arabian countries has increased over the past few years. Among the factors that were identified as playing an important role in attracting FDI in Arabian countries include availability of the right infrastructure, trade openness as well as the quality of institutions in these countries. The overall economic performance of Saudi Arabia was pointed out as having played an important role in attracting FDI.

Likewise, Tarique (2011) examined the role of FDI has had on the Saudi Arabian economy and argued that the impact of foreign firms in countries across the world is reflected in the way governments tries to attract investors into their countries. According to Tarique (2011), this was motivated by the expectations that the government would get spillover benefits, which would go a great way in improving the national income levels. The findings showed that the inflow of FDI into Saudi Arabia is influenced by a host of factors, the main one being privatization, GDP and its growth rate as well as import and export. The findings also showed that the relationship between net FDI inflow and GDP growth is a positive one while that its relationship to privatization and exports and imports is a negative one, which indicates that FDI exhibits trade sensitivity. In his conclusion Tarique (2011) argued that increasing the level of FDI is crucial to the Saudi economy since it is a sure way through which self-reliance, stability and sustainable growth can be achieved.

Comparison between Saudi Arabia and Turkey

Based on the recently released report by UNCTAD, Turkey is the leading recipient of FDI inflows in the Western Asian block, followed by Saudi Arabia.

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39 Ibid.
Turkey, unlike Saudi Arabia, has undertaken some structural and legislative reforms to attract foreign investments (Cambazoglu and Karaalp, 2014). These include tax exemptions and the formation of Investment Support and Promotion Agency of Turkey whose mandate is to attract foreign investors. In addition, Turkey’s economic and political stability as well as foreign-friendly and accommodative culture have been attributed to its remarkable performance in attracting foreign investments.\(^41\)

In 2006, Turkey recorded the highest FDI inflows, which was partially because of the public-private partnerships’ development of major infrastructure projects. Undertaking effective measures such as consolidating intellectual property rights, administrative restructuring, ending the FDI screening, and undertaking structural reforms to align Turkey’s economy in preparation for the EU accession are favorable steps forward.\(^42\) However, in 2012, FDI inflows reduced as a result of the euro zone crisis but began to rise in 2013, where they increased to $10.1 billion, which was a 5.3% decrease as compared to 2012.\(^43\) It is also worthwhile to note that the presence of wars and political instability not only in Turkey and Saudi Arabia, but also in other countries would result in reduced FDI due to fear of losses and insecurity matters.

On the other hand, FDI constitutes a large proportion of Saudi Arabia’s economy.\(^44\) The 2013 Country Profile data released by UNCTAD showed that Saudi FDI inward stock totaled to $187 billion by the end of 2011, which amounts to 34% of Saudi’s GDP. On the contrary, the FDI outflows by Saudis were minimal, totaling to only 5% of the GDP. In the last ten years, Saudi has risen as a major FDI receiving

\(^{41}\) Cambazoglu and Karaalp, *Does foreign direct investment,* 444.
\(^{42}\) Ibid.
\(^{43}\) Ibid.
country.\textsuperscript{45} For example, between 1990 and 1999, Saudi’s annual average FDI was $251 million, which increased threefold between 2000 and 2004 to $772 million and then skyrocketed to an annual average of $24 billion between 2005 and 2011. Based on these statistics, it is evident that 2005 was the defining moment for Saudi, as the FDI inflow tremendously grew six times more from $2 billion to $12 billion, a trend that was maintained until 2008. Since 2009, there has been a decline in the FDI inflows, a trend attributed to the global economic crisis and the Middle East crisis. In 2011, the FDI inflow stood at $16 billion\textsuperscript{46} as compared to Turkey’s 16.171\textsuperscript{47} billion.

\textsuperscript{45} Ibid.
\textsuperscript{46} Cambazoglu and Karaalp, \textit{Does foreign direct investment}. 444.
\textsuperscript{47} Bukhari Sillah, \textit{Human capital}, 5
CHAPTER 4

METHODOLOGY

Study’s Focus

The focus of this study was to investigate whether the investment made by foreign firms in Saudi Arabia benefit the country, and to what extent they impact the country’s economy. In order to meet this research purpose, a regression was created.

Selection and Access of Data

Data for this study was obtained from: The world development indicator Saudi Arabia which is available online on the World Bank website. Data on the country’s employment levels, economy and growth, infrastructure, the private sector as well as the financial sector and the country’s external debt was collected from the Ministry of Finance in Saudi Arabia which is an open source website. Data that compares the financial performance of foreign firms and domestic firms, the total number of jobs provided by both the domestic and local firms and the country’s GDP growth over the past years in relation to the number of foreign firms each year was collected from the Saudi Arabian Ministry of Commerce, Ministry of Economy and Planning, Saudi Arabia General Authority and Center Department of Statistics and Information of Saudi Arabia websites.

Information Gathering Method

The data collection process employed a mixed method approach that incorporated both qualitative and quantitative research approaches. The study relied upon secondary analysis as the research design, which implies that the study relied on data drawn from secondary published data, mostly websites as stated above. Secondary analysis was found to be efficient because it collects data from diverse
sources that provide accurate and rich information on the study topic.\textsuperscript{48} The data collection method started with auditing of the data sources for their credibility, originality and purpose. The purpose of data source’s auditing was to ensure that the data provided was fit for the study.\textsuperscript{49}

After identifying and auditing the data sources, the second step was to divide the research questions into qualitative and quantitative depending on whether they measure the frequency and magnitude of concepts (quantitative) or they explore the meaning and understanding of concepts (qualitative) as suggested by Creswell (2009). After grouping the type of the data into their particular categories, both the qualitative (narrative) and quantitative (numeric) data were collected concurrently.

**Data Analysis Methods**

Since the study obtained two types of data, the qualitative data was analyzed using thematic analysis while the quantitative data collected was confidentially analyzed using the E-views software.

The quantitative data analysis involved identification of both dependent and independent variables through regression analysis. First, a hypothesis that ‘investment by foreign firms has had a positive impact on the Saudi Arabian society’ was formulated. In testing this hypothesis, the following model was utilized

\[
Y \ (\text{FDI}) = B_0 + B_1 \ GDP + B_2 \ X + B_3 \ M + e_t
\]

where:

- \(Y\): Dependent Variable (Foreign direct investment).
- \(B_0\): Constant amount of investment(without any foreign investment).
- \(GDP\): Gross domestic product.
- \(X\): Exports.

---

M: Imports.

E: error.

After identifying the variables, the data was coded and categorized into themes. For example, statistical analysis confidence intervals, weights, and P-Values were set for the identified variables, which was followed by a diagnostic analysis. The diagnostic analysis helped in identifying the outliers and non-normality. Finally, the data will be entered into the E-views software and analyzed for results.

**Rigor of the Study**

The following measures were taken to enhance the study’s rigor. First, the research was undertaken in a cautious and professional manner. Data was analyzed using statistical data analysis tools that are more credible and dependable. Secondly, the data used was collected from credible sources (government websites). Third, the study used a mixed method that combined both qualitative and quantitative approaches. As a result, the weaknesses of each approach was compensated by the other, and thus; enhancing the credibility of the findings. Fourth, the use of quantitative data allowed for generalization and inferences drawing. Moreover, quantitative research approach allows for manipulation of variables, which enhances the conformability and transferability of the study findings.\(^{50}\)

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\(^{50}\) Creswell, *Research Design*, 45.
CHAPTER 5
EMPERICAL RESULTS

Findings and Results

This study aimed at analyzing whether foreign firms benefit Saudi Arabia, and the extent to which they do so. The results of the study show that FDI is benefiting the country as it has tremendously and positively impacted the Saudi economy. The findings further show that the levels of FDI have sharply increased since 2000, a trend that is associated with the Foreign Investment Act, which was passed in 2000. The pattern and nature of FDI can be explained using the number of FDI projects, the size of investment and the industry/sector. Appendix A shows both the foreign owned FDI and joint venture FDI from 1997-2006 while appendix B shows the number of foreign owned FDI projects in Saudi Arabia by sector as from 1997 – 2006.

The results show the foreign owned FDI projects constituted 20% (3,522 projects) of the total projects and have had a mix of upward and downward increase and decrease over the years. On the other hand, the number of joint venture FDI constitutes of the large share of 80% (14,147 projects) of the total FDI projects and that it has been constantly increasing since 1997. However, the total number of FDI projects (Foreign Owned FDI + Joint Venture FDI) has constantly been increasing over the year. This implies that joint venture FDI projects are more familiar in Saudi. The reason for this discrepancy is because the Saudi government encourages joint venture over foreign owned projects. For example, to start a joint venture project, the investors require only one license. However, to start a foreign owned project in Saudi,
the investor would require multiple licenses and has to undergo a long vetting process.\textsuperscript{51}

Appendix B shows the number of FDI projects by sector, and construction sector is the leading industry with the highest FDI projects followed by services, industrial, mining and lastly, agriculture. Agricultural projects are the least because of the Saudi non-farming culture and also due to the poor weather climate for agriculture.\textsuperscript{52} As a result, the numbers of FDI agricultural projects have stood at two annually since 2001 when the rest of the sectors have grown tremendously. The year 2002 had the highest number of FDI projects, which is attributed to the 2000 Foreign Investment Act that made foreign investment easy.\textsuperscript{53}

Figures 22 and 23 also show the two countries Saudi Arabia and Turkey FDI, GDP, Exports and Imports performances. According to the data presented in figure 12, the Turkey FDI was growing from 2000 to 2006 where it reached its highest of 3.8 and then started dropping from 2008 to 2010. It picked up again in 2011 and then started dropping again in 2012. The downturn in 2006 is attributed to the global financial crisis while the upturn in 2011 is as a result of economic recovery and the structural and policy changes that Turkey made in preparation to be vetted as a EU member. The downturn in 2012 is as a result of the Euro crisis since European foreign firms are the major investors in Turkey. On the other hand, Saudi Arabia’s FDI was negative until 2004, where it tremendously increased from -0.13 in 2004 to 3.69 in 2005 (see figure 22). Since 2005, Saudi’s FDI increased to reach its highest point of 8.5 in 2009, before it sharply dropped to 1.25 in 2013. The main cause of the sharp drop in 2009 is the global financial crisis, which affected most American companies.


\textsuperscript{53} Hegger, Investmet in Saudi Arabia, 10
who are the major investors in Saudi Arabia. Unlike Turkey, Saudi Arabia was most affected and its FDI levels have been highly fluctuating.

The findings on the Saudi Arabian GDP show that the country’s GDP has been increasing from 2000 until 2007 where it took a sharp downward shift before recovering again in 2009, partly as a result of the global economic crisis (See figure 4). Saudi Arabia’s mean GDP for the 2000-2013 period is $412.7879 billion with the highest being $745.27 billion. Saudi GDP for this period had a skewness of 0.415, which implies that the country’s GDP is highly skewed. Saudi Arabia’s economic performance is different compared to that of Turkey. According to the data presented in Figure 12, Turkey’s GDP has been growing since 2001 and only slightly declined in 2007 and picked up again in 2009. The mean GDP for Turkey is $536 billion with the maximum being $820.21 billion and the lowest being $196.01 billion. The skewness of Turkey’s GDP is -0.24, which implies that it is negatively skewed. This shows that Turkey’s GDP has been consistent and stable as compared to that of Saudi. The graph below shows Saudi Arabia’s nominal GDP growth rate as compared to the real GDP growth rate.
As show in the graphs above, Saudi’s nominal and real GDP growth rates have been increasing since 2002 before taking a downturn in 2009 and then picking up again. Over the last decade, Saudi’s GDP increased in threefold to $580 billion, which accounts for 20% increase and 15% when inflation is taken into account. The rising oil prices and increased production is the main factor attributed to this growth rate, while the fall in the oil prices in 2008 as a result of the global financial crisis is the main reason for the economy’s poor performance in 2009.\textsuperscript{54} However, FDI inflows have also played a major role in the country’s growth rate as shown in the graphs below.

\textsuperscript{54} Bukhari Sillah, \textit{Human capital}, 5
When the inwards FDI investment flows for between 2000 and 2011 are compared to the real and nominal GDP growth rates, a positive correlation can be seen. The FDI inflows were at their peak in 2008 and took a downward trend in 2009 just like the real and nominal GDP. However, unlike the GDP which began to rise again between 2010 and 2011, the FDI inflows levels continued to decrease since 2008. These variances are as a result of various macroeconomic factors. While the
Saudi economy was able to quickly recover from the 2008 recessionary crisis and hence the positive GDP upturn as from 2010, the foreign investors who came from countries like the U.S. were highly affected because the Western countries were hit severely as compared to Middle East economies.55

I find also show that Saudi Arabia’s import levels were low between 2000 and 2004 after which they reached a high peak in 2009 and then started reducing gradually. The mean imports were $28.96 billion, and the maximum import was $37.77 billion while the lowest was $23.78 billion (See figure 6). Figure 17 shows trends in Turkey’s imports. The findings show that Turkey’s imports have been on the increase and only reduced in 2007 and picked up again in 2009. The mean imports for Turkey stands at $26.7 billion, with the lowest being $23.09 billion and highest $32.6 billion. This shows that Turkey has slightly lower imports than Saudi.

Similarly, Saudi exports were lowest between 2000 and 2005 before they rose steeply to reach there highest in 2009 before reducing again until 2011 where they gained the increasing momentum (See Figure 7). The mean exports were $51.4 billion, with lowest exports being $62.1 billion and highest $37.7 billion. This implies that Saudi economy has a positive balance of trade because its imports are lesser than its exports, which is good for the economy. The findings displayed in figure 15 show that the mean exports for Turkey stands at $23.6 billion, with the lowest being $20.1 billion and highest $27.4 billion. Unlike Saudi Arabia, Turkey has very low exports, which imply that the balance of trade for Turkey is negative and unfavorable. The reason behind this is that Saudi Arabia is an oil-rich country and exports more oil as compared to Turkey whose main export is agricultural products, electronics, clothes, and automobiles whose value is lower as compared to that of oil and mines.56

55 Bukhari Sillah, Human capital, 6.
56 Cambazoglu and Karaalp, Does foreign direct investment, 440.
An analysis of Saudi Arabia’s FDI showed that it has been increasing gradually since 2000 to 2004 and then steeply rose between 2004 and 2008 before taking a decline curve until 2012 where it has started gaining momentum again (See Figure 9). The mean FDI was found to be 2.8, with the minimum being -1 and maximum being 8.50. Further, the standard deviation of Saudi’s FDI was found to be 3.18. Figure 9 shows Turkey’s FDI whose mean is 1.7, minimum FDI is 0.37 and maximum FDI is 3.8. Comparing Saudi Arabia and Turkey’s FDI, it is evident that Turkey has had a higher FDI as compared to Saudi Arabia.

Figure 11 shows Saudi Arabia’s competitiveness. The country’s competitiveness is measured by the ability of the country to produce goods and services that meets the international market tests. Saudi Arabia’s competitiveness was gradually increasing from 4.5 in 2007 to 5.2 in 2012 before reducing to 5.05 in 2014. When the data regarding the competitiveness of Saudi is compared with the FDI projects and FDI levels, a similar trend can be seen. When Saudi FDI levels were low, the competitiveness was also low. However, in 2012 when Saudi FDI levels and number of FDI projects were highest, Saudi competitiveness was highest also. This implies that FDI and the country’s competitiveness have a positive relationship. Turkey’s competitiveness as shown in figure 10 gives a different picture. The mean competitiveness for Turkey is 1.7 with the highest being 3.8 and lowest 0.37. This implies that Saudi Arabia is more competitive than Turkey.

The overall conclusion drawn from these findings is that FDI enhances the economic growth and competitiveness of the recipient country, which is beneficial to the firms, both local and foreign. The findings also show that the higher the FDI levels of the host country, the higher the competitiveness and economic growth measured in GDP. Therefore, countries are benefiting from FDI.
Recommendations

The research has identified that Saudi has many unfavorable determinants that hinder foreign investment. Also, the study has portrayed that Turkey has immensely benefited from FDI due to the structural changes it made in 2012. Similar findings were also seen in the case of Saudi in 2000 when it passed the Foreign Investment Act. These findings indicate that developing countries with favorable policies and measures are more likely to benefit from foreign investment as compared to those that have unfavorable policies and measures. Therefore, this study recommends for policy and structural changes in developing countries as a means of attracting more foreign investors.

The study has also identified the political stability of a region as a major determinant of FDI. While Saudi is politically stable, the surrounding region of Middle East is faced with many political challenges including the Arab uprisings in Libya and Egypt and the terrorist scares in Iraq. As a result, many investors shy away from the entire region regardless of the individual country’s stability. Therefore, this study recommends for a peace and political stability in Middle East in order to attract more investors.

Conclusion

The purpose of this study was to analyze whether foreign firms benefit Saudi Arabia, and the extent to which they do so. The study relied upon FDI data generated between 2000 and 2013. While this data is inclusive and up-to-date, it may not give a clear picture of the economic changes because 13 years may be a short period to analyze economic changes. Therefore, for the future studies, it would be better to use data lasting between 30 and 50 years, because such data gives one a clear roadmap of the economic changes.
Secondly, the study only focused on Saudi Arabia and used Turkey for comparison purposes. The transferability of this study could be strengthened by making a comparison using two other countries, one whose economy FDI inflows are below Saudi Arabia, another with similar FDI inflow as Saudi and the other whose FDI inflows are above Saudi’s. Turkey and Saudi Arabia seem to be on the same level. Therefore, it would be good to include other countries like Kuwait or UAE (they have higher FDI inflows than Saudi) and Egypt (has lower FDI inflows than Saudi).

Thirdly, since the economic crisis seem to have an effect on FDI; it would be interesting for future researchers to examine the impact of economic crisis on FDI. Some of the case studies could be the 2008 global financial crisis or the euro crisis. It would also be a significance milestone to study the impact of political unrest on FDI. All in all, the future of Saudi Arabia looks bright due to vast oil reserves and investment in the transport as well as in other industries. The government of Saudi Arabia has also invested heavily on startups and financing many students to study worldwide in the best universities with the aim of increasing innovation thereby diversifying the economy.
References


<table>
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<tr>
<th>Year</th>
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<th>Joint Venture FDI</th>
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<tr>
<td></td>
<td>Project</td>
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</tr>
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<td>344</td>
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<tr>
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<td>20%</td>
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</tr>
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<td>336</td>
<td>20%</td>
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<td>19%</td>
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<tr>
<td>2004</td>
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<tr>
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<td>362</td>
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<tr>
<td>2006</td>
<td>461</td>
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## APPENDIX B

### FOREIGN OWNED FDI PROJECTS IN SAUDI ARABIA

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<tr>
<th>Year</th>
<th>Industrial</th>
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<td>38</td>
<td>20</td>
<td>0</td>
<td>376</td>
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<td>501</td>
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<tr>
<td>1998</td>
<td>40</td>
<td>23</td>
<td>0</td>
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<td>68</td>
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<tr>
<td>1999</td>
<td>53</td>
<td>42</td>
<td>0</td>
<td>391</td>
<td>69</td>
<td>555</td>
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<tr>
<td>2000</td>
<td>70</td>
<td>22</td>
<td>1</td>
<td>394</td>
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<td>560</td>
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<tr>
<td>2001</td>
<td>330</td>
<td>329</td>
<td>2</td>
<td>384</td>
<td>78</td>
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<tr>
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<td>533</td>
<td>2</td>
<td>403</td>
<td>81</td>
<td>1394</td>
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<tr>
<td>2003</td>
<td>212</td>
<td>385</td>
<td>2</td>
<td>420</td>
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<tr>
<td>2004</td>
<td>193</td>
<td>266</td>
<td>2</td>
<td>694</td>
<td>141</td>
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<tr>
<td>2005</td>
<td>174</td>
<td>466</td>
<td>2</td>
<td>621</td>
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<td>1485</td>
<td>2086</td>
<td>9</td>
<td>3682</td>
<td>739</td>
<td>8457</td>
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</table>
FIGURE 4: Saudi Arabia GDP.

Mean: 412.7, Min: 183.0, Max: 745.2, Std.Dev: 201.7

FIGURE 5: Saudi Arabia GDP data analysis.
FIGURE 6: Saudi Arabia imports.

Mean: 28.9, Min: 23.7, Max: 37.7

FIGURE 7: Saudi Arabia imports data analysis.
FIGURE 8: Saudi Arabia exports.

Mean: 51.4, Min: 39.8, Max: 62.1

FIGURE 9: Saudi Arabia exports data analysis.
FIGURE 10: Saudi Arabia FDI.

Mean: 2.8, Min: -1, Max: 8.50, Std.Dev: 3.18

FIGURE 11: Saudi Arabia FDI data analysis.
FIGURE 12: Saudi Arabia competitiveness.

FIGURE 13: Turkey GDP.
Mean: 536.5, Min: 196.0, Max: 820.2

**FIGURE 14**: Turkey GDP data analysis.

**FIGURE 15**: Turkey exports.
Mean: 23.6, Min: 20.1, Max: 27.4

**FIGURE 16**: Turkey exports data analysis.

**FIGURE 17**: Turkey imports.
Mean: 26.7, Min: 23.09, Max: 32.6

**FIGURE 18**: Turkey imports data analysis.

**FIGURE 19**: Turkey FDI.
Mean: 1.7, Min: 0.37, Max: 3.8

**FIGURE 20:** Turkey FDI data analysis.

**FIGURE 21:** Turkey competitiveness.
<table>
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<th>Year</th>
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**FIGURE 22**: Saudi Arabia FDI, GDP, exports and imports.
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**FIGURE 23**: Turkey FDI, GDP, exports and imports