

Foreign Dependency and Economic Growth Nexus in Kenya

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ABSTRACT: Foreign dependency is an economic phenomenon, which is characterized by asymmetrical benefits, favouring specific countries at the expense of others, and impeding the growth potential of dependent economies. The main objective of the study was to determine the relationship between foreign dependency and economic growth in Kenya. To achieve this overarching aim, specific objectives have been delineated to include an evaluation of the effect of import volumes and external debt levels on economic growth in Kenya. The theoretical underpinnings of this study draw from several key economic theories and models, each offering unique insights into the dynamics of foreign dependency. This study employed a descriptive and inferential statistical design and leverages a time series dataset spanning the years 1980 to 2021, meticulously sourced from the World Bank. To facilitate a comprehensive analysis, the Autoregressive Distributed Lag (ARDL) model was applied. The empirical analysis revealed noteworthy relationships between determinants of economic growth in the Kenyan context. Specifically, imports of goods and services and external debt are all identified as having statistically significant impacts on the trajectory of economic growth in Kenya. In conclusion, these findings suggest that factors like imports and external debt contributes positively to economic growth. The study recommends that policymakers should explore strategies to attract productive external debt which will stimulate positive investment spillover effects within the economy. Emphasis should be placed on the need to bolster the import-led growth through regulatory mechanisms that safeguard local producers. Responsible external debt management is underscored as pivotal to fostering sustained and robust economic growth. Additionally, trade policies designed to facilitate import-led growth are posited as potentially beneficial for the Kenyan economy.

OPERATIONAL DEFINITION OF KEY TERMS

Economic Growth: It refers to the addition of the productive potential of an economy, which results in the economy's capability of producing more amounts of goods and services (Hunt, 2007). It is estimated as the change in the GDP of a country over one year, with inflation adjustment to allow for figures comparisons over time.

External Debt: Refers to the proportion of a country's debt borrowed from foreign lenders and represents the country's outstanding amount of liabilities that require a certain payment of principal plus interest in future (Adesola, 2009).

Gross Domestic Product: This refers to the total value of all goods and services produced over a given period usually a year. It is a monetary measure of the market value of all final goods and services produced within a country's border at a specified time (Hunt, 2007).

Foreign Dependency: It refers to global power structure where developing nations are economically dependent on developed nations, allowing the latter to exert enormous control over the economic and political behavior of the former.

INTRODUCTION

The idea of dependency calls our attention to the international system's stagnation and deplorable state of Africa, Asia, and Latin America. Dependency theory suggests a situation in which one country or region depends on another for support and growth. It claims that the Third World countries' integration into the capitalist system, which is controlled by the West and North America, is exactly what has led to the state of underdevelopment of these countries (Randall and Theobald 1998).

Particularly, a number of common attributes, including limited economic systems, rapid population expansion, and widespread inequality, characterize the underdevelopment of the third world (Woldu, 2020). These economies are also distorted and highly dependent on the developed world for the production of their finished goods.

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According to Okoli and Onah (2002), economic growth entails progress, movement, and advancement in the direction of something greater. As a result, it enhances both the physical and intangible components of life that include actions, reactions, and motions.

In his contribution, Brien (1975) articulated the view that because of their dependent frameworks, dependent countries are the ones that lack the ability to experience autonomous growth. This viewpoint appears to be in line with that of Bill Warren (1980), who argues that "dependency" refers to the complicated socio-economic connection between the advanced capitalist countries of the "center" (the United States of America, Japan, and Western Europe) and the Latin American countries of the "periphery," whereby the movements and structures of the former decisively determine those of the latter in a way that is somehow detrimental to the economic development of the latter.

According to Frank (1981), who examined these processes, "development and underdevelopment are two different sides of a universal historical process." According to the researcher, the developing nations experienced underdevelopment, or what Frank called the "development of underdevelopment," as a result of the same system of capitalist expansion that enabled their growth and development in North America and Europe.

One of the basic notions of capital globalization is that developing countries would enjoy the same growth and development as the now-"developed" nations, if they participate in global commerce and finance (Santos 2013). Unfortunately, developing nations' growth and development have never completely realized.

According to studies, Kenya still exhibits a substantial amount of sluggish economic growth notwithstanding its growing reliance on international aid and support.

This study attempts to explore the dimensions of foreign dependency and economic growth and access the impact on Africa using Kenya as a reference point. As shown by its underdeveloped industrial base, food insecurity, and reliance on foreign capital. Which has some effects and results on the country's overall socioeconomic development.

EMPIRICAL LITERATURE

External Debt

Debt reliance and its effects on economic growth have drawn more and more attention from researchers. The main determinant of a country's position in the global trade hierarchy is its level of debt reliance. Debt dependency, in the opinion of world system and dependency theorists, has detrimental effects on countries in the periphery that are just as severe as those brought on by trade dependency.

According to Akram (2010), Pakistan's foreign public debt has a negative impact on economic development due to the debt overhang. In particular, the researcher discovered that foreign debt had both a short- and long-term negative and statistically significant association with per capita GDP and investment. The ARDL technique to cointegration test was used to evaluate data from the years 1972 to 2009, which formed the basis for these findings. The findings of this study were based solely on information from one nation. Due to variations in macroeconomic environments and economic development levels, they may not be appropriate in other nations like Kenya.

Boboye and Ojo (2016) investigated how Nigeria's foreign debt affected economic development using OLS regressions. They discovered that Nigeria's per capita and national income were negatively impacted by foreign debt. This study clarifies the relationship between external debt and economic growth in a developing African nation. However, it doesn't take into account how domestic debt affects economic expansion.

According to Mukui (2013), Kenya's economic development was negatively impacted by foreign public debt and debt payments. The study also found that domestic savings and inflation had an adverse effect on economic expansion. Contrarily, economic development was boosted by capital formation and foreign direct investment. These conclusions were drawn from an analysis of Kenyan data using a linear model for the years 1980 to 2011. The research failed not evaluate the impact of domestic debt on economic growth despite using data from Kenya.

Egungwu (2018) investigated the connection between human development in Nigeria and external debt. Time series data for the years 1986 to 2015 were subjected to OLS regression analysis. According to the study, both the total amount of external debt and its repayment had a negative impact on economic expansion. The author came to an agreement that governments ought to accept foreign loans if they use them for important initiatives that may raise citizen wellbeing.

Import

According to Abdullahi et al. (2016), imports have a small but favorable influence on the GDP development of West African nations. The growth of the GDP is negatively impacted by foreign exchange. The study came to the conclusion that exports contribute to

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West Africa's economic growth and suggested that the region's nations support domestic businesses for export promotion and import replacement.

International trade and economic growth have a long-term link, according to study by Lawal and Ezeuchenne (2017), balance of trade and Export are important in both the short and long terms, but import and trade openness are both unimportant in the short term but significant over the long run. From the Granger causality test, economic growth is unidirectional with trade openness but unrelated to imports, exports, and the trade balance.

Reddy (2020) looked into the link between India's exports, imports, and economic development from 1980 to 2019. The results shows that exports and economic growth, imports and economic growth, and imports and exports all have a short-term unidirectional causal link. A long-term causal relationship between exports and economic growth was demonstrated by the author as well as between exports and imports. As a result, it can be said that imports and exports both contribute to India's economic growth. Similar to this, Maitra (2020) investigated the notion that imports will drive growth in India following reform. In the short and long terms of his study, he discovered strong evidence that the ILG hypothesis is correct, showing that imports have a major impact on India's economic growth.

Taniguchi (2018) investigated how a rise in Chinese imports affected Japan's regional labor markets. He discovered data suggesting that the rise in Chinese imports had a favorable impact on the expansion of manufacturing jobs in Japan's prefectures. Aluko and Adeyeye (2020) also investigated the relationship between imports and economic development in 41 African nations. According to their findings, the neutrality hypothesis is true in the short- and long-term for the majority of nations, with the exception of a few countries where there is a unidirectional causal relationship between imports and economic development and vice versa.

RESEARCH METHODOLOGY

Research Design

This study used descriptive and inferential statistical methods. This required gathering and analyzing secondary data that was used to determine the effect of foreign dependency and economic growth in Kenya.

Data collection procedure

The study employed secondary data with the goal of analyzing the impact of external debt and import on economic growth in Kenya. The data for the study variables was gathered from World Bank database for each of the factors of interest across the forty-one (41) year period from 1980 to 2021.

Data analysis and presentation techniques

Both descriptive and inferential statistics were used in the investigation. The data were analyzed using the Eviews 8 statistical analysis program and was based on the Autoregressive Distributed Lag (ARDL) method created by Pesaran, Shin, and Smith in 2001.

RESULTS AND DISCUSSION

Univariate Descriptive Statistics

The statistics here suggest that Kenya's GDP, import, and external debt values vary significantly across the observations, with a mean value of approximately 31 billion USD, 8.659 billion, 10.86 billion Dollars, respectively.

Table 1: Descriptive Statistics

Variable	Obs	Mean	Std. Dev.	Min	Max
GDP	42	3.102e+10	3.168e+10	5.752e+09	1.097e+11
Imports	42	8.659e+09	6.788e+09	1.539e+09	2.185e+10
External debt	42	1.086e+10	9.772e+09	3.228e+09	4.120e+10

Source: Research, 2023

Augmented Dickey Fuller (ADF) Test Results

The Table 2 presents ADF test results for variables at levels and after first difference. All the variables were non-stationary at levels, on the other hand, they all attained stationarity on the first difference. This is because their p-values were less than 5% suggests that the unit root null hypothesis was rejected.

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Table 2: ADF Stationarity Results

Variable	At levels					Remarks
	z	p-value	Critical values			
			1%	5%	10%	
GDP	5.928	1.0000	-3.641	-2.955	-2.611	Non-stationary
Imports	0.282	0.9765	-3.641	-2.955	-2.611	Non-stationary
External debt	7.811	1.0000	-3.641	-2.955	-2.611	Non-stationary
First difference						
GDP	-2.967	0.0381	-3.648	-2.958	-2.612	I(1)
Imports	-5.859	0.0000	-3.648	-2.958	-2.612	I(1)
External debt	-7.087	0.0000	-3.648	-2.958	-2.612	I(1)

Note: I (0) indicate the variables are stationary at level and I (1) variables are stationary after first difference.

Source: Research, 2023

Optimum Number of Lags to be selected

For the optimal number of lags to be taken into consideration, the various selection criteria are displayed in Table 3. The results show that, according to the Schwartz-Bayesian Information Criterion (SBIC), 2 lags at most are ideal. According to Greene (2012), there is no ideal number of lags to employ but few lags saves degrees of freedom. Thus the study adopted 2 lags maximum in interpretation of an ARDL model.

Table 3: Selection-order criteria

Sample: 1984 - 2021									
Number of obs = 38									
lag	LL	LR	df	p	FPE	AIC	HQIC	SBIC	
0	-4311.07				3.1e+92	227.162	227.238	227.377	
1	-4095.2	431.75	25	0.000	1.4e+88	217.116	217.576	218.408*	
2	-4070.84	48.708	25	0.003	1.5e+88	217.15	217.993	219.52	
3	-4035.15	71.376	25	0.000	1.1e+88	216.587	217.814	220.035	
4	-3996.68	76.953*	25	0.000	7.8e+87*	215.878*	217.488*	220.403	

Source: Research, 2023

Correlation Analysis

The values in the matrix represent correlation coefficients, which indicate the strength and direction of the linear relationship between pairs of variables.

Table 4: Pearson Correlation Coefficient

Variables	GDP	Imports	External debt
GDP	1.000		
Imports	0.945*	1.000	
External debt	0.941*	0.819*	1.000

*** $p < 0.01$, ** $p < 0.05$, * $p < 0.1$

Source: Research, 2023

GDP and Imports have strong positive to one another. The correlation coefficient of 0.945 suggests that higher GDP is associated with higher levels of Imports. The relationship is highly significant. Further the correlation coefficient of 0.941 indicates a very strong positive relationship between GDP and External Debt. This suggests that higher GDP is associated with higher levels of External Debt.

Normality Assumption Using Jarque-Bera Test

The Jarque-Bera test statistic was 1.434 and its p-value was 0.488 in Figure 1, which is higher than 0.05 and indicates that the null hypothesis cannot be ruled out. The evidence of normal distribution has thus not been in any way compromised.

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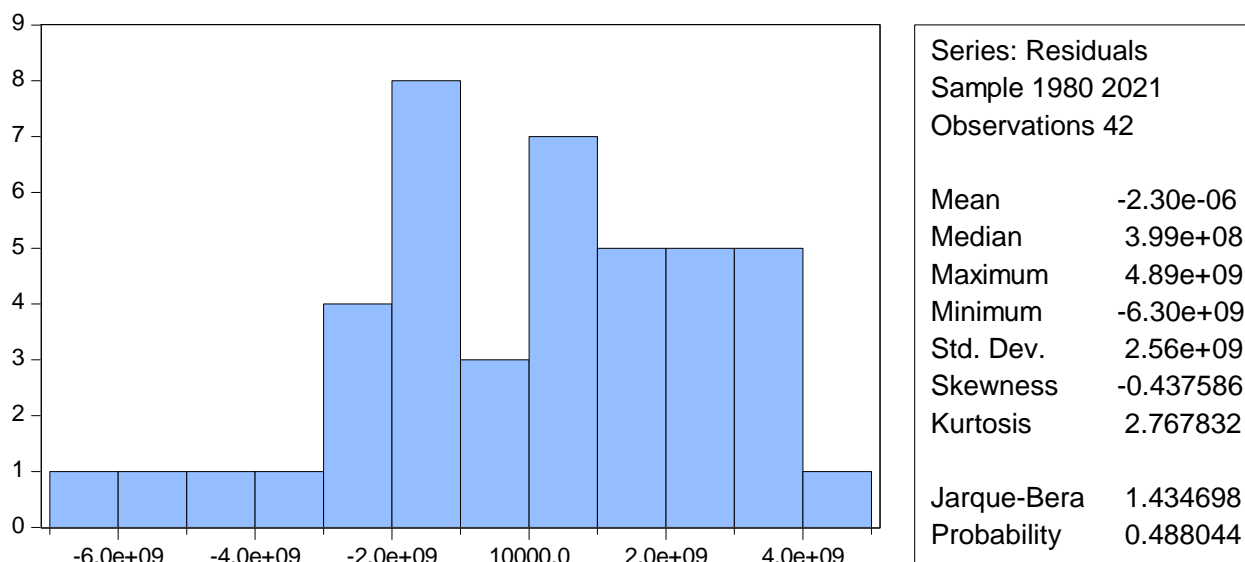


Figure 1: Jarque-Bera test for Normal Distribution of Residuals

Source: Research, 2023

Multicollinearity Using Variance Inflation Factors (VIF)

The results of the VIF test yielded values between 1.04 and 1.33. According to (Newbert, 2008), variables with high VIF of 10 signify high multicollinearity. As a result, multicollinearity does not seem to be an issue based on the outcomes of the diagnostic tests.

Table 4: VIF Measure for Multicollinearity

Variables	Variance inflation Factors (VIF)	Tolerance (1/VIF)
Imports	1.33	0.7534
External debt	1.04	0.9604
Mean VIF	1.19	

Source: Research, 2023

Serial Correlation

The results of this investigation revealed that the chi-square p-value was 0.6365. Therefore, the study concluded by accepting the null hypothesis that no serial correlation was detected. Further the findings can be supported by Durbin Watson (1951) that postulated that the d-statistic which lie between 1.5 and 2.5 indicate no serial correlation. The table show Durbin Watson statistic was 1.698 confirming no serial correlation.

Table 5: Breusch-Pagan-Godfrey For Serial Correlation

F-statistic	0.596833	Prob. F(4,37)	0.6672	
Obs*R-squared	2.545690	Prob. Chi-Square(4)	0.6365	
Scaled explained SS	1.746310	Prob. Chi-Square(4)	0.7823	
Variable	Coefficient	Std. Error	t-Statistic	Prob.
Constant	5.68E+18	2.43E+18	2.339253	0.0248
Imports	-1.40E+08	9.13E+08	-0.152981	0.8792
External Debt	-1.84E+08	2.73E+08	-0.673543	0.5048
Log likelihood	-1888.886	Hannan-Quinn criterion.	90.26089	
F-statistic	0.596833	Durbin-Watson stat	1.697849	
Prob(F-statistic)	0.667177			

Source: Research, 2023

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Homoscedasticity Using Breusch-Pagan / Cook-Weisberg

The results of this test, indicate that the model's residuals have a homoscedastic distribution. The p-values for the chi-square test statistics of 0.5531, which are higher than the significance threshold of 5% (0.05). Therefore, supporting the null hypothesis.

Table 6: Homoscedasticity Test for Residuals

Source	chi ²	Df	Prob>chi ²
Breusch-Pagan LM statistic:	0.35	1	0.5531
H ₀ : Constant Variance			

Source: Research, 2023

Model Estimation Results and Interpretation

Table 7: ARDL Regression Results

Sample: 1984 - 2021		Number of obs = 38	
F(19, 18) = 4819.79		Prob > F = 0.0000	
R-squared = 0.9998		Adj R-squared = 0.9996	
Log likelihood = -810.74624		Root MSE = 6.485e+08	

	gdp	Coef.	Std. Err.	t	P> t	[95% Conf. Interval]	
gdp							
L1.	.0272433	.130565	0.21	0.837	-.2470636	.3015501	
L2.	.5448242	.1344061	4.05	0.001	.2624476	.8272009	
L3.	.1927851	.1063266	1.81	0.087	-.0305989	.4161691	
imports							
--.	.2685934	.1110703	2.42	0.026	.0352434	.5019433	
L1.	-.1984278	.1210819	-1.64	0.119	-.4528114	.0559558	
L2.	.3665215	.1371805	2.67	0.016	.078316	.654727	
exdebt							
--.	1.44276	.2140177	6.74	0.000	.9931257	1.892395	
L1.	-.518757	.319262	-1.62	0.122	-1.189502	.1519875	
L2.	-.3329147	.3361613	-0.99	0.335	-1.039163	.373334	
L3.	-.4648294	.2337672	-1.99	0.062	-.9559562	.0262973	
_cons	-2.18e+09	6.29e+08	-3.47	0.003	-3.50e+09	-8.59e+08	

Source: Research, 2023

DISCUSSION OF THE FINDINGS

The result presented contains output for 4 lags, but from the Schwartz-Bayesian criterion, suggested at most 2 lags as the optimum lag order. This implies the study explains and discusses findings based on the zero lag (L0), lag one (L1) or two lags (L2).

For the imports, the coefficient for L0 and L2 are $\beta=0.2685$ and $\beta=0.3665$ respectively, which are statistically significant with corresponding p-value 0.026 and 0.016, indicating a positive impact of imports at lag 2 on economic growth in Kenya. While the coefficient for external debt L1 is $\beta = -0.5187$, which is marginally significant (p-value: 0.122), implying a negative impact of external debt at lag 1 on GDP. The coefficient for L2 is $\beta = -0.3329$, which is not statistically significant (p-value = 0.335).

The positive coefficient of import ($\beta = 0.269$, p-value = 0.026) implies that an increase in imports is associated with higher economic growth. This might be because imports can provide necessary raw materials, intermediate goods, and consumer products that fuel domestic production and consumption, thus positively influencing economic activity. The positive effect implies that a unit

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increase in imports causes positive change in GDP by 0.269 units. When an increase in imports per unit results in an improvement in GDP, this illustrates a situation where imports are linked to favorable economic outcomes. The significance of imports as a vital conduit for the transfer of foreign technology and knowledge into the home economy has been underscored by recent endogenous growth models (Grossman and Helpman, 2015). Imported intermediate items, such as machinery and equipment, may include new technologies, and when workers gain the skills necessary to "unbundle" these new technologies, labor productivity may rise (Thangavelu and Rajaguru, 2014).

The findings concurs with Abdullahi *et al.* (2016) who found that import has a positive impact on GDP growth in West African countries. Lawal & Ezeuchenne (2017) showed that there is a long-run imports and economic growth. The assumption of import-led development in India during the post-reform period was examined by Maitra (2020). In the short and long terms of his study, he discovered strong evidence that the ILG hypothesis is correct, showing that imports have a major impact on India's economic growth. Taniguchi (2018) investigated how a rise in Chinese imports affected Japan's regional labor markets. He discovered proof that China's import increase had a favorable impact on Japan's prefecture-level manufacturing job growth.

External debt on the other hand can be both beneficial and risky for economic growth. The positive coefficient ($\beta = 1.443$, p -value = 0.000) indicates that an increase in external debt is associated with higher economic growth. One reason for this could be that countries often borrow to finance large-scale infrastructure projects and development initiatives that can stimulate economic activity in the short and long term. However, it's important to manage debt levels to avoid potential negative consequences on financial stability and growth sustainability. The foreign borrowing by the government can affect economic growth both positively and negatively. According to Presbitero's (2012) research, developed nations are more adept at making constructive use of debt than emerging nations. According to Chenery and Strout (1966), a lack of investment and saving is the primary cause of developing and emerging nations' accumulation of foreign debt. In order to borrow money for consumption, countries with low savings will turn to the domestic or foreign debt markets, which will stabilize and smooth economic growth. Developing nations also turn to the debt market for other reasons, including low levels of investment, balanced budget deficits, and limited government revenue (Gohar *et al.* 2012). Warner (2012) found a positive correlation between foreign debt and economic growth, which is the opposite of other empirical findings. Using least square estimate, the investigation was conducted over a 20-year span on 13 developing nations.

There are internal variables that contribute to Kenya's foreign debt. These mostly relate to excessively expansionary fiscal policies and severely skewed trade policies, particularly those that imposed a strong export-bias. Deficits in the public sector have been a significant issue.

However, the findings showed that external debt had a strong positive effects on economic growth ($\beta=1.443, p\text{-value}=0.000$). Since the findings were significant An increase in external debt by one unit causes an increase in economic growth by 1.443 units. This is an implication that If the external debt is being used to finance productive investments in infrastructure, technology, and other sectors that have a positive impact on economic growth, it could lead to higher GDP. These investments might stimulate economic activity, create jobs, and increase overall productivity. The increase in external debt might attract private investment due to improved investor confidence.

CONCLUSION

The results of this study have advanced our understanding of how import and external affect Kenya's economic development. It also has a number of effects on economists, policymakers, and practitioners of the theory of economic growth. The results of this study demonstrate that more work has to be done to enhance each economic sector. Based on the findings that have been provided, here are some policy suggestions for Kenya to enhance its economic growth. These policy recommendations should be implemented with a focus on long-term economic sustainability and inclusive growth, taking into account the unique challenges and opportunities within Kenya's economic landscape. As external debt has a positive impact on economic growth, Kenya should continue to manage its debt prudently. Ensure that borrowed funds are invested in projects and initiatives that generate sufficient returns to service the debt effectively. Develop a comprehensive debt management strategy that considers both short-term and long-term implications. Given the positive impact of imports on economic growth, continue to pursue trade policies that facilitate imports of goods and services. This includes reducing trade barriers, simplifying customs procedures, and promoting trade agreements that expand access to global markets. In addition, maintainin fiscal discipline helps to ensure that government spending is sustainable. A well-managed fiscal policy can help create a stable economic environment that is attractive to investors and minimizes the risk associated with external debt. Regular assessments will help policymakers adjust strategies as needed to maximize their positive effects on economic growth.

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