

Literature On Key Challenges Influencing Foreign Direct Investment Inflows: A Case Study Of Saudi Arabia

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Abstract:

Foreign Direct Investment (FDI) is widely acknowledged as a powerful tool to boost economic growth (EG), playing a crucial role in fostering accelerated development and promoting economic growth and diversification, particularly in developed countries like Saudi Arabia (SA). This paper delves into reviewing various research studies, offering a comprehensive exploration of Foreign Direct Investment (FDI) on a global scale. Consequently, it identifies the paramount challenges within host countries that significantly influence the inflow of FDI, along with key factors and challenges that practically impact FDI in the Saudi market. It investigates the economic dependence on politics, regulatory hurdles, social and cultural considerations, infrastructure, and the impact of Vision 2030, a transformative economic and social development plan. The challenges faced by the host country in attracting FDI include the need to strike a balance between attracting FDI and protecting national interests, ensuring compliance with local regulations and standards, managing the impact on the environment and natural resources, and addressing potential negative effects on local industries and employment. Policymakers, investors, and scholars need to work together to develop strategies and policies that mitigate these challenges and maximize the benefits of FDI for both the host country and the investor.

Index Terms: Foreign Direct Investment; Economic Growth; Inflows, Saudi Arabia; Factors, Challenges; Vision 2030.

1. Introduction

Foreign Direct Investment (FDI) plays a crucial role in the economic development of countries worldwide. It is considered a significant driver of economic growth, job creation, technology transfer, and infrastructure development. Saudi Arabia, as the largest economy in the Middle East, recognizes the importance of FDI in achieving its Vision 2030 goals. However, attracting FDI to the country is not without challenges. This literature review aims to identify the key challenges influencing the inflows of FDI to Saudi Arabia through a case study approach. Methodology The case study approach will involve an in-depth analysis of existing literature, reports, and studies related to FDI in Saudi Arabia. Both qualitative and quantitative data will be collected and analyzed to provide a comprehensive understanding of the challenges. The literature review will focus on identifying the main obstacles hindering the inflows of FDI to the country. These challenges can range from regulatory barriers, political instability, cultural differences, to economic factors. By examining the existing literature, this review aims to provide insights into the specific challenges faced by Saudi Arabia and propose recommendations to address them. The literature review will begin by exploring the existing literature on FDI and its importance in economic development. It will then delve into the specific challenges faced by Saudi Arabia in attracting FDI. The review will examine studies and reports that highlight the regulatory environment, political stability, cultural factors, and economic conditions as potential obstacles. It will also analyze case studies of other countries that have successfully attracted FDI to draw lessons and best practices. The review will identify the key challenges and provide recommendations based on the findings. Conclusion In conclusion, this literature review will provide valuable insights into the key challenges influencing the inflows of FDI to Saudi Arabia. By identifying these challenges and proposing recommendations, it aims to contribute to the understanding of FDI inflows and support Saudi Arabia's efforts in attracting foreign investment for sustainable economic development.

Foreign Direct Investment (FDI) stands as a cornerstone in the economic development of nations aspiring to enlarge and diversify their resources, serving as a pivotal force for growth and advancement. This significance is particularly evident in developed countries like Saudi Arabia, where FDI fosters accelerated development and contributes to economic growth. This paper

conducts a thorough review, beginning with elucidating the meaning of FDI and exploring its various types. Furthermore, it provides an inclusive list of the advantages and disadvantages of FDI in host countries. The analysis extends to a global review of important factors influencing FDI inflows before narrowing its focus to the specific context of the Saudi market. However, as the global economy becomes increasingly interconnected, analyzing the key challenges influencing FDI in Saudi Arabia contributes to academic discourse and provides practical guidance for those involved in policy formulation and investment decision-making. Moreover, this paper aims to contribute to the ongoing dialogue surrounding FDI by shedding light on its intricate dynamics and offering actionable insights for stakeholders in the Saudi Arabian market. During the unveiling of the Saudi vision 2030 on April 25, 2016, His Royal Highness Crown Prince Mohammed bin Salman Bin Abdulaziz articulated two primary goals: firstly, to increase non-oil government revenue from SR163 billion to SR1 trillion, and secondly, to raise foreign direct investment from 3.8% to the international level of 5.7% of GDP [\[1\]](#) & [\[2\]](#). These figures underscore Saudi Arabia's concerted efforts to diversify its revenue sources beyond oil-related income, demonstrating a strategic shift toward a more balanced and sustainable economic model. In the figure 1 demonstrates these goals.

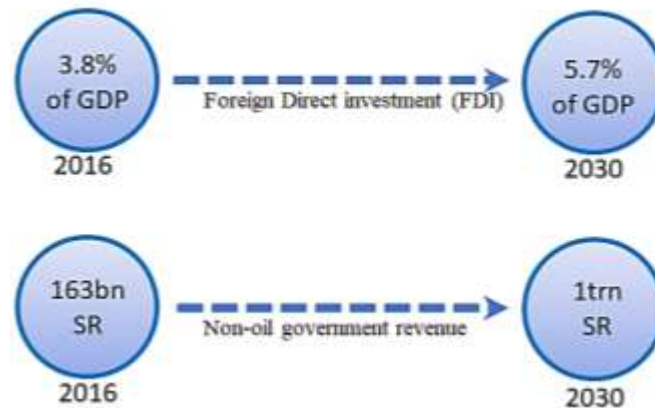


Figure 1: The primary goals of Vision 2030 A

By analyzing existing research and case studies, this review seeks to provide insights into the factors that impact foreign investment in the country. The review will focus on both internal and external challenges faced by Saudi Arabia in attracting FDI. Internal challenges refer to domestic factors such as government policies,

regulations, infrastructure, and labor market conditions. External challenges, on the other hand, encompass global economic conditions, geopolitical factors, and international competition for investment. The review will explore the interplay between these internal and external challenges and their implications for FDI inflows.

The review focuses on the significance of Foreign Direct Investment (FDI) in driving economic growth. It aims to identify the primary factors and challenges that impact the attraction of FDI globally and in Saudi Arabia. Additionally, it aims to pinpoint gaps in existing research and suggest areas for future study. The review will provide valuable insights into FDI and its implications for Saudi Arabia's economic development. The selected articles will be critically analyzed to extract key findings and insights related to the challenges faced by Saudi Arabia in attracting FDI. The review will also consider the perspectives of different stakeholders, including government agencies, policymakers, investors, and researchers, to provide a comprehensive understanding of the challenges and their implications. The findings of this literature review will highlight the key challenges that influence FDI inflows into Saudi Arabia. These challenges may include restrictive regulations, limited market openness, inadequate infrastructure, labor market conditions, bureaucratic procedures, political stability, and competition from other countries. The review will discuss the implications of these challenges on FDI inflows and potential strategies to address them. In conclusion, this literature review will provide valuable insights into the key challenges influencing FDI inflows into Saudi Arabia. By identifying these challenges and proposing strategies to address them, the review aims to contribute to understanding the factors that impact foreign investment in the country. It is hoped that the findings of this review will inform policymakers, government agencies, and other stakeholders in their efforts to attract and promote foreign direct investment in Saudi.

2. Foreign Direct Investment (FDI)

This literature review has two main sections, i.e., FDI from a global perspective, key challenges influencing the Inflow of (FDI), and primary factors and challenges in the Saudi Market (SA). The primary objective is to furnish updated insights, focusing on research about Inward Foreign Direct Investment (FDI) more specifically. This refined approach aims to provide a holistic

understanding of recent developments, emerging trends, and noteworthy findings in the field, ensuring the currency and relevance of our literature exploration.

2.1. Foreign Direct Investment (FDI) from a Global Perspective

Foreign direct investment (FDI) is a pivotal force driving economic growth globally, fostering job creation, and facilitating the exchange of technology and knowledge across nations. It is considered a key driver of globalization and international trade. Governments worldwide often employ incentives and policies to attract FDI, recognizing its potential to bring capital, expertise, and access to new markets [3], [4] & [5].

Hussain & Hague also describe Foreign Direct Investment (FDI) as representing investments made by companies or individuals from one country into another to establish business operations or acquire assets. In terms of types, Foreign Direct Investment (FDI) exists in two primary forms: Inward FDI, which entails the investment of foreign capital in a host country, and outward FDI, which refers to investments made by the host country in foreign markets. Inward FDI involves the transfer of tangible or intangible assets, making a more significant contribution to the host country's economy.

In addition, it encompasses Foreign Portfolio Investment (FPI), which typically focuses on capital gains [6]. The difference between the amount of investment flowing into and out of a country is called the Net Flow of Foreign Direct Investment. Establishing new facilities and subsidiaries in the host country, known as greenfield FDI, brings substantial benefits, fostering capacity development and contributing directly to economic growth [7]. In theory, there are two existing FDI categories, i.e., Horizontal and Vertical types. Horizontal FDI involves companies investing in the same industry abroad as they operate domestically, replicating existing operations. In contrast, Vertical FDI occurs when companies strategically distribute production processes across different countries, optimizing cost-effective resources at each production stage [8] & [9]. Based on previous studies, figure 2 illustrates a breakdown of Foreign Direct Investment (FDI).

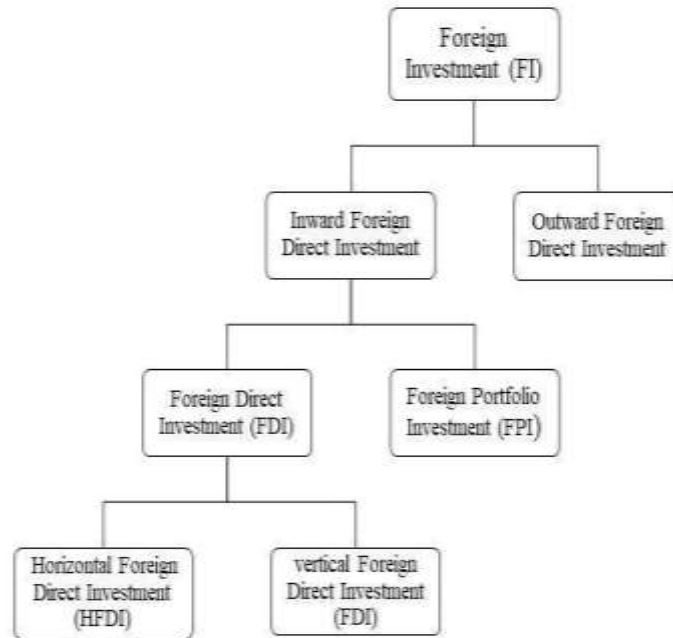


Figure 2 Breakdown of Foreign Direct Investment (FDI) [ibid].

As the relationship between foreign direct investment (FDI) and economic growth unfolds, it becomes evident that contrasting viewpoints emerge from extensive research. While some studies suggest a positive correlation between FDI and economic growth, others highlight the potential adverse effects in certain countries [3], [4], & [5]. [10] outline benefits for investors, including global expansion and cost minimization. Simultaneously, advantages for host countries involve attracting FDI, fostering economic growth, integrating technology, and promoting innovative ideas. However, potential drawbacks include the creation of dependency and prioritization of profit over host state development [11] & [12].

Table 1 below summarizes the pros and cons of key challenges affecting Foreign Direct Investment (FDI) [10] & [13].

Table 1 Key Challenges Affecting Foreign Direct Investment (FDI) [ibid]

Foreign Direct Investment	
Advantages	Disadvantages
Economic Growth Catalyst: nations with limited capital often rely on Foreign Direct Investment (FDI) as a crucial catalyst for economic growth.	Hindrance to Domestic Investment: Overreliance on FDI can hinder domestic investment.
Knowledge Transfer: FDI contributes to skill transfer, technical know-how, and business expertise in host countries.	Limited Government Control: The government may have limited control over companies with overseas bases.
Employment Opportunities: FDI increases employment opportunities in host countries.	Political and Economic Risks: FDI can be risky due to political instability and economic crises.
Transformation of Backward Areas: FDI enables the development of underdeveloped areas in a host country.	Negative Influence on Exchange Rates: FDI may negatively influence exchange rates.
Enhanced Product Quality: FDI leads to improved product quality at competitive prices.	Challenges in Trade Operations: FDI can pose roadblocks in export and import operations.
Global Market Expansion: FDI allows for expanding global market reach, providing opportunities for investors.	Government Control Over Assets: There is a risk of the government having control over foreign-owned property and assets
Improved Capital Flow: FDI results in improved capital flow into host countries.	Dominance of Multinational Companies: Multinational companies may dominate highly profitable sectors through investments in technology and intellectual assets rather than local wages.

The study conducted by [\[14\]](#) sheds light on the challenges influencing Foreign Direct Investment (FDI) dynamics in Saudi Arabia. Key elements include substantial oil revenues and government involvement in crucial industries. Despite initial challenges with negative FDI inflows until 2004, strategic policies, such as joining the World Trade Organization (WTO), led to a significant increase in FDI since 2005, even amid the global financial crisis. Furthermore, the unveiling of Saudi Arabia's Vision 2030 in 2016, articulated by Crown Prince Mohammed bin Salman Bin Abdulaziz, set ambitious goals to raise FDI from 3.8% to 5.7% of gross domestic product (GDP) to reach international standards. Based on the (General Authority for Statistics, 2016). It defines

GDP as “the sum of values added by the domestic producers to the product price, plus customs tariffs”. Alternatively, it is the sum of all outputs, less the sum of intermediate consumption plus the indirect taxes on products (taxes, subsidies, etc) not included in the output’s values”. Also, in the 2014 World Investment Report by the United Nations Conference on Trade and Development (UNCTAD), Saudi Arabia ranked third in terms of the highest number of Foreign Direct Investments (FDI) in Western Asia [\[15\]](#).

Despite lagging in moving forward to attract foreign investments to the Saudi market [\[16\]](#), returns have recorded promising numbers in recent years; the latest data from the General Authority for Statistics in 2023 highlights FDI Inflows of approximately 17 billion SAR and Outflows of around 5 billion SAR during Q3 2023, resulting in a net FDI flow of 11 billion towards 'sustainable FDI.' The data report highlights prioritizing the following criteria, i.e., low carbon footprint, strict adherence to human rights, maintaining workplace safety, preventing discrimination, and upholding transparency standards. The increasing recognition of the importance of environmental, social, and governance factors in investment decision-making drives the strategic shift towards ESG investing. ESG investing considers companies' sustainability and ethical practices, aiming to generate long-term value while considering the impact on the environment, society, and corporate governance. This shift aligns with broader goals related to sustainable development and responsible investment practices, as emphasized by the Columbia Center on Sustainable Investment

2.2. The Key Factors and Challenges Influencing the Inflow of Foreign Direct Investment (FDI) Globally and in Saudi Arabia

In the contemporary global landscape, foreign direct investment (FDI) faces diverse challenges. For developing or underdeveloped nations, FDI is a crucial driver of economic growth, often deemed the most viable option. Consequently, these countries consistently endeavor to attract investors, with certain influential factors playing a key role in enticing them [\[10\]](#).

[\[17\]](#) study sheds light on Southeast Asian countries, revealing that trade liberalization and the quality of human resources consistently exhibit positive impacts on attracting FDI. However,

factors such as the urbanization rate, population size, and tourism numbers do not significantly affect FDI in the region. [18] conducted a comprehensive analysis of FDI inflows, considering characteristics like economic growth rate, government policy, labor markets, inflation, trade openness, foreign reserves, and natural resource availability. [19] emphasized market size as a critical factor in foreign investors' evaluations, using an empirical model to assess economic variables impacting the host country. Additionally, foreign investment was highlighted as adding substantial value to an economy by increasing the availability of local capital [20].

In Iraq, [21] emphasized the strategic importance of understanding the relationship between the investment environment and FDI, pointing out the crucial roles of gross domestic product (GDP) growth rate and inflation rates. However, the model did not incorporate random factors impacting investment attraction, including political and security factors deterring foreign investment. Shifting to Africa [22], identified infrastructure gaps, low domestic savings, and price inflation as mitigating factors hindering FDI between 1970 and 2021. [23] promotes inflation targeting as a strategy to attain FDI-attractive factors, including good governance and macroeconomic stability. Analysis indicates that countries adopting inflation targeting saw a 3-percentage-point increase in FDI compared to those not implementing this approach. In context of the Saudi Arabia market, Historically, Foreign Direct Investment (FDI) has played a pivotal role in the Kingdom of Saudi Arabia (KSA), particularly in supporting oil exploration, refining, and the establishment of major conglomerates like ARAMCO and Saudi Arabian Basic Industries Company (SABIC). Beyond the oil sector, FDI has contributed significantly to infrastructure and the banking industry [17]. To attract more foreign investors, the Saudi Arabian government adjusted FDI rules and regulations in 2000, involving a comprehensive revision of corporate laws and trade-related regulations [24]. The current investment environment in Saudi Arabia is defined by key factors that attract foreign investment. These include the announcement of Saudi Vision 2030, the strategic location of Saudi Arabia, real estate opportunities, and a leading financial sector [25]. Figure 3 illustrates the three fundamental pillars identified by the Saudi government to guide its strategic direction. The first pillar centers around the aspiration for a dynamic society rooted in fulfilled lives and strong foundations.

The second pillar emphasizes the establishment of a robust economy offering promising prospects, long-term investments, a business-friendly environment, and the utilization of its strategic position. The final pillar aims to establish an ambitious nation characterized by effective governance and responsible enablement [1].



Figure 3 The three fundamental pillars identified by the Saudi vision 2030 [1]

The three pillars comprised six overarching level 1 objectives, cascading into twenty-seven branch objectives at level 2, and eventually spreading to ninety-six strategic objectives at level 3. According to the Vision2030 [Ibid], this vision was systematically cascaded into strategic objectives to facilitate effective implementation through Vision Realization programs. As outlined on the Vision2030 website, eleven Vision Realization programs are strategically leading and overseeing the implementation of initiatives executed by public sector organizations, all directed toward the achievement of the goals set forth in Vision 2030.

Engineer Khaled bin Abdulaziz Al Falih, 2023, the Minister of Investment, announced a new methodology for enhancing data quality and transparency in the Kingdom to empower investors and decision-makers. This initiative aligns with broader goals such as the National Investment Strategy, special economic zone development, global supply chain initiatives, and mega-project launches. The commitment to data enhancement supports the Kingdom's objectives and strengthens its global investment position. Various strategies can encourage foreign companies to enter the Saudi Arabian market. Incentives and benefits, such as tax incentives, access to government contracts, and simplified visa processes, can attract foreign companies. Establishing special economic zones with relaxed regulations and attractive investment opportunities is another effective strategy [26].

Figure 4 provides a visual representation of Saudi Arabia's economic growth rates spanning from 2006 to 2022. Noteworthy is the noticeable impact of governmental policies and regulatory reforms, particularly post-2016, aligning with the inception of the Saudi Vision 2030 initiative. This period witnessed a significant increase in economic growth rates, rising from around 2% in 2016 to nearly 9% by 2022. Such a substantial increase underscores the tangible benefits derived from the strategic initiatives outlined in the Vision 2030 agenda. Furthermore, figure 5 depicts the percentage of world Foreign Direct Investment (FDI) in Saudi Arabia relative to GDP from 2006 to 2022. A discernible upward trend is evident, indicating the increasing attractiveness of the Saudi market to foreign investors. This trajectory underscores the growing appeal of Saudi Arabia as an investment destination [27].

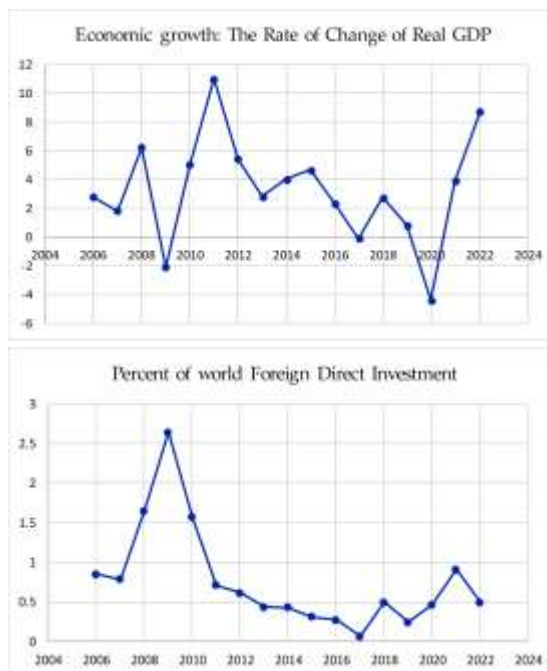


Figure 4 Economic Growth [27]

Figure 5 Percent of World Foreign Direct Investment [27]

Promoting Saudi Arabia as a strategic hub for regional and international business and providing support for foreign companies to navigate the local business environment, including assistance with licensing and regulatory compliance, are additional measures. Fostering partnerships and collaborations between

foreign and local companies facilitate knowledge transfer, technology exchange, and market entry for foreign companies [28] & [29]. In a different context, [25] indicated that GDP growth rate, domestic investments, and natural gas reserves played pivotal roles.

3. 3. Research Findings

Previous studies acknowledged the importance of diversifying economic incomes; there is a crucial need to investigate the implementation of these strategies and their tangible outcomes in achieving the targeted FDI objectives. Table 2 outlines the pivotal factors influencing the positive or negative aspects of attracting foreign direct investment in the Saudi market, providing a comprehensive overview of the key determinants discussed in the literature review.

Table 2 Factors Influencing Foreign Direct Investment in The Saudi Market

Study Year	Research Objectives	Methodological Approach	Source of date	Key Findings	References
1970 to 2015.	Examine causal relationships among domestic investment, foreign direct investment, and economic growth. Formulate strategic recommendations for enhancing the Saudi economy.	Econometric methodology and co-integration methods. ARDL models. fully modified ordinary least squares (FOLS). Dynamic ordinary least squares (DOLS). CCR estimators.	Saudi Arabian Monetary Agency (SAMA) United Nations Conference on Trade and Development (UNCTAD 2016) World Development Indicators (WDI) World Bank (World Bank 2016).	Negative bidirectional causality observed between non-oil GDP growth and both FDI and domestic capital investment. Bidirectional causality between FDI and domestic capital investment. Short-term negative impact of FDI on DCI domestic capital investment; long-term negative impact of domestic capital investment on FDI. FDI inflows crowd out DI in the short term. Positive effects of finance development and trade openness on non-oil GDP growth, FDI inflows, and domestic capital investment in the long run.	[30]

				Saudi economic growth relies on trade openness and domestic credits to the private sector	
2017 to 2021.	Assess how corporate social responsibility (CSR) and corporate governance (CG) impact foreign investor attraction as indicators of firm sustainability.	Stakeholder theory and legitimacy theory applying: Ordinary Least Squares (OLS) System Generalized Method of Moments-(GMM) estimation	Saudi stock market (Tadawul). The sample data was collected from Alragaib 2. Corporate Social Responsibility Hub (CSRhub) database.	Saudi Arabian companies should adopt global ESG frameworks to attract more foreign investment. Doing so will boost the country's economy, enhance competitive advantages, and improve sustainability levels.	[31]
2000 to 2017.	Identifying key investment determinants in KSA and examining their impact on FDI inflows.	Statistical descriptive analysis method	General Organization for Statistics. World Bank publications. Secretariat General of the Gulf Cooperation Council (Department of Economic Affairs) UNCTAD database.	The primary factors influencing investment in KSA are the GDP growth rate, domestic investments, and the availability of natural gas reserves. Government spending and inflation rate have an inverse relationship with the volume of FDI. The current investment environment needs to be enhanced to attract more FDI	[25, 32]
over a 30-year period	Identifying the key factors that impede FDI inflows and those that facilitate them in the Saudi market and also pinpointed factors that need to be eliminated to facilitate FDI and those that require improvement.	Semi-structured. Interviews. Interviews. Case study. Grounded Theory.	Conducted interviews with government officials, independent consultants, and foreign investors. An inductive approach was employed to ascertain the impact of alterations.	The industrial sector is favored for FDI while the agricultural sector is viewed less favorably. Fluctuations in oil prices have shown mixed effects on FDI. The inflation rate has no significant impact on FDI in Saudi Arabia. Existing exchange rate policies have been beneficial for attracting foreign direct investment (FDI). Alterations to exchange policies could negatively impact FDI. The study offers a concise conceptual framework for FDI research, integrating regulatory,	[15, 33]

				political, and economic factors providing a valuable resource for future FDI research.	
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The research gap identified in this study is the lack of assessments regarding the strategies used to enhance FDI in Saudi Arabia and their direct and indirect impacts on the economic goals outlined in the Vision 2030 initiative [34]. This research addresses this gap by comprehensively exploring the challenges and opportunities associated with FDI in Saudi Arabia, considering the unique socio-economic landscape and ongoing reforms under Vision 2030. By filling this research gap, the study aims to provide valuable insights and recommendations for policymakers and stakeholders involved in promoting FDI in Saudi Arabia. The challenges of FDI in Saudi Arabia include restrictions on foreign ownership, complex regulations, limited market access, and cultural differences. The research in the Foreign Direct Investment (FDI) field in Saudi Arabia has predominantly centered on examining strategies designed to attract investors. However, a notable research gap emerges after a comprehensive literature review. Specifically, there is a dearth of assessments regarding the strategies employed to enhance FDI in Saudi Arabia and their direct and indirect impacts within the economic goals outlined in the Vision 2030 initiative. This research aimed to address the gap by exploring the challenges and opportunities associated with FDI in Saudi Arabia, considering the socio-economic environment and ongoing reforms outlined in Vision 2030.

4. Conclusion and Recommendation

4.1. Conclusion

This paper has studied the significance of Foreign Direct Investment (FDI) for economic growth, particularly in the context of Saudi Arabia's Vision 2030 goals. The investigation explored the various advantages and disadvantages associated with FDI, along with the key factors influencing its inflow. The unique situation of

Saudi Arabia was highlighted, including its historical reliance on oil revenue and the government's recent efforts to attract foreign investment through strategic reforms. A critical research gap was identified: a lack of evaluation regarding the effectiveness of implemented FDI attraction strategies and their alignment with Vision 2030's economic goals. The study proposes a comprehensive framework for evaluating the effectiveness of FDI attraction strategies in Saudi Arabia. The framework consists of four key components: policy and regulation, infrastructure, business environment, and human capital. Each component was further divided into sub-components, allowing for a detailed assessment of specific indicators. The study also recommended utilizing a combination of qualitative and quantitative methods, such as expert surveys, case studies, and statistical analysis, to measure the impact of FDI attraction strategies on Saudi Arabia's economic growth.

4.2. Recommendations:

Based on the gap that was found and the literature evaluation, this study makes the following recommendations:

- Evaluate the Effectiveness of FDI Attraction Strategies: Conduct a comprehensive assessment of the various strategies implemented by Saudi Arabia to attract FDI. This evaluation should analyze the effectiveness of these strategies in achieving the specific FDI targets outlined in Vision 2030. These recommendations aim to enhance Saudi Arabia's FDI attraction strategies, align them with Vision 2030 goals, and maximize the benefits of foreign investment for the country's economy.
- Align Strategies with Vision 2030 Goals: Analyze the alignment between FDI attraction strategies and Vision 2030's economic objectives. This includes ensuring that targeted sectors for FDI, such as renewable energy and technology, receive adequate support and incentives.
- Assess Indirect Impacts: Explore the indirect impacts of FDI on Saudi Arabia's economy beyond simply increasing FDI inflows. This could involve investigating factors like job creation, knowledge transfer, and technological advancements.
- Promote Transparency and Data Quality: The Saudi government's recent focus on improving data quality and

transparency regarding FDI statistics is commendable. This initiative should be further strengthened to empower investors and attract foreign capital.

- Develop a Skilled Workforce: Saudi Arabia should fund education and training initiatives to give its workforce the know-how that foreign investors want to take advantage of FDI prospects.

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