

Impact of Foreign Direct Investment (FDI) on Manufacturing Industries: A View of Domestic Industries in Oman

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Abstract

The major objective of this study was to assess the spill over effect of Foreign Direct Investment (FDI) on domestic firms in Oman. Specifically, to assess the relationship between the FDI policy framework and FDI net inflows in Oman. Additionally, the impact of FDI net inflows on job creation in Oman was considered. The study utilized a quantitative research method where primary and secondary data were obtained from Oman's World Bank database (1984-2018) and through a field survey of manufacturing firms from diverse sectors. The primary data was collected from a research questionnaire administered to 410 respondents from nine industrial sectors, namely: Textile, Petroleum goods, Electronics, Automotive, Food & Beverages, Agriculture & Fishery, Publishing, Chemicals, and Pharmaceuticals. The outcomes of the study revealed that labour market policy and administrative procedures as a tool of FDI policy framework affect FDI net inflow in Oman. Other tools (i.e., trade policies and competition policies) of the FDI policy framework has a positive impact on FDI net inflow but did not indicate a significant impact on FDI net inflow. This study contributes significantly to the literature on the awareness level of local firms being a stakeholder of FDI policy. The study also provides an insight into the practical side as how FDI could be utilized as a device for promoting and strengthening a successful FDI policy. The study has certain limitations too: lack of actual data of jobs created through FDI, and lack of some important variables such as the business environment in current scenario. Overall, the study has successfully provided a useful insight into the phenomenon under investigation.

Keywords: FDI, Manufacturing Companies, Spillover, Economic Growth, Oman

1. Introduction

FDI is a vital source of foreign funding and can transform economies via the exchange of technological savvy, organizational and administrative expertise, and access to global markets, investment growth, productivity boost, and greater employment opportunities (Echandi et al., 2015). Foreign Direct Investment (FDI) is termed as an investment dedicated to procuring a long-lasting return in a trade, carrying out it is in an economy that is different from an investment firm, the motive behind this is to get a long-lasting return and to have an efficient marshal for the management of the business. Although the advantages of FDI are far-reaching, they could only be accessed with the help of the nation's specific policy interventions. Evidence shows that free trade and investment, accelerate countries' access to the world value chains.

Indeed, the transfer of expertise from international companies takes place not only in the form of technical developments, but also in the form of information and experience of management in level output. A thorough assessment of the spillover impacts of FDI will therefore involve not only technological changes, but also increases in production efficiency. Nevertheless, only a few research has assessed the impact of FDI's spillover as a deciding factor in comparative productivity growth or distance to the boundary. Researchers probed the effect of FDI's spillover in highlighting performance variances through Stochastic Frontier Analysis (SFA) (Mastromarco and Ghosh, 2009; Suyanto et al., 2009) or Non-stochastic Analysis (SFA), Data Analysis on Envelopment (DEA) (Kravtsova, 2008).

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It is quite difficult to come across some research works on efficient productivity and technical innovation as channels of FDI output growth. International firms are boosting competition, which also encourages domestic companies to improve efficiency.

Local businesses can benefit from international subsidiaries on how to procure, produce, transmit, handle, and adapt the technology. The importance of this impact improves with the resemblance of products manufactured by international companies (Javed & Husain, 2021). They could emulate international corporate behavior. Secondly, technologies, research and development indirectly propel local businesses (Cheung et al., 2004). The availability of modern products in local nations from foreign subsidiaries will encourage and allow local inventors to engage actively in R & D activities that result in innovation and creativity. As a result, local companies will improve their management skills and manufacturing technology, quality and achieve higher performance. Another channel for spillovers to FDI output is associated with labor mobility. Foreign companies play a pivotal role in the training and education of domestic employees than local companies. Through such training and successive job experience, employees get to know the technology and manufacturing capabilities of foreign firms (Husain & Javed, 2019a). The likelihood of local businesses employing people who have worked for a multinational corporation in the past is high (Glass and Saggi 2002).

Oman's FDI growth rate in 2017 was 15 percent relative to the fourth quarter of 2016 (Oman News Agency, 2018). The United Kingdom, led by the UAE, Kuwait, Qatar, Bahrain, the United States, India, and Switzerland, leads the list of countries that have invested in Oman. In 2017, the oil and gas industry received the highest OMR FDI of 5.16 billion, compared to the other sectors (Oman News Agency, 2018). Mellahi et al. (2003) stated that political and economic stability were the two most significant reasons for investing in Oman. Mina (2007) used data from 1980 through 2002 to do a research on the components of FDI in the GCC region. She concluded that oil capacity, use, and price adversely affected FDI, while institutional efficiency, trade accessibility, and infrastructure development motivated FDI. Consistent findings were published in research for the period 2003 to 2013, which discovered that natural resources harmed the overall FDI inflow in the GCC area (Elheddad, 2018). Findings for Arab countries also indicate a strong and important institutional quality impact for the period from 1984 to 2012. Tactically, Oman derives benefits from a shared impact of desert regions, inland mountainous terrain and related valleys, and very rich soil within the southern and geographically located shores, which all give the Sultanate a moderately prosperous agricultural, agro-processing, and fishing opportunity and unique maritime routes to India and the Far East to African countries and European nations (Husain & Javed, 2019a, 2019 b; Javed, Atallah, Aldalaien, & Husain, 2019; Javed & Husain, 2020, 2021; Javed, Husain, & Ali, 2020; Javed, Malik, & Alharbi, 2020). The Sultanate of Oman is wealthy in oil and natural gas to 5.4 barrels of oil and 23 trillion cubic meters of gas officially discovered in 2017. Despite several incentives and policy measure in 2020 which has removed the condition of minimum 30% ownership, the inflows of FDI accessed accesses to a limited number of sectors. Other policies: legal framework of dispute settlement, arbitration, investment incentives, bankruptcy laws, and property protection laws make Oman more attractive for investment from abroad (US Department of State, 2020). Therefore, contemplating the current situation, this study examines the effect of foreign direct investment on the survival of manufacturing industries in Oman and seeks answers to the following questions.

1. How do policies influence foreign direct investment into Oman?
2. How does FDI affect employment creation in Oman's industrial sector?

2. Literature Review

2.1 Concept of FDI

FDI is defined as an investment to obtain enduring profits and to acquire a minimum of 10% of the share of equity in a company that operates within a nation apart from investors from the host country (Mwilima, 2003). Kumar (2007) noted that FDI is in various forms, which may include, first, the infusion of equity capital by the parent company with the acquisition of shares in foreign partners. FDI takes place when investors located in one nation, the home nation; secures an asset in another nation with an asset management plan. According to Lipsey (2001), FDI is constantly being pursued by local companies that have benefited from the local market and these benefits include the licensing and technicalities posed to them when they ventured into the inaccessible market. FDI creates investments that may not be conceivable on their own with domestic assets. Working for large organizations linked to the global market, foreign investment enhances staff and administrative training; offers innovation that is not simply transmitted outside organizations and previously used by remote companies. It also provides more lucrative export prospects, linking the beneficiary economy to the global market such that new organizations within the host nation would be difficult to achieve (Lipsey, 2001).

2.2 Manufacturing Sector in Oman

Oman has emerged as a significant investment target in various organizations as of late, and the efforts made by publicly and privately-owned organizations, as the nation has seen crucial changes in the transport and logistics industry.

Oman currently has various types of economic zones, such as the Salalah Free Zone, the Sohar Port, and the Free Zone, as well as the Duqm Special Economic Zone Authority. Non-oil enterprises in Oman increased by 1.8 percent in 2017 compared to an annual average reduction of 1.2 percent in the recessionary period of 2015 – 2016.

2.3 Trend of FDI in Oman

The proportion of FDI inflows to GCC nations showed a decline from 1.74 percent to 1.65 percent from 2011 to 2013. Following the UAE, the Sultanate of Oman has an upstanding FDI movement path from the 1990s. In 2013, FDI recorded an increase of 56 percent compared to 9.2 percent in the UAE. Also, in conjunction with this nature of ventures in Oman, it has greatly improved to the extent that it becomes the third place even among nations of the Middle East and North Africa (MENA) and ranked as the 47th worldwide based on the efficiency of the favorable business environment due to the World Bank classification in 2013. International investment is seen as strong to Sultanate of Oman for different reasons. In any case, it implies the long-term strategic plan of the country "Vision Oman 2020" which centers on economic diversification to curtail its considerable dependence on oil as worthwhile support of the economy. Secondly, the oil wealth of the nation is small, so FDI can supplement the economy with extra resources, which will improve the viability of the country's economy.

2.4 Main FDI Driving factors in Oman.

As far as the Oman context is concerned, there is relatively little analytical work related to the FDI's driving powers in Oman. Al Shubiri (2016) probed FDI flows in Oman from 2005 to 2014, adopting two models, observed that annual GDP rise, fiscal balance to GDP ratio, investment spending as a GDP ratio, revenue velocity of large money and trade balance as a percentage of GDP, the stock traded volume and the MSM 30 share price benchmark are major determinants attracting FDI in Oman. Ibrahim and Sufian (2015) studied the motivations and predictors for FDI in Oman from 1980 to 2013, using the Co-integration and Error Correction Model (VECM) process, established that FDI flows in Oman were positively affected by the size of the market and mineral resources, and adversely affected by inflation levels and degree of transparency. The Granger causality results show that there is a unidirectional causality that runs to FDI from any scale of the economy and natural capital, indicating that FDI flows into Oman are characterized by motivations for profit-seeking and resource-seeking.

2.5 Determinants of FDI in GCC countries

Studies by Obwona (2001) highlighted the ability of FDI to contribute to the transfer of new technologies to host countries, and even indicate that this input may be responsible for more development than local investment would. Once again, the endogenous growth simulations were adopted in making this argument to analyze the impacts of FDI on spillovers of information. Thus, based on these results, it can be inferred that one way by which FDI boost economic growth is via technology transfer (which supports the concepts in the endogenous models of development). The subsequent phase is to explore to what magnitude FDI can contribute to such positive externalities, and what issues would negatively influence the magnitude of these spillovers. Farole and Winkler (2014) chooses an analytical method in chapters three and four of their study to assess the absorptive capacities encouraging FDI linkages, employing simple regressions to explain the effect of this variable on FDI spillovers. Having explained these important factors, it is obvious that the "absorptive institutional power" in the host community is a key factor in achieving positive externalities for the FDI in full. Besides, another study examines investment climate by adopting the World Bank's "ease of doing business" metric and concentrating on several developed countries (Bayraktar, 2013). The approach engaged was a basic matrix of correlations that would analyze the impact of the "ease of doing business" metrics on FDI levels; findings suggested that countries with fewer market restrictions appear to draw more FDI inflows.

Research in the MENA region also shows that structural variation like property rights is one of the significant indicators of the region's FDI inflows (Mohamed & Sidiropoulos, 2010). Besides, according to an Economic Update Report issued by the National Bank of Kuwait (2014), the GCC region aimed to improve its business climate, significantly to facilitate business factors (starting, obtaining credit, implementing contracts, etc.) To provide FDI inflows into the region.

Khayat (2020) revealed that most GCC countries are attracting foreign portfolio investment through their development policy framework. Therefore, macroeconomic factors play a significant role in influencing the choice of the country by foreign investors. Foreign direct investment is significantly dependent on the effective governance system, demand for energy, and regulations related to the use of energy (Hadj & Ghodbane, 2021). A study by Alfalih & Hadj (2020) investigating the case of Saudi Arabia indicated that market size, exchange rate legal factors impact FDI positively.

The study concluded that the characteristics of oil prices in short-run trend and openness over long time stimulate the FDI and FDI inflows are more sensitive to cost not to the amount of resources. Eissa & Elgammal (2020) has reported a positive nexus positive relationship between market growth, trade openness, inflation, infrastructure, oil price, and FDI; resources seeking FDI are not encouraged in GCC. Explaining on macroeconomic determinants of FDI Mahmood (2018) noted that the stability of the political system has a positive relationship with FDI inflows.

The proxy of natural resources has a negative association with FDI but oil rents to GDP on resource based FDI has a positive correlation. Natural resources have a high impact on resource FDI compared to non-resource FDI in GCC and issues of legal transparency affect the resource FDI favorably (Iheddad & Mohamed, 2018; Elheddad, Thapa-Parajuli & Alharthi, 2020). The tendency of allocation of FDI tends to move from manufacturing and servicing towards booming sectors due to high profits (Alhroob, Irbihat, Albashabsheh, & Javed, 2017; Javed et al., 2019; Javed & Khan, 2017; Javed, Malik, et al., 2020). Hence, FDI does not benefit different sectors directly. In the case of the United Arab Emirates, trade openness and infrastructure development have positively influenced the FDI, but human capital development harms FDI. GCC countries tried to establish flexible labor market policies, but the impact of human capital development of FDI remained negative. There is no empirical evidence that offering a flexible labor market must eliminate the adverse effect of low efficiency in human capital development (Mina, 2020). To enhance diversification strategy in Oman the government has taken certain initiatives to encourage FDI inflows through a variety of measures such as strengthening institutional factors, legal and investment policy framework, and ensuring transparency of the regulatory system (Ibrahim, Devesh & Shaukat, 2020).

2.6 FDI inflows in Oman

Foreign direct investment in the manufacturing sector has experienced a steady increase during the last five years. Oman's Foreign Direct Investment in manufacturing was reported at 1,149.400 OMR mn in 2018. The lowest level of FDI in manufacturing was seen in 2014 and later FDI has increased gradually as shown in table 2. FDI net outflow in Oman has increased during the year 2017-2018 (NATIONAL CENTER FOR STATISTICS AND INFORMATION, 2019).

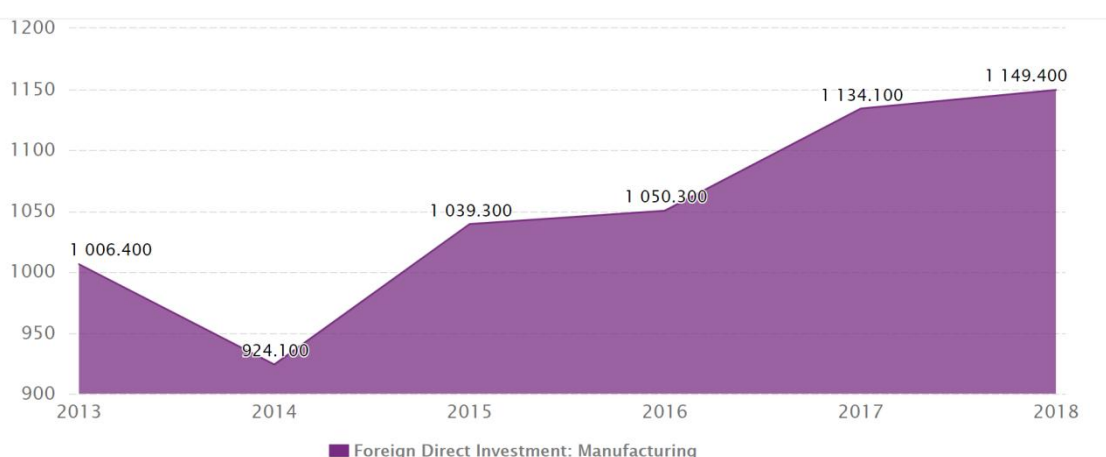


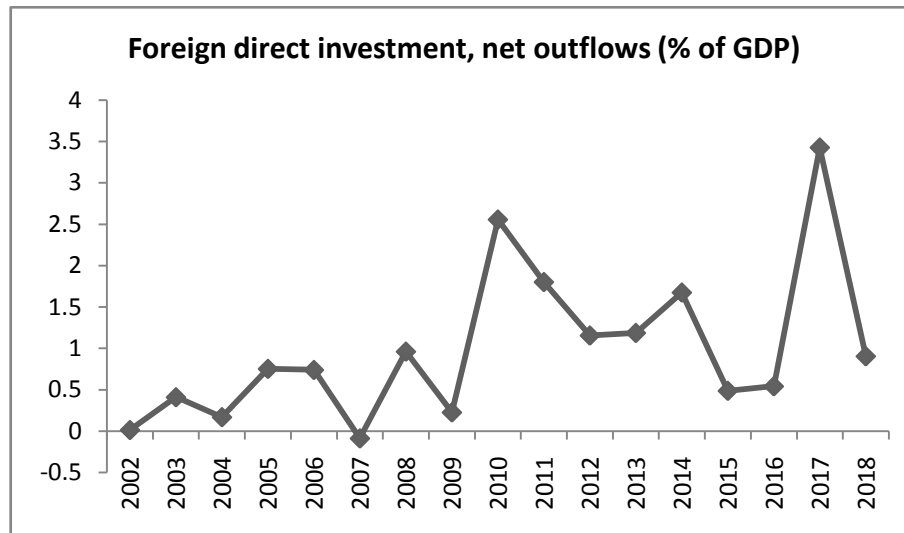
Figure 1: Foreign Direct Investment: Manufacturing

Source: www.CEICDATA.COM: National Centre for Statistics and Information

Table 1: FDI inflows in Manufacturing

Year	2014	2015	2016	2017	2018
FDI	924.1	1039.3	1050.3	1134.1	1149.4
Change	-8%	12%	1%	8%	1%

Source: www.CEICDATA.COM: National Centre for Statistics and Information

**Figure 2: FDI net out flow in Oman (2002-2018)**

3. Theoretical background and hypotheses

FDI theories and assumptions differ substantially but explore the main motivations to specific entry modes will determine to choose a theory to explain a policy framework on investment. Typically, the theory of foreign direct investment in the manufacturing sector applies to producers. This study is influenced by Baltagi et al. (2007) and further enhanced by Uttama and Péridy (2009). In their theory they pointed out the significant role of bilateral- and third-country characteristics in the context of economic integration through FDI. To stimulate empirical analysis of the impacts of foreign direct investment in manufacturing, we have proposed to study the research model. The research model in this study explores the impact of the FDI strategic framework on net FDI inflows that ultimately contribute to the improvement of macroeconomic conditions. Secondly, the study is guided by the OLI paradigm under the eclectic theory explained by (Zhu, 2008) which sets of interdependent variables. The policy framework explains certain advantages such as ownership-specific advantages, location-specific advantages, and internalization advantages. The FDI-related policies of Oman rest on benefiting from certain advantages of the economic diversification policy of government.

While there is significant FDI potential in Oman, the level of FDI inflows attracted by Oman is low. The Sultanate of Oman encourages FDI through tax incentives and exemptions in custom duties besides measures to improve macroeconomic and political stability.

Based on the evidence from the literature, determinants of FDI inflows into the region, and theoretical guidelines, the current study propose the following hypotheses.

- H1: Labor market policy has a significant impact on FDI inflow.*
- H3: Trade policies have a significant impact on FDI inflow.*
- H3: Competition policy has a significant impact on FDI inflow.*
- H4: Administrative procedures have a significant impact on FDI inflow.*
- H5: FDI net inflow significantly affects job creation.*

4. Research Methodology

The study design is explanatory, and this design is helpful in the given context as the problem under investigation is in its preliminary stage and not defined well by the existing research.

This study used a quantitative research method involving systematic empirical research by statistical, mathematical, or computational techniques into observable phenomenon (Albashaheh, Alhroob, Irbihat, & Javed, 2018; Husain & Javed, 2019a; Javed et al., 2019; Javed, Husain, et al., 2020; Javed, Khan, & Farooqi, 2020; Javed, Malik, et al., 2020; Khan, Baseer, & Javed, 2017; Khan & Javed, 2016; Malik, Khan, Faisal, Javed, & Faridi, 2020).

Quantitative research aims to test hypotheses relating to the study problem. The population focuses on manufacturing firms in Oman. Non-probability and purposive sampling was implemented in two stages. First, researchers selected 9 categories of industry, namely textile, petroleum products, technology, automobile, food & beverages, agriculture & fishery, printing, chemicals, and pharmaceuticals. The target participants were the management staff of the firms in selected industries. The selection of the participants includes owners, business managers, and financial managers. The selection of survey participants was purposive because owners, business managers, and finance managers are considered better informants of policy issues.

Among 81 industrial units, 610 participants were given questionnaires. A structured and self-administered questionnaire was used for data collection and 500 questionnaires were sent by email and 110 were distributed physically. A total of 410 usable questionnaires were received with a response rate of 67.2 %. Hypotheses were tested using SPSS; data analysis was done to predict the dependent variables (FDI inflow and job creation) through predictors.

5. Analysis and Discussion

Table 2: Demographic Characteristics of Respondents

Occupation	Frequency (Respondent)	Percent	Industry	Frequency (Companies)	Percent
Business Managers	215	52.4	Textile	16	20%
Finance Managers	134	32.7	Petroleum Products	11	14%
Owners	49	12.0	Technology	12	15%
Managing Partners	6	1.5	Automobile	9	11%
Shareholders	6	1.5	Food & Beverages	12	15%
Total	410	100.0	Agriculture & Fishery	9	11%
			Chemicals	7	9%
			Pharmaceuticals	5	6%
			Total		100%

Table 2 shows that 52.4 % of the respondents were business managers followed by 32.7 % finance managers, 12.0% owners, 1.5 % managing partners, and 1.5 shareholders. On the other hand, 20% firms in the samples were textile, technology 15%, food and beverages 15%, petroleum products 14%, automobile 11%, agriculture and fishery 11% chemicals 9%, and pharmaceuticals 6%

5.1 Hypothesis Testing

Using a multiple regression, FDI Net Inflow was predicted based on Labor Market Policy, Trade Policies, Competition Policy, and Administrative Procedures. Table 3 shows that regression equation was significant $F(6,34) = 3.029$, $p < 0.05$ with $R^2 = 0.394$ which indicates 39.4 % variance explained by the predictors. Results indicated that impact of labor market policy ($\beta = 0.418$; $t = 3.466$; $p < .05$) On FDI Net Inflow was significant. Therefore, H1 was supported. The impact of trade policies ($\beta = 0.219$; $t = 1.118$, $p > .05$) And Competition Policy ($\beta = 0.641$, $t = 1.238$, $p > .05$) Was insignificant. Hence, H2 and H3 were not supported. Administrative Procedures ($\beta = 0.286$; $t = 2.392$; $p < 0.05$) was a significant predictor of FDI Net Inflow. Therefore, the H4 was supported. The output of simple regression (Model 2) showed that the ANOVA for the model was significant $F(2,16) = 3.671$, $p < 0.05$. The predictors (FDI Net Inflow) accounted 34.4 % portion of variance in regression. The impact of FDI Net Outflow was positively significant ($\beta = .587$; $t = 2.707$; $p < 0.05$); the impact of FDI Net Inflow was insignificant ($\beta = -0.008$; $t = -0.012$; $p > 0.05$). Therefore, the H2 was supported.

Table 3: Path coefficient analysis

Model 1				Model 2			
Variables	SE	β	t	Variables	SE	β	t
(Constant)	9.540		1.513	(Constant)	3.343		7.098
Labor Market Policy	0.154	0.418	3.466*	FDI Net Inflow	2.063	0.587	2.707*
Trade Policies	0.409	0.219	1.118				

Competition Policy	0.484	0.641	1.238
Administrative Procedures	0.392	0.286	2.392*

Notes: Model 1
a. Dependent Variable: FDI Net Inflow
 $R^2=0.394$ (Predictors: (Constant), Labor Market Policy, Trade Policies, Competition Policy, Administrative Procedures)
 ANOVA: $F(6,34) = 3.029$, $p=0.021$ indicated a significant regression equation
 * $p < 0.05$ (significant), H1 and H4 supported

Notes: Model 2
a. Dependent Variable: Job Creation
 $R^2=0.344$ (Predictors: FDI Net Inflow)
 ANOVA: $F(2,16) = 3.671$, $p=0.048$ indicated a significant regression equation
 * $p < 0.05$ (significant) H5 supported

6. Discussion

The findings of the study showed that FDI Net Inflows were substantially impacted jointly by policy mechanisms (labor market policy, trade policies, competition policy, and administrative procedures). The results indicated that labor market policy and administrative procedures affect the net inflow of FDI in the country. The competition policy and trade policies had a statistical impact on FDI inflows. Further findings revealed that FDI net inflow significantly impacts job creation. The results are consistent with many of previous studies and diverge from many of the previous studies simultaneously. Overall, the outcomes of the study confirm that FDI in Oman has a significant contribution to job-creation. Certainly, this impact is due to policy measures and motives by the government. Outcomes of the study are consistent with Nunnenkamp and Spatz (2003) who theorized that FDI's position in boosting economic development in the host nation will be influenced by the various FDI motives, especially between resource-seeking, market-related, and productivity-related FDI. Regarding the insignificant relationship of trade policies, results are consistent with Razakova et al (2019) explanation that trade openness as a competing factor harms FDI inflows. Countries intended for economic diversification try to take advantage of Geo-economics.

The findings imply that assessing the variation within vertical, horizontal, and export related FDI is significantly essential. For most industries, Oman approved 100 % foreign direct investment ownership of companies; allowed international, non-GCC, businesses to acquire properties and rent land.

6.1 Theoretical Implications

Being the first study of its nature, the current study highlights the impacts of policy measures of Omani investment endeavors. The study contributed valuable addition to literature on investment related to Oman through empirical evidence. This study contributes significantly to awareness and good knowledge on how FDI could be utilized as a device for promoting and strengthening the private market in local businesses and assisting regulators and decision-makers in formulating a more successful FDI policy. As domestic markets shrink and world markets grow, FDI policy in the oil-producing economies must stop being dependent on local markets and shift policy focus from local dependence on foreign investment.

6.2 Practical Implications

The outcomes of this study provide a practical guideline in improving policy effectiveness and instruments. Change in business strategy is also required to provide a clearer understanding of the processes that best promote information transfer from FDIs and ties to the local business environment. The role of the private sector, especially manufacturing is vital in achieving the objectives of the long-term vision of Oman. Domestic request for products and services is lower because Oman depends largely on imports. Policymakers in Oman may enact policies that would safeguard foreign investments and successful collaboration and communication between local and foreign entities will add to the diversity of networks of local firms and will enhance their learning capabilities.

Outcomes of the present research help evaluate the spillover effect of inward investment in Oman in a broader sense. Policymakers can improve FDI policy instruments to attract more inward investment because its spillover benefits the local firms through learning. In the future, the creation of links between foreign and domestic firms in manufacturing will help sustainable economic development. Particularly, formation of a mechanism to connect spillover affects inward investment through non-market transactions.

6.3 Future research

Future research may cover other variables and intervening factors: impact of the economic environment after COVID 19 and benefits of collaboration resulting from spillovers of FDI in Oman. The outcomes of this research essential merit further research in the same direction, including other sectors of the economy. This will

portray a big picture of the economy as how the economy is benefiting from FDI policies. Additionally, the inclusion of other intervening variables such as transparency and ease of doing business in Oman will make research in this topic more valuable and meaningful.

7. Conclusion

The main objective of the study was to assess the relationship between Foreign Direct Investment (FDI) and the manufacturing companies in Oman. Using a quantitative research method, the study revealed that labour market policy and administrative procedures as a tool of FDI policy framework affect FDI net inflow in Oman. Other tools (i.e., trade policies and competition policies) of the FDI policy framework have a positive impact on FDI net inflow but did not indicate a significant impact on FDI net inflow. The outcomes also revealed that FDI net inflow significantly impacts job creation in Oman.

Based on the outcomes of the study, we conclude that foreign direct investment spill over is not substantially advantageous for domestic firms in manufacturing industries. The study draws the attention of policymakers to the implementation of policies that are more effective and attractive in achieving objectives of economic diversification and sustainable.

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