

Research Article

The Role of Foreign Direct Investment on Economic Growth: Evidence from Comoros

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Abstract: This study examined the relationship between Foreign Direct Investment (FDI) and economic growth in Comoros from 1981 to 2022. While some prior research finds a positive impact of FDI on growth, other studies report negligible effects or ambiguity in the relationship. The current analysis employed the autoregressive distributed lag bounds testing approach after confirming stationarity and cointegration. The results of the analysis indicated a long-run relationship among variables influencing growth based on the bounds test. However, individual variables did not significantly impact growth in the level's equation. This suggests policymakers should explore additional determinants or economic indicators beyond those analyzed in this study, such as structural changes, to more meaningfully influence domestic production in Comoros. Further examination of other growth drivers could provide insights to optimize foreign capital inflows.

Keywords: Foreign direct investment, Economic growth, ARDL-Model, Comoros.

I. INTRODUCTION

Foreign Direct Investment (FDI) is increasingly recognized to be a critical component of economic growth, especially in developing countries like Comoros. The archipelago has long been dealing with economic problems, most of which include low economic growth rates, high percentages of poverty, and few capital resources. FDI can be a transformative contributor by providing the necessary amount of financial resources, transferring technology, and managerial abilities that can stimulate economic activity and improve productivity. However, despite the potential, Comoros could only lure a certain volume of average FDI inflows worth 0.6 percent of GDP between 2011 and 2020, which in turn became an indicator of the barriers of structure that discourage investment.

This manuscript examines the role of FDI in the promotion of economic growth in Comoros. By analyzing the connection between FDI and economic growth, this study offers insights into how Comoros can utilize foreign investments to achieve sustainable development as well as improve the welfare of its population.

According to the theoretical literature, FDI supplies capital that can be used for investment in infrastructure, industries, and services (Ahmad & Hamdani, 2003). For Comoros, raising FDI could bridge gaps in both physical and human capital that have constrained economic growth since time immemorial. Foreign investors bring along newer technologies and new ways of doing things, which might be more efficient than domestic ones (Yusuf et al., 2020). FDI may spur new entrepreneurial activities and expansions of already existing businesses that eventually open up new jobs. Even so, FDI faces various barriers in Comoros, most of which include a fragile institutional setup, a lowly infrastructural base, and remote geography. This sums up to unfavorable investment conditions for FDI (World Bank, 2023). Improving the destination attractiveness for foreign investment involves addressing such challenges.

Studies on FDI-growth nexus produced mixed results reflecting the diversified and sector-specific nature of the relationship.

The country that has been adopted as the base for study purposes is Bangladesh, and its Panel Vector Error Correction Model (Panel VECM) was applied to six sectors with inflows of FDI in the time span 2007-2019. The result indicated a unidirectional causality from Real Gross Domestic Product (RGDP) towards Real Foreign Direct Investment (RFDI), and thus, it would mean economic growth drives the FDI rather than the vice versa case of the reverse process (Ai-jun et al. 2024). This signifies that the policy should be sector-specific so FDI could attract it, resulting in a better economic growth scenario. One Malaysian study from 1970 to 2005 established the fact that there was a very positive correlation between FDI and economic growth. In fact, a 1% growth in FDI could eventually increase the value of RGDP by 0.046%, which means it is one of the prime movers behind the economy of Malaysia in question (Har Wai Mun et al. 2008).



Yimer (2022) focused on the impact of FDI on the economic growth of Africa between 1990 and 2016. It was established through a dynamically common correlated effect approach in an error-correction model that the short-run effect is found to be insignificant in the economies analyzed, even though the long-run impact of FDI on economic growth is significantly positive. This means that although FDI does contribute positively to growth in the long term, its short-term influence is not possibly as high.

This would conduct a validity test in its assertion by focusing on a series of trade interactions/interplay involving exports coupled with foreign direct investment/engagement to assess a plausible impact it may influence through economic growth within its sampling of 45 nations and all through their years across Africa from 1990 through 2014. Therefore, researchers would exploit the use of an enhanced, endogenously established model of economic growth combined with a technique called Dynamic Systems General Method of Moment that would resolve endogeneity issues among the applied research. The results of the study provide robust support for the Bhagwati hypothesis, showing that the interaction of trade and FDI significantly contributes to economic growth. The results are crucial for policymakers, who should develop credible export-promotion strategies and direct FDI towards export-oriented sectors as part of long-term development plans in African countries.

Agbloyor et al. (2016) analyzed the nexus between FDI, institutions, and economic growth across different country environments in sub-Saharan Africa. The paper employed a two-step generalized method of moments estimator with Weidmeijer corrected standard errors and orthogonal deviations to empirically examine the relationships. When analyzing the full sample, the study found no evidence that FDI promotes growth. Again, they failed to establish any meaningful link between FDI and economic growth in a subsample excluding countries with developed financial markets. However, they found a direct, positive relationship between FDI and economic growth in a sample that excluded countries with abundant natural resources. One important implication of this study is that countries, depending on their unique characteristics, will have to focus on policy formulation aimed at reaping better economic growth from the inflow of FDI. With that understanding of country-specific facts, a government can strategically and well-design frameworks of the rules of the game for maximal growth benefits associated with the inflow of foreign investments.

Yeboua, K. The nexus between FDI and the economic growth of African countries has been probed (2020) through the role of institutional development. The author analyzed the data of 27 African countries over the period of 1990-2017 by using the panel smooth transition regression model. The results show that FDI significantly promotes economic growth in countries where institutional development exceeds a certain threshold. In contrast, however, FDI in less developed countries tends to either have adverse or negligible impacts on growth. This affirms the critical importance of stronger institutional frameworks in unlocking gains from FDI for an African continent to grow ahead.

Seyoum et al. (2015) examine the Granger causal relationship between foreign direct investment (FDI) and economic growth (measured by real GDP growth) using annual panel data from 23 African countries spanning 1970 to 2011. The study employs recent panel econometric techniques to account for non-stationarity and cross-sectional dependence when analyzing the FDI-growth nexus. The empirical results indicate a two-way Granger causality between FDI and economic growth. Moreover, the causal link is shown to not be homogeneous across countries. Specifically, unidirectional causality is observed running from FDI to GDP growth in Egypt, Gabon, and Mauritania. Meanwhile, causality runs from GDP growth to FDI in Côte d'Ivoire, Kenya, South Africa, and Zambia. The findings are robust when estimating the relationship between FDI as a share of gross capital formation and real GDP growth. Overall, the analysis reveals diverse FDI-growth dynamics across African nations over the long timeframe examined.

Considering the extensive empirical research establishing the relationship between foreign direct investment (FDI) and economic growth, yet lacking analyses specific to Comoros, this study aims to examine the impact of FDI on growth in Comoros over the period 1981 to 2022. Using the autoregressive distributed lag (ARDL) regression approach, the analysis seeks to fill this knowledge gap by exploring the FDI-growth nexus in the Comoros context. The ARDL technique is well-suited for the study's time-series dataset to investigate the presence and nature of any long-run relationship between FDI inflows and domestic economic expansion, as measured by GDP, after controlling other influential factors. By focusing on Comoros, the findings aim to provide country-specific insight into how FDI may influence growth dynamics in this developing island nation over multiple decades.

To address the research aims, this study seeks to answer the following questions:

What is the nature and magnitude of the relationship between foreign direct investment (FDI) and economic growth in Comoros?

The following hypotheses are proposed:

Ha1: There is a statistically significant positive relationship between FDI inflows and economic growth in Comoros.

Ha2: There is a statistically significant negative relationship between FDI inflows and economic growth in Comoros.

Examining these hypotheses will elucidate how FDI impacts overall domestic production and whether certain sectors are more influential in driving national economic expansion through foreign capital in Comoros. The findings aim to provide nuanced insight into FDI-growth dynamics that can help guide policy efforts to maximize the growth effects of attracting foreign capital across industries in Comoros.

II. RESEARCH METHOD

In this section, the study outlines the research methodology employed. The analysis is grounded in an empirical examination of time series data from Comoros, covering the period from 1981 to 2022. Data was obtained from the World Bank Development Indicators. The study applied the Autoregressive Distributed Lag (ARDL) regression technique to assess the long-run and short-run relationships between economic growth and Foreign Direct Investment (FDI) in Comoros.

Econometrics model:

$$RGDP_{i,t} = \sum_{t=1}^p \sigma_t RGDP_t - 1 + \sum_{t=1}^q \beta_{1t} FDI_t - 1 + \sum_{t=1}^q \beta_{2t} DCPS_{i,t} - 1 + \sum_{t=1}^q \beta_{4t} EXPORT_t - 1 + \sum_{t=t}^q \beta_{8t} GDSV_t - 1 + ECM_{t-1} + \varepsilon_{i,t}$$

Whereas,

RGDP: Annual real GDP growth

FDI: foreign direct investment inflow as a share of GDP

DCPS: domestic credit provided to the private sector as a share of GDP.

EXPORT: export as a share of GDP.

GDSV: gross domestic saving as a share of GDP.

ECM: error correction model.

ε: random error.

III. DATA ANALYSIS

Table 1: Descriptive statistics

	RGPG	FDI	EXPORT	DCPS	GDSV
Mean	0.3280	0.4094	9.3120	8.7306	-1.5972
Median	0.5741	0.2630	8.8363	6.4933	-0.0429
Maximum	8.7177	2.2597	12.9090	17.9884	1.6819
Minimum	-7.7824	-0.3164	5.6718	3.8787	-10.5847
Std. Dev.	2.8533	0.5565	1.2999	4.5868	2.7745
Skewness	-0.4717	1.9426	1.1144	0.7458	-1.7129
Kurtosis	5.8682	6.6641	5.9301	1.9968	5.2413
Obs.	42	42	42	42	42

Table 1 presents descriptive statistics for five economic variables: Real GDP Growth (RGPG), Foreign Direct Investment (FDI), Exports (EXPORT), Domestic Credit to Private Sector (DCPS), and Gross Domestic Savings (GDSV). Each statistic provides insights into the distribution and characteristics of the data for these variables.

A) Key Statistics Results

a. Mean

RGPG: The average growth rate is 0.3280, indicating modest overall growth in real GDP over the sample period. FDI: The average value of FDI is 0.4094, suggesting a relatively low level of foreign direct investment. EXPORT: The mean export value is 9.3120, indicating a moderate level of exports. DCPS: The average domestic credit to the private sector is 8.7306, reflecting a reasonable level of credit availability. GDSV: The mean gross domestic savings are -1.5972, indicating that, on average, savings are negative, which may suggest a tendency to dissave or a deficit in savings relative to investment.

b. Median

RGPG: The median value of 0.5741 is higher than the mean, suggesting a right-skewed distribution with some higher growth rates. FDI: The median of 0.2630 is lower than the mean, indicating a few high values that influence the average. EXPORT: The median export value of 8.8363 is lower than the mean, suggesting a right-skewed distribution. DCPS: The

median of 6.4933 is significantly lower than the mean, indicating that the distribution is skewed by higher values. GDSV: The median of -0.0429 is close to zero, indicating that while the average is negative, many observations are near zero.

c. Maximum and Minimum

RGPG: The maximum growth rate is 8.7177, while the minimum is -7.7824, indicating significant variability in growth rates. FDI: The maximum FDI is 2.2597, and the minimum is -0.3164, suggesting that while there are positive investments, there are also periods of disinvestment. EXPORT: Exports range from a minimum of 5.6718 to a maximum of 12.9090, indicating a relatively stable export environment. DCPS: The maximum value is 17.9884, while the minimum is 3.8787, showing a wide range of credit availability. GDSV: The maximum savings value is 1.6819, while the minimum is -10.5847, indicating significant fluctuations in savings behavior.

d. Standard Deviation

RGPG: A standard deviation of 2.8533 describes a high variability in regard to growth rates. FDI: The standard deviation is at 0.5565, which reveals there is moderate variability in terms of foreign direct investment. EXPORT: A standard deviation of 1.2999 is a sign of some level of variability as regards the exports. DCPS: A standard deviation of 4.5868 means there is high variability between the domestic credit levels. GDSV: This standard deviation of 2.7745 has represented variability in saving levels.

e. Skewness

RGPG: With a skewness value of -0.4717, it has little left skewness; hence, some lower growth rates will be seen. FDI: A skewness of 1.9426 displays strong right skewness, suggesting the presence of several extreme values that are high.

EXPORT: A skewness value of 1.1144 suggests moderate right skewness, and there are, therefore, a few high export values. DCPS: 0.7458: The skewness is of moderate right-skewed values, which implies that it has higher values pulling up the average. GDSV: The skewness is -1.7129, a strong left skew, which indicates that the majority of observations are grouped around the lower savings values.

f. Kurtosis:

RGPG: Kurtosis value is 5.8682, which means that the distribution is leptokurtic. Therefore, this distribution is very highly peaked and heavy-tailed compared to the normal distribution. FDI: Kurtosis value is 6.6641. Hence, it is a very high peak distribution with heavy-tailed ones. EXPORT: The kurtosis value is 5.9301, which means the distribution is leptokurtic. DCPS: Kurtosis value is 1.9968, meaning platykurtic. It means this distribution is flat in comparison with the normal distribution. GDSV: Kurtosis value is 5.2413. Thus, it has been said that this is a leptokurtic distribution.

Observations: All the variables have 42 observations; hence, the sample size is uniform for all variables.

B) Implications of the Results

Economic Growth: Since the positive mean RGPG indicates that the economy has been growing, but since it has a high variance, the growth rates of an economy can vary hugely.

Investment Climate: The FDI skewness and kurtosis indicate that it had periods of high investments with significant fluctuations, thereby pointing to instability in the investment climate.

Export Performance: The average and distribution of exports being midway suggest that though exports are positive to the economy, there is a prospect for export strategy improvement.

Availability of Credit: The high standard deviation of DCPS indicates that credit availability varies widely, which influences economic growth as well as investment.

Saving Behaviour: The negative meaning of GDSV and very high variability indicate that saving behavior might be a concern with possible effects on long-term investment and economic stability.

Descriptive Statistics: It summarises the overall view of all the economic variables. A summary of the descriptive statistics gives details on areas of growth and variability, as well as concerns that policymakers may want to address to improve the stability and growth of the economy.

Table 2: Correlations analysis

	RGDP	FDI	EXPORT	DCPS	GDSV
RGDP	1.0000	-0.1508	0.1186	-0.0025	-0.0110
FDI	-0.1508	1.0000	0.0933	0.2490	-0.1635
EXPORT	0.1186	0.0933	1.0000	0.5698	-0.2848

DCPS	-0.0025	0.2490	0.5698	1.0000	-0.8469
GDSV	-0.0110	-0.1635	-0.2848	-0.8469	1.0000

The correlation matrix shown in Table 2 explains relationships between five economic variables - Real GDP (RGDP), Foreign Direct Investment (FDI), Exports (EXPORT), Domestic Credit to Private Sector (DCPS), and Gross Domestic Savings (GDSV) - and their range runs from -1 to +1, which respectively holds for perfect positive correlation, -1 for perfect negative, and 0 as holding no correlation.

C) Key Observations

a. Annual real GDP growth (RGDP):

FDI: There is a weak negative correlation (-0.1508) between RGDP and FDI, suggesting that higher levels of FDI are associated with lower levels of RGDP, although this relationship is not strong.

EXPORT: The correlation with EXPORT is weakly positive (0.1186), indicating a slight tendency for higher exports to be associated with higher RGDP.

DCPS: The correlation with DCPS is negligible (-0.0025), suggesting no meaningful relationship.

GDSV: The correlation with GDSV is also very weak (-0.0110), indicating no significant relationship.

b. Foreign direct investment FDI

EXPORT: The correlation with EXPORT is weak (0.0933), indicating that changes in FDI do not have a strong relationship with export levels.

DCPS: There is a moderate positive correlation (0.2490) with DCPS, suggesting that higher levels of FDI are associated with increased domestic credit to the private sector.

GDSV: The correlation with GDSV is weakly negative (-0.1635), indicating that higher FDI may be associated with lower levels of gross domestic savings.

c. Export

DCPS: The correlation with DCPS is strong (0.5698), indicating a significant positive relationship. This suggests that as domestic credit for the private sector increases, exports also tend to increase, highlighting the importance of credit availability for export growth.

GDSV: The correlation with GDSV is moderately negative (-0.2848), suggesting that higher export levels may be associated with lower gross domestic savings.

d. Domestic credit provided to private sector DCPS

GDSV: There is a strong negative correlation (0.8469) between DCPS and GDSV, indicating that as domestic credit to the private sector increases, gross domestic savings tend to decrease significantly. This suggests a potential trade-off between credit availability and savings, where increased borrowing may reduce the propensity to save.

1. Gross domestic saving (GDSV):

The correlations with other variables indicate that GDSV is negatively associated with both DCPS and EXPORT, suggesting that higher savings may come at the expense of credit availability and export growth.

D) Implications of the Results

Low relations of RGDP with FDI, DCPS, and GDSV indicate that these factors are not contributing much to economic growth within the context of this research. Other variables or policies will be required from the policymakers in order to improve RGDP.

Importance of Domestic Credit: The strong positive correlation between DCPS and EXPORT indicates the importance of access to credit in export activities. Improved credit availabilities may prove to be a strategy for boosting exports and, as a consequence, economic growth.

Savings vs Credit: The negative correlation of DCPS and GDSV suggests that savings might be negatively related to credit. This implies that, for a healthy economy, policymakers may have to make a decision about balancing these two.

Though the correlations of FDI are rather weak with other variables, it suggests that even though FDI has popularly been labeled as a growth promoter, the impact might be very limited in this case. Still, further research that exactly depicts the conditions under which the factor FDI effectively contributes to economic growth may be indicated.

Hence, the correlation matrix may sum up to understanding relationships, if any, among major economic variables and thenceforth may reveal a couple of areas where there could be an intervention from a policy standpoint or the understanding of growth dynamics required on some other fronts.

Table 3: Unit root test

Augmented Dickey-Fuller				Phillips-Perron		
Variables	Level	t-Statistic	Prob.*	Level	t-Statistic	Prob.*
RGDP	I (0)	-7.8724	0.0000	I (0)	-7.7577	0.0000
FDI	I (1)	-10.2754	0.0000	I (0)	-3.9573	0.0039
Export	I (0)	-3.9167	0.0043	I (0)	-3.8079	0.0058
DCPs	I (1)	-6.4238	0.0000	I (1)	-6.4329	0.0000
GDSV	I (1)	-8.8814	0.0000	I (10)	-9.4861	0.0000

Table 3: unit root tests ADF and PP tests for some of the variables RGDP FDI Export DCPs GDSV.

RGDP Real Gross Domestic Product ADF Test: the t-statistic is -7.8724. The p-value is 0.0000; hence, it indicates that RGDP is stationary at level I (0). PP Test: the t-statistics are -7.7577 with a p-value of 0.0000, and they indicate that RGDP is stationary at level I (0). Hence, this also implies that RGDP has no unit root; it can be said to be stationary in nature, hence not differentiable, and appropriate to model without a difference.

ADF Test: FDI The t-statistic gives -10.2754 with a p-value of 0.0000. Hence, FDI is stationary at level I (1). PP Test: The t-statistic shows -3.9573 with a p-value of 0.0039. In this case, it also holds the stationary level of I (0). This implies that this result set states that FDI perhaps stands differenced at its stationary level as non-stationary on its ADF test.

Export: ADF Test: t statistics is -3.9167 at a p-value of 0.0043, signifying export has become stationary at level I (0). PP Test: T-statistics of -3.8079, as well as p-value being 0.0058, proves the null hypothesis that export has become stationary at level I (0). Thus, it, like the RGDP, does not have a unit root. It thus cannot be differentiated and will perfectly be usable for any purposes of analysis as it becomes stationary.

DCPs, ADF Test: t-statistic = -6.4238, and the p-value is 0.0000. Hence, DCPs are stationary at level I (1). PP Test: The t-statistics = -6.4329 with a p-value of 0.0000, and hence DCPs are stationary at level I (1). That is, DCPs show very strong evidence for stationarity, and hence, DCPs can be taken for analysis without further differencing.

GDSV, ADF Test: The t-statistics are -8.8814, with the p-value = 0.0000, which shows that GDSV is stationary at level I (1). PP Test: The t-statistic was -9.4861, which had a p-value = 0.0000 and showed that GFCF was stationary at level I (1). Implication: There is strong evidence of stationarity for GDSV as well. Therefore, it can be used without further differencing in analysis.

From the results, it can be found that RGDP, Export, DCPs, and GDSV are all stationary at level I(0), so no further differencing is required. This is good for time series modeling because it simplifies this task. FDI and DCPs are stationary at level I(1), which means they may be differentiated to become stationary to allow further analyses.

This has emerged as an important condition in determining the validity of any given econometric model because data that is not stationary can lead to spurious regression.

Table 4: Johnsn -Cointegration test

Hypothesized No. of CE(s)	Eigenvalue	Trace Statistic	0.05 Critical Value	Prob.**
None *	0.696635	102.2765	69.81889	0.0000
At most 1 *	0.441873	54.56373	47.85613	0.0103
At most 2 *	0.347287	31.23696	29.79707	0.0039
At most 3	0.298216	14.17225	15.49471	0.0083
At most 4	0.000177	0.007068	3.841465	0.9324

The results in Table 5 indicate that there are at least three significant cointegrating relationships among the variables. This means that these variables tend to move together in the long run, which essentially implies a stable long-term relationship despite short-term fluctuations.

In light of more than one cointegrating equation existing, we have grounds to proceed further in analyzing a Vector Error Correction Model in view. This captures both the short-run dynamics as well as the long-run interplay between the variables analyzed. The existence of such cointegration indicates here that the variables have relevant and meaningful relations with each other. This might even reflect on potential economic theory or worthwhile associations that deserve additional

examination. For instance, should these variables represent economic indicators, then their long-term relationship could be used either to make policy decisions or predict economic activity. Summary-wise, the results provided by the Johansen cointegration test in Table 5 offer enough evidence toward long-run relationships among the variables involved, hence encouraging integration within a framework that captures their dynamics via a VECM.

Table 5: ARDL Long Run Form and Bounds Test Selected Model: ARDL (1, 0, 0, 0, 0)

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	-3.287796	3.638135	-0.903704	0.3723
RGDPG (-1) *	-1.229150	0.162168	-7.579465	0.0000
FDI**	-0.552040	0.868737	-0.635451	0.5293
EXPORT**	0.543904	0.485224	1.120933	0.2699
DCPS**	-0.170750	0.252658	-0.675814	0.5036
GDSV**	-0.207364	0.351278	-0.590313	0.5588
* p-value incompatible with t-bounds distribution. ** Variable interpreted as $Z = Z(-1) + D(Z)$.				
F-Bounds Test		Null Hypothesis: No levels of relationship		
Test Statistic	Value	Signif.	I (0)	I (1)
			Asymptotic: n=1000	
F-statistic	10.08950	10%	2.2	3.09
k	4	5%	2.56	3.49
		2.5%	2.88	3.87
		1%	3.29	4.37

Table 5 presents the long-run relationship between FDI and other macroeconomic variables and economic growth in Comoros.

Long-run relationship: The highly significant F-Bounds value indicates that there is a presence of a long-run relationship in the variables influencing RGPG while the individual variables are found to be insignificant in their levels equation. Adjustment: The negative coefficient of great magnitude for RGDPG (-1) indicates there will be correction of such short-run deviations from a long-run growth path, pointing towards an economic stability perspective.

The lack of significant effects from FDI, Export, Domestic credit provided to the private sector as a share of GDP (DCPS), and gross domestic saving as a share of GDP (GDSV) in the long run suggests that policymakers may need to explore other factors or variables that could influence RGPG more effectively. This could involve looking into structural changes or other economic indicators that were not factored into this model.

In summary, while the ARDL model suggests there is a long-run relationship that impacts economic growth in the form of RGDPG, its individual contribution is not statistically significant. Hence, further exploration should be conducted into other factors that could influence economic growth.

IV. CONCLUSION

Foreign Direct Investment, FDI, is also considered the most important variable for stimulating economic growth, but it has not established a certain relationship with economic growth. Some analyses show a positive effect on economic growth from FDI, whereas others claim the effect of FDI to be quite small. Another reason to be concerned here is that the relationship is not much analyzed in the Comoros case.

This research study analyzes the relationship between FDI and economic growth in Comoros from 1981 to 2022. The study begins by testing for stationarity and cointegration and determines that the models are fitted to the ARDL long-run bounds test. The results of the ARDL analysis confirmed that there is a long-term relationship among the variables affecting economic growth, though individual variables do not exhibit any significant effects in the levels equation. Thus, findings call for policymakers to further research other factors or variables that may better influence economic growth. This investigation may include structural changes or other economic indicators that were not considered in this study.

Interest Conflicts

The author(s) declared(s) that there is no conflict of interest concerning the publishing of this paper.

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